

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE DEPARTMENT OF EDUCATION

In the Matter of:

Independent School District #271
(Bloomington)

and

Intermediate District #287

**AMENDED
FINDINGS OF FACT,
CONCLUSIONS OF LAW,
AND DECISION**

This matter was referred to the Office of Administrative Hearings (OAH) by the Department of Education for a contested case proceeding and final decision, pursuant to Minn. Stat. § 14.57(a) (2014).¹

An evidentiary hearing was held before Administrative Law Judge Ann O'Reilly on June 23, 24, 25, 26, 27, and 30, 2014.

David L. Holman, Holman Law Offices, appeared on behalf of Independent School District #271 (Bloomington). Sara Ruff, Attorney at Law, and Anne Becker, General Counsel, appeared on behalf of Intermediate School District #287 (Intermediate District or District). Daron Korte, Chief Legal Counsel, observed the proceedings on behalf of the Department of Education (Department).

POST-HEARING PROCEDURAL HISTORY

After the hearing, the parties submitted post-hearing briefs. After reviewing the post-hearing briefs and arguments, the Administrative Law Judge requested additional information from the parties, including additional exhibits, which were marked by the judge as Exhibits A through Z and AA. The Judge concluded that she could not decide the matter without reviewing the requested legal documents.²

¹ See Notice and Order for Prehearing Conference and Hearing dated October 20, 2013.

² For a detailed explanation of why the additional documents were requested by the Administrative Law Judge and how those documents were entered into the hearing record without objection by the parties, see Order Partially Granting and Partially Denying Intermediate District's Motion for Reconsideration and Order Denying Bloomington's Motion for Reconsideration, dated June 29, 2015, which is incorporated herein by reference.

The hearing record closed on December 19, 2014, upon receipt of the last post-hearing correspondence and the issuance of an Order Supplementing the Hearing Record to include Exhibits A-Z and AA.³

On January 7, 2015, the Administrative Law Judge issued the original Findings of Fact, Conclusions of Law, and Decision in this matter.⁴

On January 16, 2015, the Intermediate District timely filed a Motion for Reconsideration. On February 2, 2015, Bloomington filed a cross Motion for Reconsideration. Oral argument on the Motions for Reconsideration was held on March 12, 2015. At the Motion hearing on March 12, 2015, the Intermediate District requested the opportunity to reopen the hearing record and offer additional exhibits related to the real property transactions that are at issue in this matter.⁵

The Administrative Law Judge gave the parties until April 10, 2015, to enter into stipulations regarding the inclusion of additional documents into the hearing record. The Judge agreed to allow the supplementation of the hearing record with additional evidence if the parties could agree on the documents to be included into the hearing record.⁶ The parties were unable to agree to the inclusion of additional exhibits into the hearing record.⁷

The Administrative Law Judge then requested that the Intermediate District provide a list of the additional documents it wished to include in the hearing record, and asked that Bloomington respond to each of those documents.⁸ The Judge gave the parties until June 19, 2015, to complete that process.⁹ The Intermediate District sent a list of 26 additional documents it sought to include in the hearing record.¹⁰ Each of the documents was in existence and would have been available to the District prior to the hearing of this matter.¹¹ Bloomington opposed the admission of each of the documents.¹²

On June 29, 2015, the Administrative Law Judge issued an Order granting in part and denying in part the Intermediate District's Motion for Reconsideration; and denying Bloomington's Motion for Reconsideration.¹³ The Order also denied the Intermediate

³ See Order Supplementing Hearing Record with Additional Exhibits, dated December 19, 2014.

⁴ See Findings of Fact, Conclusions of Law, and Decision, dated January 7, 2015.

⁵ See Transcript of Motion Hearing, dated March 12, 2015, at T. 13-14.

⁶ *Id.* at 60-64.

⁷ See e-mail correspondence to Administrative Law Judge Ann O'Reilly from David Holman, legal counsel for Bloomington, dated April 10, 2015.

⁸ See e-mail correspondence from Administrative Law Judge Ann O'Reilly to counsel for the parties dated May 21, 2015.

⁹ *Id.*

¹⁰ See correspondence to Administrative Law Judge Ann O'Reilly from Anne Becker and Katherine Wiik, counsel for the Intermediate District, dated June 4, 2015.

¹¹ *Id.*

¹² See correspondence to Administrative Law Judge Ann O'Reilly from David Holman, counsel for Bloomington, dated June 19, 2015.

¹³ See Order Partially Granting and Partially Denying Intermediate District's Motion for Reconsideration and Order Denying Bloomington's Motion for Reconsideration, dated June 29, 2015.

District's request to supplement the hearing record with additional exhibits.¹⁴ The Order Partially Granting and Partially Denying the Intermediate District's Motion for Reconsideration and Denying Bloomington's Motion for Reconsideration, dated June 29, 2015, is incorporated by referenced into this Amended Findings of Fact, Conclusions of Law, and Decision (Decision).

This Amended Findings of Fact, Conclusions of Law, and Decision reflects the changes made to the original Findings of Fact, Conclusions of Law and Decision upon reconsideration. Accordingly, this Decision represents the **final order** in this case, subject to the parties' rights to appeal to the Minnesota Court of Appeals.

STATEMENT OF THE ISSUES

1. Upon its withdrawal from the Intermediate District, what is Bloomington's proportionate share of the Intermediate District's assets and liabilities based upon Bloomington's enrollment, financial contribution, usage, or other factor or combination of factors?

2. If Bloomington's proportionate share of the Intermediate District's assets exceeds Bloomington's proportionate share of the Intermediate District's liabilities, how should Bloomington's share of the Intermediate District's net assets be disbursed to Bloomington so as to minimize financial disruption to the Intermediate District?

SUMMARY OF DECISION

Based upon Bloomington's enrollment, financial contribution, usage and other factors, Bloomington's proportionate share of the Intermediate District's assets and liabilities is **\$90,751.00**. All or a portion of said amount may be paid to Bloomington by the Intermediate District through non-member tuition credits for Bloomington students to enroll in the Intermediate District. The parties are directed to agree to a payment schedule that minimizes financial disruption to the Intermediate District and its remaining Member Districts. If the parties cannot agree to a payment schedule by **July 15, 2015**, the Administrative Law Judge shall determine the payment schedule, payment type, and the interest, if any, to be applied to the balance owed, after allowing additional written argument by the parties.

Based upon an application of the law, the arguments of counsel, and the evidence in the hearing record, the Administrative Law Judge makes the following:

¹⁴ *Id.*

FINDINGS OF FACT

INTRODUCTION

1. This matter involves the withdrawal of Bloomington from the Intermediate District pursuant to Minn. Stat. § 123A.24 (2014), and the distribution of assets and the assignment of liabilities associated therewith.¹⁵

2. The Intermediate District is a consortium of member school districts created under Minn. Stat. § 136D.21 (2014), to provide special education and other services to students of participating districts.¹⁶ Bloomington was a member of the Intermediate District for approximately 40 years: from the District's inception in 1968 until Bloomington's withdrawal on June 30, 2011.¹⁷

3. Neither the Intermediate District's Joint Powers Agreement with its members nor its Bylaws address the financial implications of a member district's withdrawal from the collective.¹⁸

4. The parties agree that Minn. Stat. § 123A.24 governs Bloomington's withdrawal from the Intermediate District.¹⁹ Section 123A.24 provides, in pertinent part:

Subdivision 1. **Distribution of assets and liabilities.**

(a) If a district withdraws from a cooperative unit defined in subdivision 2, the distribution of assets and assignment of liabilities to the withdrawing district shall be determined according to this subdivision.

(b) The withdrawing district remains responsible for its share of debt incurred by the cooperative unit according to section 123B.02, subdivision 3. The district and cooperative unit may mutually agree, through a board resolution by each, to terms and conditions of the distribution of assets and the assignment of liabilities.

(c) If the cooperative unit and the district cannot agree on the terms and conditions, the commissioner²⁰ shall resolve the dispute by determining the district's proportionate share of assets and liabilities based on the district's enrollment, financial contribution, usage, or other factor or combination of factors determined appropriate by the commissioner. The assets must be

¹⁵ See *id.*

¹⁶ Testimony (Test.) of Sandra Lewandowski at Transcript (T.) 434-35, 437, 443-44.

¹⁷ *Id.* at T. 437; Test. of Les Fujitake at T. 30; Exhibits (Ex.) 21, 102.

¹⁸ Test. of S. Lewandowski at T. 451-52.

¹⁹ See the parties' respective Post-Hearing Briefs filed on August 25, 2014.

²⁰ The statute refers to the Minnesota Commissioner of Education. See Minn. Stat. §§ 123A.01, subd. 1, 120A.05, subd. 4 (2014).

disbursed to the withdrawing district in a manner that minimizes financial disruption to the cooperative unit.

5. After its withdrawal, Bloomington and the Intermediate District were unable to agree on the terms and conditions of the distribution of assets and assignment of liabilities.²¹

6. As a result, on May 25, 2012, the Intermediate District and Bloomington participated in mediation.²² That mediation was unsuccessful.²³

7. On May 31, 2012, the Intermediate District advised the Commissioner that the District and Bloomington were unable to agree to the distribution of assets and assignment of liabilities required by Bloomington's withdrawal.²⁴ The Intermediate District made a formal request that the Commissioner resolve the dispute pursuant to Minn. Stat. § 123A.24.²⁵

8. The Commissioner expressed that she had never been asked to exercise the authority granted by Minn. Stat. § 123A.24, and scheduled a meeting with the parties to discuss resolution.²⁶

9. The Commissioner met with the parties on two occasions to resolve the matter informally.²⁷ Despite her efforts, the Commissioner was unable to resolve the matter with the parties. The Commissioner concluded, "The Minnesota Department of Education does not have the technical knowledge or expertise to make an appropriate determination of the correct valuation of Bloomington's share of the Intermediate's assets and liabilities."²⁸ As a result, the Commissioner referred the matter to the Office of Administrative Hearings for an evidentiary hearing and final decision pursuant to Minn. Stat. § 14.57(a).²⁹

10. The parties agree that Bloomington is not prohibited by law or contract from withdrawing from the Intermediate District.³⁰ The parties disagree, however, on the value of Bloomington's share of assets and liabilities, as well as the manner in which disbursement should occur so as to minimize financial disruption to the Intermediate District.³¹

²¹ See the parties' Post-Hearing Briefs filed on August 25, 2014.

²² Ex. 111.

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.*

²⁶ Ex. 113.

²⁷ See Notice and Order for Prehearing Conference and Hearing at 2.

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.*

11. The parties stipulate to the following list of issues upon which disagreement exists: (1) the value of assets and liabilities associated with real estate in which the Intermediate District has a legal interest; (2) the amount of pension and other post-employment benefits for which Bloomington is responsible; and (3) Bloomington's proportionate share of the Intermediate District's assets and liabilities.³²

12. Minnesota Statutes, section 123A.24, subdivision 1(c), vests the Commissioner of Education (Commissioner) with the authority to resolve the dispute between Bloomington and the Intermediate District. The Commissioner has submitted this dispute to the Office of Administrative Hearings for final determination pursuant to Minn. Stat. § 14.57 (2014).³³ The following constitutes the final agency decision in this matter.³⁴

CREATION AND FINANCING OF INTERMEDIATE DISTRICT #287

13. In the late 1960s, the Minnesota legislature passed legislation authorizing the creation of three "intermediate school districts," each to be comprised of two or more independent school districts in the Minneapolis/St. Paul metropolitan area.³⁵ The legislation, in its current form, allows individual school districts to "enter into agreements to accomplish jointly and cooperatively the acquisition, betterment, construction, maintenance, and operation of technical colleges and the provision of facilities for and instruction in special education, and driving of motor vehicles."³⁶

14. An "intermediate school district" is defined in Minnesota law as "a district with a cooperative program...offering integrated services for secondary, postsecondary, and adult students in the areas of vocational education, special education, and other authorized services."³⁷

15. Federal and state laws prescribe specific requirements on the type of programming public schools must offer, including the special education schools must provide to all eligible students.³⁸ Governmental funding to individual school districts, however, is often insufficient to cover all costs of providing the required services.³⁹

16. The intended purpose and function of an intermediate school district is to enable independent school districts to combine their resources and offer technical and special education to their students in a more cost-effective manner.⁴⁰ By pooling resources and sharing expenses, individual school districts are able to offer their students

³² *Id.*

³³ *See id.*

³⁴ Minn. Stat. § 14.57.

³⁵ 1967 Minn. Laws ch. 822; 1969 Minn. Laws ch. 775; 1969 Minn. Laws ch. 1060.

³⁶ *See* Minn. Stat. § 136D.21.

³⁷ Minn. Stat. § 136D.01 (2014).

³⁸ Test. of L. Fujitake at T. 28-29.

³⁹ *Id.*

⁴⁰ *Id.*

specialized programming that the individual districts may be unable to fully or economically provide on their own.⁴¹

17. Intermediate School District #287 was first established in 1968.⁴² Its original members included 13 Independent School Districts (ISD) in Hennepin and Wright Counties, including: ISD #270 (Hopkins); ISD #271 (Bloomington); ISD #272 (Eden Prairie); ISD #273 (Edina); ISD #276 (Minnetonka); ISD #277 (Westonka); ISD #278 (Orono); ISD #279 (Osseo); ISD #280 (Richfield); ISD #281 (Robbinsdale); ISD #283 (St. Louis Park); ISD #284 (Wayzata); and ISD #286 (Brooklyn Center) (collectively referred to as the “Participating School Districts” or “Member Districts”).⁴³

18. There are three intermediate school districts in the State of Minnesota: (1) Intermediate District #287; (2) Intermediate School District #917, which serves independent school districts in Dakota and Goodhue Counties; and (3) Intermediate District #916, which serves independent school districts in Anoka, Ramsey and Washington Counties.⁴⁴

19. Intermediate School District #287 is the largest of the three intermediate school districts in Minnesota.⁴⁵ The District currently serves approximately 11,996 full- and part-time students from both its Member Districts and non-member districts.⁴⁶

Memoranda of Agreement Establishing Intermediate District #287

20. To create the Intermediate District in 1968, the original Member Districts executed a Memorandum of Agreement setting forth the terms and conditions of the joint powers entity.⁴⁷ The Memorandum of Agreement was subsequently amended in 1972.⁴⁸

21. In 2008, the Superintendent of the Intermediate District determined that it was advisable for the Member Districts to review the 1972 Memorandum of Agreement, and reconfirm their commitment to each other and to the Intermediate District.⁴⁹ As a result, the District drafted, and the Member Districts unanimously executed, a new Memorandum of Agreement, effective on January 1, 2009.⁵⁰ The 2009 Memorandum of Agreement is the most current joint powers agreement for the Intermediate District.⁵¹ The Memoranda of Agreements executed in 1968, 1972, and 2009 are the only organizational

⁴¹ *Id.*

⁴² Ex. 102.

⁴³ Test. of S. Lewandowski at T. 442-44; Ex. 102.

⁴⁴ See Minn. Stat. § 136D.01-.94 (2014).

⁴⁵ Test. of S. Lewandowski at T. 435.

⁴⁶ http://www.district287.org/clientuploads/FACT_Sheets/District_287_Fact_Sheet%20Nov_21_2013.pdf.

⁴⁷ Ex. 102.

⁴⁸ *Id.*

⁴⁹ Test. of S. Lewandowski at T. 446-49; Ex. 102.

⁵⁰ Ex. 102.

⁵¹ *Id.*

documents detailing the terms and conditions of the Member Districts' joint powers arrangement.

22. The 2009 Memorandum of Agreement (Agreement) provides that each Member District shall have one representative on the Intermediate District School Board.⁵² As such, each Member District has an equal voice in the management and operation of the Intermediate District, irrespective of the number of students enrolled in the District.⁵³

23. The Agreement further provides that "Neither members nor member representatives shall have individual liability for the debts and obligations of the District. Member and member representative liability is determined by law."⁵⁴ Thus, debts and obligations incurred by the District remain the liabilities of the Intermediate District, and do not become liabilities of the individual Member Districts.⁵⁵

24. With respect to the withdrawal of Member Districts from the collective, the Agreement states:

Withdrawal of any Member. Any member may withdraw from the District and cause its representative to cease to function in such capacity upon written notice given to the Clerk of the Board before February 1 of any year, such notice to be accompanied by a certified copy of an appropriate resolution of the school board of such member authorizing and directing such withdrawal of the member from the Intermediate District. Any such withdrawal by a member shall be effective June 30 of the following fiscal year.⁵⁶

25. The Agreement does not, however, address how the assets and liabilities of the Intermediate District should be distributed or allocated upon withdrawal of a Member District.⁵⁷ The Agreement is also silent as to a withdrawing Member District's liability for debts of the Intermediate District after withdrawal.⁵⁸

26. While the Agreement does not give direction as to how assets and liabilities shall be distributed upon the withdrawal of a Member District, the Agreement does address the distribution of assets and liabilities upon dissolution of the collective.⁵⁹ The Agreement provides:

⁵² *Id.*

⁵³ *Id.*

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.* The fiscal year for the Intermediate District runs from July 1 to June 30 of each year.

⁵⁷ Ex. 102.

⁵⁸ *Id.*

⁵⁹ *Id.*

Dissolution of Intermediate District. The District shall continue in existence until two-thirds of its membership agree upon dissolution at an annual meeting or special meeting called for the purpose of considering dissolution.

Distribution of Assets upon Dissolution. Upon dissolution of the District, any assets remaining after payment or reservation for debts and liabilities shall be divided among all members of the District as a majority of the members of the Board at the time of dissolution may determine in their discretion. To the extent possible all assets of the District shall be converted to cash prior to dissolution.⁶⁰

Financing of Intermediate School Districts

27. Intermediate school districts in Minnesota do not have the authority to issue bonds or levy taxes to pay for school facilities.⁶¹ The legislature only vests such powers in independent school districts, not intermediate districts.⁶² Thus, to subsidize the operation of programs, the payment of staff, the acquisition of real estate, and the construction of school facilities, intermediate districts must rely on the tax and levy authority of their member districts.⁶³ Member districts tax their residents and then pay the intermediate district for programming and facilities.⁶⁴

28. Intermediate District #287 is primarily funded by two main sources: (1) “tuition costs” charged to Member Districts and non-member districts; and (2) “lease levies” imposed on Member Districts.⁶⁵ The income from tuition is used to pay operating costs, staff costs, and programming costs.⁶⁶ The income from lease levies is used to pay for capital costs, such as real estate leases and acquisitions.⁶⁷

29. The District’s daily operations are primarily funded by the tuition payments made by Member Districts and non-member independent school districts that enroll their students in the programs offered by the Intermediate District.⁶⁸ The tuition amount is different for each of the programs offered by the Intermediate District [i.e., special education, technical education, educational services provided through an Area Learning Center (ACL), education provided to English Language Learners (ELL), etc.].⁶⁹

⁶⁰ *Id.*

⁶¹ See Minn. Stat. § 136D.281, subd. 8; see also Test. of Mae Hawkins at T. 874.

⁶² Test. of M. Hawkins at T. 874.

⁶³ *Id.*

⁶⁴ *Id.* at T. 874, 926-29.

⁶⁵ *Id.* at T. 925; Test. of S. Lewandowski at T. 437. Other sources of funding include the Safe School Levy and Health and Safety Levy. Test. of S. Lewandowski at T. 437.

⁶⁶ Test. of M. Hawkins at T. 925-27; Test. of S. Lewandowski at T. 437.

⁶⁷ Test. of M. Hawkins at T. 925; Test. of S. Lewandowski at T. 625-26.

⁶⁸ Test. of M. Hawkins at T. 925-29.

⁶⁹ *Id.*

30. Each year, as part of the establishment of various education funding formulas, the Commissioner sets the per-pupil tuition for each of the Intermediate District's programs.⁷⁰ The tuition amount is based upon the Intermediate District's funding requirements and obligations, less any federal subsidies or grants received.⁷¹ The same tuition amount is charged to Member Districts and non-member districts.⁷²

31. Non-member districts, however, are also charged an access fee on a per-pupil basis.⁷³ While non-member school districts are able to enroll their students in the programs offered by the Intermediate District, space is often limited and preference is given to students from Member Districts.⁷⁴

32. Because the Intermediate District does not have the authority to issue bonds and levy taxes, it must rely on other mechanisms to finance its facility costs.⁷⁵ To finance capital expenses, such as the District's interests in real estate, each Member District is assessed a lease levy.⁷⁶ The lease levy is used to pay the costs of the contractual agreements that the Intermediate District enters into to acquire interests in real estate and facilities.⁷⁷

33. The amount of the lease levy is based upon the amount of the District's lease obligations divided among the Member Districts based upon the Average Daily Membership of each Member District (i.e., the average number of students each Member District sends to the Intermediate District).⁷⁸

34. Non-member districts do not share in the cost of the lease levies.⁷⁹

INTERMEDIATE DISTRICT'S REAL ESTATE INTERESTS

35. For over 40 years, Bloomington was an active member of the Intermediate District.⁸⁰ During that time, the Intermediate District acquired legal interests in six real properties:

(1) The District Service Center, located in Plymouth, MN;

(2) A residential condominium in Robbinsdale, MN;

⁷⁰ *Id.* at 885-86.

⁷¹ Test. of S. Lewandowski at T. 437.

⁷² Test. of M. Hawkins at T. 927-28.

⁷³ *Id.*

⁷⁴ Test. of S. Lewandowski at T. 633

⁷⁵ Test. of M. Hawkins at T. 907.

⁷⁶ *Id.* at T. 925-29.

⁷⁷ *Id.* at T. 925.

⁷⁸ *Id.* at T. 926.

⁷⁹ *Id.* at T. 927-28.

⁸⁰ Test. of L. Fujitake at T. 30; Test. of S. Lewandowski at T. 437.

- (3) The Edgewood Education Center, located in Brooklyn Park, MN;
- (4) The South Education Center, located in Richfield, MN;
- (5) The West Education Center, located in Minnetonka, MN; and
- (6) The North Educational Center, located in New Hope, MN.⁸¹

36. From its inception in 1968 until approximately 2005, the Intermediate District owned one building: the District Service Center (DSC Property), located in Plymouth.⁸² The District purchased the DSC Property in 1972, and has used the building for administrative offices and storage space since that time.⁸³

37. The District owns the DSC Property free and clear of any mortgages or other encumbrances.⁸⁴ Legal title to the property is held by the Intermediate District, and the District has a fee simple interest in the DSC Property.⁸⁵

38. The market value of the DSC Property is disputed by the parties in this action.

39. From 1968 until 2005, the District was operating all of its educational programs out of leased retail space and unused facilities owned by Member Districts.⁸⁶ Beginning in approximately 2004, under the direction of then Assistant Superintendent Sandra Lewandowski (Lewandowski), the Intermediate District decided that its former practice of renting facility space to conduct its programming was inefficient and inadequate.⁸⁷

40. According to Lewandowski, the leased facilities were no longer providing safe or effective educational environments for their special needs students, and often required extensive retrofitting or remodeling to meet the District's requirements.⁸⁸ Remodeling the rented facilities to meet the District's needs was expensive, and, because the District did not own the properties, the District could not recoup its investment in the improvements at the end of the lease terms.⁸⁹

41. Consequently, the District embarked on a long-term facilities planning process to investigate whether it was more efficient or economical for the District to

⁸¹ Exs. 1-13, 104-07, A-Z; *see also* Test. of L. Fujitake at T. 56-58.

⁸² Test. of S. Lewandowski at T. 445-46, 626-29; Ex. 4 at 49.

⁸³ Ex. 4 at 1, 10, 49.

⁸⁴ Test. of Robert Lutz at T. 228; Ex. AA.

⁸⁵ Ex. AA.

⁸⁶ Test. of S. Lewandowski at T. 445-46, 626-29.

⁸⁷ *Id.*

⁸⁸ *Id.*

⁸⁹ *Id.*

purchase facilities rather than rent space.⁹⁰ After much study, the District decided that it should purchase real estate and build its own facilities to suit the District's unique needs.⁹¹

42. As an intermediate school district, the District does not have the legal authority to levy taxes or issue bonds to pay for the construction of new facilities.⁹² Therefore, unless the District was able to purchase a property in cash, creative financing was required to acquire real property.⁹³ The District found such creative financing in the use of certificates of participation and lease purchase agreements, which will be more specifically described below.

43. In 2005, the Intermediate District purchased a residential condominium in Robbinsdale, Minnesota (Robbinsdale Condo or Condo) to use for educational programming. The District hold legal title to the Condo, and owns the property free and clear of any mortgages. The District has a fee simple interest in the Condo. The parties do not dispute that the market value of the Robbinsdale Condo is \$50,000.⁹⁴

44. Between 2004 and 2010, the District acquired legal interests in four other real properties: the West Education Center (WEC Property) in 2004; the South Education Center (SEC Property) in 2006; the Edgewood Education Center (EEC Property) in 2010; and the North Education Center (NEC Property) in 2010.⁹⁵ The District's legal interest in each of these properties was acquired using financing vehicles involving certificates of participation and long-term lease agreements.⁹⁶

45. During the time that the Intermediate District was acquiring its interests in all of these real properties, Bloomington was a full, participating Member District of the Intermediate District.⁹⁷ Bloomington voted in favor of the Intermediate District acquiring a legal interest in the Robbinsdale Condo, the EEC Property, the SEC Property, and the WEC Property.⁹⁸ Bloomington ultimately opposed the Intermediate District's decision to acquire a legal interest in the NEC Property.⁹⁹

46. A detailed explanation of the District's real estate transactions is set forth below.

⁹⁰ *Id.*

⁹¹ *Id.*

⁹² *Id.* at T. 437.

⁹³ *Id.*

⁹⁴ See Bloomington's Post-Hearing Brief.

⁹⁵ See Exs. A, B, D, E, I, J, K, L, R, S, T.

⁹⁶ See Exs. A-W.

⁹⁷ Test. of L. Fujitake at T. 30; Test. of S. Lewandowski at T. 437.

⁹⁸ The parties do not dispute that Bloomington voted in favor of the District acquiring legal interests in the Robbinsdale Condo, EEC Property, SEC Property, and SEC Property.

⁹⁹ Ex. 22.

Financing of Real Estate Acquisitions by the Intermediate District

47. Because the Intermediate District does not have the legal authority to levy taxes or issue bonds, it must rely on other methods to finance the acquisition of real property and the construction of school facilities. In recent years, the Intermediate District has used certificates of participation and various forms of leases to finance its real estate acquisitions.¹⁰⁰

48. To establish these types of financing arrangements, the Intermediate District worked with a lender to finance the purchase of real property and the construction of facilities.¹⁰¹ Rather than entering into promissory notes and mortgages with the lender, as is done in traditional financing arrangements, the District and the lender entered into long-term leases in which the lender generally takes title to the property and serves as the lessor, and the District becomes the lessee of the property.¹⁰² Title to the property generally remains with the lender and the District obtains a possessory interest via a lease agreement.¹⁰³

49. Under the lease agreements, the District and lender agree to a fixed interest rate which is applied to the principal amount paid by the lender for the acquisition and construction of the property.¹⁰⁴ The principal and interest are then amortized over a period of years and divided into a "lease payment" or "rent payment," payable once or twice yearly by the District to the lender.¹⁰⁵

50. Under the terms of these lease agreements, the lender generally remains the owner of record until the last lease payment is made, at which time unencumbered legal title to the property is conveyed to the District.¹⁰⁶ As a result, the District does not own or have marketable legal title to the property (and, thus, cannot convey title to the property to a third party) until: (1) all lease payments are made at the end of the lease term; or (2) the District exercises its option to purchase the property and prepays the lease prior to the expiration of the lease term.¹⁰⁷ Thus, during the lease term and until the District exercises its option to purchase the property, the District holds only possessory and leasehold interests in the property.¹⁰⁸ Legal title remains vested in the lender.¹⁰⁹

¹⁰⁰ See Exs. A-W; Test. of M. Hawkins at T. 907-08.

¹⁰¹ Exs. A-W.

¹⁰² Exs. A-W.

¹⁰³ Exs. A-W.

¹⁰⁴ Exs. A-W.

¹⁰⁵ Exs. A-W.

¹⁰⁶ Exs. A, D, F, I, J, N, R.

¹⁰⁷ Exs. A, D, F, I, J, N, R.

¹⁰⁸ Exs. A, D, F, I, J, N, R.

¹⁰⁹ Exs. A, D, F, I, J, N, R.

51. What distinguishes these leases from typical commercial leases is that the District's leases all contain non-appropriation provisions, as required by state law.¹¹⁰ These non-appropriation clauses permit the District to terminate the lease at the end of any fiscal year without further liability.¹¹¹ Upon early termination, the District forfeits all rent payments made prior to termination and the lender retains all right and title to the property, similar to a contract for deed.¹¹²

52. To recoup the cost of the property and construction, and to minimize its financial risk, the lender issues certificates of participation to outside investors in amounts roughly equal to the amount paid by the lender for the acquisition and construction of the property.¹¹³ Thus, the investors, not the lender, carry the financial risk of the District's early termination or default.

53. A certificate of participation is a financing vehicle by which an investor purchases a share of an income stream arising out of an agreement, in this case, lease revenues.¹¹⁴ According to the Municipal Securities Rulemaking Board, a certificate of participation is defined as:

An instrument evidencing a pro rata share in a specific pledged revenue stream, usually lease payments by the issuer that are typically subject to annual appropriation. The certificate generally entitles the holder to receive a share, or participation, in the payments from a particular project. The payments are passed through the lessor to the certificate holders. The lessor typically assigns the lease and the payments to a trustee, which then distributes the payments to the certificate holders.¹¹⁵

54. Certificates of participation are an alternative to bond financing, in that they allow a governmental entity the ability to avoid legal restrictions, if any, on the type or

¹¹⁰ See, e.g., Minn. Stat. §§ 126C.40, subd.1(d), 465.71 (2014); see also Exs. A, D, F, I, J, N, R, U.

¹¹¹ Exs. A, D, F, I, J, N, R.

