



OFFICE OF THE
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TO: **Mayor Jordan**
City Council

CC: **Susan Norton**, Chief of Staff
Paul Becker, Chief Financial Officer
Jonathan Curth, Development Services Director

FROM: **Kit Williams**, City Attorney

A handwritten signature in blue ink, appearing to read "Kit Williams", with a horizontal line underneath.

DATE: **June 7, 2022**

RE: TheatreSquared's Attorney's Response to my legal and constitutional concerns about their requested second amendment of its June 2016 Lease with the City

Yesterday I was provided Cliff McKinney's four-page memo questioning my concerns about the legality and constitutionality of the lease amendment sought by TheatreSquared (T2). Mr. McKinney as a well respected and knowledgeable real estate attorney who should be commended for volunteering his time and effort to assist T2 for the last several years on legal matters concerning this lease Agreement.

Constitutional Danger

However, municipal law and Arkansas Constitutional prohibitions and requirements for cities are specialized areas of the law with which most private lawyers are not very familiar. This unfamiliarity can sometimes cause confusion. For example, Mr. McKinney claims in his memo supplied to us that my analysis of Arkansas Constitution, Article 12, §5 "is in error," because that provision was amended by Amendment 82 which "states 'Infrastructure needs may include, but *are not limited to*: . . . ' (McKinney's emphasis) and then enumerates the list which the City Attorney referenced. The legislature clearly did not intend for this to be an exhaustive list." McKinney's memo

That is factually incorrect regarding application of Article 12 § 5's prohibition. Mr. McKinney mistakenly quoted from the wrong Arkansas Constitutional provision (Amendment 82) which is entitled: "**Issuance of general obligation bonds**" to find his "but are not limited to" language which is found nowhere within Article 12 § 5. A quick scan of the title of Amendment 82 (to which I had never referred) and its language would reveal that Amendment 82 has nothing to do with cities or with appropriating city taxpayer funds. Rather, Amendment concerns only **state issued bonds**. Amendment 82 empowers the legislature to "authorize the Arkansas Development Finance Authority to issue general obligation bonds to finance infrastructure or other needs to attract large development projects." It has no application or relevance to Article 12 § 5 or cities and the prohibition of appropriating city taxpayer money for corporations, even nonprofit corporations.

As I properly and correctly informed you in my memo of May 25th, Arkansas Constitution, Article 12, §5 prohibits cities from obtaining or appropriating money except for certain expressly listed economic development projects. Since theater infrastructure or services are not within that list, they remain within the Constitutional prohibition: "No county, city. . .shall. . .obtain or appropriate money for. . .any corporation. . . ." Fayetteville's violation of that prohibition would constitute an illegal exaction that could cost our taxpayers millions of dollars just as Fayetteville suffered in the early 90's after legal mistakes by my predecessors.

I have worked carefully these last two decades as Fayetteville City Attorney to avoid the illegal exaction problems of the past by warning our City Council when a popular idea was so legally or constitutionally iffy that it constituted a danger of a substantial loss of taxpayer funds if we would be sued. Those few times that I have had to issue a strong warning were thankfully always heeded by a City Council who honored their fiduciary duty to protect our taxpayers' money even if there might have been strong support to take a chance.

Valid, Adequate, Fair, and Equitable Consideration Required

Another legal and practical difference between municipal governments and private persons or business is how the "consideration" needed for a valid contract would be measured. "Consideration" in the legal sense means what one party to the contract promises, pays, or furnishes to the other party for what that party promises, pays, or furnishes in return. There are obviously far more contracts between private parties than contracts in which the government is a

party. Thus, private attorneys generally work with and litigate about contracts between two private parties. They know that Courts do not usually weigh the value of the consideration in private party contracts with which private attorneys are most familiar. Private attorneys are probably aware that inadequacy of consideration in a private parties' contract is not a concern.

