

ORIGINAL

IN THE SUPREME COURT OF OHIO

Hope Academy Broadway Campus, et al.,	:	
	:	Case No. 2013-2050
Appellants,	:	
	:	On Appeal from the Franklin County
v.	:	Court of Appeals, Tenth Appellate
	:	District
White Hat Management, LLC, et al.,	:	
	:	
Appellees.	:	

REPLY BRIEF OF APPELLANTS HOPE ACADEMY BROADWAY CAMPUS, ET AL.¹

Karen S. Hockstad (0061308)
Counsel of Record
 Gregory P. Mathews (0078276)
 DINSMORE & SHOHL LLP
 191 W. Nationwide Blvd., Suite 300
 Columbus, Ohio 43215
 (614) 628-6930 (telephone)
 (614) 628-6890 (facsimile)
 karen.hockstad@dinsmore.com
 gregory.mathews@dinsmore.com

James D. Colner (0012376)
 Adam M. Galat (0081068)
 SHUMAKER, LOOP & KENDRICK, LLP
 41 South High Street, Suite 2400
 Columbus, Ohio 43215
 (614) 628-4459 (telephone)
 (614) 463-1108 (facsimile)
 jcolner@slk-law.com
 agalat@slk-law.com
*Counsel for Appellants Hope Academy
 Broadway Campus, et al.*

C. David Paragas (0043908)
 Kevin R. McDermott (0019256)
 Amy Ruth Ita (0074520)
 BARNES & THORNBURG, LLP
 41 South High Street, Suite 3300
 Columbus, Ohio 43215
 (614) 628-0096 (telephone)
 (614) 628-1433 (facsimile)
 dparagas@btlaw.com
 kmcdermott@btlaw.com
 aita@btlaw.com
*Counsel for Appellees White Hat
 Management, LLC, et al.*
 Todd Marti, Esq. (0019280)
 Assistant Attorney General
 30 East Broad Street, 17th Floor
 Columbus, Ohio 43215
 (614) 644-7250 (telephone)
 (866) 524-1226 (facsimile)
 Todd.marti@ohioattorneygeneral.gov
Counsel for Ohio Department of Educ.

¹ Appellants include Hope Academy Broadway Campus (in receivership); Hope Academy Cathedral Campus (in receivership); Hope Academy Lincoln Park Campus, n/k/a Lincoln Prep; Hope Academy Chapelside Campus, n/k/a Green Inspiration Academy; Hope Academy University Campus, n/k/a Middlebury; Hope Academy Brown Street Campus, n/k/a Colonial Prep; Life Skills Center of Cleveland, n/k/a Invictus; Life Skills Center of Akron, n/k/a Towpath; Hope Academy West Campus, n/k/a West Prep; and Life Skills Center Lake Erie, n/k/a Lake Erie International.

FILED
 AUG 25 2014
 CLERK OF COURT
 SUPREME COURT OF OHIO

Table of Contents

Table of Authorities	iii
Introduction.....	1
Argument	2
I. This appeal is not moot because property ownership must be determined to resolve the Schools’ breach-of-contract claims.....	2
II. Public funds do not immediately lose their public nature once transferred to White Hat because White Hat has to use the funds to carry out a government function and purchase property on behalf of the Schools.	4
A. In <i>Oriana House</i> , the Court recognized that public funds do not immediately lose their public nature.	4
B. The Schools’ first proposition narrowly resolves the public-funds question without altering contractual rights or obligations.	6
C. The Schools’ first proposition is not “unworkable.”	8
D. The Schools did not waive the arguments presented in their first proposition.	10
III. Funding from the Ohio Department of Education, by its nature, requires personal property to be titled in the name of a public school.	10
A. The management agreements determine ownership of personal property based on “the nature of the funding source.”	10
B. The Schools’ second proposition is not overly broad.	12
IV. White Hat owes a fiduciary duty to the Schools because it is a public official that operates the Schools as their duly authorized representative and agent.	13
A. White Hat became an agent and fiduciary based on the nature of its undertaking.	13
B. White Hat is a public official.	16
Conclusion	19
Proof of Service	21

Table of Authorities

Cases

<i>Abrams v. Worthington</i> , 169 Ohio App.3d 94, 2006-Ohio-5516, 861 N.E.2d 920 (10th Dist.).....	14
<i>Aultman Hosp. Assn. v. Community Mut. Ins. Co.</i> , 46 Ohio St.3d 51, 544 N.E.2d 920 (1989).....	1
<i>Berge v. Columbus Community Cable Access</i> , 136 Ohio App.3d 281, 736 N.E.2d 517 (10th Dist. 1999).....	15
<i>Cincinnati Golf Management v. Testa</i> , 132 Ohio St.3d 299, 2012-Ohio-2846, 971 N.E.2d 929.....	14, 16
<i>Cordray v. Internatl. Preparatory Sch.</i> , 128 Ohio St.3d 50, 2010-Ohio-6136, 941 N.E.2d 1170.....	16, 18, 19
<i>Cristino v. Bur. of Workers' Comp.</i> , 10th Dist. Franklin No. 12AP-60, 2012-Ohio-4420.....	17
<i>Eyerman v. May Kay Cosmetics, Inc.</i> , 967 F.2d 213 (6th Cir. 1992).....	14
<i>First Bank of Marietta v. Mascrate</i> , 79 Ohio St.3d 503, 684 N.E.2d 38 (1997).....	18
<i>Grigsby v. O.K. Travel</i> , 118 Ohio App.3d 671, 693 N.E.2d 1142 (1st. Dist. 1997).....	14
<i>Guth v. Allied Home Mtge. Capital Corp.</i> , 12th Dist. Clermont No. CA2007-02-029, 2008-Ohio-3386.....	15
<i>Haluka v. Baker</i> , 66 Ohio App. 308, 34 N.E.2d 68 (9th Dist. 1941).....	13
<i>Hartong v. Makary</i> , 106 Ohio App.3d 145, 665 N.E.2d 704 (9th Dist. 1995).....	11
<i>Hope Academy Broadway Campus v. White Hat Mgt., LLC</i> , 10th Dist. Franklin No. 12AP-496, 2013-Ohio-5036.....	5, 8
<i>In re Appeal of Suspension of Huffer from Circleville High School</i> , 47 Ohio St.3d 12, 546 N.E.2d 1308 (1989).....	3
<i>Oriana House, Inc. v. Montgomery</i> , 108 Ohio St.3d 419, 2006-Ohio-1325, 844 N.E.2d 323.....	4, 5