¹¹² Exs. A, D, F, I, J, N, R. A "contract for deed" is defined as "[a]n agreement by a seller to deliver the deed to the property when certain conditions have been met, such as completion of payments by purchaser." BLACK'S LAW DICTIONARY at 227 (Abridged 6th ed. 1991). A contract for deed can also sometimes be referred to as a "contract sale," an "installment contract," or a "land contract." See APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL (5th ed. 2010). A "contract sale" is defined as "[a] sale in which the title to the property or goods remains with the seller until the buyer has fulfilled the terms of the contract, which usually call for payment in full. *Id.* at 44. An "installment contract" is defined as "[a] type of purchase contract in which payment is made in prescribed installments that are usually forfeited if default occurs; in the sale of real property, title is not normally transferred until all payments under the contract are made. *Id.* at 101-102. A "land contract" is defined as "[a] contract in which a purchaser of real estate agrees to pay a portion of the purchase price when the contract is signed and additional sums, at intervals and in amounts specified in the contract, until the purpose price is paid and the seller delivers the deed; used primarily to protect the seller's interest in the unpaid balance because reversion to clear title can be accomplished more quickly than could be under a mortgage." *Id.* at 108.

¹¹³ Exs. A-W.

¹¹⁴ See <http://www.investopedia.com/terms/c/certificateofparticipation.asp>.

¹¹⁵ See <http://www.msrb.org/Glossary/Definition/CERTIFICATE-OF-PARTICIPATION-COP.aspx>.

amount of debt that the entity may acquire.¹¹⁶ According to the District's real estate expert (who the District presented as the expert to explain the District's real estate financing arrangements), certificate of participation financing allows a school district to "circumvent" the legal restrictions that limit the amount of debt that a school district may acquire,¹¹⁷ and serves a function similar to school bonding but without the need for public approval of a referendum. As the District's expert explained:

A COP [certificate of participation] is a form of financing used by municipal or government entities. It is different from a bond used by these entities in that they are secured by lease revenues. *Municipal or government entities use this financial instrument to circumvent restrictions that might exist on the amount of debt they may acquire.* A COP is structured so that ownership of the land, building, or equipment being financed is vested in a third-party entity who then leases the land, building or equipment back to the public agency conducting the financing, giving that agency the use or occupancy of the land, building, or equipment in return for lease payments from its general fund. The third-party remits the lease payments to investors of the COP.¹¹⁸

¹¹⁶ Exs. 105, 106, 107 at cover letter ("A [certificate of participation] is a form of financing used by municipal or government entities. It is different from a bond used by these entities in that they [COPs] are secured by lease revenues. Municipal or government entities use this financial instrument *to circumvent restrictions that might exist on the amount of debt they may acquire.*) Emphasis added. See also <http://www.investopedia.com/terms/c/certificateofparticipation.asp>. According to Electronic Municipal Statistics (eMuni), an organization that provides information relating to the U.S. municipal bond market, a certificate of participation is explained as:

A form of lease revenue bond that permits the investor to participate in a stream of lease payments, installment payments, or loan payments relating to the acquisition or construction of specific equipment, land, or facilities. In theory, the certificate holder could foreclose on the equipment or facility financed in the event of default, but so far no investor has ended up owning a piece of a school house or a storm drainage system. A very popular financing device in California since Proposition 13 because COP issuance does not require voter approval. **COPs are not viewed legally as "debt" because payment is tied to an annual appropriation by the government body. As a result, COPs are seen by investors as providing weaker security and often carry ratings that are a notch or two below an agency's general obligation rating.**

<http://www.emuni.org/glossary.php> (emphasis added).

Unlike municipal or school bonds, certificates of participation are taxable, meaning that the holders/investors must pay taxes on the return from the investment. Test. of M. Hawkins at 907-08. As a result, the interest charged to the District on certificates of participation is higher than with bonds because the income to the investors is taxable and the financing arrangement has a higher risk than do bonds. *Id.*

¹¹⁷ Exs. 105, 106, 107 at cover letter (In explaining the District's use of certificate of participation financing to purchase real estate, Robert Strachota states, "A [certificate of participation] is a form of financing used by municipal or government entities. It is different from a bond used by these entities in that they [COPs] are secured by lease revenues. Municipal or government entities use this financial instrument *to circumvent restrictions that might exist on the amount of debt they may acquire.*") Emphasis added.

¹¹⁸ Exs. 105, 106, 107 at cover letter (emphasis added).

55. In the case of the Intermediate District and its use of certificates of participation at issue in this case, the “third party” holding title to the properties is generally the bank or lender.¹¹⁹

56. In conjunction with the issuance of certificates of participation, the lender enters into trust agreements whereby the lender acts as the trustee for all lease payments made by the District.¹²⁰ The lender collects the District’s lease payments each year and pays off the certificates of participation as they mature and as interest comes due.¹²¹ In this way, the lender acts as an administrator and intermediary between the investors and the District.

57. Under this complex arrangement of lease agreements, trust agreements, and certificates of participation, all parties seek to benefit. The certificate of participation holders hope to receive a return on their investment, which, because the investment involves a public school district, often has low risk of default. The lender receives administrative fees for its services as the facilitator and intermediary for the transaction without risk. The Intermediate District is able to finance the acquisition of property over time without a mortgage, without the issuance of bonds, without referenda, and without its own tax levy. The practical effect is that this type of financing arrangement allows an intermediate school district to avoid any restrictions that may exist on the district’s authority to purchase real property, incur debt, or enter into long-term contracts.¹²²

58. The difference between an independent school district and an intermediate district is an important one for understanding why the Intermediate District used this type of financing. When an independent school district seeks to acquire new facilities, it must seek voter approval through a referendum authorizing it to issue bonds to finance the purchase and to levy taxes to pay for the bonds.¹²³ Intermediate districts do not have their own voters or the authority to levy taxes.¹²⁴ Therefore, Intermediate District #287

¹¹⁹ Exs. A, D, F, I, J, N, R.

¹²⁰ Exs. B, G, L, O, S, V.

¹²¹ Exs. B, G, L, O, S, V.

¹²² See generally Exs. A-W; see also Exs. 105, 106, 107 at cover letter (“Municipal or government entities use this financial instrument to circumvent restrictions that might exist on the amount of debt they may acquire.”) Emphasis added. Note that a school district may lease real property with an option to purchase under a lease-purchase agreement, whereby title to the property is retained by the seller or vendor or assigned to a third party as security for the purchase price. Minn. Stat. § 465.71 (2014). The school district must, however, have the right to terminate the lease-purchase agreement at the end of any fiscal year during its term. *Id.* Lease-purchase agreements are subject to statutory provisions applicable to school districts and the purchase of real property. *Id.* If the amount of the contract for the purchase of real property is less than \$1,000,000.00, the obligation created by the lease-purchase agreement shall not be included in the calculation of “net debt” for purposes of Minn. Stat. § 475.53 and shall not constitute “debt” under any other statutory provision. *Id.* Minnesota Statute section 475.53 provides that “no school district shall be subject to a net debt in excess of 15 percent of the estimated market value of all taxable property situated within its corporate limits....” The lease-purchase agreements at issue in this case all exceeded \$1,000,000.00. See Exs. A, D, F, I, J, N, R, U.

¹²³ Test. of M. Hawkins at T. 907.

¹²⁴ *Id.*

looked to more creative financing, using a combination of certificates of participation and long-term leases in lieu of bonds or mortgages to finance their acquisitions.¹²⁵

59. When the Intermediate District decided to acquire interests in real property and build new facilities, it did not have to go to taxpayers for passage of a referendum granting it authority to issue bonds and levy taxes.¹²⁶ Instead, the Intermediate District's Board simply voted to approve a lease-purchase agreement and accompanying certificates of participation, and then, once approved, imposed lease levies on its Member Districts to cover the costs of the leases.¹²⁷ Thus, by using lease-purchase agreements and certificates of participation, the Intermediate District was able to acquire real estate without the authority to levy taxes and without the public scrutiny of bond referenda.¹²⁸ While the taxpayers in Member Districts are ultimately responsible for these capital costs, they are not provided any opportunity to vote on or approve (or disapprove) the obligations like they would if an independent school district was acquiring the same facilities.

West Education Center (WEC)

60. In approximately 2004, the Intermediate District Board unanimously voted on a resolution to acquire an interest in real property located at 11140 Bren Road West, Minnetonka, Minnesota, and to remodel the existing building so that it could be used as a school facility by the District.¹²⁹ This property is referred to as the West Education Center or WEC Property.

61. To finance the purchase, the District entered into various agreements with Wells Fargo Brokerage Services, LLC (Wells Fargo Brokerage) and Wells Fargo Bank, N.A. (Wells Fargo Bank).¹³⁰

WEC Lease

62. On August 31, 2004, the District and Wells Fargo Brokerage executed a Lease Agreement (WEC Lease), whereby Wells Fargo Brokerage, as lessor, agreed to purchase the WEC Property and lease it to the District, as lessee.¹³¹ To fund the purchase of the land and building costs, Wells Fargo Brokerage agreed to deposit \$9,000,000 into a construction escrow fund.¹³²

63. On August 31, 2004, Wells Fargo Brokerage purchased the WEC Property for \$4,500,000.00.¹³³ Said amount was deducted from the construction fund, leaving the

¹²⁵ *Id.*

¹²⁶ *Id.*

¹²⁷ *Id.* at T. 907-08.

¹²⁸ *See id.*

¹²⁹ Ex. 106 at 3-4.

¹³⁰ Exs. D-H.

¹³¹ Ex. D.

¹³² *Id.* at 9; Ex. E.

¹³³ Ex. 106 at 4.

remainder of the \$9,000,000.00 in the fund, from which the District drew and paid the construction costs.¹³⁴

64. Under the WEC Lease, the District agreed to pay rent to Wells Fargo Brokerage in 40 bi-annual installments in an amount equal to \$9,000,000.00 plus interest, amortized over 20 years.¹³⁵

65. The WEC Lease permitted the District to terminate the lease at the end of each year if the District Board failed to appropriate funds sufficient to pay the rent.¹³⁶ In addition, the WEC Lease allowed for the prepayment of rental payments and an option to purchase the WEC Property before the end of the lease term.¹³⁷

66. The WEC Lease provided that upon payment of the final rent payment, or upon the exercise of the option to prepay and purchase the property, legal title to the property and its improvements would be conveyed to the Intermediate District for one dollar.¹³⁸

WEC Refunding Lease and WEC Ground Lease

67. In 2009, the District decided to refinance the WEC Lease to obtain a more favorable interest rate.¹³⁹ On July 15, 2009, the District entered into a series of agreements with the Wells Fargo Bank, which combined in a Refunding Lease Agreement (WEC Refunding Lease).¹⁴⁰

68. To fund the refinance, Wells Fargo Bank issued Certificates of Participation (COP) Series 2009A, in the principal amount of \$8,570,000.00 (COP Series 2009A), to pay off the amount remaining under the WEC Lease.¹⁴¹ Once the option to purchase was exercised under the original WEC Lease using the COP funds, title to the land was conveyed to the District.¹⁴²

69. To provide security to Wells Fargo Bank for refinancing the WEC Lease, however, the District conveyed an interest in the WEC land back to the bank using a long-term Ground Lease Agreement (WEC Ground Lease), which gave a possessory interest in the WEC Property to the bank.¹⁴³

¹³⁴ Ex. E.

¹³⁵ Ex. D at Schedule 1.

¹³⁶ *Id.* at 11.

¹³⁷ *Id.*

¹³⁸ *Id.* at 11, 26.

¹³⁹ Ex. F at iv.

¹⁴⁰ Exs. F, G, H.

¹⁴¹ Ex. F.

¹⁴² Ex. X.

¹⁴³ Ex. H.

70. At the same time, the District and Wells Fargo Bank entered into a Trust Agreement (WEC Trust Agreement), whereby the District conveyed its interest in the WEC Ground Lease to Wells Fargo Bank, allowing the bank to lease the WEC Property back to the District via the WEC Refunding Lease Agreement.¹⁴⁴

71. Pursuant to the WEC Refunding Lease, Wells Fargo Bank is leasing the property back to the District for \$8,570,000.00, plus interest, payable in 31 lease payments, due bi-annually from February 1, 2010, through February 1, 2025.¹⁴⁵ Unless earlier terminated as provided for in the lease, the lease term is from July 15, 2009, to February 1, 2025.¹⁴⁶ Upon payment of the final lease payment on February 1, 2025, Wells Fargo Bank shall convey all of its interest in the WEC Property back to the District, allowing the District to have clear and unencumbered title to the property.¹⁴⁷

72. According to the WEC Refunding Lease, “The School District has determined that the Lease Payments hereunder during the Agreement Term represent the fair value of the use of the Premises.”¹⁴⁸

73. Under the WEC Trust Agreement, Wells Fargo Bank, as trustee for the owners of the COP Series 2009A, receives all lease payments due from the District under the WEC Refunding Lease, and shall use those payments to pay interest on and satisfy the COP Series 2009A, as they mature.¹⁴⁹

74. The WEC Refunding Lease allows the District to purchase the WEC Property for an amount sufficient to pay off the COP Series 2009A, or prepay the unpaid lease payments before the expiration of the lease term.¹⁵⁰ The WEC Refunding Lease provides:

Section 4.3 Trustee’s Interest in the Premises. Upon payment or prepayment of the Lease Payments and Additional Lease Payments¹⁵¹ due hereunder or discharge of the School District’s obligation to make the Lease Payments and Additional Lease Payments in accordance with Article VIII hereof [Option to Purchase or Prepay], and in either event upon defeasance of the Certificates in accordance with the Trust Agreements, full and unencumbered legal title to the Premises shall pass to the School District, and the Trustee shall have no further interest therein. In such event, the Trustee and its officers shall take all actions necessary to authorize, execute, and deliver to the School District any and all documents necessary

¹⁴⁴ Ex. G.

¹⁴⁵ Ex. F at Ex. B.

¹⁴⁶ *Id.* at 12.

¹⁴⁷ *Id.*

¹⁴⁸ *Id.* at 5.

¹⁴⁹ Ex. G.

¹⁵⁰ Ex. F at 13, 22; Ex. B

¹⁵¹ Additional Lease Payments include fees and expenses incurred by the Trustee, costs incident to the payment of the COP Series 2009A, and other costs. Ex. F at 10-11.

to vest in the School District, all of the Trustee's right, title, and interest in and to the Premises, free and clear of all liens, leasehold interests, encumbrances (other than Permitted Encumbrances), including, if necessary, a release of any and all interests or liens created under the provisions of this Agreement and the Ground Lease.¹⁵²

Section 4.5 Purchase Option; Conveyance of Title. At any time when the purchase price for the Premises, together with any unpaid or delinquent interest, has been fully paid or provided for, whether by (i) payment of all Lease Payments and Additional Lease Payments, or (ii) payment or provision for payment of the Purchase Price provided in Article VIII [Option to Purchase or Prepay] hereof, then the purchase of the Premises by the School District shall be deemed to have occurred. The Trustee shall thereupon deliver to the School District such instruments of conveyance or release as, in the opinion of the School District, may be necessary to release any interests of the Trustee in the Premises and to convey title to the School District.¹⁵³

75. Thus, upon the full payment or prepayment of the lease payments, or upon the payment of the purchase price set forth in the WEC Refunding Lease, unencumbered title to the WEC Property will be conveyed to the District.¹⁵⁴ However, until all lease payments are made, or until the District exercises its option to prepay the lease or purchase the property, the District's title to the WEC Property remains fully encumbered by the bank's possessory interest in the property under the WEC Ground Lease.¹⁵⁵

76. Consequently, while the District may have record title to the WEC Property, such title is fully encumbered by the WEC Refunding Lease and WEC Ground Lease, preventing the District from selling or otherwise conveying the property to a third party.¹⁵⁶ To that end, the WEC Refunding Lease expressly provides that the District "will not mortgage, sell, assign, transfer or convey the Premises or any portion thereof during the Term of this Agreement."¹⁵⁷

77. The District, nonetheless, may still terminate the WEC Refunding Lease at the end of any fiscal year without further liability to the bank or COP Series 2009A holders.¹⁵⁸ Pursuant to the non-appropriation clauses in the WEC Refunding Lease:

Section 4.7 Nonappropriation by School District. If the School Board of the School District (the "School Board") does not appropriate or budget moneys sufficient to pay the Lease Payments and reasonably estimated

¹⁵² *Id.* at 12.

¹⁵³ *Id.* at 13.

¹⁵⁴ *Id.* at 12-13, 22.

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*; *see also* Ex. X.

¹⁵⁷ Ex. F at 23.

¹⁵⁸ *Id.* at 13.

Additional Lease Payments coming due in the next Fiscal Year, as determined by a specific provision in the School District's budget for the Fiscal Year in question so stating, the School District shall be deemed to have terminated this Agreement... In the event of termination of this Agreement as provided in this Section, the School District shall surrender possession of the Premises to the Trustee in accordance with Section 4.4 hereof and convey to the Trustee or release its interest in the Premises within ten (10) days after the expiration of the current Fiscal Year.¹⁵⁹

Section 4.4. Surrender of Premises. Upon termination of the Term of this Agreement pursuant to [non-appropriation] or [default]...the School District shall surrender the Premises to the Trustee in the condition in which they were originally received from the Trustee, except as repaired, rebuilt, restored, altered or added to as permitted or required hereby, ordinary wear and tear excluded....

Section 4.9 Effect of Termination. Upon termination of this Agreement as provided in Section 4.7, the School District **shall not be responsible for the payment of any Lease Payments or Additional Lease Payments coming due with respect to succeeding Fiscal Years....**¹⁶⁰

78. More importantly, the WEC Refunding Lease does not obligate the District to appropriate funds necessary to continue the lease.¹⁶¹ According to Section 2.1(i) of the WEC Refunding Lease:

Except to the extent specifically provided herein, the School District is not obligated to appropriate or otherwise provide moneys for the payment of the Lease Payments or any other amounts coming due hereunder, and in the event the School District terminates this Agreement in accordance with Section 4.2(a) thereof, the School District shall not be liable for general, special[,] incidental, consequential or other damages resulting therefrom. This Agreement does not constitute a general obligation of the School District, and the full faith and credit and taxing powers of the School District is not pledged for the payment of the Lease Payments or other amounts coming due, or other actions required to be performed herein.¹⁶²

79. The WEC Refunding Lease further provides:

¹⁵⁹ *Id.*

¹⁶⁰ *Id.* (emphasis added).

¹⁶¹ *Id.* at 6.

¹⁶² *Id.*

Nothing in this Agreement, the Ground Lease Agreement, the Trust Agreement or the Certificates [of Participation] shall be deemed to obligate the School District to continue this Agreement beyond any then-current Fiscal Year or to obligate the School District to budget or appropriate moneys or to pay Lease Payments or Additional Lease Payments due following the end of the then-current Fiscal Year.¹⁶³

80. Thus, as long as the District pays rent through the end of the fiscal year, it can terminate the lease at any time without default or further obligation to Wells Fargo Bank beyond that fiscal year.¹⁶⁴ Upon either termination or default, the Intermediate District's entire liability is for the rent owed for the then-current fiscal year and no more, so long as the District vacates the property within 10 days.¹⁶⁵

81. If the District were to terminate or default on the WEC Refunding Lease, the District would continue to have legal title to the WEC Property, but it would not be able to use, possess, or occupy the property due to the WEC Ground Lease with Wells Fargo Bank, which would continue to fully encumber the property until 2035.¹⁶⁶

82. Under the Ground Lease, Wells Fargo Bank maintains a leasehold/possessory interest in the WEC Property until February 1, 2035, or until: (1) full payment or prepayment of rent is made under the WEC Refunding Lease; (2) the District exercises its option to purchase the property under the WEC Refunding Lease; or (3) the bank receives repayment of all of its administrative costs and expenses, plus an amount equal to the principal component of the rent due under the WEC Refunding Lease as of February 1, 2025.¹⁶⁷ Thus, unless the WEC Refunding Lease is paid in full, the District's title to the property is fully encumbered by the WEC Ground Lease, preventing the District from selling or otherwise conveying the property.¹⁶⁸

83. With respect to future liability or indebtedness, the WEC Refunding Lease expressly provides:

Section 3.4 Source of Lease Payments. Notwithstanding any other provision apparently to the contrary, this Agreement shall not constitute a general obligation of the School District, and the full faith and credit of the School District are not pledged for the payment of the Lease Payments or Additional Lease Payments or the performance by the School District of its other obligations hereunder. The Lease Payments and Additional Lease

¹⁶³ *Id.* at 8.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.* at 6-8, 13-14, 24-25.

¹⁶⁶ See Exs. F, H, X.

¹⁶⁷ Ex. H at 4. The WEC Refunding Lease term expires on February 1, 2025. Ex. F. The WEC Ground Lease term is through February 1, 2035, but allows early termination upon payment of all administrative costs and expenses, plus an amount equal to the principal component of the rent due under the WEC Refunding Lease through February 1, 2025. Ex. H.

¹⁶⁸ Ex. H.

Payments shall be paid, and other obligations of the School District hereunder shall be met, solely from the amount appropriated by the School Board of the District for such purpose in the School District's annual budget, **and shall constitute a current expense of the School District for the Fiscal Year then in effect. This Agreement shall not constitute an indebtedness, liability or mandatory payment obligation of the School District within the meaning of the Constitution or the laws of the State of Minnesota.**¹⁶⁹

84. Under the express terms of the WEC Refunding Lease, the lease shall not constitute a long-term debt or liability of the District, and shall only be considered a current yearly expense for the District.¹⁷⁰

85. As of June 30, 2011, the District continued to occupy the WEC Property and had not terminated the WEC Refunding Lease. Nor had the District exercised its option to prepay the WEC Refunding Lease. In addition, the WEC Ground Lease continued to encumber the WEC Property, prohibiting the District from conveying, selling, or otherwise disposing of the property.¹⁷¹

86. According to the Certificate of Title for the WEC Property, the Intermediate District is the owner of an estate in the WEC Property, subject to Wells Fargo Bank's interest in the WEC Ground Lease.¹⁷²

87. As of June 30, 2011, the principal amount outstanding on the WEC Refunding Lease was \$7,590,000.00.¹⁷³

South Education Center (SEC)

88. In late 2005, the Intermediate District Board unanimously voted to acquire an interest in real property located at 7450 Penn Avenue South, Richfield, Minnesota, and to construct a new school facility on the property.¹⁷⁴ This property is referred to as the South Education Center or SEC Property.

89. To finance the purchase, the District entered into various agreements with Wells Fargo Brokerage and Wells Fargo Bank.¹⁷⁵

¹⁶⁹ Ex. F. at 7-8 (emphasis added).

¹⁷⁰ *Id.*

¹⁷¹ Exs. H, X.

¹⁷² Ex. X.

¹⁷³ Ex. 108 at 41.

¹⁷⁴ Ex. P.

¹⁷⁵ Exs. I-O.

SEC Land Lease

90. On January 6, 2006, the Intermediate District and Wells Fargo Brokerage executed a Lease Agreement (SEC Land Lease), whereby Wells Fargo Brokerage, as lessor, agreed to purchase land, and lease it to the District, as lessor.¹⁷⁶ The intended purpose of the acquisition was to enable the District to construct a new building (the SEC) on the property and ultimately purchase the SEC Property (land and building) from the bank.¹⁷⁷

91. The purchase price for the land was \$7,500,000.00.¹⁷⁸ At the time of purchase, the land contained an existing building which the District intended to demolish and replace with a new facility.¹⁷⁹

92. The SEC Land Lease provided for rent to be paid by the District in 42 bi-annual installments, in an amount equal to \$7,600,000.00, plus interest, amortized over 21 years.¹⁸⁰ The term of the SEC Land Lease was from January 6, 2006,¹⁸¹ to January 1, 2028, unless earlier terminated by the District, with the last rent payment due on January 1, 2028.¹⁸²

93. Like the WEC Lease, the SEC Land Lease permitted the District to terminate the lease at the end of each year if the District Board failed to appropriate funds sufficient to pay the rent.¹⁸³ In addition, the SEC Land Lease allowed for the prepayment of rent and an option to purchase the SEC Property before the end of the lease term.¹⁸⁴

94. The SEC Land Lease provided that upon tender of the final rent payment, or upon the exercise of the option to prepay and purchase the property, legal title to the SEC Property would be conveyed to the Intermediate District for one dollar.¹⁸⁵ Until that time, however, title remains with Wells Fargo Brokerage.

SEC Building Lease

95. On October 10, 2006, the District and Wells Fargo Brokerage entered into a second Lease Agreement (SEC Building Lease), whereby Wells Fargo Brokerage, as

¹⁷⁶ Ex. I.

¹⁷⁷ *Id.* at 2.

¹⁷⁸ Ex. 107 at 3. Strachota's Appraisal states that the purchase price was \$7,500,000.00. *Id.* However, the SEC Land Lease is for \$7,600,000.00. Ex. I.

¹⁷⁹ Ex. 107 at 3-4.

¹⁸⁰ Ex. I at Schedule 1.

¹⁸¹ The first payment of the rent was not due until July 1, 2007. *Id.*

¹⁸² *Id.*

¹⁸³ *Id.* at 11.

¹⁸⁴ *Id.* at 11, 26.

¹⁸⁵ *Id.* at 26.

lessor, agreed to fund the construction of a new building on the SEC Property and to lease the building to the District, as lessee.¹⁸⁶

96. The construction costs funded by Wells Fargo Brokerage totaled \$25,400,000.00.¹⁸⁷ Under an Escrow Agreement dated October 10, 2006, Wells Fargo Brokerage deposited \$25,400,000.00 into an escrow account against which the District could draw to pay the construction costs of the new building.¹⁸⁸

97. Wells Fargo Brokerage then issued Certificates of Participation Series 2006A (COP Series 2006A) to investors in the principal amount of \$25,400,000.00, with a maturity date of November 1, 2032.¹⁸⁹

98. To provide security for the COP Series 2006A, Wells Fargo Brokerage, Wells Fargo Bank, and the District entered into a Trust Agreement dated October 10, 2006 (SEC Building Trust), whereby Wells Fargo Bank was appointed as trustee.¹⁹⁰ Wells Fargo Brokerage then assigned its interest in the SEC Building Lease to Wells Fargo Bank, as the trustee.¹⁹¹

99. As trustee, Wells Fargo Bank holds in trust, for the benefit of the COP Series 2006A owners, Wells Fargo Brokerage's interest in the SEC Building Lease, as well as the rents received from the Intermediate District under the SEC Building Lease.¹⁹² From the rents received, Wells Fargo Bank pays interest on, and will eventually pay off, the COP Series 2006A.¹⁹³

100. The SEC Building Lease provides that rent be paid by the District in 52 bi-annual installments, in an amount equal to \$25,400,000.00, plus interest, amortized over 26 years.¹⁹⁴ The term of the lease is from October 10, 2006,¹⁹⁵ to November 1, 2032, unless earlier terminated, with the last rent payment due on November 1, 2032.¹⁹⁶

101. While the District represents that it will maintain its existence during the term of the lease or assure the assumption of its obligations by its successor, there is nothing in the SEC Building Lease that prevents the Intermediate District from terminating the lease at any time.¹⁹⁷ Indeed, the SEC Building Lease expressly provides:

¹⁸⁶ Ex. J.

¹⁸⁷ *Id.* at Schedule 1.

¹⁸⁸ Ex. K.

¹⁸⁹ Ex. L at Ex. A.

¹⁹⁰ Ex. L.

¹⁹¹ *Id.*

¹⁹² *Id.*

¹⁹³ *Id.*

¹⁹⁴ Ex. J at Schedule 1.

¹⁹⁵ The first rent payment was not due until May 1, 2007. *Id.*

¹⁹⁶ *Id.*

¹⁹⁷ *Id.* at 10, 18.

Section 4.06 Termination by Lessee upon Non-appropriation. The Lessee shall have the right to terminate this Lease, in whole but not in part, at the end of any Fiscal Year of the Lessee, in the manner and subject to the terms specified in this Section, in the sole event that the Governing Body fails to appropriate money sufficient for the continued performance of this Lease by the Lessee after the end of such Fiscal Year, as evidence by the passage of a resolution specifically prohibiting the Lessee from performing its obligations under this Lease and from using any moneys to pay the Rent due under this Lease in the next succeeding Fiscal Year and all subsequent Fiscal Years. The Lessee may effect such termination by giving the Lessor a written notice of termination as provided in this Section and by paying to the Lessor any Rent and other amounts which are due and have not been paid at or before the end of its then current Fiscal Year....In the event of termination of this Lease as provided in this Section, the Lessee shall deliver possession of the Leased Property to the Lessor and shall convey to the Lessor or release its interest in the Leased Property with ten (10) days after termination of this Lease.

Upon termination of this Lease as provided in this Section, the Lessee shall not be responsible for the payment of any Rent coming due with respect to succeeding Fiscal Years....

...Therefore, an event of non-appropriation under this Lease or the aforementioned Lease Agreement dated January 6, 2006 [SEC Land Lease], under which the Land and the Building are being financed, will be considered by Lessee and Lessor an event of non-appropriation under both.¹⁹⁸

102. Upon termination of the SEC Building Lease by default or non-appropriation, the District must surrender possession of the SEC Property.¹⁹⁹ As long as the District properly exercises its right to terminate the contract and possession of the property is surrendered to the bank within 10 days, the District's financial liability is limited to the rent due in the fiscal year of termination.²⁰⁰ All rent paid prior to termination, however, is forfeited, and title to the property does not transfer to the District.²⁰¹

103. A 2006 Amendment to the SEC Building Lease further clarifies that a termination of either the SEC Building Lease or SEC Land Lease shall be considered a termination of both leases.²⁰² Moreover, the Amendment expressly states that legal title

¹⁹⁸ *Id.* at 10.

¹⁹⁹ *Id.* at 27.

²⁰⁰ *Id.* at 10, 22-23; see also Ex. M.

²⁰¹ Ex. J at 10, 22-23.