"Mere inadequacy of consideration will not void a contract. It has been said that adequacy is a matter for the parties to consider at the time the contract is made, and not for the courts at the time it is sought to be enforced." *Landmark Savings Bank v. Weaver-Bailey Construction*, 293 Ark 545, 739 S.W. 2d 166,169 (Ark. App. 1987)

"Consideration is not insufficient merely because it is inadequate." *Stewart v. Combs*, 368 Ark. 121, 243 S.W. 2d 294, 299 (2006).

So how can I say that this proposed amendment to the Lease Agreement must be supported by adequate, fair and equitable consideration to be valid? The Arkansas Attorney General and courts along with the Arkansas Constitution place additional limits on the power and authority of cities to make contracts.

"(N)othing in the constitution precludes the county (another local government covered in Article 12 § 5) from contracting with a private nonprofit charity, so long as the contract is supported by **adequate consideration**" Arkansas Attorney General Opinion No. 2001 -135 (Citing other Attorney General Opinions and Court cases.) The Arkansas Supreme Court while interpreting Article 12 § 5 held:

"This section of our Constitution was not meant to apply as a limitation on the ability of the municipal corporation to acquire private property for a public purpose in exchange for **fair and equitable consideration.**" *City of Fort Smith v. Bates*, 260 Ark. 777, 544 S.W. 2d 523, 527 (1976) (emphasis added).

So why must cities receive fair, adequate and equitable consideration for a contract to be valid when private persons or businesses do not? It may be to protect the taxpayers. This may be the same reason why cities are constitutionally prohibited from just giving away taxpayer dollars to a "corporation, association, institution or individual." (Article 12 § 5) When a person makes a contract, it is the person's own money that is at risk and might be wasted if there is inequitable and inadequate consideration. When a city makes a contract, it would be the taxpayers' money that would be at risk and could be

wasted if the consideration was not adequate, fair and equitable. The people enacting the Arkansas Constitution and our Judges evidently believed that constitutional and legal protections may sometimes be necessary to prevent government officials who might otherwise be too generous with the taxpayers' money. The local governments have at least some fiduciary duty to preserve and conserve the taxpayers' money. This may be part of the reason that the people enacted Article 12 § 5 into the Constitution and why the Courts require fair, adequate, and equitable consideration to support a city contract.

The Proposed Amendment Endangers The Whole Lease Agreement

Mr. McKinney cites that the lease provision that states: "As a primary consideration to support the Lease Agreement, TheatreSquared, Inc. agrees it will fund raise and construct a major theatrical performance facility on the Premises." I agree that this is a very important part of the overall consideration to support the 100 year lease in two ways. First, the City needed assurance that this very valuable acre lot would not lie useless and unused if TheatreSquared failed to secure sufficient funding to build their project. Attorneys should protect their clients from worst case scenarios like that.

Secondly, although the City legally owns the land and thus, the building, the City has no right to use or otherwise enjoy any other normal possessory rights of the building during the century long lease term. The major consideration for our taxpayers of this provision would be the City's future full possessory rights in 100 years to possess, use and control this still functional and well-maintained building. The City was assured this theater building and grounds would be in good condition because TheatreSquared, Inc. in the Lease Agreement had twice promised to maintain and repair the building throughout this entire lease term of 100 years. Without such promise of proper repair and maintenance of the theater building throughout the 100 year term, the City's future possessory rights of a potentially dilapidated 100 year building with failing mechanical systems would have little, if any, value for our citizens. That is why TheatreSquared's promises to maintain and repair their building during the entire lease term is vital to the consideration supporting this 100 year Lease Agreement.

Must be new consideration to support Amendment

The first place in the Lease Agreement for this promise was in Paragraph (8) **Maintenance by TheatreSquared, Inc.** "TheatreSquared, Inc. shall at its sole cost, risk and expense: (i) maintain the Premises in good condition and repair. . (ii) keep the Premises in a clean, safe and sanitary condition; (iii) make, or cause

to be made, all necessary repairs, whether interior, exterior or structural, on the Premises and (iv) provide for the reasonable care, landscaping and cleaning of the Premises." This maintenance promise is also part of Paragraph (3) Rental and clearly explains what the "maintain" means in the Representations and Warranties of TheatreSquared, Inc. below.