²⁰² Ex. M.

to the SEC Property shall not transfer to the District until full payment is made under both the SEC Building Lease and the SEC Land Lease.²⁰³

104. In addition to allowing the District to terminate the lease at any time, the SEC Building Lease also allows for the prepayment of rent and an option to purchase the SEC Property before the end of the lease term.²⁰⁴ According to the agreement:

Section 4.05 Prepayment of Rents. There is expressly reserved to the Lessee the right, and the Lessee is authorized and permitted, on any Payment Date on or after November 1, 2016, to prepay in whole but not in part[,] the Rent payable under Section 2.01 hereof as described in Section 10.01 hereof, and the Lessor agrees to accept such prepayment of Rent when the same is tendered by the Lessee.

Section 10.01 Option to Purchase Lease Property. On any Payment Date, on or after November 1, 2016, during the Lease Term, the Lessee may elect to terminate this Lease upon payment of the Total Payment Due plus the Termination Value set forth in Schedule 1 hereto with respect to such date, and on such termination date, the Lessee may exercise its option to purchase the New Leased Building....The Lessee shall have, and is hereby granted, an option to purchase the New Leased Building for One Dollar (\$1.00) at the expiration of the Lease Term if full payment or prepayment of all Rent has been made in accordance with the provisions hereof

Section 10.02 Conveyance on Exercise of Option to Purchase. On the exercise of any option to purchase granted herein, the Lessor will upon payment of the purchase price deliver or cause to be delivered to the Lessee documents conveying to the Lessee all of the right, title and interest of the Lessor in and to the real and personal property being purchased

105. Thus, upon remittance of the final rent payment, or upon the exercise of the option to prepay and purchase the property, legal title to the SEC Property will be conveyed to the Intermediate District for one dollar.²⁰⁵ Until this happens, however, legal title remains with Wells Fargo Bank.²⁰⁶

106. With respect to future liability or indebtedness, the SEC Building Lease expressly provides:

Section 4.07 Not General Obligation. Notwithstanding any other provision of this Lease Agreement, this Lease Agreement shall not

²⁰³ *Id.*

²⁰⁴ Ex. J. at 10, 25.

²⁰⁵ *Id.*

²⁰⁶ *Id.*

constitute a general obligation of the Lessee, and the full faith and credit of the Lessee are not pledged for the payment of the Rent or the performance by the Lessee of its other obligations hereunder. The Rent shall be paid, and the other obligations of the Lessee shall be met, solely from the amount appropriated by the Governing Body for such purpose in the Lessee's annual budget **and shall constitute a current expense of the Lessee for the Lessee's Fiscal Year then in effect. Nothing in this Lease Agreement shall be deemed to obligate the Lessee to budget or appropriate moneys or to pay Rent due following the end of its then-current Fiscal Year. This Lease Agreement shall not constitute an indebtedness of the Lessee** within the meaning of the Constitution or the Laws of the State of Minnesota.²⁰⁷

107. Thus, according to the SEC Building Lease, the lease does not constitute a long-term debt or liability of the District, and shall only be considered a current yearly expense for the District.²⁰⁸

108. This is confirmed in the COP Series 2006A, which expressly warns the investors:

THE OBLIGATION OF THE INTERMEDIATE DISTRICT TO MAKE LEASE PAYMENTS UNDER THE LEASE IS NOT A GENERAL OBLIGATION OF THE INTERMEDIATE DISTRICT TO WHICH ITS FULL FAITH AND CREDIT AND ABILITY TO LEVY AD VALOREM TAXES WITHOUT LIMITATION AS TO RATE OR AMOUNT ARE PLEDGED. THE INTERMEDIATE DISTRICT IS OBLIGATED ONLY TO MAKE LEASE PAYMENTS FOR MONEYS APPROPRIATED FOR SUCH PURPOSE BY THE SCHOOL BOARD OF THE INTERMEDIATE DISTRICT. THE INTERMEDIATE DISTRICT IS NOT OBLIGATED TO MAKE ANY SUCH APPROPRIATION, AND IN THE EVENT THAT THE INTERMEDIATE DISTRICT'S SCHOOL BOARD FAILS TO APPROPRIATE MONEY TO PAY SUCH LEASE PAYMENTS IN ANY FISCAL YEAR OF THE INTERMEDIATE DISTRICT, THE LEASE WILL TERMINATE AT THE END OF THE LAST FISCAL YEAR FOR WHICH SUCH FUNDS WERE SO APPROPRIATED AND THE LESSEE WILL HAVE NO FURTHER OBLIGATION TO MAKE LEASE PAYMENTS UNDER THE LEASE.²⁰⁹

109. As of June 30, 2011, the District continued to occupy the SEC Property and had not terminated the SEC Building Lease.²¹⁰ Nor had the District exercised its option to purchase the property or prepay the SEC Building Lease.²¹¹

²⁰⁷ *Id.* at 10-11 (emphasis added).

²⁰⁸ *Id.*

²⁰⁹ Ex. L at Ex. A (emphasis in original).

²¹⁰ Ex. 107.

²¹¹ *Id.*

110. As of June 30, 2011, the principal amount outstanding on the SEC Building Lease was \$25,753,734.00.²¹²

SEC Lease Purchase Agreement/Refunding Lease

111. In 2010, the Intermediate District decided to refinance the SEC Land Lease to make the SEC Land Lease and SEC Building Lease “parity obligations.”²¹³ By this time, however, Bloomington had already noticed its withdrawal from the Intermediate District.²¹⁴

112. On June 30, 2010, Wells Fargo Bank and the Intermediate District entered into a Lease-Purchase Agreement (SEC Refunding Lease) for the purpose of refinancing the SEC Land Lease.²¹⁵

113. As part of the SEC Refunding Lease, Wells Fargo Bank and the District entered into a Trust Agreement dated June 30, 2010 (SEC Land Trust).²¹⁶ Under the SEC Land Trust and SEC Refunding Lease, Wells Fargo Bank exercised the District’s option to prepay the rent and terminate the 2006 SEC Land Lease.²¹⁷ This refinance did not impact the District’s obligations under the SEC Building Lease.²¹⁸

114. Upon prepayment of the 2006 SEC Land Lease, Wells Fargo Securities, LLC, as successor to the lessor, Wells Fargo Brokerage, deeded title to the SEC Property to Wells Fargo Bank.²¹⁹ Unlike the transaction involving the WEC Property, title to the SEC Property was not conveyed to the District.²²⁰

115. At the same time, the District agreed to lease the SEC Property from Wells Fargo Bank under the new SEC Refunding Lease terms.²²¹ The SEC Refunding Lease provides that the District will pay rent in an amount equal to \$7,405,000.00, plus interest, amortized over 17 years and paid in 35 bi-annual installments from January 1, 2011 to January 1, 2028.²²² The term of the lease is from June 30, 2010, to January 1, 2028, unless earlier terminated, with the last rent payment due on January 1, 2028.²²³

²¹² Ex. 108 at 40.

²¹³ Ex. N at 1. As “parity obligations,” a default under the SEC Refunding Lease would result in a default under the SEC Building Lease and vice versa. *Id.* According to the SEC Refunding Lease, “the [SEC] Refunding Lease and the [SEC] Building Lease are secured equally and ratably and on a parity basis with respect to the Land and all improvements thereon[.]” *Id.*

²¹⁴ Ex. 21. Bloomington’s Notice of Withdrawal was served on the District on January 29, 2010. *Id.*

²¹⁵ Ex. N at 1.

²¹⁶ Ex. O.

²¹⁷ Exs. N, O.

²¹⁸ Ex. J.

²¹⁹ Ex. N at 7; Ex. O.

²²⁰ Ex. N at 7; Ex. O; *see also* Ex. Y.

²²¹ Ex. N.

²²² *Id.* at 10, Ex. B.

²²³ *Id.* at 8, 10.

116. In turn, Wells Fargo Bank issued and sold Certificate of Participation Series 2010 (COP Series 2010) in the principal amount of \$7,405,000.00 to investors.²²⁴

117. Under the SEC Land Trust, Wells Fargo Bank, as trustee for the owners of the COP Series 2010, receives all lease payments due from the District under the SEC Refunding Lease.²²⁵

118. During the term of the SEC Refunding Lease, legal title to the SEC Property remains with Wells Fargo Bank.²²⁶ As expressly stated in Article IX of the SEC Refunding Lease:

Section 9.1. Title. During the Term of this Lease, legal title to the Land and any and all replacements, substitutions and modifications thereto shall be in the Lessor....²²⁷

119. The SEC Refunding Lease provides that “[t]he District shall be deemed to have purchased Lessor’s interest in the Land upon payment of all Rental Payments and other amounts due hereunder....”²²⁸

120. In addition, the SEC Refunding Lease allows the District to prepay the lease and purchase the property prior to the date of the last rental payment in 2025.²²⁹ The SEC Refunding Lease provides:

Section. 11.2 Purchase Option. Unless the District is then in default hereunder, the District may purchase the interest in the Land subject hereto on any business day on or after February 1, 2020, by depositing with Lessor all Rental Payments and other amounts then due hereunder, the application Purchase Option Price shown in Exhibit B, and additional interest, if any accrued to the date of exercise of the payment option. In such event the provisions of Section 11.3 shall apply. Lessee may exercise its rights under Article XI only if it simultaneously exercises its rights under Article X of the Building Lease.²³⁰

Section 11.3 Release of Lessor’s Interest. Upon payment by Lessee of all Rental Payments and other amounts due hereunder, Lessee shall have no further obligations under this Lease and Lessor and its officers shall take all actions necessary to authorize, execute and deliver to Lessee any and all documents necessary to vest in Lessee, all of Lessor’s right, title and

²²⁴ *Id.* at Debt Service Schedule.

²²⁵ Ex. O.

²²⁶ Ex. N at 20; Ex. Y.

²²⁷ Ex. N at 18.

²²⁸ *Id.* at 20.

²²⁹ *Id.*

²³⁰ *Id.* (emphasis in original).

interest in and to the Land, free and clear of all liens, leasehold interest and encumbrances arising under the provisions of this Lease.²³¹

121. According to the SEC Refunding Lease:

Section 4.3. Trustee's Interest in the Land. Upon payment of all Rental Payments due hereunder...or exercise of the option to purchase pursuant to Article XI hereof, full and unencumbered legal title to the Land shall pass to the District, and the Trustee shall have no further interest therein.²³²

Section. 4.7. Purchase; Conveyance of Title. At any time when all Rental Payments and all other amounts due hereunder have been paid...or upon exercise of the option to purchase pursuant to Article XI hereof, then the purchase of the Land by the District shall be deemed to have been completed. The Trustee shall thereupon deliver to the District such instruments of conveyance or release as, in the opinion of counsel, may be necessary to release any interests of the Trustee in the Land.²³³

Section 9.1. Title. ...Upon the payment by the District of all Rental Payments as indicated in Exhibit B...or exercise of the option to purchase pursuant to Article XI hereof, full and unencumbered legal title to the Land shall pass to the District, and the Lessor shall have no further interest therein; and the Lessor shall execute and deliver to the District such documents as the District may request to evidence the passage of legal title to the Land to the District and the termination of the Lessor's interest therein.²³⁴

122. Thus, upon the full payment of rent or upon the exercise of the option to purchase, title to the property shall be conveyed to the District.²³⁵ However, until all lease payments are made, or until the District exercises its option to prepay and purchase the property, legal title to the SEC Property remains with Wells Fargo Bank.²³⁶

123. According to the SEC Refunding Lease, while the District "presently intends" to continue the lease for the entire term; plans to "take all actions necessary" to approve budgets with appropriations sufficient to pay the rent; and "reasonably believes" that moneys can and will be lawfully appropriated, the District may nonetheless terminate the SEC Refunding Lease at the end of any fiscal year without further liability.²³⁷ According to the Lease:

²³¹ *Id.*

²³² *Id.* at 8.

²³³ *Id.* at 9.

²³⁴ *Id.* at 18 (emphasis in original).

²³⁵ *Id.* at 8, 18, 20.

²³⁶ *Id.*

²³⁷ *Id.* at 5.

Section 4.5. Termination by the District. The District shall have the right to terminate this Lease, in whole but not in part, at the end of any Fiscal Year of the District, in the manner and subject to the terms specified in this Section and Section 4.7, if the governing body does not appropriate or budget moneys sufficient to pay the Rental Payments coming due in the next Fiscal Year. The District may effect such termination by giving the Trustee a written notice of termination, as evidenced by a resolution of the governing body specifically determining not to provide moneys to pay Rental Payments for the succeeding Fiscal Year and all future Fiscal Years, and stating the governing body's determination to terminate this Lease, and by paying to the Trustee any Rental Payments which are due and have not been paid at or before the end of its then current Fiscal Year....An event of non-appropriation under this Lease will be deemed a failure to appropriate money sufficient for continued operation of the Land and improvements thereon. Therefore, an event of non-appropriation under this Lease or the [SEC] Building Lease will be considered by the Lessee and Lessor an event of non-appropriation under both.²³⁸

Section 4.6. Effect of Termination. Upon termination of this Lease as provided in Section [4.5], the District shall not be responsible for the payment of any additional Rental Payments coming due with respect to the succeeding Fiscal Years....²³⁹

Section 4.4. Surrender of Land. Upon termination of the Term of this Lease pursuant to Section 4.2(a) [non-appropriation] or (c) [default],...the District shall surrender the Land to the Trustee in the condition in which it was originally received from the Trustee, except as repaired, rebuilt, restored, altered or added to as permitted or required hereby, ordinary wear and tear excluded.²⁴⁰

Section 13.3. Return of Land. Upon the expiration or termination of this Lease prior to the payment of all Rental Payments in accordance with Exhibit B, the District shall return the Land to the Lessor in the condition, repair, appearance and working order required in Section 8.2....²⁴¹

124. Thus, as long as the District pays rent through the end of the fiscal year, it can terminate the lease at any time without default or further obligation to Wells Fargo Bank beyond that fiscal year.²⁴² Upon either termination or default, the Intermediate

²³⁸ *Id.* at 8-9.

²³⁹ *Id.* at 9.

²⁴⁰ *Id.* at 8.

²⁴¹ *Id.* at 24 (emphasis in original).

²⁴² *Id.* at 8-9, 10, 22-24.

District's entire liability is for the rent owed for the then-current fiscal year and no more, so long as the District vacates the property within 10 days.²⁴³

125. With respect to future liability or indebtedness, the SEC Refunding Lease expressly provides:

Section 5.2. Current Expense. The obligations of the District under this Lease, including its obligation to pay the Rental Payments, in any Fiscal Year for which this Lease is in effect, **shall constitute a current expense of the District for such Fiscal Year and shall not constitute an indebtedness of the District within the meaning of the Constitution and laws of the State.** Nothing herein shall constitute a pledge by the District of any taxes or other moneys, other than moneys lawfully appropriated from time to time by or for the benefit of the District in the annual budget of the School Board and the proceeds or Net Proceeds to the Land, to the Payment of any Rental Payment or other amount coming due hereunder.²⁴⁴

126. Under the express terms of the SEC Refunding Lease, the lease obligations do not constitute a long-term debt or liability of the District, and shall only be considered a current yearly expense for the District.²⁴⁵

127. As of June 30, 2011, the District continued to occupy the SEC Property and had not terminated the SEC Refunding Lease.²⁴⁶ Nor had the District exercised its option to purchase the property or prepay the SEC Refunding Lease.²⁴⁷

128. As of June 30, 2011, the principal amount of rent outstanding under the SEC Refunding Lease was \$7,290,000.00.²⁴⁸

129. According to the Certificate of Title for the SEC Property, Wells Fargo Bank is currently the "owner of an estate in fee simple" in the SEC Property.²⁴⁹

Edgewood Education Center (EEC)

130. In approximately 2008 or 2009, the Intermediate District Board unanimously voted on a resolution to acquire an interest in the Edgewood Elementary School in

²⁴³ *Id.*

²⁴⁴ *Id.* at 10 (emphasis added).

²⁴⁵ *Id.*

²⁴⁶ Ex. 107.

²⁴⁷ *Id.*; see also Ex. Y.

²⁴⁸ Ex. 108 at 41.

²⁴⁹ Ex. Y.

Brooklyn Park, Minnesota, referred to herein as the Edgewood Education Center or EEC Property.²⁵⁰

131. To finance the purchase, the District entered into two agreements with Wells Fargo Bank: a Lease Purchase Agreement and a Trust Agreement.²⁵¹

132. On January 1, 2010, the District and Wells Fargo Bank executed a Lease Purchase Agreement (EEC Lease), whereby Wells Fargo Bank, as lessor, agreed to purchase the EEC Property and facility and lease it to the District, as lessee.²⁵² The term of the EEC Lease is from July 20, 2010, through January 20, 2025, unless earlier terminated by the District.²⁵³ The EEC Lease expires upon the final scheduled rent payment on January 20, 2025.²⁵⁴

133. On or about January 7, 2010, Wells Fargo Bank purchased the EEC Property for a net sale price of \$5,211,436.00.²⁵⁵ To finance the purchase, Wells Fargo Bank issued two certificates of participation to investors: COP Series 2010A totaling \$3,200,000.00, and COP Series 2010B, totaling \$2,050,000.00.²⁵⁶ COP Series 2010A matures on February 1, 2020, and COP Series 2010B matures on February 1, 2025.²⁵⁷

134. Contemporaneous with the execution of the EEC Lease, Wells Fargo Bank and the Intermediate District entered into a Trust Agreement whereby the bank serves as trustee for the owners of the COPs.²⁵⁸ As trustee, Wells Fargo Bank holds in trust the EEC Property, the bank's interest in the EEC Lease, and all rental payments made by the District under the EEC Lease.²⁵⁹ The owners of the COPs are the sole beneficiaries of the trust.²⁶⁰ The corpus of the trust is Wells Fargo Bank's interest in the EEC Lease and all rental payments made by the District under the EEC Lease.²⁶¹

135. The rental payments set forth in the EEC Lease are paid separately for each of the two COPs.²⁶² The rental payments due equal the sum of the COPs issued plus interest, amortized over the term of the COPs (10 or 15 years, respectively).²⁶³ Bi-annual

²⁵⁰ The parties did not present evidence on when the District's Board approved a resolution to acquire an interest in the EEC Property. However, the fact that all Members Districts supported the District's acquisition of an interest in the EEC Property is not disputed by the parties.

²⁵¹ Exs. A, B.

²⁵² Ex. A.

²⁵³ *Id.* at Ex. B.

²⁵⁴ *Id.*

²⁵⁵ Ex. 3 at 48; Ex. 105 at 4. The exact purchase date is different in the two appraisals.

²⁵⁶ Ex. B at Ex. B. Series 2010A is tax exempt and Series 2010B is taxable. *Id.* Under the COPs, interest payments are made every six months and principal is paid annually. *Id.*

²⁵⁷ Ex. C.

²⁵⁸ Ex. B.

²⁵⁹ *Id.* at 5.

²⁶⁰ *Id.*

²⁶¹ *Id.*

²⁶² Ex. A at Ex. B.

²⁶³ *Id.*

rental payments are due from the Intermediate District to Wells Fargo Bank: from July 2010 to January 2020, for COP Series 2010A; and from July 2010 to January 2025, for COP Series 2010B.²⁶⁴

136. Upon the full payment of all rental payments, title to the property shall be conveyed to the District.²⁶⁵ However, until full payment is made, legal title to the property remains with Wells Fargo Bank, not the District.²⁶⁶ The District's only legal interest in the property during the lease term is possessory and that of a lessee.²⁶⁷ Accordingly, until the full payment of the purchase price (i.e., all rental payments are made), the District maintains only a leasehold (i.e., possessory) interest in the property.²⁶⁸

137. Section IX of the EEC Lease expressly provides:

Section 9.1. Title. During the Term of this Lease, legal title to the Land and Facilities and any and all repairs, replacements, substitutions and modifications thereto shall be in the Lessor [Wells Fargo Bank], subject to the District's interest under this Lease. Upon the payment by the District of all Rental Payments as indicated in Exhibit B, or prepayment by the District thereof pursuant hereto, full and unencumbered legal title to the Land and Facilities shall pass to the District, and the Lessor shall have no further interest therein; and the Lessor shall execute and deliver to the District a quitclaim deed to evidence the passage of legal title to the Land and Facilities to the District and the termination of the Lessor's interest therein.²⁶⁹

138. According to the EEC Lease, while the District "presently intends" to continue the lease for the entire term; plans to "take all actions necessary" to approve budgets with appropriations sufficient to pay the rent; and "reasonably believes" that moneys can and will be lawfully appropriated, the District may nonetheless terminate the EEC Lease at the end of any fiscal year without further liability.²⁷⁰

139. Like all the other lease agreements described above, the EEC Lease contains the following non-appropriation provisions:

Section 4.5. Termination by the District. The District shall have the right to terminate this Lease, in whole but not in part, at the end of any Fiscal Year of the District, in the manner and subject to the terms specified in this Section and Section 4.6, if the governing body does not appropriate or budget moneys sufficient to pay the Rental Payments coming due in the

²⁶⁴ *Id.*

²⁶⁵ *Id.* at 8, 19.

²⁶⁶ *Id.* at 19.

²⁶⁷ *Id.*

²⁶⁸ *Id.*

²⁶⁹ *Id.* (emphasis in original).

²⁷⁰ *Id.* at 5-6, 8-9.

next Fiscal Year, as determined by the District's budget for the Fiscal Year in question....In the event of termination of this Lease as provided in this Section, the District shall surrender possession of the Land and Facilities to the Trustee in accordance with Section 4.4 and convey to the Trustee or release its interests in the Land and Facilities under this Lease within ten (10) days after the expiration of the then-current term of this Lease.²⁷¹

Section 4.6. Effect of Termination. Upon termination of this Lease as provided in Section 4.5, the District shall not be responsible for the payment of any additional Rental Payments coming due with respect to succeeding Fiscal Years....²⁷²

140. In addition, the EEC Lease does not obligate the District to appropriate funds necessary to continue the Lease.²⁷³ According to Section 2.1(h) of the EEC Lease:

Except to the extent specifically provided herein, the government body is not obligated to appropriate or otherwise provide moneys for the payment of the Rental Payments or any other amounts coming due hereunder; and in the event of Non-Appropriation²⁷⁴ by the governing body, **the District shall not be liable for general, special, incidental, consequential or other damages resulting therefrom**, except as provided in Section 4.6 hereof.²⁷⁵

141. Consequently, the District may terminate the Lease at the end of any fiscal year if the District's Board does not appropriate or budget moneys sufficient to pay the rental payments coming due in the next fiscal year.²⁷⁶ Moreover, such early termination would not result in any liability for the District beyond the current fiscal year.²⁷⁷ As expressly stated in the EEC Lease:

...This Lease does not constitute a general obligation of the District, and the full faith and credit and taxing powers of the District are not pledged for the

²⁷¹ *Id.* at 8-9.

²⁷² *Id.* at 9.

²⁷³ *Id.* at 5-6.

²⁷⁴ "Non-appropriation" is defined in the EEC Lease as:

The failure of the School Board of the District to appropriate moneys for any Fiscal Year of the District sufficient for the continued performance of this Lease by the District, as evidenced by the passage of a resolution specifically prohibiting the District from performing its obligations under this Lease, and from using any moneys to pay the Rental Payments due under this Lease for a designated Fiscal Year and all subsequent Fiscal Years.

Id. at 2.

²⁷⁵ *Id.* at 5-6 (emphasis added).

²⁷⁶ *Id.*

²⁷⁷ *Id.*

payment of the Rental Payments or other amounts coming due, or other actions required to be performed.²⁷⁸

Section 5.2 Current Expense. The obligations of the District under this Lease, including its obligation to pay the Rental Payments, in any Fiscal Year for which this Lease is in effect, **shall constitute a current expense of the District for such Fiscal Year and shall not constitute an indebtedness of the District within the meaning of the Constitution and laws of the State**. Nothing herein shall constitute a pledge by the District of any taxes or other moneys other than moneys lawfully appropriated from time to time by or for the benefit of the District in the annual budget of the School Board and the proceeds of Net Proceeds of the Land and Facilities, to the payment of any Rental Payment or other amount due hereunder.²⁷⁹

142. Accordingly, the EEC Lease does not constitute a long-term debt, and shall only be considered a current yearly expense or “appropriation” for the District.²⁸⁰

143. Upon early termination of the EEC Lease, the District must pay the rent remaining due for the current fiscal year and surrender possession of the property.²⁸¹ The EEC Lease states:

Section 4.4 Surrender of Land and Facilities. Upon termination of the Term of this Lease pursuant to Section 4.2., clauses (a) or (c), or upon exercise by the Trustee of its rights to take possession of the Land and Facilities under Section 13.2, the District shall surrender the Land and Facilities to the Trustee in the condition in which they were originally received from the Trustee, except as repaired, rebuilt, restored, altered or added to as permitted or required thereby, ordinary wear and tear excepted.²⁸²

Section 13.3. Return of Land and Facilities. Upon the expiration or termination of this Lease prior to the payment of all Rental Payments in accordance with Exhibit B, the District shall return the Land and Facilities to the Lessor....²⁸³

144. All rental payments made prior to termination are, thus, forfeited to Wells Fargo Bank, and do not represent any equity in the property as to the Intermediate

²⁷⁸ *Id.* at 5.

²⁷⁹ *Id.* at 10 (emphasis added).

²⁸⁰ *Id.*

²⁸¹ *Id.*

²⁸² *Id.* at 8.

²⁸³ *Id.* at 25 (emphasis in original).

District.²⁸⁴ Wells Fargo Bank, as trustee for the COP investors, would then be able to re-let the property to another lessee or sell it to pay off the COPs.²⁸⁵

145. Under the EEC Lease, the Intermediate District would not be liable for the remainder of the rental payments, for any deficiency upon sale or re-letting, or for any other damages as a result of early termination.²⁸⁶ This is true whether the EEC Lease is terminated by the District or the District defaults on its obligations.²⁸⁷ The remedies available to Wells Fargo Bank on the District's default are limited to the rent due for the current fiscal year, unless the District fails to vacate the property within 10 days.²⁸⁸

146. According to the Certificate of Title for the EEC Property, Wells Fargo Bank is the "owner of an estate in fee simple" in the EEC Property.²⁸⁹

147. As of June 30, 2011, the District continued to occupy the EEC Property and had not terminated or prepaid the EEC Lease, and had not exercised its option to purchase the property.

148. As of June 30, 2011, the principal amount outstanding for rent payments under the EEC Lease was \$4,975,000.00: \$2,925,000.00 for COP Series 2010A; and \$2,050,000.00 for COP Series 2010B.²⁹⁰

North Education Center (NEC)

149. On December 17, 2009, the Board of the Intermediate District voted on a resolution to purchase land and construct a new facility in New Hope, Minnesota, called the North Education Center (NEC or NEC Property).²⁹¹ Bloomington was the only Member District that voted against this acquisition.²⁹² The resolution nonetheless passed, and the Intermediate District proceeded with its plan to purchase land and construct the NEC, over Bloomington's objection.²⁹³

150. Approximately one month after the Intermediate District voted to acquire an interest in land and construct the NEC — over Bloomington's objection — Bloomington voted to withdraw from the Intermediate District.²⁹⁴

²⁸⁴ *Id.* at 23-25.

²⁸⁵ *Id.*

²⁸⁶ *Id.*; see also Ex. B at Ex. B (COP).

²⁸⁷ Ex. A at 23-25.

²⁸⁸ *Id.*

²⁸⁹ Ex. Z.

²⁹⁰ Ex. 108 at 41.

²⁹¹ Ex. 22. The resolution was "to enter into negotiations with Robbinsdale Area School for the purchase of land to replace Hostermann and to continue to work with TSP, Inc. to develop a schematic design for a new North Education Center." *Id.*

²⁹² *Id.*

²⁹³ *Id.*

²⁹⁴ Ex. 21. Bloomington's Notice of Withdrawal was served on the Intermediate District on January 29, 2010.

151. Despite Bloomington's withdrawal, on November 18, 2010, the Intermediate District and U.S. Bank National Association (U.S. Bank) entered into a Lease Purchase Agreement (NEC Lease), Trust Agreement (NEC Trust Agreement), and Ground Lease and Easement Agreement (NEC Ground Lease) related to the NEC Property and the construction of a building thereon.²⁹⁵

152. A First Supplemental Lease Purchase Agreement (NEC Supplemental Lease), First Supplemental Trust Agreement (NEC Supplemental Trust Agreement), and First Supplemental Ground Lease Agreement and Easement Agreement (NEC Supplemental Ground Lease) were executed by the Intermediate District and U.S. Bank on May 19, 2011.²⁹⁶ The NEC Lease and the NEC Supplemental Lease shall be collectively referred to as the "NEC Lease, as supplemented."²⁹⁷

153. The total cost for U.S. Bank to purchase the property and build the NEC facility was \$33,865,000.00²⁹⁸

154. Like the WEC, SEC, and EEC Properties, the purchase and construction of the NEC Property was financed through U.S. Bank's issuance of two Certificates of Participation: COP Series 2010E in the amount of \$29,790,000.00, financing the cost of the land purchase and the construction of the building; and COP Series 2011A in the amount of \$4,075,000.00, financing the cost to construct a third floor addition to the building (COP Series 2010E and COP Series 2011A shall be collectively referred to herein as the "NEC COPs").²⁹⁹

155. Pursuant to the NEC Trust Agreement and NEC Supplemental Trust Agreement, the proceeds from the sale of the NEC COPs (less U.S. Bank's administrative fees) were deposited into a trust fund acquisition account (NEC Trust Fund), out of which all costs for the acquisition and construction of the NEC Property were to be paid.³⁰⁰

156. Like the other lease agreements described above, the NEC Lease provides that the District is "not obligated to appropriate or otherwise provide moneys for the payment of the Rental Payments or any other amounts coming due" under the lease in any fiscal year; and "in the event of Non-Appropriation by governing body, the District shall not be liable for general, special, incidental, consequential or other damages resulting therefrom."³⁰¹

²⁹⁵ Exs. R, S, T.

²⁹⁶ Exs. U, V, W.

²⁹⁷ The NEC Supplemental Lease provides for the construction of a third floor addition to the NEC Property at a cost of \$4,075,000. See Ex. U.

²⁹⁸ Ex. 108 at 41.

²⁹⁹ Exs. R, S, U, V.

³⁰⁰ Exs. S and V.

³⁰¹ Ex. R at 5-6.

157. Similarly, the District has the right to terminate the lease at the end of any fiscal year if the District's Board "does not appropriate or budget moneys sufficient to pay the Rental Payments coming due in the next Fiscal Year."³⁰² In the event of termination, "the District shall not be responsible for the payment of any additional Rental Payments coming due with respect to succeeding Fiscal Years," unless the District fails to vacate the premises.³⁰³

158. The rent payments due under the NEC Lease are also not considered "debt" by the District.³⁰⁴ The NEC Lease expressly provides:

Section 5.2. Current Expense. The obligations of the District under this Lease, including its obligation to pay the Rental Payments, in any Fiscal Year for which this Lease is in effect, shall constitute a current expense of the District for such Fiscal Year and shall not constitute an indebtedness of the District within the meaning of the Constitution and laws of the State. Nothing herein shall constitute a pledge by the District of any taxes or other moneys, other than moneys lawfully appropriated from time to time by or for the benefit of the District in the annual budget of the School Board and the proceeds or Net Proceeds of the Facilities, to the payment of any Rental Payment or other amounts coming due hereunder.³⁰⁵

159. If the District does not terminate the NEC Lease, as supplemented, and completes all rental payments due under the leases, the District will eventually acquire an unencumbered interest in the NEC property.³⁰⁶ However, during the term of the lease, "legal title to the Facilities and any and all repairs, replacements, substitutions, and modifications thereto shall be in the Lessor [U.S. Bank];" and the District shall "not mortgage, sell, assign, transfer or convey the Facilities or any portion thereof."³⁰⁷

160. To provide additional security for the bank, the NEC Property is also fully encumbered by the NEC Ground Lease and NEC Supplemental Ground Lease, which give U.S. Bank a full possessory interest in the NEC Property in the case of the District's default or early termination of the NEC Lease, as supplemented.³⁰⁸ The NEC Ground Lease and NEC Supplemental Ground Lease fully encumber the NEC Property until February 2039, unless the District completes all payments due under the NEC Lease, as supplemented, or exercises its option to prepay all rent due prior to the completion of the full lease term.³⁰⁹

³⁰² *Id.* at 8.

³⁰³ *Id.* at 8-9.

³⁰⁴ *Id.* at 10.

³⁰⁵ *Id.*

³⁰⁶ *Id.* at Ex. B; Ex. U at Ex. B.

³⁰⁷ Ex. R at 18, 21.

³⁰⁸ Exs. T, W.

³⁰⁹ Exs. T, W.

161. As of June 30, 2011, the Intermediate District had not terminated the NEC Lease, as supplemented, and had not exercised its option to prepay the lease to obtain clear title to the NEC Property.

162. As of June 30, 2011, the principal amount outstanding on the NEC Lease and NEC Supplemental Lease was \$33,865,000.00: \$29,790,000.00 under the NEC Lease; and \$4,075,000.00 under the NEC Supplemental Lease.³¹⁰

EMPLOYEE BENEFIT AND PENSION PLAN OBLIGATIONS OF THE DISTRICT

163. In addition to the value of real estate interests held by the Intermediate District, the parties disagree as to the amount and allocation of liability related to pension and other post-employment benefits owed to employees of the District.

164. The Intermediate District offers its employees various employment benefits, including: a flexible benefit cafeteria plan; a multi-employer-funded retirement plan administered by the Teachers' Retirement Association (TRA) or the Public Employees' Retirement Association (PERA); post-employment insurance benefits (referred to herein as other post-employment benefits or OPEB); and a District-funded, defined benefit pension plan (Pension Benefits Plan).³¹¹

165. The District's contributions to the retirement plans administered by the TRA and PERA are established by statute and are paid by the District to these plans each year as the benefits are earned.³¹² The amounts paid are calculated to cover the future benefits owed.³¹³ Accordingly, these benefits, and the amount paid to these plans, are not in dispute.

166. Similarly, the flexible benefit cafeteria plan is paid on a monthly basis by the District to an outside plan administrator.³¹⁴ These amounts are paid in full each year and are not future obligations of the District.³¹⁵ Therefore, they are not in dispute.

167. In contrast, the District's self-funded OPEB and Pension Benefits Plan are unfunded future obligations of the District.³¹⁶ The parties disagree as to: (1) whether these benefits are liabilities that should be included in the calculation of assets and liabilities for purposes of distribution upon Bloomington's withdrawal from the District; and (2) if these benefits constitute liabilities owed, how they should be calculated and allocated to Bloomington.

³¹⁰ Ex. 108 at 41.

³¹¹ *Id.* at 44-51.

³¹² *Id.* at 48-51.

³¹³ *Id.*

³¹⁴ *Id.* at 51.

³¹⁵ *Id.*

³¹⁶ Ex. 23; Ex. 108 at 45-46.

Other Post-Employment Benefits

168. All employees who retire from the Intermediate District have the option under state law³¹⁷ to continue their medical insurance coverage through the District from the time of retirement until the employee reaches the age of eligibility for Medicare.³¹⁸ As a benefit to some of its employees, the Intermediate District pays all or part of the employee's medical and/or dental insurance premiums from the date of retirement until the date the retiree is eligible for Medicare.³¹⁹ Eligibility for this benefit is based on years of service, minimum age requirements, and membership in certain employee groups.³²⁰

169. Post-employment insurance benefits paid by the District differ by collective bargaining unit and are established in the collective bargaining agreements.³²¹ Therefore, they are contractual obligations of the District.³²²

170. As of June 30, 2011, there were 730 active OPEB plan participants and 43 retired OPEB plan participants.³²³ The number of employees receiving the benefits and the cost of the insurance premiums change year-to-year.³²⁴ Therefore, the District's contribution obligation changes each year, and its future obligations can only be estimated, but cannot be concretely determined.³²⁵

171. While the District is contractually obligated to pay these on-going benefits, the Intermediate District does not set aside funds to cover these future expenses, and there are no invested plan assets earmarked to pay for these future benefits.³²⁶ As a result, the District's future OPEB obligations are unfunded in advance and are paid on an annual basis, as costs, as they arise.³²⁷

172. The District's actual cost of OPEB differs year-to-year depending on how many retirees receive the benefit that year and what type of insurance benefits those retirees receive.³²⁸ Each year during the budgeting process, the District projects how many retired employees will receive OPEB for the next fiscal year.³²⁹ The District then calculates the estimated cost of OPEB for the year and budgets accordingly to pay for the costs as they come due (i.e., as eligible retirees receive the benefit).³³⁰ Payments are

³¹⁷ Minn. Stat. § 471.61 (2014).

³¹⁸ Ex. 23; Ex. 108 at 45-46.

³¹⁹ Ex. 23; Ex. 108 at 45-46.

³²⁰ Ex. 23; Ex. 108 at 45-46.

³²¹ Ex. 23; Ex. 108 at 45-46.

³²² Ex. 23; Ex. 108 at 45-46.

³²³ Ex. 23; Ex. 108 at 45-46.

³²⁴ Ex. 23; Ex. 108 at 45-46.

³²⁵ Test. of Mark Schulte at T. 852.

³²⁶ *Id.* at T. 839, 844.

³²⁷ *Id.*

³²⁸ *Id.* at T. 851-53.

³²⁹ *Id.*

³³⁰ *Id.*

then made out of the District's general operating fund as an employee expense.³³¹ This is referred to as "pay-as-you-go" financing.³³² It means that OPEB are treated as costs when the benefit is paid, as opposed to recognizing OPEB as a vested obligation at the time the benefit is earned by the employee.³³³ There is risk in this type of financing because no funds are being set aside or saved to pay for the future benefits that are accruing.

173. In 2009, the Intermediate District began following Governmental Accounting Standards Board (GASB) Statement No. 45. GASB Statement No. 45 establishes standards for measuring, recognizing, and displaying OPEB values on financial statements.³³⁴

174. Prior to 2009, the District did not include any calculation of future obligations for OPEB on the District's financial statements.³³⁵ Because the District finances its OPEB obligations on a "pay-as-you-go" basis, OPEB were only recognized on the financial statements when the promised benefits were paid, not as they accrued or were earned.³³⁶ As a result, the District's future obligations to pay OPEB were not noted on financial statements as future liabilities.³³⁷

175. GASB Statement No. 45 changed that practice to ensure that future OPEB obligations are estimated and recognized on financial statements.³³⁸ This ensures that government entities recognize their future obligations and assess potential demands on future cash flow.³³⁹ Without recognizing the accruing liability, a government entity risks being unable to fund the obligation when it is due for payment, many years after it was earned by the employee.³⁴⁰

176. Under GASB Statement No. 45, the District's financial statement must include the annual required contribution (ARC) required to meet the District's future OPEB liability.³⁴¹ The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal OPEB costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.³⁴²

177. Professional accounting standards promulgated by GASB require that school districts prepare an actuarial report to estimate OPEB liabilities every two years.³⁴³

³³¹ *Id.*

³³² Ex. 108 at 44.

³³³ *Id.*

³³⁴ Ex. 109.

³³⁵ Test. of M. Schulte at T. 847-48.

³³⁶ *Id.*

³³⁷ *Id.*

³³⁸ Ex. 109.

³³⁹ *Id.*

³⁴⁰ *Id.*

³⁴¹ Ex. 108 at 45.

³⁴² *Id.*

³⁴³ Test. of M. Schulte at T. 825.

The actuarial figures are then included in the District's audited financial statements as footnotes.³⁴⁴

178. In compliance with the GASB requirements, the District hired the actuarial firm of Van Iwaarden and Associates (Van Iwaarden) to calculate its estimated liability for OPEB so that the District's OPEB ARC could be included in the District's 2011 Audited Financial Statement.³⁴⁵

179. To calculate the value of the OPEB, Van Iwaarden actuaries reviewed the District's collective bargaining agreements to establish the employees' entitlements to benefits and the scope of those benefits.³⁴⁶ Next, the actuaries reviewed census data, insurance data, and employee data.³⁴⁷ From there, the actuaries estimated how many employees will elect to receive the OPEB benefits; when the employees are likely to receive the benefits; and the amount that the employees are likely to receive in the future.³⁴⁸

180. From this data, the actuaries calculated the District's actuarial accrued liability (AAL): the estimated liability associated with the OPEB that has been accrued or earned by employees up to the valuation date.³⁴⁹ In this case, the date of valuation is July 1, 2011.³⁵⁰ The District's AAL does not include any liability for benefits that will be accrued in the future or based on future service.³⁵¹

181. The actuaries then compared the AAL with the funds set aside by the District to pay future OPEB liabilities, and determined the District's unfunded actuarial accrued liability (UAAL).³⁵² Because the District does not set aside funds to cover future OPEB obligations, the AAL and the UAAL are the same amounts.³⁵³

182. AAL and UAAL figures are not definite.³⁵⁴ They are only estimates, based upon actuarial assumptions, of what the District's future liability may be based upon current conditions.³⁵⁵ What the District will actually pay in the future for these benefits could be significantly different, depending on future changes in health care laws, insurance laws, employee mortality, employee attrition, etc.³⁵⁶

³⁴⁴ *Id.*

³⁴⁵ *Id.* at T. 828.

³⁴⁶ *Id.* at T. 836.

³⁴⁷ *Id.* at T. 837.

³⁴⁸ *Id.* at T. 838.

³⁴⁹ *Id.*

³⁵⁰ *Id.*

³⁵¹ *Id.*

³⁵² *Id.* at T. 839.

³⁵³ *Id.*

³⁵⁴ *Id.* at T. 858.

³⁵⁵ *Id.*

³⁵⁶ *Id.*

183. Van Iwaarden estimated that the District's AAL and UAAL for OPEB earned by employees as of July 1, 2011, was \$9,532,459.00.³⁵⁷

184. Bloomington offered no evidence to dispute the District's calculation of AAL and UAAL for OPEB earned by employees as of July 1, 2011. Instead, Bloomington argues that it is not liable for any of this amount because the District pays its pension liabilities on a "pay-as-you-go" basis. In the alternative, Bloomington disputes its proportionate share of this amount.

Severance Benefits Payable and Compensated Absences Payable

185. Van Iwaarden actuaries also determined the District's estimated future liability for accrued compensated absences³⁵⁸ as of July 1, 2011.³⁵⁹ The District's auditors splits these "accrued compensated absences" into two types: "compensated absences payable," meaning accrued vacation payable at years end; and "severance benefits payable," meaning early retirement incentive benefits payable to former employees.³⁶⁰ Both benefit liabilities are paid by the District out of its general fund each year.³⁶¹

186. As of July 1, 2011, the estimated future liability for "severance benefits payable" was \$5,758,291.00.³⁶² This amount, when discounted to 2011 dollars, is estimated to be \$4,731,848.00.³⁶³ According to the Intermediate District's expert actuary, the discounted amount for severance benefits payable is closer to \$4.5 million.³⁶⁴ However, Bloomington does not dispute the Intermediate District's accountant's calculation of \$4,731,848.00.³⁶⁵ Bloomington only disputes its proportionate share of this liability.³⁶⁶ Accordingly, the stipulated amount for severance benefits payable by the District as of June 30, 2011, is \$4,731,848.00.

187. With respect to compensated absences payable (i.e., accrued vacation payable) to employees as of June 30, 2011, the District's accountants and actuaries

³⁵⁷ Ex. 129

³⁵⁸ Compensated absences are absences for which employees are entitled to be paid, such as earned vacation, sick leave, severance, and sabbatical leave. See GASB Statement No. 16 at <http://www.gasb.org/st/summary/gstsm16.html>. Accordingly, "accrued compensated absences" means paid time off that employees have earned but have not yet taken. *Id.* The Administrative Law Judge takes judicial notice of GASB Statement No. 16, pursuant to Minn. R. 14.60, subd. 4 and Minn. R. 1400.8100, subp. 2.

³⁵⁹ Test. of M. Schulte at T. 842; Ex. 129.

³⁶⁰ Ex. 23, Ex. 108 at 41.

³⁶¹ Ex. 23, Ex. 108 at 41.

³⁶² Ex. 129 at 11; Test. of M. Schulte at T. 841-42, 854-57 (comments by Bloomington's attorney David Holman).

³⁶³ Ex. 129 at 11; Test. of M. Schulte at T. 841-42, 854-57; see also Ex. 103 at Table 2.

³⁶⁴ Test. of M. Schulte at T. 842.

³⁶⁵ See *id.* at T. 854-57 (comments by Bloomington's attorney David Holman).

³⁶⁶ *Id.*

calculated the amount to be \$375,937.00.³⁶⁷ Bloomington did not present evidence to dispute this amount or Bloomington's liability therefor.

Pension Benefits Plan

188. The Intermediate District also offers a self-funded Pension Benefits Plan to certain of its eligible employees.³⁶⁸ The pension benefits offered under the plan are set forth in the collective bargaining agreements between the District and its employee units.³⁶⁹ Therefore, like OPEB, the pension benefits are contractual obligations of the District.³⁷⁰ In addition, because the District's pension liability has already been earned by its employees as part of their total compensation for past service, as promised in the collective bargaining agreements, it cannot be lawfully reduced once an employee retires.³⁷¹

189. Eligibility for pension benefits is based upon years of service, minimum age requirements, and membership in certain employee groups.³⁷² The amount of the pension benefit differs by individual and bargaining unit.³⁷³ The District's payment obligations under the Pension Benefits Plan differ year-to-year based upon the number of retirees receiving the benefit that year and the amount of the recipients' individual benefits.³⁷⁴

190. As of June 30, 2011, there were 730 active participants in the District's Pension Benefits Plan.³⁷⁵

191. While the District is contractually obligated to pay these pension benefits on an on-going basis, the Intermediate District does not escrow funds to cover these future expenses, and there are no invested plan assets earmarked to pay for these future benefits.³⁷⁶ In other words, the District's Pension Benefits Plan is unfunded, and the benefits are paid when recipients collect the benefit (i.e., receive their pensions). An amount to cover the promised benefit is not set aside by the District when the benefits are earned or as they accrue.³⁷⁷

192. Each year, the District projects the amount of the pension benefits it will be required to pay for the next fiscal year and budgets accordingly to pay for that year's

³⁶⁷ Ex. 23, Ex. 108 at 40.

³⁶⁸ Ex. 108 at 46-48.

³⁶⁹ *Id.*

³⁷⁰ *Id.*

³⁷¹ *See, e.g., Housing and Redevelopment Authority of Chisholm v. Norman*, 696 N.W.2d 329, 337-38 (Minn. 2005).

³⁷² Ex. 108 at 46-48.

³⁷³ *Id.*

³⁷⁴ *Id.*

³⁷⁵ Ex. 23, Ex. 108 at 46.

³⁷⁶ Ex. 108 at 46-47.

³⁷⁷ *Id.*

costs.³⁷⁸ Like the District's OPEB obligations, financing of the District's Pension Benefit Plan is on a "pay-as-you-go" basis.³⁷⁹ The expenses are paid out of the District's general operating fund as costs, and there is no escrowing of funds as the benefits are earned by the employees.³⁸⁰

193. According to the District's actuarial expert, the AAL for the District's pension as of July 1, 2011, was \$409,117.00.³⁸¹ Because the District's employee pension obligations are paid on a "pay-as-you-go" basis each year, there is no amount set aside for payment of this future obligation.³⁸² Therefore, the UAAL for the District's employee pension plan as of July 1, 2011, was the same as the AAL, \$409,177.00.³⁸³

194. Bloomington offered no evidence to dispute the calculation of the Intermediate District's long-term pension liability. Instead, Bloomington argues that it is not liable for any of this amount because the District pays its pension liabilities on a "pay-as-you-go" basis.³⁸⁴ In the alternative, Bloomington disputes its proportionate share of this amount.³⁸⁵

WITHDRAWAL OF BLOOMINGTON FROM INTERMEDIATE DISTRICT

195. In 2006, Les Fujitake (Fujitake) was appointed as the Superintendent of the Bloomington Public Schools.³⁸⁶ Upon his appointment, Fujitake discovered that the Bloomington School District (ISD #271) was "very unstable".³⁸⁷ Since approximately 1995, Bloomington had been cutting programs and staff, increasing class sizes, closing schools, and not maintaining its facilities.³⁸⁸ As a result, residents of the district were losing confidence in the quality of the educational services being provided.³⁸⁹

196. As Superintendent, Fujitake determined that Bloomington had to cut costs to remain competitive.³⁹⁰ Among other things, Fujitake began to evaluate Bloomington's membership in the Intermediate District.³⁹¹

197. A review of Bloomington's use of the services provided by the Intermediate District showed that Bloomington was the highest consumer of special education services

³⁷⁸ *Id.*

³⁷⁹ *Id.* at 46.

³⁸⁰ *Id.*

³⁸¹ Ex. 129 at 12.

³⁸² Ex. 108 at 46.

³⁸³ Ex. 129 at 12.

³⁸⁴ See Bloomington's Post-Hearing Brief.

³⁸⁵ *Id.*

³⁸⁶ Test. of L. Fujitake at T. 27.

³⁸⁷ *Id.* at T. 27-28.

³⁸⁸ *Id.*

³⁸⁹ *Id.*

³⁹⁰ *Id.* at T. 28, 33.

³⁹¹ *Id.* at T. 28.

of all Member Districts.³⁹² Fujitake discovered that only 10 percent of Bloomington students required special education services, but that 20 percent of Bloomington's budget was spent on those services.³⁹³

198. Fujitake set out to determine whether Bloomington could provide its students with the same services in-house that the Intermediate District provided; or whether either of the other two metropolitan intermediate districts could provide the same services to Bloomington more economically.³⁹⁴

199. Fujitake concluded that Bloomington could save a significant amount of money by withdrawing from the Intermediate District and joining Intermediate School District 917.³⁹⁵

200. Fujitake then reviewed the 2009 Memorandum of Agreement and determined that Bloomington had a right to withdraw from the Intermediate District.³⁹⁶ The Agreement was silent, however, as to how the Intermediate District's assets and liabilities would be calculated and attributed to Member Districts upon withdrawal.³⁹⁷

201. Fujitake thus looked to Minn. Stat. § 123A.24, which provides that if an intermediate district and withdrawing member district cannot agree on the distribution of assets and liabilities, the Commissioner shall resolve the dispute by determining the withdrawing district's "proportionate share of assets and liabilities based on the district's enrollment, financial contribution, usage, or other factor or combination of factors determined appropriate by the commissioner."³⁹⁸

202. Guided by the Agreement and Minn. Stat. § 123A.24, Fujitake set out to determine Bloomington's financial exposure if it opted to withdraw from the cooperative.³⁹⁹ To estimate the financial implications of Bloomington's withdrawal, Fujitake reviewed the Intermediate District's audited financial statements, which showed

³⁹² Ex. 103 at Table 1.

³⁹³ Test. of L. Fujitake at T. 28.

³⁹⁴ *Id.* at T. 28-32.

³⁹⁵ *Id.* at T. 34, 36, 53. Ultimately, Bloomington concluded that its withdrawal from the Intermediate District saved Bloomington approximately \$200,000 per year. *Id.* at T. 34.

³⁹⁶ *Id.* at T. 37.

³⁹⁷ *Id.* at T. 37-38; *see also* Ex. 101.

³⁹⁸ Test. of L. Fujitake at T. 41.

³⁹⁹ *Id.* at T. 41-42

that the District had assets exceeding its liabilities.⁴⁰⁰ As a result, Fujitake concluded that Bloomington would not owe money to the Intermediate District if Bloomington withdrew.⁴⁰¹ Indeed, Fujitake determined that the Intermediate District would be required to pay out assets to Bloomington.⁴⁰²

203. Relying upon the information set forth in the Intermediate District's audited financial statements, Fujitake recommended to the Bloomington School Board that Bloomington withdraw from the Intermediate District.⁴⁰³ Notably, Bloomington's decision to withdraw occurred just one year after reconfirming its commitment to the Intermediate District by executing the 2009 Memorandum of Agreement.⁴⁰⁴

204. On January 28, 2010, the Bloomington School Board passed a resolution to withdraw from the Intermediate District effective July 1, 2011.⁴⁰⁵ A Notice of Withdrawal and a certified copy of the resolution were served on the Intermediate District on January 29, 2010.⁴⁰⁶

205. Prior to 2011, no Member District had ever withdrawn from the Intermediate District.⁴⁰⁷

206. The parties stipulate that Bloomington's Notice of Withdrawal was valid and timely, and that Bloomington had the legal right to withdraw from the Intermediate District.⁴⁰⁸ The Intermediate District's fiscal year runs from July 1 to June 30 each year. Accordingly, Bloomington gave notice of its withdrawal mid-way through fiscal year 2010, but the withdrawal was not effective until the end of fiscal year 2011 (June 30, 2011), giving the District approximately one-and-a-half years to prepare for Bloomington's withdrawal.⁴⁰⁹

⁴⁰⁰ *Id.* at T. 41, 55. It appears that Fujitake is referring to the financial statement for fiscal year 2011, but such financial statement would not have been available to him until after June 30, 2011. The Intermediate District's audited financial statements for fiscal year 2009 and fiscal year 2010 were not admitted into evidence. The audited financial statement for 2011 states that the Intermediate District had net assets of \$4,584,233.00 in fiscal year 2010 and net assets of \$13,768,147.00 in fiscal year 2011. See Ex. 108 at 16. The record is silent as to whether the Intermediate District had net assets in fiscal year 2009. According to his testimony, Fujitake was evaluating whether Bloomington should withdraw from the Intermediate District in 2009. Therefore, Fujitake would have had to rely upon financial information from fiscal year 2009 or earlier, not the audited financial statement from fiscal year 2011.

⁴⁰¹ Test. of L. Fujitake at T. 41.

⁴⁰² *Id.*

⁴⁰³ *Id.*

⁴⁰⁴ See Exs. 21, 101, 102.

⁴⁰⁵ Ex. 21.

⁴⁰⁶ *Id.*

⁴⁰⁷ Test. of S. Lewandowski at T. 437.

⁴⁰⁸ See the parties' Post-Hearing Briefs filed on August 25, 2014.

⁴⁰⁹ The 2009 Memorandum of Agreement provides that notices of withdrawal received by February 1 are effective June 30 of the following fiscal year. See Ex. 101 at 2. This is also consistent with Minn. Stat. § 123B.02, subd. 3(c) (2014).

2011 AUDITED FINANCIAL STATEMENT

207. Pursuant to Minn. Stat. § 123B.77, subd. 3 (2014), by December 31 of each year, the Intermediate District must file an audited financial statement with the Commissioner for the preceding fiscal year.

208. In 2011, the certified public accounting firm of Malloy, Montague, Karnowski, Radosevich & Co., P.A. (MMKR) prepared an audited financial report for the Intermediate District for the fiscal year ending June 30, 2011 (hereafter referred to as the “2011 Audited Financial Statement”).⁴¹⁰

209. The Intermediate District filed the 2011 Audited Financial Statement with the Commissioner on or before December 31, 2011, as required by Minn. Stat. § 123B.77, subd. 3 (2010).⁴¹¹ The 2011 Audited Financial Statement showed that the Intermediate District had assets in the amount of \$117,152,119.00 and liabilities in the amount of \$103,383,972.00.⁴¹² As a result, the 2011 Audited Financial Statement declared that the Intermediate District had net assets (i.e., assets in excess of liabilities) in the amount of \$13,768,147.00.⁴¹³

210. The assets included in the 2011 Audited Financial Statement included the land and buildings used for the NEC, SEC, WEC, DSC, and EEC Properties, as well as the Robbinsdale Condo.⁴¹⁴ The asset value attributed to the land and buildings associated with the SEC, WEC, DSC, and EEC Properties and Robbinsdale Condo was \$52,665,400.00.⁴¹⁵ The asset value attributed to the NEC Property, which was then in the early process of construction, was \$5,458,349.00.⁴¹⁶

211. The values attributed to the real properties in the 2011 Audited Financial Statement were determined on a cost basis; that is, the value of the land was the original purchase price paid by the bank for the property, and the value of the buildings was the actual cost of construction.⁴¹⁷

212. The 2011 Audited Financial Statement also included, as an asset of the District, the amount remaining in the NEC Trust Fund as of June 30, 2011. The NEC Trust Fund, less accrued interest of \$39,746.00, is denoted in the 2011 Audited Financial Statement as, “Restricted Assets – temporarily restricted cash and investments for capital projects” (Restricted Assets).⁴¹⁸

⁴¹⁰ Exs. 23, 108.

⁴¹¹ Exs. 23, 108.

⁴¹² Ex. 23 at 16; Ex. 108 at 16.

⁴¹³ Ex. 23 at 16; Ex. 108 at 16.

⁴¹⁴ Ex. 23 at 40-41; Ex. 108 at 40-41.

⁴¹⁵ Ex. 23 at 39; Ex. 108 at 39.

⁴¹⁶ Ex. 23 at 39; Ex. 108 at 39. As of June 30, 2011, the NEC was still under construction and \$5,458,349 was the amount paid as of that date for construction of the building. See Test. of Gary Dosdall at T. 704.

⁴¹⁷ Test. of G. Dosdall at T. 665-66.

⁴¹⁸ Ex. 108 at 16, 18, 19.

213. As of June 30, 2011, the NEC Property was in the early stages of construction. The amount remaining in the NEC Trust Fund as of June 30, 2011, was \$28,961,846.00, including accrued interest of \$39,746.00.⁴¹⁹ There was also a construction bill for the NEC Property owing as of June 30, 2011, in the amount of \$1,637,047.00.⁴²⁰ Said invoice remained outstanding and had not yet been deducted from the NEC Trust Fund.⁴²¹ The 2011 Audited Financial Statement included the amount to be paid (\$1,637,047.00) in the District's overall "accounts and contracts payable" amount of \$2,495,498.00.⁴²²

214. The District's accountants included the amounts in the NEC Trust Fund as a "Restricted Asset" of the District because the funds were not liquid assets available to the District for its unfettered use.⁴²³ Rather, the Restricted Assets were the proceeds from the NEC COPs, which were held in trust by U.S. Bank and expressly earmarked for the acquisition and construction of the NEC Property, as required in the NEC Trust Agreement and NEC Supplemental Trust Agreement.⁴²⁴

215. The liabilities set forth in the 2011 Audited Financial Statement also included "long-term liabilities" related to the financing of the SEC building (\$25,753,734.00) and the Certificates of Participation issued by the banks to finance the Intermediate District's interest in the WEC, SEC, EEC, and NEC Properties (totaling \$53,720,000.00).⁴²⁵ The amounts included as "liabilities" were the principal amounts remaining to be paid after June 30, 2011, provided that the lease-purchase agreements or refunding leases associated with those properties were not terminated, and the contracts were paid to completion.⁴²⁶ Because interest had not yet been accrued, interest was not included in the determination of the "liabilities."⁴²⁷

216. The break-down of "liabilities" for each property, as set forth in the 2011 Audited Financial Statement, was as follows:

⁴¹⁹ Ex. 108 at 13, 16, 18, 19.

⁴²⁰ *Id.*

⁴²¹ *Id.*

⁴²² *Id.* at 18-19.

⁴²³ *Id.* at 13, 16, 18, 19.

⁴²⁴ Exs. S and V.

⁴²⁵ Ex. 108 at 41.