"(3) Rental.

As primary rental for the Premises, TheatreSquared, Inc. agrees to faithfully perform all of the Representations and Warranties of TheatreSquared, Inc. contained in Paragraph 36 of this Lease Agreement."

"(36) Representations and Warranties of TheatreSquared, Inc. TheatreSquared, Inc. hereby covenants and warrants to the City of Fayetteville that:

...

(C) At all times during Term, TheatreSquared shall operate, manage and **maintain the Premises** at the corner of West Avenue and Spring Street in Fayetteville, Arkansas competently"

It cannot be disputed that TheatreSquared covenanted to the City and our citizens to faithfully maintain its building competently at all times during the 100 year term of the Lease Agreement. Maintenance was spelled out as one of its three covenanted duties, along with operating and managing the theater. Shifting probably the most expensive duty that TheatreSquared had promised to accomplish in its Warranties and forcing Fayetteville taxpayers to assume the maintenance and repair expenses strikes at the heart of this Lease Agreement.

Mr. McKinney points to the large investment made into the theater building and claims it "constitutes significantly more consideration on the part of TheatreSquared than the mere maintenance and upkeep of the aforementioned building." What Mr. McKinney ignores is that the Lease Agreement required both the construction and 100 years of maintenance and repair. TheatreSquared promised the City Council and our citizens it would both build and maintain the theater building. As to the costs "of mere maintenance" (which clearly includes all repairs pursuant to the Lease Agreement), we should remember that after three decades of service, the Walton Arts Center's necessary rehabilitation and enhancement project (on the same lot) cost many millions of dollars, maybe even more than its initial construction cost. With this lease term extending not three decades but ten, the future costs to our taxpayers of shifting the maintenance and repairs expenses that TheatreSquared had promised to pay would cost our

citizens many millions of dollars during the term of this 100 year lease. I do not believe that there is fair, equitable, and adequate consideration to support such a major expense shift caused by the proposed amendment to the Lease Agreement.

Mr. McKinney argues that TheatreSquared's proposed amendment which would agree to present the same quantity of performances as presented in 2019 instead of 2015 would be a substantial increase of consideration. This claimed 30% increase in the number of performances cannot support the massive expenses shifted to the taxpayers in the amendment. When weighed against the millions of dollars that Fayetteville's taxpayers would have to pay for the amendment's changes, a small increase in performances is insignificant as consideration for our taxpayers. He also claims higher attendance and staffing are additional considerations to support the Amendment even though neither party considered them as any consideration at all in the lease and did not even mention either attendance, staffing, or estimated economic impact in the Lease Agreement or their proposed Amendment. Therefore, these are not proper subjects to even be considered by the City Council as potential considerations.

Conclusion

Fayetteville is lucky that the Executive Director, Artistic Director, and Board of Directors of TheatreSquared, Inc. had the vision and determination to grow this local theater group and then secure grants and other assistance to be able to build an outstanding theater facility in Fayetteville's Entertainment District. Mayor Jordan and the City Council were right to provide the requested 100 year Lease of an acre parking lot for no cash payment to the City. The Mayor and City Council were wise to invest \$3.1 Million into this building even though the City would have no possessory rights for a century.

The Lease Agreement, even with no cash payments to the City, and the Three Million One Hundred Thousand Dollar investment into TheatreSquared's building, are legal and constitutional because all of the Lease Agreement's provisions work together to ensure Fayetteville taxpayers are receiving fair, equitable, and adequate consideration. Yanking three important financial supports: maintenance and repair; building insurance, and most utility payments; from the legal considerations supporting the \$3.1 Million investment and this Lease Agreement would endanger the entire lease. As City Attorney, I cannot recommend passing the Resolution to adopt Lease Agreement No. 2 as presented by TheatreSquared, Inc.