⁴²⁶ *Id.*

⁴²⁷ *Id.*

Property	Original Amount	Principal Outstanding
WEC	\$ 8,570,000.00	\$ 7,590,000.00
SEC (building)	\$25,400,000.00	\$25,753,734.00
SEC (land)	\$ 7,405,000.00	\$ 7,290,000.00
EEC (COP 2010A)	\$ 3,200,000.00	\$ 2,925,000.00
EEC (COP 2010B)	\$ 2,050,000.00	\$ 2,050,000.00
NEC	\$29,790,000.00	\$29,790,000.00
NEC (addition)	\$ 4,075,000.00	\$ 4,075,000.00
Total:		\$79,473,734.00 ⁴²⁸

217. The 2011 Audited Financial Statement's Statement of Net Assets did not include as liabilities the total cost of OPEB and pension benefits accrued by, but yet unpaid to, employees.⁴²⁹ Rather, the Statement of Net Assets included as liabilities only the estimated Annual Required Contribution (ARC) for OPEB (\$960,472.00) and the ARC for pension benefits (\$185,433.00) (referred to as the "net OPEB obligation" and "net annual pension costs").⁴³⁰ As a result, the 2011 Audited Financial Statement's calculation of net assets did not include the AAL or UAAL (i.e., the long-term liability) attributable to the OPEB and pension obligations.⁴³¹ This is because the District does not set aside monies to pay these future liabilities and, instead, pays them yearly on a "pay-as-you-go" basis.⁴³²

218. The 2011 Audited Financial Statement also included figures for Severance Benefits Payable and Compensated Absences Payable.⁴³³ Severance Benefits Payable consist of early retirement incentive benefits payable to former employees.⁴³⁴ Severance benefit liabilities are paid from the General Fund.⁴³⁵ According to the 2011 Audited Financial Statement, "Annual payments to retire the severance benefit liabilities have not been determined and will depend on actual employee turnover."⁴³⁶ The parties do not dispute the District's liability for, or the amount of, the Severance Benefits Payable set forth in the 2011 Audited Financial Statement (\$4,731,848.00).⁴³⁷

219. Similarly, the parties do not dispute the amount stated for Compensated Absences Payable to employees. Compensated Absences Payable represent accrued vacation payable at year-end.⁴³⁸ Compensated absences are paid from the General Fund.⁴³⁹ According to the 2011 Audited Financial Statement, "Annual payments to retire

⁴²⁸ *Id.* at 40-41.

⁴²⁹ *Id.* at 16.

⁴³⁰ *Id.* at 40, 45-51.

⁴³¹ *Id.* at 16, 40.

⁴³² *Id.* at 44-48

⁴³³ *Id.* at 40-41.

⁴³⁴ *Id.* at 41.

⁴³⁵ *Id.*

⁴³⁶ *Id.*

⁴³⁷ *Id.* at 40.

⁴³⁸ *Id.* at 41.

⁴³⁹ *Id.*

compensated absences payable have not been determined and will depend on employee turnover and actual employee absences.”⁴⁴⁰ Nonetheless, the parties do not dispute the District’s liability for, or the amount of, Compensated Absences Payable set forth in the 2011 Audited Financial Statement (\$375,937.00).⁴⁴¹

220. Based upon the figures in the District’s 2011 Audited Financial Statement, Bloomington concluded that the District had assets exceeding liabilities in the amount of \$13,768,147.00.⁴⁴²

221. Bloomington then calculated the number of students that it had enrolled in the District in the 2010-2011 school year in relation to the total number of students enrolled in the District.⁴⁴³ Bloomington calculated that it had 6.52 percent of the students enrolled in the Intermediate District in 2010-2011.⁴⁴⁴ Using this percentage (6.52%), Bloomington opined that it was entitled to 6.52 percent of the net assets stated on the District’s 2011 Audited Financial Statement, plus a percentage of any monies received by the District arising out of a pending Minnesota Department of Education Special Education appeal.⁴⁴⁵

VALUATIONS OF THE REAL ESTATE INTERESTS

222. Unlike Bloomington, the Intermediate District did not rely on its 2011 Audited Financial Statement to determine Bloomington’s proportionate share of assets and liabilities under Minn. Stat. § 123A.24.

223. Instead, the Intermediate District hired a real estate appraiser to prepare appraisals of the real properties in which the District holds a legal interest, as well as an actuarial expert to determine the AAL and UAAL attributable to the OPEB and pension liabilities.⁴⁴⁶

224. The District initially advised its real estate appraisers that the intended use of the appraisals was for “internal planning” so as to obtain the most fair and “unbiased” valuation of the properties⁴⁴⁷ The District did not explain to the appraiser initially that the purpose of the appraisals was to determine Bloomington’s share of the District’s assets and liabilities as a result of Bloomington’s withdrawal.⁴⁴⁸ The District merely directed the appraiser to determine the market value of the properties in 2010 and 2011.⁴⁴⁹

⁴⁴⁰ *Id.*

⁴⁴¹ *Id.* at 40.

⁴⁴² *Id.* at 16.

⁴⁴³ *Id.* at 16-18.

⁴⁴⁴ *Id.*

⁴⁴⁵ *Id.*

⁴⁴⁶ Exs. 129, 134, 135.

⁴⁴⁷ Exs. 5, 6; Test. of M. Hawkins at T. 907.

⁴⁴⁸ Exs. 5, 6; see also Test. of Robert Strachota at T. 490, 494-96; Test. of S. Lewandowski at T. 479-84.

⁴⁴⁹ Exs. 5, 6; see also Test. of Robert Strachota at T. 490, 494-96; Test. of S. Lewandowski at T. 479-84.

225. It was not until 2012 that the District advised its real estate appraiser of the full intended use of the real estate appraisals.⁴⁵⁰ After that, the appraiser drastically reversed his initial valuation conclusions and reduced his valuation conclusions for the EEC, WEC, and SEC Properties **by over \$26 million dollars.**⁴⁵¹ The progression of the changes to value made by the Intermediate District's appraiser is set forth below.

2010 Appraisals of SEC and WEC Properties

226. On or about August 12, 2010, the Intermediate District first retained Shenhon Company (Shenhon) to prepare appraisals on the DSC, SEC, and WEC Properties.⁴⁵² According to the retainer agreement, Shenhon agreed to prepare a "Restricted Use Appraisal Report" for each of the properties.⁴⁵³ The retainer agreement between the District and Shenhon states:

Shenhon Company will prepare the appraisals presented in a restricted use report format using the sales comparison and income approaches to value to estimate the market value of each subject property....The appraisal reports will comply with Uniform Standards of Professional Appraisal Practice (USPAP) guidelines.⁴⁵⁴

227. The retainer agreement further provides:

Shenhon Company will preserve the confidential nature of information received from the client, in accordance with established professional standards. The client agrees to preserve the confidential format and content of the appraisal report. The report and the appraiser's identity are not to be used in whole or in part, outside the client's organization, without prior written approval, except for review by auditors and legal counsel, and by the representatives of taxing authorities.⁴⁵⁵

228. A "Restricted Use Appraisal Report" is a written appraisal report prepared under the Uniform Standards of Professional Appraisal Practice Rules 2-2(c), 8-2(c), or 10-2(b).⁴⁵⁶ A Restricted Use Appraisal Report is permitted to contain the minimal detail required under the USPAP and is intended to be relied upon only by the client, not any

⁴⁵⁰ Ex. 118.

⁴⁵¹ Compare Exs. 7-10 and Exs. 104-07.

⁴⁵² Ex. 135.

⁴⁵³ *Id.*

⁴⁵⁴ *Id.*

⁴⁵⁵ *Id.*

⁴⁵⁶ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 170 (5th ed. 2010).

other party.⁴⁵⁷ The 2014-2015 edition of the USPAP changed the name of this type of report to a “Restricted Appraisal Report.”⁴⁵⁸

229. According to the Appraisal Standards Board of the Appraisal Foundation, which develops, interprets, and amends the USPAP, the scope of work required to prepare a value conclusion articulated in a Restrict Appraisal Report and full Appraisal Report remains the same:

The scope of work required to develop credible assignment results is independent of the report format. The research and analysis required for credible results in an assignment would be the same whether the appraiser prepared an Appraisal Report or a Restricted Appraisal Report to communicate the results. Similarly, the scope of work is unaffected if the assignment results are presented in an oral appraisal report.⁴⁵⁹

230. Therefore, while a Restricted Use Appraisal Report is not prepared for anyone other than the intended user (i.e., the client hiring the appraisal), the reliability and methods used to arrive at a value conclusion should be no different whether that conclusion is articulated in a Restricted User Appraisal Report or a full Appraisal Report.⁴⁶⁰ The only difference between the two types of reports is the intended user and the amount of supporting detail contained in the report.⁴⁶¹

231. On August 13, 2010, Shenehon prepared Restricted Use Appraisal Reports on the SEC and WEC Properties.⁴⁶² Christopher Stockness and John Flaherty, licensed real estate appraisers, prepared the appraisal reports on behalf of Shenehon.⁴⁶³

⁴⁵⁷ See Uniform Standards of Professional Appraisal Practice 2012-2013 Edition. The Administrative Law Judge takes judicial notice of the USPAP pursuant to Minn. Stat. § 14.60, subd. 4 and Minn. R. 1400.8100, subp. 2.

⁴⁵⁸ See Uniform Standards of Professional Appraisal Practice 2014-2015 modifications; see also <http://www.appraisers.org/Disciplines/Appraisal-Review-Management/arm-news-and-events/2014/01/07/2014-15-uspap-modifications-released>, explaining the changes.

⁴⁵⁹ See The Appraisal Foundation Appraisal Standards Board 2014-2015 USPA Q&A issued October 9, 2013 (reprinted in http://www.ok.gov/oid/documents/123113_USPAP%20Doc.pdf). The Administrative Law Judge takes judicial notice of the Appraisal Standards Board’s interpretations of USPAP, pursuant to Minn. Stat. § 14.60, subd. 4 and Minn. R. 1400.8100, subp. 2.

⁴⁶⁰ *Id.*

⁴⁶¹ *Id.* (“The use of an Appraisal Report is appropriate for any appraisal assignment in which the client may need to understand the appraiser’s rationale, or for an assignment in which the client may not have specialized knowledge about the subject property. When there are any intended users other than the client, an Appraisal Report is the only written option that is allowed under USPAP. [π] The Standard Rules for an Appraisal Report establish the minimum level of information that must be included in the report. The appraiser must decide if additional detail or explanation is required, given the intended use and intended users of the report.”).

⁴⁶² Exs. 5, 6. Bloomington did not offer into the hearing record copies of the Restricted Use Appraisal Reports for the DSC Property, although the retainer agreement between the District and Shenehon states that Shenehon would prepare appraisal reports for that property as well. See Ex. 135.

⁴⁶³ Exs. 5, 6.

232. In its 2010 appraisals for the WEC and SEC Properties, Shenehon determined the “estimated market value” of each property. “Market value” is defined as:

The most probable price that the specified property interest should sell for in a competitive market after a reasonable exposure time, as of a specified date, in cash, or in terms equivalent to cash, under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably, for self-interest, and assuming that neither is under duress.⁴⁶⁴

233. In both of its 2010 appraisal reports, Shenehon appraised the market value of the leased fee interest and the fee simple interest of the WEC and SEC Properties.⁴⁶⁵

234. A “leased fee interest” is defined as “[a] freehold (ownership interest) where the possessory interest has been granted to another party by creation of a contractual landlord-tenant relationship (i.e., a lease).”⁴⁶⁶ A leased fee interest is held by the lessor, generally the owner of the property.

235. A “fee simple interest” is defined as “[a]bsolute ownership [of a property] unencumbered by any other interest or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat.”⁴⁶⁷ A fee simple estate “is one in which the owner is entitled to the entire property, *with unconditional power of disposition*....”⁴⁶⁸

236. In both of its 2010 appraisal reports, Shenehon concluded that the highest and best use for the WEC and SEC Properties, as improved, is for the continued use of the properties as school buildings.⁴⁶⁹

237. Shenehon evaluated three approaches to determine market value: the cost approach; sales comparison approach; and the income capitalization approach.⁴⁷⁰ The three valuation approaches are described by Shenehon as follows:

Cost Approach

The cost approach is based upon the principle that a prudent buyer will not pay more for a property than the cost to develop a new or substitute property with the same utility. This approach is useful in valuing new or proposed construction, special-purpose properties, and properties that are not frequently exchanged in the market.

⁴⁶⁴ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 122-23 (5th ed. 2010); *see also* Ex. 5 at 5; Ex. 6 at 5; Ex. 7 at 5; Ex. 8 at 5; Ex. 9 at 5; and Ex. 10 at 4.

⁴⁶⁵ Exs. 5, 6.

⁴⁶⁶ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 111 (5th ed. 2010).

⁴⁶⁷ *Id.* at 78.

⁴⁶⁸ BLACK’S LAW DICTIONARY 427 (Abridged 6th ed. 1991) (emphasis added).

⁴⁶⁹ Ex. 5 at 13; Ex. 6 at 14.

⁴⁷⁰ Exs. 5, 6.

In the cost approach, the value of the property is derived by adding the estimated land value to the cost of constructing a reproduction or replacement improvement and then subtracting the amount of depreciation from all causes (that is, wear and tear on the property, design and plan deficiencies, or neighborhood and market influences). This technique can also be employed to derive information needed in the sale comparison and income capitalization approaches to value.

Sales Comparison Approach

The sales comparison approach is based upon the principle of substitution. In other words, a buyer will not pay more to acquire a substitute property of similar utility and desirability within a reasonable timeframe. The sales comparison approach is useful when a number of similar properties have recently sold or are currently for sale in the subject's market. This method is often used for properties that are not usually purchased for their income-producing capability such as owner-occupied properties.

In the sales comparison approach, similar properties are compared to the subject property. Adjustments are made to the known sale price for the various differences between the comparable property and the subject property, and the adjusted prices are used to estimate the probable price at which the subject property would sell if offered on the open market.

Income Capitalization Approach

The income capitalization approach is based upon the principle of anticipation. Any property that generates income can be valued using the income capitalization approach. When more than one approach to value is used to develop an opinion of value for an income-producing property, the value indication produced by the income capitalization approach might be given greater weight than that of the other approaches in the final reconciliation of value indications.

In the income capitalization approach, rental income of the property is calculated and deductions are made for vacancy and collection loss, and expenses. The prospective net operating income of the property is then estimated. To support this estimate, historical operating statements for the subject property and comparable properties are reviewed. An applicable capitalization method and appropriate capitalization rate are developed and used in computations that result in an indication of value.⁴⁷¹

238. Shenehon used only the sales comparison and income capitalization approaches to estimate the value of the WEC Property.⁴⁷² Under the sales comparison

⁴⁷¹ Ex. 6 at 15; see also Ex. 5 at 14; Ex. 7 at 15; Ex. 8 at 15; Ex. 9 at 15; Ex. 10 at 14; Ex. 104 at 31; Ex. 105 at 30; Ex. 106 at 30; Ex. 107 at 39.

⁴⁷² Ex. 6.

approach, Shenehon determined that the market value for a fee simple interest in the property was \$6,875,000.00.⁴⁷³ Using the income capitalization approach, Shenehon estimated that the market value for a fee simple interest in the property was \$4,100,000.00, and the market value for a leased fee interest in the property was \$7,750,000.00.⁴⁷⁴ Reconciling these figures, Shenehon concluded that the overall estimated market value of the WEC Property as of August 13, 2010, was \$7,700,000.00.⁴⁷⁵

239. Shenehon conducted a similar analysis for the SEC Property.⁴⁷⁶ Again, Shenehon used only the sales comparison and income capitalization approaches to estimate the value of the property.⁴⁷⁷ Under the sales comparison approach, Shenehon determined that the market value of the fee simple interest in the SEC Property was \$32,700,000.00.⁴⁷⁸ Using the income capitalization approach, Shenehon estimated that the market value of the fee simple interest was \$8,000,000, and the market value for the leased fee interest was \$34,300,000.00.⁴⁷⁹ Reconciling these figures, Shenehon concluded that the overall estimated market value of the SEC Property as of August 13, 2010, was \$34,000,000.00.⁴⁸⁰

2011 Appraisals of WEC, SEC, DSC, and EEC Properties

240. In August 2011, after Bloomington had officially withdrawn from the District, the Intermediate District retained Shenehon to conduct new appraisals of the WEC, SEC, DSC, and EEC Properties, using a valuation date of June 30, 2011, the effective date of Bloomington's withdrawal.⁴⁸¹

241. Again in its retainer letter, Shenehon agreed to prepare Restricted Use Appraisal Reports for each of the properties.⁴⁸² The intended use of the appraisals was "to conclude a market value of the subject propert[ies] for [the District's] internal planning purposes."⁴⁸³

242. Restricted Use Appraisal Reports were prepared on the WEC, SEC, DSC, and EEC Properties by licensed real estate appraisers Christopher Stockness and Robert Strachota on behalf of Shenehon.⁴⁸⁴

⁴⁷³ *Id.* at 20.

⁴⁷⁴ *Id.* at 22-26.

⁴⁷⁵ *Id.* at cover letter, 26.

⁴⁷⁶ Ex. 5.

⁴⁷⁷ *Id.*

⁴⁷⁸ *Id.* at 21.

⁴⁷⁹ *Id.* at 23-28.

⁴⁸⁰ *Id.* at cover letter, 28.

⁴⁸¹ Ex. 134.

⁴⁸² *Id.*

⁴⁸³ Ex. 7 at 3; Ex. 3; Ex. 9 at 3; Ex. 10 at 3.

⁴⁸⁴ Exs. 7-10.

243. In each of the 2011 appraisals, Shenehon utilized only the sales comparison and income capitalization approaches to value.⁴⁸⁵ The cost approach was not used or considered.⁴⁸⁶

244. In its reports, Shenehon incorporated the newer definition of “market value,” set forth in the *Uniform Standards of Professional Appraisal Practice* (USPAP), 2010-2011 Edition, as:

The most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. Implicit in this definition are the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

1. Buyer and seller are typically motivated;
2. Both parties are well informed or well advised and acting in what they consider their own best interests;
3. A reasonable time is allowed for exposure in the open market;
4. Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and
5. The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.⁴⁸⁷

2011 Appraisal of DSC Property

245. Unlike the EEC, SEC, or WEC Properties, the Intermediate District owns the DSC Property in fee simple. Therefore, the only interest appraised by Shenehon was the fee simple interest in the property.⁴⁸⁸ Using the sales approach, Shenehon determined that the market value of the DSC Property was \$2,750,000.00.⁴⁸⁹ Using the income capitalization approach, Shenehon estimated that the market value of the property was \$2,675,000.00.⁴⁹⁰ Reconciling the two approaches to value, Shenehon concluded that the estimated market value of the DSC Property as of June 30, 2011, was \$2,700,000.00.⁴⁹¹

⁴⁸⁵ Exs. 7-10.

⁴⁸⁶ Exs. 7-10.

⁴⁸⁷ See Ex. 7 at 5; Ex. 8 at 5; Ex. 9 at 5; Ex. 10 at 4.

⁴⁸⁸ Ex. 7.

⁴⁸⁹ *Id.* at 19.

⁴⁹⁰ *Id.* at 23.

⁴⁹¹ *Id.* at cover letter, 24.

2011 Appraisal of EEC Property

246. Next, Shenehon appraised the EEC Property.⁴⁹² Because the EEC Property is subject to a lease agreement, Shenehon valued both the fee simple and leased fee interests.⁴⁹³ Shenehon did not value the District's leasehold interest⁴⁹⁴ in the property.⁴⁹⁵

247. Under the sales comparison approach, Shenehon determined that the market value for a fee simple interest in the EEC Property was \$4,050,000.00.⁴⁹⁶ Using the income capitalization approach, Shenehon estimated that the market value for a fee simple interest in the property was \$4,675,000.00, and the market value for a leased fee interest (i.e., lessor's interest) was \$4,575,000.00.⁴⁹⁷

248. Shenehon's appraisal report states, "The fee simple and leased fee values fall within a relatively tight range, *but we believe a buyer would focus on the lease fee value.*"⁴⁹⁸ Reconciling these approaches to value, Shenehon concluded that the estimated market value of the EEC Property as of June 30, 2011, was \$4,500,000.00.⁴⁹⁹

2011 Appraisal of WEC Property

249. Shenehon appraised the WEC Property in a similar fashion.⁵⁰⁰ Again, Shenehon valued both a fee simple interest and a leased fee interest in the property.⁵⁰¹ Shenehon did not appraise the District's leasehold interest in the property.⁵⁰²

250. Under the sales comparison approach, Shenehon determined that the market value for a fee simple interest in the WEC Property was \$6,550,000.00.⁵⁰³ Using the income capitalization approach, Shenehon estimated that the market value for a fee simple interest was \$4,050,000.00, and the market value for the leased fee interest was \$7,675,000.00.⁵⁰⁴ The report states:

It is our opinion that a potential buyer would purchase the subject [WEC Property] on its leased fee value. We conclude the value of the subject

⁴⁹² Ex. 9.

⁴⁹³ *Id.*

⁴⁹⁴ A "leasehold interest" is defined as "[t]he tenant's possessory interest created by a lease." APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 111 (5th ed. 2010).

⁴⁹⁵ Ex. 9.

⁴⁹⁶ *Id.* at 20.

⁴⁹⁷ *Id.* at 22-29.

⁴⁹⁸ *Id.* at 29 (emphasis added).

⁴⁹⁹ *Id.* at cover letter, 30.

⁵⁰⁰ Ex. 8.

⁵⁰¹ *Id.*

⁵⁰² *Id.*

⁵⁰³ *Id.* at 20.

⁵⁰⁴ *Id.* at 22-28.

property as indicated by the income capitalization approach is \$7,675,000.⁵⁰⁵

251. Reconciling the valuation approaches, Shenehon concluded that the estimated market value of the WEC Property as of June 30, 2011, was \$7,600,000.00.⁵⁰⁶

2011 Appraisal of SEC Property

252. In a similar fashion, Shenehon appraised the SEC Property.⁵⁰⁷ Although the District does not hold a leased fee or ownership interest in the SEC Property, Shenehon valued both a fee simple interest and a leased fee interest in the property.⁵⁰⁸ Shenehon did not value the District's leasehold interest in the property.⁵⁰⁹

253. In valuing the interests, Shenehon employed only the sale comparison and income capitalization approaches to valuation.⁵¹⁰ Shenehon did not use the cost approach even though the SEC Property had recently been constructed in 2008.⁵¹¹ This was true despite the fact that Shenehon describes the cost approach as, "useful in valuing new or proposed construction, special-purposes properties, and properties that are not frequently exchanged in the open market."⁵¹²

254. Using the sales comparison approach, Shenehon determined that the market value of the SEC Property was \$34,835,000.00: \$535,000.00 for excess land and \$34,300,000.00 for the remaining land and school facility.⁵¹³

255. Using the income capitalization approach, Shenehon estimated the value of both a fee simple and leased fee interest.⁵¹⁴ Shenehon estimated that the market value for the fee simple interest under the income capitalization approach was \$7,625,000.00; whereas, the market value for the leased fee interest was \$31,250,000.00.⁵¹⁵ Although the valuations for the fee simple and leased fee interests were wildly divergent, Shenehon concluded that the value of the leased fee interest was the most accurate for purposes of determining the property's value on the open market.⁵¹⁶ Shenehon's report states:

It is our opinion that a potential buyer of the subject [SEC Property] would purchase the subject [property] based on its leased fee value. We conclude

⁵⁰⁵ *Id.* at 28 (emphasis added).

⁵⁰⁶ *Id.* at cover letter, 30.

⁵⁰⁷ Ex. 7.

⁵⁰⁸ *Id.*

⁵⁰⁹ *Id.*

⁵¹⁰ *Id.*

⁵¹¹ *Id.*

⁵¹² *Id.* at 15.

⁵¹³ *Id.* at 23.

⁵¹⁴ *Id.* at 24-33.

⁵¹⁵ *Id.*

⁵¹⁶ *Id.* at 33.

the value of the subject property as indicated by the income capitalization approach is \$31,250,000.⁵¹⁷

256. Shenehon's report continues, "Since [sic] the real estate under appraisal is income[-]producing property, the leased fee income capitalization approach is given primary consideration in concluding the final value conclusion."⁵¹⁸

257. Reconciling the valuation approaches, Shenehon concluded that the estimated market value of the SEC Property as of June 30, 2011, was \$31,300,000.00.⁵¹⁹

Intermediate District Changes its Opinions as to the Properties' Values

258. In 2012, Bloomington and the Intermediate District engaged in extensive settlement discussions, including a mediation session and facilitated discussions with the Commissioner.⁵²⁰ During the negotiations, the Intermediate District voluntarily disclosed to the Commissioner and Bloomington the 2010 and 2011 restrict appraisal reports prepared by Shenehon.⁵²¹

259. After negotiations with Bloomington broke down, the District, its legal counsel, and its financial experts, met with the real estate appraisers from Shenehon who had prepared the 2010 and 2011 appraisals of the DSC, EEC, WEC, and SEC.⁵²²

260. On October 2, 2012, the District met with Robert Strachota (Strachota), the President of Shenehon Company and one of the signatories of the 2011 appraisals.⁵²³ Shenehon is a licensed real estate appraiser, a Member of the Appraisal Institute (MAI), a Master Certified Business Appraiser (MCBA), a Counselor of Real Estate (CRE), and a Fellow of the Institute of Business Appraisers.⁵²⁴

261. During the October 2, 2012 meeting, the District advised Strachota of the exact reason that the District had requested the appraisals to be conducted in 2010 and 2011: that is, to determine Bloomington's share of the assets and liabilities associated with the various properties.⁵²⁵

262. The next day, October 3, 2012, Strachota wrote a letter to Sara Ruff, legal counsel for the Intermediate District.⁵²⁶ In his letter, Strachota reversed his professional

⁵¹⁷ *Id.* (emphasis added).

⁵¹⁸ *Id.* at 34.

⁵¹⁹ *Id.* at cover letter, 34.

⁵²⁰ Exs. 111-13, 119-22; see *also* Notice and Order for Prehearing Conference and Hearing at 2.

⁵²¹ Ex. 117 at 6.

⁵²² Test. of M. Hawkins at T. 904-07.

⁵²³ *Id.*

⁵²⁴ Ex. 104 at D-1; Ex. 105 at D-1; Ex. 106 at D-1; Ex. 107 at E-1.

⁵²⁵ Ex. 104 at D-1; Ex. 105 at D-1; Ex. 106 at D-1; Ex. 107 at E-1; Test. of R. Strachota at T. 498-99; 584-85.

⁵²⁶ Ex. 118.

opinions articulated in the appraisals he prepared for the EEC, SEC, and WEC Properties in 2010 and 2011.⁵²⁷

263. Rather than using the valuation of the leased fee interest, Strachota asserted that the values of the fee simple interests are the more accurate estimate of the properties' fair market values.⁵²⁸ To justify his abrupt reversal, Strachota asserted, for the first time, that the lease agreements encumbering the EEC, WEC, and SEC Properties are actually "mortgage obligations" for the District, and that when such "mortgages" are paid off, the properties will be conveyed to the District for one dollar.⁵²⁹

264. As a result, Strachota made an about-face and concluded that the fee simple interest is the legal interest that should be valued for purposes of allocating the District's assets and liabilities because that is the legal interest that the District holds in the properties.⁵³⁰ Strachota's analysis, however, ignores the fact that the District did not, in fact, have an alienable fee simple interest in the EEC, WEC, or SEC Properties as of June 30, 2011.

2014 Appraisals of the DSC, EEC, WEC, and SEC Properties

265. In preparation for the hearing in this matter, the Intermediate District retained Shenehon to prepare all new appraisals for the DSC, EEC, WEC, and SEC Properties.⁵³¹ Strachota prepared each of these new appraisals.⁵³² Strachota's 2014 appraisals erroneously assume that the Intermediate District held an existing and fully alienable fee simple interest in all of the properties as of June 30, 2011.⁵³³

2014 Appraisal of DSC Property

266. On or about March 5, 2014, Strachota prepared a new appraisal for the DSC Property.⁵³⁴ Because the Intermediate District owns the DSC Property in fee simple, Strachota only valued the District's fee simple interest in the property.⁵³⁵

267. Strachota appraised the DSC Property using both the cost approach and income capitalization approach to value.⁵³⁶ Using the cost approach, Strachota opined that the value of the property was \$3,000,000.00.⁵³⁷ Using the income capitalization

⁵²⁷ *Id.*

⁵²⁸ *Id.*

⁵²⁹ *Id.*; Test. of R. Strachota at T. 498-501.

⁵³⁰ E, 118; Test. of R. Strachota at T. 498-501

⁵³¹ Exs. 104-07.

⁵³² Exs. 104-07.

⁵³³ Exs. 104-07.

⁵³⁴ Ex. 104.

⁵³⁵ *Id.*

⁵³⁶ *Id.*

⁵³⁷ *Id.* at 46.

approach, Strachota opined that the value of the property was \$2,900,000.00.⁵³⁸ Reconciling these two approaches, Strachota concluded that the market value of the DSC Property as of June 30, 2011, was \$3,000,000.⁵³⁹ This amount was \$300,000.00 higher than Strachota's 2011 appraisal of the same property.⁵⁴⁰

2014 Appraisal of EEC Property

268. On or about March 5, 2014, Strachota prepared a new appraisal for the EEC Property.⁵⁴¹ In his appraisal, Strachota erroneously states that the "Intermediate District 287 purchased the property on January 7, 2010."⁵⁴² In reality, as of June 30, 2011, the District had not exercised its option to purchase the property under the EEC Lease Agreement and held only a leasehold interest in the EEC Property.⁵⁴³ Wells Fargo Bank was the only party holding title to, and having a fee simple interest in, the property.⁵⁴⁴

269. In support of his erroneous assumption, Strachota asserts that the EEC Lease Purchase Agreement and related COPs are the functional equivalent to a sale and mortgage transaction, and that the District's interest in the EEC Property is that of a fee simple owner, not a lessee.⁵⁴⁵ Strachota erroneously states:

The current payments made by the Intermediate District 287 to Wells Fargo Bank represent the repayment of a mortgage. They do not represent market rent negotiated between two arm's-length parties. It is our opinion that there is no leased fee interest for a lease payment that is a function of a mortgage note.⁵⁴⁶

270. As a result, Strachota abandoned his previous opinion that a reasonable buyer in the open market would purchase the EEC Property based upon the value of a leased fee interest.⁵⁴⁷ Instead, Strachota appraised only a fee simple interest in the EEC Property.⁵⁴⁸

⁵³⁸ *Id.*

⁵³⁹ *Id.*

⁵⁴⁰ *Id.*; see also Ex. 7 at 24.

⁵⁴¹ Ex. 105.

⁵⁴² *Id.* at 4.

⁵⁴³ See Exs. A, B.

⁵⁴⁴ See Exs. A, B.

⁵⁴⁵ Ex. 105 at cover letter, 3-4. Notably, Strachota was presented as an expert in real estate appraisal, not as a legal expert. There is no evidence that Strachota — or any of the other real estate appraisers presented by the parties in the hearing — have any legal training or expertise to make a determination as to the legal interest that the Intermediate District has in the EEC, DSC, SEC, WEC, and NEC Properties. The District's legal interests in the real properties are determined by the legal and title documents contained in Exhibits A through Z and AA. It does not appear in the record that any of the real estate appraiser witnesses had ever reviewed all of the documents contained in Exhibits A through Z and AA.

⁵⁴⁶ Ex. 105 at cover letter.

⁵⁴⁷ See Ex. 9 at 29-30.

⁵⁴⁸ Ex. 105

271. Strachota's 2014 appraisal of the EEC Property adopts the definition of "fee simple estate" contained in the Appraisal Institute's DICTIONARY OF REAL ESTATE APPRAISAL, as:

Absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the government powers of taxation, eminent domain, police power, and escheat.⁵⁴⁹

272. As of June 30, 2011, however, the Intermediate District did not have a fee simple estate in the EEC Property.⁵⁵⁰ The District's interest in the EEC Property was that of a lessee (i.e., a leasehold interest) with an unexercised option to purchase the property in the future.⁵⁵¹

273. Nonetheless, Strachota concluded that the value of a fee simple interest in the EEC Property as of June 30, 2011, was \$4,000,000.00.⁵⁵² Strachota's 2014 appraisal of the EEC Property was \$500,000.00 less than his 2011 appraisal of the same property.⁵⁵³ In his 2011 appraisal, Strachota opined that the estimated market value of the EEC Property as of June 30, 2011, was \$4,500,000.00.⁵⁵⁴

2014 Appraisal of WEC Property

274. On or about March 5, 2014, Strachota prepared a third appraisal of the WEC Property.⁵⁵⁵ Unlike Shenehon's previous two appraisals of the WEC Property conducted in 2010 and 2011, Strachota concluded this time that there was no "leased fee interest" in the property to be valued, and that the WEC Lease Agreement and related COP financing resulted in the District having the functional equivalent to a fee simple interest in the property.⁵⁵⁶

275. As a result, Strachota abandoned his previous opinion that a reasonable buyer in the open market would purchase the WEC Property based upon the value of a leased fee interest.⁵⁵⁷

276. However, the Intermediate District did not have an alienable ownership interest in the WEC Property as of June 30, 2011.⁵⁵⁸ Instead, the District's interest in the WEC Property was fully encumbered by the WEC Ground Lease and WEC Trust

⁵⁴⁹ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 78 (5th ed. 2010).

⁵⁵⁰ See Exs. A, B.

⁵⁵¹ Exs. A, B.

⁵⁵² Ex. 105 at 43.

⁵⁵³ Ex. 9 at 30.

⁵⁵⁴ *Id.*

⁵⁵⁵ Ex. 106.

⁵⁵⁶ *Id.* at cover letter, 3-4.

⁵⁵⁷ See Ex. 8 at 28.

⁵⁵⁸ See Exs. F, G, H.

Agreement, under which the District conveyed its interests in the property to Wells Fargo Bank to hold in trust, subject to the terms of the WEC Refunding Lease Agreement.⁵⁵⁹ Under the WEC Refunding Lease Agreement, Wells Fargo Bank is leasing the WEC Property back to the District.⁵⁶⁰ In addition, the WEC Refunding Lease Agreement specifically provides that the District shall “not mortgage, sell, assign, transfer, or convey” the WEC Property “or any portion thereof” during the term of the agreement.⁵⁶¹ Thus, the District’s true interest in the WEC Property as of June 30, 2011, was merely possessory.⁵⁶² The District did not hold a fee simple interest in the Property.

277. Without addressing the complexities of the District’s interest in the WEC Property, Strachota concluded that the value of a fee simple interest in the WEC Property as of June 30, 2011, was \$3,650,000.00.⁵⁶³ Strachota’s 2014 appraisal of the WEC Property was \$3,950,000.00 less than his 2011 appraisal of the same property and \$4,050,000.00 less than his 2010 appraisal of the same property.⁵⁶⁴ In his 2011 appraisal, Strachota opined that the estimated market value of the WEC Property as of June 30, 2011, was \$7,600,000.00.⁵⁶⁵ In his 2010 appraisal, Strachota’s company opined that the estimated market value of the WEC Property as of August 13, 2010, was \$7,700,000.00.⁵⁶⁶

2014 Appraisal of SEC Property

278. On or about March 5, 2014, Strachota prepared a third appraisal for the SEC Property.⁵⁶⁷ Unlike Shenehon’s previous two appraisals of the SEC Property conducted in 2010 and 2011, Strachota concluded this time that there was no leased fee interest in the property to be valued, and that the SEC Refunding Lease Agreement and related COP financing resulted in the District having the functional equivalent to a fee simple interest in the property.⁵⁶⁸ As a result, Strachota abandoned his previous opinion that a reasonable buyer in the open market would purchase the SEC Property based upon the value of a leased fee interest.⁵⁶⁹

279. Contrary to Strachota’s erroneous assertions regarding the District’s ownership interest in the property, as of June 30, 2011, the Intermediate District did not have a fee simple interest in the SEC Property.⁵⁷⁰ The District’s only legal interest in the

⁵⁵⁹ Exs. F, G, H.

⁵⁶⁰ Ex. F.

⁵⁶¹ *Id.* at 23.

⁵⁶² Exs. F, G, H.

⁵⁶³ Ex. 106 at 43.

⁵⁶⁴ *Id.*; see also Ex. 8 at 29; Ex. 6 at 26.

⁵⁶⁵ Ex. 8 at 29.

⁵⁶⁶ Ex. 6 at 26.

⁵⁶⁷ Ex. 107.

⁵⁶⁸ *Id.* at cover letter, 3; see also Exs. 5, 7.

⁵⁶⁹ Ex. 107 at cover letter, 3; see also Exs. 5, 7.

⁵⁷⁰ See Exs. I, O, Y.

SEC Property was that of a lessee (i.e., a leasehold interest) with an unexercised option to purchase the property in the future.⁵⁷¹

280. Nonetheless, Strachota concluded that the value of a fee simple interest in the SEC Property as of June 30, 2011, was \$9,000,000.00.⁵⁷² Strachota's 2014 appraisal of the SEC Property was \$22,300,000.00 less than his 2011 appraisal of the same property, and \$25,000,000.00 less than his 2010 appraisal of the same property.⁵⁷³ In his 2011 appraisal, Strachota opined that the estimated market value of the SEC Property as of June 30, 2011, was \$31,300,000.00.⁵⁷⁴ In its 2010 appraisal, Strachota's company opined that the estimated market value of the SEC Property as of August 13, 2010 was \$34,000,000.00.⁵⁷⁵

Bloomington's Expert Real Estate Appraisals and Reviews

281. To counter Strachota's appraisals of the DSC, EEC, WEC, and SEC Properties, Bloomington hired its own expert real estate appraiser, Robert Lunz (Lunz) of Nicollet Partners, Inc., to conduct an evaluation of the properties⁵⁷⁶ Lunz is a licensed real estate appraiser and broker, a Member of the Appraisal Institute (MAI), and a Counselor of Real Estate (CRE).⁵⁷⁷

282. Lunz conducted his own appraisals of the DSC and EEC Properties, but conducted only "appraisal reviews" of Shenehon's 2011 appraisals of the WEC and SEC Properties to reach his valuation conclusions.⁵⁷⁸

Lunz's Appraisal of the DSC Property

283. On or about February 28, 2014, Lunz completed a full, "retroactive" appraisal on the DSC Property.⁵⁷⁹ Because the District holds legal title to the DSC Property and owns the property in fee simple, Lunz appraised only the fee simple interest in the property as of June 30, 2011.⁵⁸⁰

284. Like Shenehon, Lunz determined that the highest and best use of the DSC Property, as improved, is the continued use as a general office building.⁵⁸¹ Lunz used

⁵⁷¹ Exs. I, O, Y.

⁵⁷² Ex. 107.

⁵⁷³ Ex. 7 at 34; Ex. 5 at 28.

⁵⁷⁴ Ex. 7 at 34.

⁵⁷⁵ Ex. 5 at 28.

⁵⁷⁶ Exs. 1-4.

⁵⁷⁷ Exs. 1-4.

⁵⁷⁸ Exs. 1-4.

⁵⁷⁹ Ex. 4.

⁵⁸⁰ *Id.* at 20.

⁵⁸¹ *Id.* at 88.

both a sales comparison approach, as well as an income (direct capitalization) approach to value.⁵⁸² Lunz did not apply a cost approach to value, due to the property's age.⁵⁸³

285. Under the sales comparison approach, Lunz opined that the market value of the property as of June 30, 2011, was \$4,100,000.00.⁵⁸⁴ Using the income approach, Lunz estimated that the market value of the property as of June 30, 2011, was \$3,630,000.00.⁵⁸⁵ Overall, Lunz determined that “the most probable buyer” of the DSC Property would be “an owner-user who would rely heavily” on the sale comparison approach to value.⁵⁸⁶ Reconciling the figures from the two valuation approaches, Lunz concluded that the “retrospective market value” of the DSC Property as of June 30, 2011, was \$4,000,000.00.⁵⁸⁷

Lunz Appraisal of the EEC Property

286. On or about February 28, 2014, Lunz conducted a full, “retroactive” appraisal of the EEC Property as of June 30, 2011.⁵⁸⁸

287. Like Shenehon, Lunz determined that the highest and best use of the EEC Property, as improved, is the continued use as a school or other type of public service or educational facility.⁵⁸⁹

288. Based upon the highest and best use of the property as improved, Lunz set out to determine market value based upon comparable sales and income-producing opportunities involving school properties in the area.⁵⁹⁰ Lunz was not provided with a copy of the EEC Lease or other financing documents related to the property. Therefore, Lunz could not evaluate any existing leased fee or leasehold interest in the property.⁵⁹¹

289. Nor could Lunz identify enough comparable school leases in the area to make an accurate value opinion using the income approach to value.⁵⁹² Because of the lack of sufficient rental data to develop an income approach to value, Lunz concluded that “the most probable buyer” of the EEC Property would be “an owner-user who would rely heavily” on comparable school sales in the area.⁵⁹³

⁵⁸² *Id.* at 89.

⁵⁸³ *Id.*

⁵⁸⁴ *Id.* at 90-102.

⁵⁸⁵ Ex. 4 at amended appraisal.

⁵⁸⁶ *Id.*

⁵⁸⁷ *Id.*

⁵⁸⁸ Ex. 3.

⁵⁸⁹ *Id.* at 73.

⁵⁹⁰ Test. of R. Lunz at T. 217-28.

⁵⁹¹ *Id.* at T. 218-19.

⁵⁹² *Id.*

⁵⁹³ Ex. 3 at 84.

290. Using six comparable sales of school properties in the Twin Cities metropolitan area occurring between February 2009 and August 2012, Lunz concluded that the “retrospective market value” of a fee simple interest in the EEC Property as of June 30, 2011, was \$4,010,000.00.⁵⁹⁴ Lunz’s value opinion was based solely on the sales comparison approach to value and the six sales analyzed in his report.⁵⁹⁵

Lunz’s Appraisal Review of Shenehon’s 2011 Restricted Use Appraisal of the SEC Property

291. With respect to the SEC Property, Lunz conducted only an appraisal review of the 2011 Restricted Use Appraisal Report prepared by Shenehon of the SEC Property (Exhibit 7).⁵⁹⁶ An appraisal review is “[t]he act or process of developing and communicating an opinion about the quality of another appraiser’s work that was performed as part of an appraisal, appraisal review, or appraisal consulting assignment.”⁵⁹⁷ An appraisal review is not an independent appraisal.⁵⁹⁸

292. Overall, Lunz concurred with the final market value reached by Strachota in Shenehon’s 2011 appraisal of the SEC Property.⁵⁹⁹

293. Unlike Strachota, Lunz acknowledged that the Intermediate District does not have a fee simple or leased fee interest in the SEC Property.⁶⁰⁰ Nonetheless, Lunz concluded that, for purposes of estimating the market value of the property in this matter, the leased fee interest is the most accurate indication of value because it best represents the “value-in-use” of the property, as well as what a potential buyer would pay for the specialized property in the marketplace.⁶⁰¹

294. “Value-in-use” is defined as “[t]he value of a property assuming a specific use, which may or may not be the property’s highest and best use on the effective date of the appraisal.”⁶⁰² “Value-in-use may or may not be equal to the market value but is different conceptually.”⁶⁰³

295. According to Lunz, because both he and Strachota find that the highest and best use of the property, as improved, is for continued use as a school building, an

⁵⁹⁴ *Id.* at 75-84.

⁵⁹⁵ Ex. 3.

⁵⁹⁶ Ex. 1.

⁵⁹⁷ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 11 (5th ed. 2010); see also Uniform Standards of Professional Appraisal Practices (USPAP) 2010-2011 Edition.

⁵⁹⁸ *Cf.* APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 11 (5th ed. 2010).

⁵⁹⁹ Ex. 1

⁶⁰⁰ *Id.* Notably, Lunz was presented as a real estate appraisal expert, not a legal expert. In addition, the record does not support a finding that Lunz reviewed Exhibits A through Z and AA prior to providing his valuation opinion.

⁶⁰¹ Ex. 1.

⁶⁰² APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 206 (5th ed. 2010).

⁶⁰³ *Id.*

appraisal of the property for the District must consider the value of the property in relation to its current use — as a school property under lease by the District.⁶⁰⁴

296. Lunz explained that the value of the leased fee interest is the most accurate reflection of the true market value because it captures the property's value as it is currently being used — as a school building leased by a highly credit-worthy governmental entity under a long-term, income-producing lease.⁶⁰⁵ According to Lunz, Strachota's valuation of a fee simple interest ignores the existing lease arrangement and does not capture the value-in-use of the property.⁶⁰⁶

297. Lunz explained that any valuation of the SEC Property must necessarily include an evaluation of the SEC lease agreements, which establish an agreed-upon rent amount and income-producing stream. This amount can then be used in the income approach to determine the fee simple value of the property.

298. According to Lunz, Strachota's value opinion of the fee simple interest completely ignores the value of the existing lease agreements. However, Lunz explains, Strachota ultimately captures that lease income value in his value opinion of the leased fee interest. Accordingly, Lunz ultimately agreed with Strachota's final valuation.

299. Thus, while the District does not actually hold the leased fee interest, Lunz concurred with Strachota's original opinion that the leased fee value is the most accurate reflection of the market value of the SEC Property to the District, as well as to a probable buyer.⁶⁰⁷ According to Lunz, this leased fee value is really the market value of the property itself.

300. While Lunz and Strachota go about valuing the property in different ways, they ultimately agree that the final market value is best represented by what Strachota refers to as the value of the leased fee interest.

301. Lunz asserted that Strachota was correct in his 2011 appraisal of the SEC Property, in which Strachota opined that a potential buyer would purchase the SEC Property based upon its leased fee value.⁶⁰⁸ Ultimately, Lunz concurred with Strachota's methods of valuing the leased fee interest in the property, and agreed with Strachota's reconciled market value of \$31,300,000.00.⁶⁰⁹

302. Lunz maintained, however, that Strachota's final valuation inadvertently failed to include the value of the excess parcel of land, which Strachota valued at \$535,000.00.⁶¹⁰ Accordingly, Lunz concluded that the estimated market value of the SEC

⁶⁰⁴ Ex. 1.

⁶⁰⁵ *Id.*

⁶⁰⁶ *Id.*

⁶⁰⁷ *Id.*

⁶⁰⁸ *Id.*

⁶⁰⁹ *Id.*

⁶¹⁰ *Id.*

Property as of June 30, 2011, based upon Strachota's valuation approach and reconciliation, was actually \$31,835,000.00, not \$31,300,000.00.⁶¹¹

Lunz's Appraisal Review of Shenehon's 2011 Restricted Use Appraisal of the WEC Property

303. In a similar fashion, Lunz conducted an appraisal review of the 2011 Restricted Use Appraisal Report prepared by Shenehon of the WEC Property (Exhibit 8).⁶¹² Overall, Lunz concurred with the final market value reached by Strachota in his 2011 appraisal of the WEC Property (\$7,600,000.00).⁶¹³

304. Lunz concluded that, although the District does not have a leased fee interest in the WEC Property, the leased fee interest is the correct interest to be valued when determining the District's real estate assets.⁶¹⁴ This is because the leased fee interest best represents the property's value-in-use for the District.⁶¹⁵ According to Lunz, when valuing a specialized property like a school building for the user of the property, the value-in-use must be considered and given substantial weight.⁶¹⁶

305. Lunz asserted that the value of the leased fee interest is the most accurate reflection of the value-in-use to the District, as well as the overall market value, because it captures the WEC Property's value as it is currently being used as a school building.⁶¹⁷ Lunz, therefore, agreed with Strachota's conclusion in the 2011 Shenehon appraisal, in which Strachota opined that a potential buyer would purchase the WEC Property based upon its leased fee value.⁶¹⁸

306. In addition, Lunz concurred with Strachota's valuation approaches and methods of valuing the leased fee interest in the property.⁶¹⁹ As a result, Lunz accepted Strachota's reconciled market value of \$7,600,000.00 for the WEC Property.⁶²⁰ According to Lunz, Strachota's market valuation of the property at \$7,600,000.00 is an accurate reflection of what the property is actually worth to both to the Intermediate District in a value-in-use basis, as well as to a potential buyer on a market value basis.⁶²¹

Summary of Competing Real Estate Appraisals

⁶¹¹ *Id.*

⁶¹² Ex. 2.

⁶¹³ *Id.*

⁶¹⁴ *Id.*

⁶¹⁵ *Id.*

⁶¹⁶ *Id.*

⁶¹⁷ *Id.*

⁶¹⁸ *Id.*

⁶¹⁹ *Id.*

⁶²⁰ *Id.*

⁶²¹ *Id.*

307. A summary of the various valuation conclusions reached by the parties' respective appraisers is set forth below:⁶²²

Property	Shenehon 2010 Appraisal	Shenehon 2011 Appraisal	Shenehon 2014 Appraisal	Lutz Appraisal/Review
SEC Property	\$34,000,000.00	\$31,300,000.00	\$9,000,000.00	\$31,835,000.00
WEC Property	\$7,700,000.00	\$7,600,000.00	\$3,650,000.00	\$7,600,000.00
EEC Property	N/A	\$4,500,000.00	\$4,000,000.00	\$4,010,000.00
DSC Property	N/A	\$2,700,000.00	\$3,000,000.00	\$4,500,000.00

BLOOMINGTON'S ENROLLMENT IN THE DISTRICT FROM 2000-2011

308. The parties generally agree that Bloomington is only entitled to receive its fair and proportionate share of the District's assets, and that Bloomington remains liable for its fair and proportionate share of the District's liabilities. The parties, however, disagree as to how Bloomington's proportionate share should be calculated.

309. Based upon the value opinions made in the 2014 Shenehon Appraisals, and the inclusion of Van Iwaarden's estimate of the District's unfunded actuarial accrued liability for OPEB and pension benefits, the Intermediate District calculates that as of June 30, 2011, the District's liabilities exceeded its assets in the amount of \$28,928,690.00.⁶²³ As a result, the District asserts that Bloomington owes the District payment for its proportionate share of the District's net liabilities.

310. In contrast, Bloomington argues that the District's assets exceeded its liabilities as of June 30, 2011, in the amount of \$117,152,119.00, as represented on the District' 2011 Audited Financial Statement.⁶²⁴ As a result, Bloomington asserts that it is entitled to a lump sum payout from the District for Bloomington's proportionate share of the District's net assets.

311. The parties' respective calculation methods for determining Bloomington's "proportionate share" is described below.

Intermediate District's Calculation of Bloomington's Proportionate Share of Net Liabilities

312. To determine Bloomington's proportionate share of the assets and liabilities, the Intermediate District calculated the total amount of tuition payments invoiced to Member Districts each year from the 2000-2001 school year through the 2010-2011 school year.⁶²⁵ Next, the District calculated the amount that each Member District was invoiced for tuition each of those same years.⁶²⁶ Using these two figures, the District determined the percentage of the overall tuition that each Member District was invoiced

⁶²² See Exs. 1-10; 104-07.

⁶²³ Ex. 103 at Table 2.

⁶²⁴ Ex. 108 at 16.

⁶²⁵ Test. of G. Dosdall at T. 698-99; Ex. 103 at Tables 1, 2.

⁶²⁶ Test. of G. Dosdall at T. 698-99; Ex. 103 at Tables 1, 2.

(and presumably paid) each of the 11 years. The District deems these percentages as the “ratio of tuition paid” by each Member District.

313. According to the Intermediate District’s calculations, Bloomington’s percentage of Member District tuition paid from 2001 to June 30, 2011 (i.e., the “11-year weighted average ratio of tuition paid”) was 9.105 percent (9.105%).⁶²⁷ The percentages for each fiscal year (FY) are as follows:

2000-2001 (FY 2001)	11.5681%
2001-2002 (FY 2002)	11.6244%
2002-2003 (FY 2003)	10.7503%
2003-2004 (FY 2004)	11.6522%
2004-2005 (FY 2005)	11.6887%
2005-2006 (FY 2006)	10.0864%
2006-2007 (FY 2007)	8.5570%
2007-2008 (FY 2008)	8.1960%
2008-2009 (FY 2009)	7.5642%
2009-2010 (FY 2010)	6.6381%
2010-2011 (FY 2011)	4.8241%
11-Year Average	9.1050% ⁶²⁸

314. As these numbers indicate, starting in 2005 Bloomington began to steadily decrease the number of students it was sending to the Intermediate District.⁶²⁹ By the 2010-2011 school year, Bloomington’s share of the total Member District tuition received was only 4.8 percent.⁶³⁰

315. Because the number of students sent to the Intermediate District steadily declined after 2005, the Intermediate District argues that each real estate asset should be allocated in relation to the year that the property was placed in service; and that Bloomington’s proportionate share of that asset should correspond to the percentage that Bloomington contributed to the District’s tuition that year.⁶³¹ For example, for a building that was “put into service” by the District in fiscal year 2006, Bloomington’s proportionate share of that asset should be 10.08 percent.⁶³² For a building that was “put into service” by the District in fiscal year 2011, Bloomington’s proportionate share should be 4.82 percent, etc.⁶³³ For all other assets, the District uses the percentage of tuition paid by Bloomington for the last year of its membership in the District (i.e., the 2010-2011 year).⁶³⁴

⁶²⁷ Ex. 103 at Tables 1, 2.

⁶²⁸ *Id.*

⁶²⁹ *Id.*

⁶³⁰ *Id.*

⁶³¹ Test. of G. Dossdall at T. 698-707; Ex. 103 at Table 2.

⁶³² Test. of G. Dossdall at T. 698-707; Ex. 103 at Table 2.

⁶³³ Test. of G. Dossdall at T. 698-707; Ex. 103 at Table 2.

⁶³⁴ Test. of G. Dossdall at T. 698-707; Ex. 103 at Table 2.

316. The Intermediate District argues for a similar calculation with respect to liabilities.⁶³⁵ For general liabilities, the District argues that Bloomington's proportionate share should correspond to the percentage of tuition paid by Bloomington for the last year that Bloomington was a Member District (i.e., 2010-2011).⁶³⁶ For real estate liabilities, however, the District argues that Bloomington's percentage of tuition paid for the year each property was "put into service" should apply.⁶³⁷ For all other long-term liabilities, the District argues that Bloomington's 11-year weighted average of tuition paid should apply (9.10%).⁶³⁸

317. The Intermediate District argues that this calculation results in an overall tuition paid average for Bloomington of 9.08 percent.⁶³⁹ The District contends that this percentage (9.08%), when applied to the net liabilities that the District asserts it had in 2011 (\$28,928,690.00), results in Bloomington owing the Intermediate District \$2,625,534.00.⁶⁴⁰

318. Accordingly, the Intermediate District seeks recovery from Bloomington in the amount of \$2,625,534.00.

Bloomington's Calculation of its Proportionate Share of Net Assets

319. Bloomington's calculation of its proportionate share of assets and liabilities is much simpler and easier to apply. Bloomington bases its percentage calculations solely on the last year that it was a member of the Intermediate District (i.e., the 2010-2011 school year).⁶⁴¹

320. In addition, rather than use tuition paid as the basis to determine Bloomington's proportionate share, Bloomington relies on the Average Daily Membership (ADM) (i.e., the average number of students enrolled) in each of the District's programs during the 2010-2011 school year.⁶⁴² According to Bloomington, the ADM data for 2010-2011 was as follows:

⁶³⁵ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶³⁶ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶³⁷ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶³⁸ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶³⁹ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶⁴⁰ Test. of G. Dosdall at T. 698-707; Ex. 103 at Table 2.

⁶⁴¹ Exs. 16, 18.

⁶⁴² Ex. 16; Ex. 18 at 6; Test. of Rod Zivkovich at T. 109.

Program Category	District Total	Bloomington Total	Bloomington %
ALC /ELL ⁶⁴³	467.92	43.03	9.20%
Career & Technology	141.00	10.21	7.24%
Special Education	594.29	25.17	4.24%
TOTAL:	1,203.21	78.41	6.52% ⁶⁴⁴

321. Based upon this data, Bloomington asserts that its percentage of the Intermediate District's total enrollment for the 2010-2011 school year was 6.52 percent (6.52%).⁶⁴⁵ Consequently, Bloomington asserts that it is entitled to 6.52 percent of the Intermediate District's net assets.⁶⁴⁶

322. Bloomington did not provide ADM data for any years prior to fiscal year 2011.⁶⁴⁷ Therefore, while Bloomington's calculation method is simpler, it does not include data from previous years or provide a long-term enrollment average, which would take into account Bloomington's varying enrollment figures over the course of the last 40 years.

323. Nonetheless, Bloomington asserts that if its 2010-2011 ADM percentage is applied to the net assets stated on the District's 2011 Audited Financial Statement (\$13,768,147.00), less \$5,711,435.00 in stipulated adjustments,⁶⁴⁸ it is entitled to a payment from the Intermediate District of \$585,549.00 [\$13,768,147.00 net assets, less \$5,711,435.00 in adjustments = \$8,056,712.00 multiplied by a "usage factor" of .0652 = \$525,297.62].⁶⁴⁹

324. Accordingly, in sum, Bloomington seeks recovery from the Intermediate District in the amount of \$525,297.62.

⁶⁴³ Area Learning Center/ English Language Learner.

⁶⁴⁴ Exs. 16, 18.

⁶⁴⁵ Exs. 16, 18.

⁶⁴⁶ Exs. 16, 18.

⁶⁴⁷ Exs. 16, 18.

⁶⁴⁸ See Bloomington's Post-Hearing Brief at 2-3. Bloomington stipulates to the testimony of Mae Hawkins, in which she explained that the Intermediate District reimbursed a total of \$5,711,435 to Member Districts for tuition reimbursements and Medical Assistance for overpayments. *Id.*; see Test. of M. Hawkins at T. 885-89. In fact, the District reimbursed Medical Assistance over \$1,700,000, but only deducted \$823,329 from the balance sheet. Test. of M. Hawkins at 887-88. Accordingly, the adjustment of \$5,711,435 is undisputed.

⁶⁴⁹ Ex. 18.

DISPUTED AND UNDISPUTED FIGURES IN THE DISTRICT'S 2011 ADJUSTED BALANCE SHEET

325. To simplify the parties' arguments, and to decipher between disputed and undisputed line items, the following adjusted balance sheet was used by the parties at the hearing to identify the figures in dispute:⁶⁵⁰

ASSETS

	Stipulated Value	Stipulated Adjustment	Subtotal
Cash and Investments	\$3,764,135.00		\$3,764,135.00
Accts and Interest Receivable	\$628,731.00 ⁶⁵¹		\$628,731.00
Due from other units	\$28,256,161.00	(\$5,711,435.00)	\$22,544,726.00
Inventory	\$1,850.00		\$1,850.00
Prepaid Items	\$113,611.00		\$113,611.00
Restricted cash/invest. (NEC Trust Fund)	\$28,652,100.00 ⁶⁵²		\$28,652,100.00
Real Estate:			
South Educ. Center	Disputed		Disputed
West Educ. Center	Disputed		Disputed
District Service Center	Disputed		Disputed
Edgewood Educ. Center	Disputed		Disputed
Robbinsdale Condo	\$50,000.00		\$50,000.00
North Educ. Center (Construction in Progress)	\$5,458,349.00 ⁶⁵³		\$5,458,349.00
Other Capital Leases:			
Equipment, less accumulated depreciation	\$2,823,913.00	(\$2,256,894.00 in depreciation) ⁶⁵⁴	\$567,019.00
Assets under Capital Lease	\$1,820,432.00		\$1,820,432.00

⁶⁵⁰ See Ex. 103 at Table 2; Ex. 18 at "Exhibit A."

⁶⁵¹ This amount includes \$39,746.00 in interest accrued by the NEC Trust Fund. See Ex. 108 at 18-19.

⁶⁵² This amount does not include interest of \$39,746.00 accrued on the NEC Trust Fund account.

⁶⁵³ Despite its vote in opposition to the acquisition of the NEC Property, Bloomington did not dispute its obligations under the NEC lease agreements. See Bloomington's Post-Hearing Brief. Bloomington and the Intermediate District agree that the "asset" value of the NEC Property is the book value of the construction-in-progress as of June 30, 2011.

⁶⁵⁴ Test. of Phillip Williams at T. 386.

LIABILITIES

	Stipulated Value	Amount Remaining on Future Obligation as of June 30, 2011 (Assuming No Termination of Real Estate Leases)	Subtotal
Aid Anticipation Cert.	\$3,590,000.00		\$3,590,000.00
Salaries and Comp.	\$2,157,696.00		\$2,157,696.00
Accts and Contracts Payable	\$2,495,498.00 ⁶⁵⁵		\$2,495,498.00
Due to other Govt Units	\$2,124,866.00		\$2,124,866.00
Unearned Revenue	\$7,231,493.00		\$7,231,493.00
Accrued Interest ⁶⁵⁶	\$706,489.00		\$706,489.00
Unamortized Premiums	\$0		\$0
Capital Leases:			
North Vector	\$76,600.00		\$76,600.00
Technology	\$450,064.00		\$450,064.00
Real Estate Leases			
SEC Building Lease		\$25,753,734.00	
WEC Refunding Lease COP 2009A		\$7,590,000.00	
SEC Land Lease COP 2010C		\$7,290,000.00	
EEC Lease COP 2010A		\$2,925,000.00	
EEC Lease COP 2010B		\$2,050,000.00	
NEC Building Lease COP 2010E		\$29,790,000.00	
NEC Land Lease COP 2011A		\$4,075,000.00	
Premium on Liabilities	\$96,177.00 ⁶⁵⁷		\$96,177.00

⁶⁵⁵ This amount includes \$1,637,047.00 for NEC construction work payable as of June 30, 2011, from the NEC Trust Fund.

⁶⁵⁶ It is unclear in the hearing record from what source(s) this interest accrued. Therefore, because it is undisputed, it remains as a liability to be allocated to Bloomington.

⁶⁵⁷ In its Motion for Reconsideration, the District argues that the Administrative Law Judge failed to include a conclusion of law related to "premium on liabilities" totaling \$96,177.00. This liability was addressed both in the original Findings of Fact and Conclusions of Law as an undisputed figure. At the hearing, neither

	Stipulated Value	Amount Remaining on Future Obligation as of June 30, 2011 (Assuming No Termination of Real Estate Leases)	Subtotal
Deferred Charges	(\$1,272,335.00) ⁶⁵⁸		(\$1,272,335.00)
Long Term EE Costs			
Severance Payable	\$4,731,848.00		\$4,731,848.00
Compensated Absences	\$375,937.00		\$375,937.00
Net OPEB Obligation	Disputed	\$9,532,459.00	
Net Pension	Disputed	\$409,117.00	

IMPACT OF WITHDRAWAL ON OTHER MEMBER DISTRICTS

326. The Intermediate District presented several witnesses to testify to the financial disruption to the District that resulted from Bloomington’s withdrawal, and to explain why Bloomington should not be released from its obligations under the District’s long-term real estate leases.

327. Dennis Peterson, Ph.D. (Peterson), the Superintendent of the Minnetonka School District (ISD #276), explained that as a result of Bloomington’s withdrawal the 12 remaining Member Districts have had to absorb Bloomington’s share of the Intermediate District’s long-term obligations.⁶⁵⁹ These long-term obligations include the rent payments due under the real estate leases, as well as the ongoing OPEB and pension costs for employees who accrued the benefits during the 40 years Bloomington was a member of the District.⁶⁶⁰

328. Peterson explained that if Bloomington is not held responsible for its share of the on-going costs related to the long-term leases and the employee-accrued OPEB and pension benefits, other Member Districts will be encouraged to withdraw from the District to avoid future obligations.⁶⁶¹ Peterson warned that, potentially, a few remaining

party presented any evidence about this amount. In addition, both parties stipulated that it was an undisputed liability. See Ex. 103 at Table 2; Ex. 18 at “Exhibit A.”

⁶⁵⁸ In its Motion for Reconsideration, the District argues that the Administrative Law Judge failed to include a conclusion of law related to “deferred change on liabilities issued” totaling - \$1,272,335.00. This liability was addressed both in the original Findings of Fact and Conclusions of Law as an undisputed figure. At the hearing, neither party presented any evidence disputing this amount. In addition, both parties agreed that it was an undisputed “liability.” See Ex. 103 at Table 2; Ex. 18 at “Exhibit A.”

⁶⁵⁹ Test. of Dennis Peterson at T. 751-52

⁶⁶⁰ *Id.*

⁶⁶¹ *Id.* at T. 753-55.

school districts could be left “holding the bag” for all of the rental payments due under the various real estate leases, as well as all future liability for benefits accrued by employees in prior years.⁶⁶² According to Peterson, these risks present a “potential for rapid succession” and result in a high amount of uncertainty for the remaining Member Districts.⁶⁶³

329. Peterson noted that the Member Districts have not approved an agreement to address member withdrawal and the distribution of assets and liabilities because they are waiting for the resolution of this matter.⁶⁶⁴ Nonetheless, Peterson expressed Minnetonka’s support for the asset and liability calculations and distribution method proposed by the Intermediate District in this action.⁶⁶⁵ Overall, Peterson stated that the Member Districts seek a valuation and distribution process that is fair to the remaining Member Districts, as well as repeatable in the future.⁶⁶⁶

330. Jeff Priess (Priess), the Executive Director of Business Services for the Robbinsdale School District (ISD #281), testified to the impact that Bloomington’s withdrawal has had on his school district.⁶⁶⁷ According to Priess, Robbinsdale experienced a \$50,000.00 increase in its lease levy in the first year after Bloomington’s withdrawal.⁶⁶⁸ Priess expressed concern about the amount of time this process has taken, but did not indicate that the Member Districts were in agreement as to how assets and liabilities should be allocated in the event of future withdrawals by other Member Districts.⁶⁶⁹

331. Kelly Benusa (Benusa) is the Director of Business Services for the Osseo School District (IDS #279). Benusa stated that Osseo experienced an \$85,000.00 annual increase in its lease levy as a result of Bloomington’s withdrawal because its proportionate share of the lease levy went from 24.4 percent to 25.9 percent.⁶⁷⁰ According to Benusa, all remaining Member Districts have been forced to assume a greater percentage of the Intermediate District’s costs and obligations after Bloomington’s departure.⁶⁷¹ Benusa acknowledged that enrollment in the Intermediate District did not decrease after Bloomington’s withdrawal, meaning that Member Districts (or non-member districts) are sending more students to the Intermediate District to take the place of Bloomington’s student population.⁶⁷²

⁶⁶² *Id.* at T. 755.

⁶⁶³ *Id.*

⁶⁶⁴ *Id.* at T. 753.

⁶⁶⁵ *Id.* at T. 754.

⁶⁶⁶ *Id.* at T. 752-53.

⁶⁶⁷ Test. of Jeff Priess at T. 761-81.

⁶⁶⁸ *Id.* at T. 765.

⁶⁶⁹ *Id.* at T. 765-67, 769-70

⁶⁷⁰ Test. of Kelly Benusa at T. 789.

⁶⁷¹ *Id.* at T. 789-90

⁶⁷² *Id.* at T. 798.

332. Benusa expressed support for the calculation of assets and liabilities, as well as the allocation methods proposed by the Intermediate District in this case.⁶⁷³ Benusa noted that, to date, the Member Districts have not been able to agree on a method for valuation and disbursement of assets and liabilities upon Member District withdrawal.⁶⁷⁴

333. Mae Hawkins (Hawkins), the Intermediate District's Director of Finance, testified that the lease levies for the remaining 12 Member Districts increased after Bloomington's departure.⁶⁷⁵ According to Hawkins, Bloomington paid approximately \$280,000.00 per year towards the lease payments.⁶⁷⁶ After Bloomington withdrew, the remaining Member Districts had to absorb that amount unless the District terminated the leases.⁶⁷⁷ The range of increase for the remaining Member Districts each year was between \$1,150.00, for districts with fewer students, to \$85,100.00 each year, for districts with the most students attending the Intermediate District.⁶⁷⁸

334. Because only Member Districts are responsible for lease levies, non-member districts that send students to the Intermediate District do not share in the cost of facilities.⁶⁷⁹ Thus, even if non-member school district students take the place of Bloomington students, it does not reduce the impact on the remaining Member Districts' lease levy payments resulting from Bloomington's withdrawal.⁶⁸⁰

335. In contrast, tuition is paid by both Member Districts and non-member districts.⁶⁸¹ The amount received in tuition is used by the Intermediate District to pay employee costs, including OPEB and pension benefits.⁶⁸² Thus, both non-member and new member districts will absorb the on-going cost of OPEB and pension benefits because these costs are paid each year on a "pay-as-you-go" basis.⁶⁸³ Hence, if Bloomington continues to send its students to the Intermediate District as a non-member district as it is currently doing for some students, then Bloomington will continue to pay for OPEB and pensions even if it is required to contribute to these costs in this proceeding.⁶⁸⁴

336. Hawkins explained that Member Districts seek a withdrawal valuation and distribution process that is repeatable and does not leave the remaining school districts

⁶⁷³ *Id.* at T. 791-92, 801.

⁶⁷⁴ *Id.* at T. 800.

⁶⁷⁵ Test. of M. Hawkins at T. 891-92.

⁶⁷⁶ *Id.*

⁶⁷⁷ *Id.*

⁶⁷⁸ *Id.*

⁶⁷⁹ Test. of K. Benusa at T. 798-99.

⁶⁸⁰ *Id.*

⁶⁸¹ Test. of M. Hawkins at T. 927-28.

⁶⁸² *Id.* at T. 929.

⁶⁸³ *Id.* at T. 928.

⁶⁸⁴ *Id.* at T. 919. Hawkins acknowledged that if Bloomington is required to contribute its proportionate share toward the UAAL for the OPEB and pension benefits as of June 30, 2011, then Bloomington should receive a reduction in tuition for any students that it enrolls as a non-member district. *Id.*

liable for all of the District's future expenses, including future lease payments.⁶⁸⁵ Therefore, the Intermediate District and its Member Districts support, for purposes of this hearing, the valuation and distribution method proposed by Gary Dossdall, the District's accounting expert from Froehling Anderson.⁶⁸⁶

337. To the extent any Finding of Fact are more properly deemed Conclusions of Law, or to the extent any Conclusion of Law is more properly deemed a Finding of Fact, such findings or conclusions are hereby adopted as such.

Based upon the foregoing Findings of Fact, the Administrative Law Judge makes the following:

CONCLUSIONS OF LAW

1. The Commissioner of Education (Commissioner) has jurisdiction to decide this matter pursuant to Minn. Stat. §§ 123A.24, subd. 1 and 14.57(a).

2. The Office of Administrative Hearings has the authority to decide this matter pursuant to the authority delegated by the Commissioner and acknowledged by the parties, pursuant to Minn. Stat. § 14.57(a).

3. To cease participating in, or providing financial support for, any of the services or activities related to an agreement with an intermediate district, or to terminate participation in the cooperative unit itself, a school district's board must adopt a resolution and notify the other parties to the agreement of its decision on or before February 1 of any year.⁶⁸⁷ The cessation or withdrawal shall be effective June 30 of the following fiscal year.⁶⁸⁸

4. Bloomington properly served its Notice of Withdrawal from the Intermediate District on January 29, 2010. Accordingly, Bloomington's withdrawal from the Intermediate District was proper and effective on June 30, 2011.

5. Minnesota law provides that if an independent school district withdraws from an intermediate school district, the distribution of assets and assignment of liabilities to the withdrawing district shall be determined by Minn. Stat. § 123A.24.

6. According to Minn. Stat. § 123A.24, the withdrawing school district and the intermediate district may mutually agree to terms and conditions of the distribution of assets and the assignment of liabilities.⁶⁸⁹ If, however, the intermediate district and the

⁶⁸⁵ *Id.* at T. 893.

⁶⁸⁶ *Id.* at T. 898.

⁶⁸⁷ Minn. Stat. § 123B.02, subd. 3(c).

⁶⁸⁸ *Id.*

⁶⁸⁹ Minn. Stat. § 123A.24, subd. 1(b).

withdrawing district cannot agree on the terms and conditions, the Commissioner shall resolve the dispute.⁶⁹⁰

7. The Commissioner shall resolve the dispute by determining the withdrawing district's "proportionate share" of assets and liabilities based on the withdrawing district's enrollment, financial contribution, usage, or other factor or combination of factors determined appropriate by the Commissioner.⁶⁹¹ In addition, the assets must be disbursed to the withdrawing district in a manner that minimizes financial disruption to the cooperative unit.⁶⁹²

VALUATION OF ASSETS AS OF JUNE 30, 2011

8. According to BLACK'S LAW DICTIONARY, an "asset" is:

Property of all kinds, real and personal, tangible and intangible, including *inter alia*, for certain purposes, patents and causes of action which belong to any person including a corporation and the estate of a decedent. The entire property of a person, association, corporation, or estate that is applicable or subject to the payment of his or her or its debts.⁶⁹³

9. More specifically for purposes of this case, an "asset" is defined by the DICTIONARY OF REAL ESTATE APPRAISAL as:

- (1) Generally, something that can be converted to cash and other economic equivalent.
- (2) Any owned property that has economic value, including financial assets (cash or bonds), business interests, intangible assets (copyrights and trademarks), and physical assets (real and personal property).
- (3) In general business usage, something owned by a business and reflected in the owner's balance sheet.⁶⁹⁴

Robbinsdale Condominium

10. The Intermediate District holds title to the Robbinsdale condominium in fee simple, free and clear of any financial encumbrances. Therefore, it is an asset that must be distributed as part of Bloomington's withdrawal from the District.

⁶⁹⁰ *Id.* (c).

⁶⁹¹ *Id.*

⁶⁹² *Id.*

⁶⁹³ BLACK'S LAW DICTIONARY 78 (Abridged 6th ed. 1991).

⁶⁹⁴ APPRAISAL INSTITUTE, DICTIONARY OF REAL ESTATE APPRAISAL 13 (5th ed. 2010).

11. The parties stipulate that the value of this asset is \$50,000.00.⁶⁹⁵

District Service Center

12. The Intermediate District holds legal title to the DSC Property and owns the property in fee simple, free and clear of any financial encumbrances. Therefore, it is an asset that must be distributed as part of Bloomington's withdrawal from the District.

13. The Administrative Law Judge adopts the appraisal of the DSC Property conducted by Robert Strachota on March 5, 2014. According to that appraisal, the fair market value of the DSC Property as of June 30, 2011, was \$3,000,000.00.

Edgewood Education Center

14. Under the express terms of the EEC Lease, the Intermediate District has no title or equity in the EEC Property unless and until the District makes all rent payments due under the lease through 2025, or exercises its option to purchase the property prior to the end of the lease term.⁶⁹⁶

15. As of the date of Bloomington's withdrawal from the District on June 30, 2011, the District had not paid all rent due under the contract, nor had it exercised its option to purchase the property. Therefore, title to the EEC Property had not transferred to the District, and was held by Wells Fargo Bank. The Intermediate District's interest in the property was that of a tenant or lessee holding a leasehold estate, with an unexercised option to purchase the property.

16. A "leasehold" is defined as "a tenant/lessee's possessory estate in land, granted by a landlord/lessor who holds an estate of larger duration in the same land."⁶⁹⁷ A "leasehold interest" is "a tenant's possessory interest created by a lease."⁶⁹⁸

17. As of June 30, 2011, the Intermediate District had no ownership interest in, and held no legal title to, the EEC Property. As a result, the District did not have a fee simple interest in the property, and any valuation of a fee simple interest in the property is irrelevant for determining the value of *the District's* legal interest in the property.⁶⁹⁹

18. In addition, as of June 30, 2011, the Intermediate District did not hold a leased fee interest in the EEC Property. A "leased fee interest" is defined as "[a] freehold (ownership interest) where the possessory interest has been granted to another party by creation of a contractual landlord-tenant relationship (i.e., a lease)."⁷⁰⁰ As a result, the

⁶⁹⁵ See Bloomington's Post-Hearing Brief at 7.

⁶⁹⁶ Ex. A at 19.

⁶⁹⁷ BLACK'S LAW DICTIONARY 616 (Abridged 6th ed. 1991).

⁶⁹⁸ APPRAISAL INSTITUTE, DICTIONARY OF REAL ESTATE APPRAISAL 111 (5th ed. 2010).

⁶⁹⁹ According to property records, Wells Fargo Bank maintained a fee simple interest in the EEC Property as of June 30, 2011, subject to the District's possessory interest arising out of the EEC Lease. See Ex. Z.

⁷⁰⁰ APPRAISAL INSTITUTE, DICTIONARY OF REAL ESTATE APPRAISAL 111 (5th ed. 2010).

District did not have a leased fee interest in the EEC Property, and any valuation of a leased fee interest in the property is irrelevant for determining the value of the District's interest in the property.⁷⁰¹

19. As of June 30, 2011, Wells Fargo Bank held legal title to the EEC Property and was the only party with a fee simple or leased fee interest in the EEC Property.

20. The "asset" that the Intermediate District held as of June 30, 2011, was the District's interest in the EEC Property, not the bank's interest. The District's legal interest was limited to a leasehold interest and nothing more. Consequently, the District's leasehold interest is the asset to be valued as of June 30, 2011.

21. The value of a leasehold interest is "the difference between the total remaining rent under the lease, and the rent [a] lessee would currently pay for similar space for the same time period."⁷⁰² Thus, if the total rent remaining under a lease is \$100,000.00, and the rent the lessee would currently pay for similar space for a similar term is \$200,000.00, the value of the lessee's leasehold interest would be \$100,000.00 – a positive leasehold.⁷⁰³ Conversely, if the total rent remaining under a lease is \$100,000.00, and the rent the lessee would currently pay for similar space for the same term is \$50,000.00, the value of the lessee's leasehold interest would be a *negative* \$50,000.00 – resulting in a "negative leasehold."⁷⁰⁴ In the latter example, there would be no value in the lessee's leasehold interest.⁷⁰⁵

22. No expert testified as to the value of the Intermediate District's leasehold interest in the EEC Property. However, because the rent paid under the EEC Lease was approximately market rent or greater, there was no positive value in the District's leasehold interest.⁷⁰⁶ Thus, the Intermediate District held a negative leasehold interest.

23. By withdrawing from the collective, Bloomington forfeited its rights and interest in the EEC Property after June 30, 2011. Thus, Bloomington can claim no legal interest in the EEC Property should the District someday exercise its option to purchase the property.

24. If the District eventually tenders its final rent payment or earlier exercises its option to purchase the EEC Property, all rent previously paid will be applied toward the final purchase price, similar to a contract for deed. Until that occurs, however, all amounts paid under the EEC Lease are simply rent payments for which no equity in the property is earned. The same is true if the District terminates the EEC Lease prior to the end of

⁷⁰¹ Under the EEC Lease, Wells Fargo Bank held the leased fee interest in the EEC Property as of June 30, 2011. See Ex. A.

⁷⁰² BLACK'S LAW DICTIONARY 616-17 (Abridged 6th ed. 1991).

⁷⁰³ A "positive leasehold" is "[a] lease situation in which the market rent is greater than the contract rent." APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 147 (5th ed. 2010).

⁷⁰⁴ A "negative leasehold" is "a lease situation in which the market rent is less than the contract rent." *Id.* at 132.

⁷⁰⁵ *Id.*

⁷⁰⁶ Ex. 3 at 82; Ex. 105 at 39-40.

the lease term — all monies paid are forfeited and title to the EEC Property is never conveyed to the District.

25. Because the Intermediate District had not exercised its option to purchase the EEC Property or paid all rent due under the EEC Lease prior to June 30, 2011, the value of the District's interest in the EEC Property as of June 30, 2011, is limited to the value of the District's leasehold interest at the time of withdrawal and no more. As of June 30, 2011, the District held a negative leasehold interest in the EEC Property, causing the District's interest in the property to be of no current value. Therefore, Bloomington's proportionate share of this asset is zero.

South Education Center

26. Under the express terms of the SEC Building Lease and SEC Refunding Lease, the Intermediate District has no legal title or equity in the SEC Property unless and until the District makes all rent payments due under the respective leases, or exercises its option to purchase the property prior to the end of the lease terms.⁷⁰⁷

27. As of the date of Bloomington's withdrawal from the District on June 30, 2011, the District had not paid all rent due under the SEC Building Lease or SEC Refunding Lease, nor had the District exercised its option to purchase the property. Therefore, legal title to the SEC Property had not transferred to the District, and was held by Wells Fargo Bank. The Intermediate District's interest in the property was that of a tenant or lessee holding a leasehold estate, with an unexercised option to purchase the property.

28. As of June 30, 2011, the Intermediate District had no ownership interest in, and held no legal title to, the SEC Property. As a result, the District did not have a fee simple interest in the property, and any valuation of a fee simple interest in the property is irrelevant for determining the value of *the District's* legal interest in the property.⁷⁰⁸

29. In addition, as of June 30, 2011, the Intermediate District did not hold a leased fee interest in the SEC Property.⁷⁰⁹ Wells Fargo Bank held the leased fee interest in the SEC Property.⁷¹⁰ Consequently, any valuation of a leased fee interest in the SEC Property is irrelevant for determining the value of *the District's* interest in the property.⁷¹¹

30. The asset that the Intermediate District held as of June 30, 2011, was the District's legal interest in the SEC Property, not the bank's legal interest. The District's

⁷⁰⁷ Exs. J, M, N.

⁷⁰⁸ According to property records, Wells Fargo Bank maintained a fee simple interest in the SEC Property as of June 30, 2011, subject to the District's possessory interest arising out of the SEC Building Lease and SEC Refunding Lease. See Ex. Y.

⁷⁰⁹ *Id.*

⁷¹⁰ *Id.*

⁷¹¹ Under the SEC Building Lease and SEC Refunding Lease, Wells Fargo Bank held a leased fee interest in the SEC Property as of June 30, 2011. See Exs. J, M, N.

legal interest was limited to a leasehold interest and nothing more. Consequently, the District's leasehold interest is the asset to be valued as of June 30, 2011.

31. No expert testified as to the value of the Intermediate District's leasehold interest in the SEC Property. However, because the rent paid under the SEC Lease was approximately market rent or greater, there was no positive value in the District's leasehold interest.⁷¹² Thus, the Intermediate District held a negative leasehold interest.

32. By withdrawing from the collective, Bloomington forfeited its rights and legal interest in the SEC Property after June 30, 2011. Bloomington can claim no interest in the SEC Property should the District someday exercise its option to purchase the property.

33. If the District eventually tenders its final rent payment or exercises its option to purchase the SEC Property, all rent previously paid will be applied toward the final purchase price, similar to a contract for deed. Until that occurs, however, all amounts paid under the SEC Building Lease and SEC Refunding Lease are simply rent payments for which no equity in the property is earned. The same is true if the District terminates the SEC Building Lease and SEC Refunding Lease prior to the end of the leases' terms -- all monies paid are forfeited and title to the property is never conveyed to the District.

34. Because the Intermediate District had not exercised its option to purchase the SEC Property, and had not paid all rent due under the SEC Building Lease and SEC Refunding Lease, the value of the District's interest in the SEC Property as of June 30, 2011, is limited to the value of the District's leasehold interest at the time of withdrawal and no more. As of June 30, 2011, the District held a negative leasehold interest in the SEC Property, causing the District's interest in the property to be of no current value. Therefore, Bloomington's proportionate share of this asset is zero.

West Education Center

35. Unlike the EEC Property and SEC Property, the Intermediate District holds legal title to the WEC Property.⁷¹³ Such title was conveyed by Wells Fargo Brokerage Services to the District upon the refinance of the WEC Lease, and is evidenced by the Certificate of Title No. 1308505 (Exhibit X).

36. "Title" as used in real property law, is defined as "[t]he formal right of ownership of property."⁷¹⁴ "Legal title" is defined as "[title] cognizable or enforceable in a court of law...the apparent right of ownership and possession, but which carries no beneficial interest in the property."⁷¹⁵

⁷¹² Ex. 7 at 31; Ex. 107 at 61-62.

⁷¹³ Ex. X.

⁷¹⁴ BLACK'S LAW DICTIONARY 1033 (Abridged 6th ed. 1991).

⁷¹⁵ *Id.* at 623.

37. However, while the Intermediate District holds evidence of legal title to the WEC Property, the District does not have marketable title to the property. “Marketable title” is defined as “title which is free from encumbrances and any reasonable doubt as to its validity...which readily can be sold or mortgaged...”⁷¹⁶ This is because the District’s legal interest in the WEC Property is fully encumbered by: (1) the WEC Ground Lease, under which Wells Fargo Bank has a possessory interest in the property; and (2) the WEC Refunding Lease, under which the District cannot mortgage, sell, assign, convey, transfer, or otherwise dispose of the property.⁷¹⁷

38. The WEC Ground Lease gives Wells Fargo Bank a possessory interest in the WEC Property until February 1, 2035, or until the District: (1) pays all rent due under the WEC Refunding Lease; (2) exercises its “option to purchase” the property and prepay the rent; or (3) defaults under the WEC Refunding Lease, in which case the trustee, Wells Fargo Bank, takes possession of the property.⁷¹⁸

39. The WEC Refunding Lease gives the Intermediate District a possessory interest in the WEC Property so long as the lease is not terminated and so long as the District does not default under the lease.⁷¹⁹

40. Consequently, under the WEC Ground Lease and WEC Refunding Lease, both Wells Fargo Bank and the Intermediate District have leasehold and leased fee interests in the WEC Property. Wells Fargo Bank has a leasehold (i.e., lessee) interest in the property under the WEC Ground Lease, and a leased fee (i.e., lessor) interest in the property under the WEC Refunding Lease. In turn, the Intermediate District has a leasehold (i.e., lessee) interest in the property under the WEC Refunding Lease, and a leased fee (i.e., lessor) interest in the property under the WEC Ground Lease.

41. By the express terms of the WEC Refunding Lease, the Intermediate District cannot mortgage, sell, assign, transfer, or convey the WEC Property or any portion thereof during the lease term.⁷²⁰ Thus, the District’s legal interest in the WEC Property is fully encumbered by the WEC Refunding Lease and WEC Ground Lease until the District fulfills all of its payment obligations under the WEC Refunding Lease.

42. As of June 30, 2011, the Intermediate District had not paid all rent due under the WEC Refunding Lease, nor had it exercised its “option to purchase” the property by prepaying rent in accordance with the WEC Refunding Lease. Therefore, the WEC Property was fully encumbered by the WEC Refunding Lease and WEC Ground Lease; and could not be mortgaged, sold, assigned, transferred, conveyed, or disposed of by the District.

⁷¹⁶ *Id.* at 670.

⁷¹⁷ Exs. F, H.

⁷¹⁸ Exs. F at 24-25, H at 4.

⁷¹⁹ Ex. F.

⁷²⁰ *Id.* at 23.

43. A “fee simple interest” is defined as “[a]bsolute ownership [of a real property] *unencumbered by any other interest* or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat.”⁷²¹ A fee simple estate “*is one in which the owner is entitled to the entire property, with unconditional power of disposition....*”⁷²²

44. While legal title to the WEC Property was held in the name of the Intermediate District, the Intermediate District did not have a fee simple interest in the WEC Property as of June 30, 2011. The Intermediate District’s interest in the WEC Property was fully encumbered by: (1) Wells Fargo Bank’s leasehold interest in the property under the WEC Ground Lease and WEC Trust Agreement; and (2) the WEC Refunding Lease Agreement which prohibited the District from mortgaging, selling, assigning, transferring, conveying, other otherwise disposing of the property. Therefore, the Intermediate District did not have a fee simple interest in the WEC Property as of June 30, 2011.

45. Although the Intermediate District did not have a fee simple interest in the WEC Property as of June 30, 2011, it did have a leased fee interest in the property as of June 30, 2011, pursuant to the terms of the WEC Ground Lease. Accordingly, the asset value of the WEC Property as of June 30, 2011, should be measured by the market value of a leased fee interest in the property, not a fee simple interest in the property.

46. The Administrative Law Judge concludes that the most reasonable appraised value of the WEC Property is \$7,600,000.00, as determined by real estate appraisal experts Robert Lunz and Robert Strachota (in his more reliable 2011 Appraisal).

47. The total amount outstanding on the WEC Refunding Lease as of June 30, 2011, was \$7,590,000.00.⁷²³ The WEC Property, if considered an asset, also had a corresponding liability of \$7,590,000.00 before the District could mortgage, sell, assign, transfer, convey, or otherwise dispose of the property. Consequently, as of June 30, 2011, the WEC Property had a net value to the District of only \$10,000.00 (\$7,600,000.00 - \$7,590,000.00 = \$10,000.00).

North Education Center

48. On December 17, 2009, the Intermediate District Members passed a resolution to acquire an interest in the NEC Property and construct a new facility.⁷²⁴ Bloomington was the only Member District that opposed the measure.⁷²⁵

⁷²¹ APPRAISAL INSTITUTE, THE DICTIONARY OF REAL ESTATE APPRAISAL 78 (5th ed. 2010) (emphasis added).

⁷²² BLACK’S LAW DICTIONARY 427 (Abridged 6th ed. 1991) (emphasis added).

⁷²³ Ex. 103 at Table 2; Exs. 2, 6, 8, 106.

⁷²⁴ Ex. 22.

⁷²⁵ *Id.*

49. On January 28, 2010 – just a month after the District passed a resolution to acquire an interest in the NEC Property over Bloomington’s objection – the Bloomington School Board passed a resolution withdrawing from the Intermediate District.⁷²⁶ The Intermediate District was notified of Bloomington’s withdrawal on January 29, 2010.⁷²⁷

50. Minnesota law provides that before incurring “debt,” the governing body of an intermediate district must adopt a resolution proposing to incur debt and articulating the proposed financial effect of the debt upon each participating district.⁷²⁸ Within 120 days of receiving the resolution of the governing body, the school board of the participating district shall adopt a resolution stating:

- (1) Its concurrence with incurring other debt;
- (2) Its intention to cease participating in or providing financial support for the service or activity related to the debt; or
- (3) Its intention to terminate participation in the cooperative agreement.⁷²⁹

51. If a school district concurs with the debt while it is a member of the intermediate district, it remains liable for the debt even after its withdrawal from the intermediate district.⁷³⁰

52. However, if, within 120 days of the intermediate district’s resolution to incur the debt, a member district notices: (1) its intention to cease participating in or providing financial support for the debt; or (2) withdraws from the district, the member district shall not be liable for the debt.⁷³¹

53. While the Intermediate District concedes that the NEC Lease, as supplemented, does not create a “debt” for which Bloomington is liable, the clear intent of Minn. Stat. § 123B.02, subd. 3 (2014), is to enable a member school district to withdraw from a cooperative unit if it disagrees with a debt, liability, or financial obligation that the cooperative unit incurs over its objection.

54. By opposing the resolution to acquire the NEC Property, and timely noticing its withdrawal from the Intermediate District, Bloomington is not subject to the NEC Lease, as supplemented, or any of the other agreements related to the NEC Property.

⁷²⁶ Ex. 21.

⁷²⁷ *Id.*

⁷²⁸ Minn. Stat. § 123B.02, subd. 3(d) (2014). This provision also addresses the issuance of bonds, but because intermediate districts do not have the legal authority to issue bonds, this clause of the statute is not applicable. See *also* Minn. Stat. § 123A.24, subd. 1(b).

⁷²⁹ Minn. Stat. § 123B.02, subd. 3(d).

⁷³⁰ Minn. Stat. § 123B.02, subd. 3(d), (e) (2014).

⁷³¹ *Id.*

55. The Intermediate District knew of Bloomington's opposition to the NEC acquisition, and it knew of Bloomington's withdrawal from the District, before it executed the NEC Lease, NEC Supplemental Lease, and related agreements. Notwithstanding Bloomington's opposition and withdrawal, the Intermediate District Members decided to continue with the acquisition and construction of the NEC Property without Bloomington's continued contribution to the project.

56. Because Bloomington opposed the acquisition of the NEC Property, and immediately withdrew from the District after the District voted to acquire an interest in the NEC Property, it would be inequitable for Bloomington to share in either the value of the NEC Property or NEC Trust Fund as assets, or be subject to the liabilities associated with the NEC Lease, as supplemented.

57. Therefore, the NEC Property, including all assets attributable to the NEC Trust Fund, as well as the District's obligations under the NEC Lease, as supplemented, shall be removed from the calculation of the District's assets and liabilities subject to disbursement and allocation in this case.

58. To that end, the following amounts shall be **excluded** from the calculation of the District's assets to be distributed to Bloomington:

- \$28,652,100.00 in the NEC Trust Fund as of June 30, 2011.
- \$39,746.00 in accrued interest attributable to the NEC Trust Fund. This amount shall be subtracted from the Districts "accounts and interest" assets.
- \$5,458,349.00 for NEC Construction Work in Progress (i.e., value of the NEC Property as of June 30, 2011).

59. In addition, the following amounts shall be **excluded** from the calculation of the District's liabilities to be allocated to Bloomington:

- \$29,790,000.00, the outstanding amount owed under the NEC Lease, as of June 30, 2011.
- \$4,075,000.00, the outstanding amount owed under the NEC Lease, as supplemented, as of June 30, 2011.
- \$1,637,047.00 in construction costs payable for the NEC Property as of June 30, 2011. This amount shall be subtracted from the District's "accounts and contracts payable" liability of \$2,495,498.00.

Other Assets

60. Aside from the EEC Property, SEC Property, WEC Property, and NEC Property, the Intermediate District and Bloomington stipulate to the value of all other assets listed on the 2011 Audited Financial Statement.⁷³² Those assets include:

- cash and temporary investments totaling \$3,764,135.00;
- accounts receivable and interest totaling \$588,985.00;⁷³³
- amounts due from other governmental units totaling \$28,256,161.00;
- inventory totaling \$1,850.00;
- prepaid items totaling \$113,611.00;
- equipment valued at \$2,823,913.00, less stipulated⁷³⁴ accumulated depreciation of \$2,256,894.00, resulting in an equipment value of \$567,019.00; and
- non-real estate assets held under capital leases valued at \$1,820,432.00.⁷³⁵

CALCULATION OF LIABILITIES AS OF JUNE 30, 2011

61. Upon withdrawal, the withdrawing school district remains responsible for its share of “debt” incurred by the cooperative unit “according to Minn. Stat. § 123B.02, subd. 3.”⁷³⁶

Real Estate Leases and Agreements

62. The Intermediate District stipulates that the rent obligations set forth in the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, do not constitute “debt” and do not contribute to the District’s debt limit set forth in Minn. Stat. § 475.53 (2014).⁷³⁷

⁷³² See Exs. 23, 108; Ex. 103 at Table 2.

⁷³³ This amount excludes \$39,746.00 in interest accrued on the NEC Trust Fund. See Ex. 108 at 18-19.

⁷³⁴ Test. of Phillip Williams at T. 386.

⁷³⁵ Exs. 23, 108; Ex. 103 at Table 2.

⁷³⁶ Minn. Stat. § 123A.24, subd. 1(b).

⁷³⁷ See e-mail correspondence from Anne Becker, legal counsel for the Intermediate District, dated December 8, 2014, on file and of record in this case. Note also that the 2009 Memorandum of Agreement provides that “Neither members nor member representatives shall have individual liability for the debts and obligations of the District.” See Ex. 102.

63. Minnesota Statutes, section 475.53, subdivision 4, provides that no school district shall be subject to net debt in excess of 15 percent of the estimated market value of all taxable property situated within its corporate limits.

64. To that end, each lease agreement at issue in this case expressly exempts the rent due under the leases from the Intermediate District's "debt" limit. To wit:

- The EEC Lease expressly provides that the obligations under the lease, including the obligation to pay rent, "shall constitute a current expense of the District for such Fiscal Year and shall not constitute an indebtedness of the District....⁷³⁸"
- The WEC Refunding Lease expressly provides that the obligations under the lease, including the obligation to pay rent, "shall constitute a current expense of the District for the Fiscal Year then in effect" and "shall not constitute an indebtedness, liability or mandatory payment obligation" of the District.⁷³⁹
- The SEC Refunding Lease expressly provides that the obligations under the lease, including the obligation to pay rent, "shall constitute a current expense of the District for such Fiscal Year and shall not constitute an indebtedness of the District....⁷⁴⁰"
- The SEC Building Lease expressly provides that the obligations under the lease, including the obligation to pay rent, "shall constitute a current expense" of the District for the fiscal year then in effect and "shall not constitute an indebtedness" of the District.⁷⁴¹
- The NEC Lease, as supplemented, expressly provides that the obligations under the lease, including the obligation to pay rent, "shall constitute a current expense" of the District for the fiscal year then in effect and "shall not constitute an indebtedness" of the District.⁷⁴²

65. As a result, the obligations to pay rent under the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, are not "debts" for which Bloomington has a continued obligation under Minn. Stat. § 123A.24, subd. 1(b), after its withdrawal on June 30, 2011.

⁷³⁸ Ex. A. at 10.

⁷³⁹ Ex. F. at 7-8.

⁷⁴⁰ Ex. N. at 10.

⁷⁴¹ Ex. J at 10-11.

⁷⁴² Ex. R at 10; Ex. U.

66. A “liability” is broader in scope than a “debt.” BLACK’S LAW DICTIONARY defines “liability” to include “all character of debts and obligations.”⁷⁴³

67. Minnesota Statutes section 123B.02, subdivision 3(f), expressly provides that an independent school district that is part of an intermediate district may not obligate itself to participate in and provide financial support for an agreement with a cooperative unit to provide building space for a term of more than two years.⁷⁴⁴ Therefore, Bloomington cannot be liable for any rent or lease payments due under real estate leases, agreements, or contracts that exceed two years.

68. In compliance with Minn. Stat. § 123B.02, subd. 3(f), the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, are all year-to-year leases terminable at will by the Intermediate District upon its non-appropriation of funds.⁷⁴⁵ The leases all permit the Intermediate District to terminate the leases at the end of any fiscal year if the Intermediate District’s Board decides not to appropriate moneys sufficient to pay the rent in its budget for the next fiscal year.⁷⁴⁶

69. The leases further provide that upon non-appropriation and termination, the Intermediate District’s liability is limited to the rent due for the current fiscal year, and no other damages or liabilities are owed.⁷⁴⁷

70. The Intermediate District is in full control of whether to continue the leases or terminate them by non-appropriation. If the District decides to terminate the leases prior to the end of the lease term, the District has no on-going liability to pay rent or other damages. The District simply loses its interest in the properties; and all amounts paid in rent prior to termination are forfeited.

71. The Intermediate District’s obligations under the leases are similar to those arising under a contract for deed.⁷⁴⁸ If a contract for deed is terminated prior to the end of the contract term or payment of the full purchase price, the property reverts back to the vendor and all amounts paid by the vendee are forfeited.⁷⁴⁹

⁷⁴³ BLACK’S LAW DICTIONARY 631 (Abridged 6th ed. 1991).

⁷⁴⁴ The statute provides that an agreement may allow the district an option to renew for an additional two years. Minn. Stat. § 123B.02, subd. 3(f).

⁷⁴⁵ See Ex. A at 8-9 (EEC Lease); Ex. F at 6, 8, and 13 (WEC Refunding Lease); Ex. J at 10 (SEC Building Lease); Ex. N at 8-9 (SEC Refunding Lease); Ex. R at 5, 8-9 (NEC Lease).

⁷⁴⁶ Ex. A at 8-9 (EEC Lease); Ex. F at 6, 8, and 13 (WEC Refunding Lease); Ex. J at 10 (SEC Building Lease); Ex. N at 8-9 (SEC Refunding Lease); Ex. R at 5, 8-9 (NEC Lease).

⁷⁴⁷ Ex. A at 5-6, 8-9; Ex. F at 6, 13; Ex. J at 10, 22-23; Ex. N at 8-9, 10, 22-24; Ex. R at 5-6, 8-9, 10.

⁷⁴⁸ A “contract for deed” is defined as “[a]n agreement by a seller to deliver the deed to the property when certain conditions have been met, such as completion of payments by purchaser.” BLACK’S LAW DICTIONARY at 227 (Abridged 6th ed. 1991).

⁷⁴⁹ As succinctly explained in *In re Butler*, 552 N.W.2d 226, 230 (Minn. 1996):

In Minnesota, one remedy available to a vendor upon the vendee's defaulting under the terms of the contract for deed is the vendor's ability to cancel the contract pursuant to Minnesota Statutes section 559.21. A statutory cancellation of a contract for deed results

72. The obligations created under the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, are incurred on a year-to-year basis when the District votes to appropriate funds to pay the rents due for the next year. By tying the rent obligation to appropriations, and limiting the damages that the bank may seek upon the District's early termination and default, the Intermediate District affirmatively limited its liabilities under the leases to the current fiscal year, as required by Minn. Stat. §§ 123B.02, subd. 3(f), 465.71. Consequently, the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, do not represent long-term liabilities of the District, but rather annual expenses which are appropriated in the budgeting process.

73. Bloomington gave its notice of withdrawal from the District on January 29, 2010. Its withdrawal was not effective until June 30, 2011. The Intermediate District had the opportunity to terminate the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, by not appropriating moneys for the leases for fiscal year 2011 (and beyond), and by not proceeding with the acquisition of the NEC Property.

74. Instead, the remaining Member Districts continued with the acquisition and construction of the NEC Property; and voted each year after Bloomington's withdrawal to appropriate the moneys to pay rent under the EEC Lease, SEC Building Lease, SEC Refunding Lease, WEC Refunding Lease, and NEC Lease, as supplemented. The remaining Member Districts did this to preserve the District's interest in the properties, with the intent of someday acquiring clear and unencumbered title to the properties. However, by appropriating the funds each year after Bloomington's withdrawal, the remaining Member Districts accepted new liabilities each year for which Bloomington is not responsible.

75. The clear intent of Minn. Stat. § 123B.02, subd. 3(f) is to limit an independent school district's liabilities for facility leases to no more than two years. The additional intent of the statute is to allow school districts to withdraw from a cooperative unit, and "cease participating in and providing financial support for the activities of" the cooperative.⁷⁵⁰

76. Minnesota Statutes, section 123A.24, subdivision 1(b), provides that a withdrawing district remains liable for its share of "debt" incurred by the cooperative, subject to Minn. Stat. § 123B.02, subd. 3. The Intermediate District specifically structured its real estate acquisitions to allow it to terminate the leases at any time without further obligation. As a result, each of the leases expressly provides that the obligation to pay rent is not a debt for the District – or a continuing liability for which damages may be

in the vendee's forfeiture of all payments made and restoration of full legal and equitable title in the property to the vendor. This result is different from that in a mortgage foreclosure sale, where the defaulting party may receive proceeds of a mortgage foreclosure sale above the amount owed on the property.

⁷⁵⁰ Minn. Stat. § 123B.02, subd. 3.

sought – but rather, a yearly appropriation or expense. Consequently, the rental obligations arising under the leases must be treated as yearly expenses, not long-term liabilities, upon the withdrawal of a Member District.

77. Bloomington paid its share of rent for the real estate leases through June 30, 2011, and owes no further obligation under the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented. All obligations of the Intermediate District arising out of appropriations for rent payments made after June 30, 2011, are the obligations of the Intermediate District, not Bloomington.

78. The District specifically structured its real estate acquisitions as year-to-year leases. As a result, the leases permit the District to terminate the contracts at any time and avoid continued liability in the event that the District decides not to appropriate funds for rent in any fiscal year. The District cannot now claim that the leases impose a greater obligation on its withdrawing member than the leases impose on the District itself.

79. The Administrative Law Judge, therefore, concludes that Bloomington has no liability for, and owes no debt on, obligations arising under the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, after June 30, 2011. Each time that the District appropriated moneys to pay the EEC Lease, WEC Refunding Lease, SEC Building Lease, SEC Refunding Lease, and NEC Lease, as supplemented, after June 30, 2011, it resulted in a new annual expense/liability for which Bloomington is not responsible. Accordingly, the “liabilities” of the District as of June 30, 2011, shall not include amounts due and outstanding under these leases after June 30, 2011.

Other Post-Employment Benefits (OPEB) and Pension Benefits

80. The Other Post-Employment Benefits and Pension Benefits owed to the Intermediate District’s employees are contractual obligations which arise under the collective bargaining agreements the District has entered into with its unions.

81. Once earned, these benefits are part of the employees’ total compensation for past service and cannot be lawfully reduced once an employee retires.⁷⁵¹ As a result, the OPEB and Pension Benefits are debts, obligations, and/or liabilities⁷⁵² of the District from the dates that the benefits are earned, regardless of when or how they are paid or accounted for in the District’s financial reports.

⁷⁵¹ See *Norman*, 696 N.W.2d at 337-38.

⁷⁵² A “debt” is “[a] fixed and certain obligation to pay money or some other valuable thing or things, either in the present or in the future.” BLACK’S LAW DICTIONARY 279 (Abridged 6th ed. 1991). A “liability” is “all character of debts and obligations...any kind of debt or liability, either absolute or contingent, express or implied...” *Id.* at 631. An “obligation” is “any duty imposed by law, promise, contract, relations of society, courtesy, kindness, etc.” *Id.* at 740.

82. By accepting the services and labor of the District's employees and being a member of the District when these collective bargaining agreements were executed, Bloomington is responsible for its proportionate share of the total liability related to the OPEB and Pension Benefits earned but not yet received by the District's employees as of June 30, 2011.

83. Bloomington has been a member of the Intermediate District since its inception in 1968. Therefore, it has an obligation to pay its proportionate share of all OPEB and Pension Benefits earned by employees from 1968 to June 30, 2011.

84. The fact that the Intermediate District pays its OPEB and Pension Benefit obligations on an annual "pay-as-you-go" basis does not negate the District's on-going debt and liability for the amounts earned but unpaid as of June 30, 2011.

85. Bloomington did not present any evidence to contradict the District's calculation of its unfunded actuarial accrued liability or the OPEB and Pension Benefits. The UAAL is the amount required to pay all OPEB and Pension Benefits accrued by, but yet unpaid to, District employees as of the date of valuation (June 30, 2011). While the UAAL is an actuarial estimate and may differ from the amount the District will actually pay in the future, the UAAL is the best calculation of the future obligation available to the Administrative Law Judge at this time.

86. In addition, Bloomington did not present any testimony or evidence of how the OPEB and Pension Benefits can be "trued up" or reconciled in the future to ensure that the amount attributed to Bloomington in this hearing is consistent with the total amount actually paid by the District in the future.

87. At this time, a final determination is necessary to allocate the District's liabilities. Minnesota Statutes, section 123A.24, requires that the assets and liabilities of an intermediate district be determined upon a district's withdrawal. Therefore, the determination cannot be deferred until the District's exact liability is known, which could take decades.

88. By withdrawing from the Intermediate District, Bloomington subjected itself to payment of the future liability in a lump sum, rather than over time as they become due. Therefore, an actuarial calculation is necessary to determine the District's accrued liability for these obligations as of June 30, 2011.

89. The unrefuted evidence presented at hearing establishes that the value of the Intermediate District's UAAL for OPEB earned but not yet paid to District employees as of June 30, 2011, is \$9,532,459.00. Bloomington is liable for its proportionate share of this amount, as set forth below.

90. The unrefuted evidence presented further establishes that the current value of the Intermediate District's UAAL for Pension Benefits earned but not yet paid to District

employees as of June 30, 2011, is \$409,117.00. Bloomington is liable for its proportionate share of this amount, as set forth below.

Undisputed Liabilities

91. The parties do not dispute the calculation of the Intermediate District's liabilities as of June 30, 2011, for the following items:

- aid anticipation certificates totaling \$3,590,000.00;
- salaries and compensated absences payable in the amount of \$2,157,696.00;
- accounts and contracts payable totaling \$858,451.00;⁷⁵³
- amounts due to other governmental units totaling \$2,124,866.00;
- unearned revenue totaling \$7,231,493.00;
- accrued interest payable totaling \$706,489.00;
- capital lease payable for North Vector in the amount of \$76,600.00;
- capital lease payable for technology in the amount of \$450,064.00;
- premium on liabilities issued totaling \$96,177.00;⁷⁵⁴
- deferred charges on liabilities issued totaling [-\$1,272,335.00];⁷⁵⁵

⁷⁵³ The amount stipulated to by the parties was \$2,495,498.00. However, this amount (\$2,495,498.00) included \$1,637,047.00 owed by the District for construction work performed on the NEC Property as of June 30, 2011. See Ex. 108 at 18-19. The Administrative Law Judge has determined that the amount owed for construction of the NEC Property is not a debt, liability, or obligation for which Bloomington is responsible. See Conclusion of Law No. 55. Accordingly, \$1,637,047.00 has been subtracted from the stipulated sum of "accounts and contracts payable."

⁷⁵⁴ In its Motion for Reconsideration, the District argues that the Administrative Law Judge failed to include a conclusion of law related to "premium on liabilities" totaling \$96,177.00. This liability was addressed both in the original Findings of Fact and Conclusions of Law as an undisputed figure. At the hearing, neither party presented any evidence related to this amount. In addition, both parties agreed that it was an undisputed "liability." Accordingly, this amount remains in the liabilities to be allocated to Bloomington.

⁷⁵⁵ In its Motion for Reconsideration, the District argues that the Administrative Law Judge failed to include a conclusion of law related to "deferred charges on liabilities" totaling -\$1,272,335.00. This "liability" was addressed both in the original Findings of Fact and Conclusions of Law as an undisputed figure. At the hearing, neither party presented any evidence related to this amount. In addition, both parties agreed that it was an undisputed "liability." Accordingly, this amount remains in the liabilities to be allocated to Bloomington.

- severance benefits payable to employees in the amount of \$4,731,848.00; and
- compensated employee absences payable totaling \$375,937.00.⁷⁵⁶

92. Bloomington is liable for its proportionate share of these amounts, as set forth below.

BLOOMINGTON'S PROPORTIONATE SHARE OF THE DISTRICT'S ASSETS AND LIABILITIES

93. Minnesota law provides that if an intermediate district and a withdrawing member district cannot agree on the terms and condition of the district's withdrawal, the Commissioner "shall resolve the dispute by determining the district's proportionate share of assets and liabilities based on the district's enrollment, financial contribution, usage, or other factor or combination of factors determined appropriate" by the Commissioner.⁷⁵⁷

94. Pursuant to Minn. R. 1400.7300, subp. 5 (2013), the party proposing that action be taken must prove the facts at issue by a preponderance of the evidence. In addition, a party asserting an affirmative defense shall have the burden of proving the existence of the defense by a preponderance of the evidence.⁷⁵⁸

95. As the party initiating this action through its withdrawal from the Intermediate District, Bloomington has the burden to establish, by a preponderance of the evidence, the amount of its proportionate share of the assets it claims to be owed from the Intermediate District, less its proportionate share of liabilities owed to the District, based upon Bloomington's enrollment, financial contribution, usage, and other factors.⁷⁵⁹

96. As set forth above, Bloomington has established by a preponderance of the evidence that the District's assets exceed its liabilities and that Bloomington is entitled to a proportionate share of those assets.

97. Bloomington has further established by a preponderance of the evidence that its proportionate share of the District's assets and liabilities is 6.52 percent, representing the percentage of Bloomington students enrolled in the Intermediate District programs in the 2010-2011 school year, the last school year in which Bloomington was a Member District.

98. The 6.52 percent multiplier is representative of Bloomington's enrollment in the District and its usage of all of the District's services in the year immediately preceding withdrawal. As a result, it is consistent with the factors that the Commissioner must apply

⁷⁵⁶ See Exs. 18, 18B, 18D, 23, 108; Ex. 103 at Table 2.

⁷⁵⁷ Minn. Stat. § 123A.24, subd.1(c).

⁷⁵⁸ Minn. R. 1400.7300, subp. 5.

⁷⁵⁹ Minn. Stat. § 123A.24, subd. 1(c); Minn. R. 1400.7300, subp. 5; see also Order Allocating Burdens of Proof dated February 10, 2014.

when determining a withdrawing district's proportionate share of an intermediate district's assets and liabilities under Minn. Stat. § 123A.24, subp. 5(c).

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FINAL RECONCILIATION AND DECISION

99. The following represents the Administrative Law Judge's final reconciliation of the Intermediate District's assets and liabilities to be allocated and Bloomington's proportionate share thereof:

ASSETS TO BE DISBURSED	
	Value as of June 30, 2011
Cash and Investments	\$3,764,135.00
Accounts and Interest Receivable	\$588,985.00 ⁷⁶⁰
Due from other units	\$22,544,726.00
Inventory	\$1,850.00
Prepaid Items	\$113,611.00
Restricted cash/invest.	\$0
Real Estate:	
South Educ. Center	\$0
West Educ. Center	\$10,000.00
District Service Center	\$3,000,000.00
Edgewood Educ. Center	\$0
Robbinsdale Condo	\$50,000.00
North Educ. Center (Construction in Progress)	\$0
Other Capital Leases:	
Equipment (\$2,823,913.00), less depreciation of \$2,256,894.00	\$567,019.00
Assets under Cap Lease	\$1,820,432.00
SUBTOTAL:	\$32,460,758.00

⁷⁶⁰ This amount excludes \$39,746.00 in accrued interest on the NEC Trust Fund. See Ex. 108 at 18-19.

LIABILITIES TO BE ALLOCATED	Owing as of June 30, 2011
Aid Anticipation Cert.	\$3,590,000.00
Salaries and Comp.	\$2,157,696.00
Accts and Contracts Payable	\$858,451.00 ⁷⁶¹
Due to other Govt Units	\$2,124,866.00
Unearned Revenue	\$7,231,493.00
Accrued Interest ⁷⁶²	\$706,489.00
Unamortized Premiums	\$0
Capital Leases:	
North Vector	\$76,600.00
Technology	\$450,064.00
Real Estate Leases	
SEC Building Lease	\$0
WEC Refunding Lease COP 2009A	\$0
SEC Land Lease COP 2010C	\$0
EEC Lease COP 2010A	\$0
EEC Lease COP 2010B	\$0
NEC Building Lease COP 2010E	\$0
NEC Land Lease COP 2011A	\$0
Premium on Liabilities	\$96,177.00
Deferred Charges on Liabilities Issued	(\$1,272,335.00)
Long Term EE Costs	
Severance Payable	\$4,731,848.00
Compensated Absences	\$375,937.00
Net OPEB Obligation	\$9,532,459.00
Net Pension	\$409,117.00

⁷⁶¹ This amount reflects the exclusion of \$1,627,047.00 due as of June 30, 2011, to be paid toward the construction of the NEC Property for which Bloomington is not responsible [\$2,945,498.00 - \$1,627,047.00 = \$858,451.00]. See Ex. 108 at 18-19.

⁷⁶² It is unclear in the hearing record from what source(s) this interest accrued. Therefore, because it is undisputed, it remains as a liability to be allocated to Bloomington.

LIABILITIES TO BE ALLOCATED	Owing as of June 30, 2011
SUBTOTAL	\$31,068,862

Assets	Less Liabilities	= Net Assets	Multiplied by Bloomington's Proportionate Share	TOTAL
\$32,460,758.00	\$31,068,862.00	\$1,391,896.00	.0652 (6.52%)	\$90,751.00

Distribution to Minimize Financial Disruption

100. Minnesota Statutes, section 123A.24, subdivision 1(c), provides that the Intermediate District's assets must be disbursed to Bloomington in a manner that minimizes financial disruption to the Intermediate District.

101. As the party proposing that certain action be taken, Bloomington carries the burden to establish, by a preponderance of the evidence, that a disbursement of assets to Bloomington will not impose a financial disruption to the Intermediate District.⁷⁶³

102. The evidence does not establish that requiring the Intermediate District to pay Bloomington a sum of \$90,751.00 will cause significant financial disruption to the District, given the District's net worth.

103. Accordingly, the Intermediate District shall pay Bloomington **\$90,751.00**, representing Bloomington's fair and proportionate share of the Intermediate District's net assets as of June 30, 2011.

104. Minnesota Statutes, section 123A.24, subdivision 1(c), gives the Commissioner discretion to disburse assets and allocate liabilities in a manner that is just and reasonable based upon the withdrawing district's enrollment, financial contribution, usage, *or any other factor or combination of factors determined appropriate by the Commissioner.*⁷⁶⁴

105. All or a portion of Bloomington's share of the District's net assets may be paid by the Intermediate District to Bloomington in the form of non-member tuition credits for Bloomington students to enroll in the Intermediate District, as determined by the parties.

106. The parties are directed to agree to a payment schedule that minimizes financial disruption to the Intermediate District and its remaining Member Districts.

107. If the parties are unable to agree to a payment schedule by **July 15, 2015**, the Administrative Law Judge shall determine the payment schedule, payment type, and

⁷⁶³ See Minn. Stat. § 123A.24, subd. 1(c); Minn. R. 1400.7300, subp. 5.

⁷⁶⁴ Emphasis added.

the amount of interest, if any, to be applied to the balance owed, after allowing additional written argument by the parties.

Dated: June 29, 2015

s/Ann C. O'Reilly

ANN C. O'REILLY
Administrative Law Judge

Reported: Digitally Recorded; Transcript Prepared

NOTICE

Pursuant to Minn. Stat. § 14.57(a), the Commissioner of the Department of Education has, by Order dated October 20, 2013, declared that the Report of the Administrative Law Judge in this proceeding constitutes the final decision in the case.

MEMORANDUM

Intermediate school districts provide complex and critical education services to students that independent school districts generally cannot replicate in a cost-effective manner on their own. It is important to note that Bloomington was one of the highest users of the Intermediate District's services during the 40+ years that the District has been in existence. Throughout that time, Bloomington received the benefits of the joint endeavor, as well as decades of labor and services from the District's employees.

During Bloomington's years as an active participant in the Intermediate District, the District entered into numerous contracts to acquire interests in six real properties. In the course of just seven years, from 2004 to 2011, the Intermediate District executed contracts for over \$149,515,000.00 in real estate. This is a significant amount of real estate investment for an intermediate district that has no taxing or levying authority, and no obligation to seek voter approval for such acquisitions and expenditures.

With the exception of the NEC Property, Bloomington fully supported the District's execution of the contractual agreements to acquire a legal interest in the properties. Now, as a result of Bloomington's withdrawal, the remaining 12 Member Districts must shoulder a greater share of the District's yearly expenses and contractual obligations unless they decide to discontinue appropriations for the leases. This presents a significant dilemma and financial burden to the remaining Member Districts – a burden not anticipated by the Member Districts when the majority of the real estate contracts were executed.

Given Bloomington's contribution to the Intermediate District's financial predicament, it is reasonable to allow the Intermediate District to pay Bloomington a majority of its share of the District's net assets through the use of tuition credits. The parties are directed to agree to a repayment plan that is agreeable to both parties. If the parties are unable to agree to a reasonable repayment plan by June 1, 2015, the Administrative Law Judge will issue a final order directing the type and amount of repayment, including interest.

Finally, while the Intermediate District would prefer that the Administrative Law Judge create a "repeatable" withdrawal plan for the District and its remaining Members, the issue in this case is specific to Bloomington's withdrawal and the unique circumstances surrounding Bloomington's departure at a critical time in the District's expansion.

The type of "buy out" plan that the Intermediate District seeks can only be created through contract or statute, not a decision of the Commissioner or an Administrative Law Judge in this proceeding. As this case demonstrates, the withdrawal of a member from a collective, like any corporate buy-out or dissolution, can be complicated, time-consuming, and, most of all, costly for all parties involved. The Intermediate District and its Members are well advised to devise buy-in and buy-out agreements before any other Members join or withdraw from the collective.

The Administrative Law Judge has gone to great lengths to thoroughly address all legal issues, facts, and laws applicable to Bloomington's withdrawal so that the Intermediate District and its remaining Members can thoroughly evaluate these issues and develop contractual agreements to avoid future litigation or hardship to any party. While neither party may be satisfied with the result in this case, it is the responsibility of the Intermediate District and its Members, or the lawmakers of this State, to write the final chapter of this complicated saga.

Finally, the Administrative Law Judge expressly incorporates the Order Partially Granting and Partially Denying the Intermediate District's Motion for Reconsideration and Denying Bloomington's Motion for Reconsideration into these Amended Findings of Fact, Conclusions of Law, and Decision.

A. C. O.