<i>Paterson v. Equity Trust Co.</i> , 11th Dist. Lorain No. 11CA009993, 2012-Ohio-860.....	15
<i>Queen City Terminals, Inc. v. Gen. Am. Transp. Corp.</i> , 73 Ohio St.3d 609, 653 N.E.2d 661 (1995).....	10
<i>Riester v. Riverside Community Sch.</i> , 257 F.Supp.2d 968 (S.D. Ohio 2002).....	6, 16
<i>Seringetti Constr. Co. v. Cincinnati</i> , 51 Ohio App.3d 1, 553 N.E.2d 1371 (1st Dist. 1988).....	11
<i>State v. McKelvey</i> , 12 Ohio St.2d 92, 232 N.E.2d 391 (1967).....	17
<i>State ex rel. Linndale v. Masten</i> , 18 Ohio St.3d 228, 480 N.E.2d 777 (1985).....	1, 4
<i>State ex rel. Oriana House, Inc. v. Montgomery</i> , 110 Ohio St.3d 456, 2006-Ohio-4854, 854 N.E.2d 193.....	5, 6
<i>State ex rel. Smith v. Maharry</i> , 97 Ohio St. 272, 119 N.E. 822 (1918).....	4, 11, 12
<i>State ex rel. Yovich v. Bd. of Edn. of Cuyahoga Falls City School Dist.</i> , 10th Dist. Franklin No. 91AP-1325, 1992 Ohio App. LEXIS 3323 (June 23, 1992).....	7, 8
<i>Strock v. Pressnell</i> , 38 Ohio St.3d 207, 527 N.E.2d 1235 (1988).....	1, 13

Statutes

R.C. 117.01	16, 18, 19
R.C. 117.10	4, 17, 18
R.C. 149.43	5
R.C. 3314.024	1, 17, 18
R.C. 3314.04	1, 2
R.C. 3314.074	13
R.C. 3314.08	13

Other Sources

1 Restatement of the Law 2d, Agency, Section 13 (1958) 14

Restatement of the Law 3d, Agency, Section 1.01 (2006) 14, 16

Restatement of the Law 3d, Agency, Section 1.02 (2006) 14

Restatement of the Law 3d, Agency, Section 8.01 (2006) 14

Introduction

The practical issue in this appeal is whether the management agreements require White Hat to serve as purchasing agent for the Schools when it buys personal property with Ohio Department of Education funds. Answering this question depends on the nature of Ohio Department of Education funds, particularly when they are in White Hat's hands. The answer also depends on the obligations White Hat has as a community-school operator. The Schools' propositions of law provide the framework necessary to resolve these issues by accounting for White Hat's public role and parsing its obligations consistently with existing Ohio law. White Hat and the amici curiae respond with hyperbole and mischaracterizations of the Schools' arguments. Three arguments pervade their briefs, but none has substance.

First, White Hat relies on R.C. 3314.024 and 3314.04 to argue that the General Assembly exempted community-school operators from public accountability, except for certain accounting they provide community schools when they receive more than 20 percent of a school's annual gross revenues. White Hat argues that it is governed by its own set of laws and that generally-applicable laws do not apply to it. To the contrary, the General Assembly has not foreclosed the application of longstanding Ohio law to community-school operators. The Court's acceptance of the Schools' position would not supplant the General Assembly because the Schools' propositions are not legislative in nature. The Schools ask the Court to apply the law concerning public funds, contract interpretation, and fiduciaries, areas traditionally in the province of courts. *See State ex rel. Linndale v. Masten*, 18 Ohio St.3d 228, 229, 480 N.E.2d 777 (1985) (public funds); *Aultman Hosp. Assn. v. Community Mut. Ins. Co.*, 46 Ohio St.3d 51, 53, 544 N.E.2d 920 (1989) (contract interpretation); *Strock v. Pressnell*, 38 Ohio St.3d 207, 216, 527 N.E.2d 1235 (1988) (fiduciary duties). In seeking to avoid the legal duties that ordinarily accompany the receipt and handling of public funds, White Hat fails to explain why these generally-applicable

laws do not apply. Although R.C. 3314.04 provides that “state laws and rules pertaining to schools, school districts, and boards of education” generally do not apply to community schools, it does not exempt community schools or their operators from all laws except R.C. Chapter 3314. The Court should reject White Hat’s argument that adoption of the Schools’ propositions of law would invade the province of the legislature.

Second, White Hat repeatedly argues that the Schools’ propositions threaten freedom-of-contract principles. Yet White Hat fails to explain how its freedom is threatened. The Schools seek only to enforce the parties’ written agreements and ask the Court to give meaning to the purchasing-agent provision. White Hat steadfastly ignores the significance of that provision.

Third, White Hat argues that the Court must rule in its favor because it took financial risk before the Schools opened. The Court should reject White Hat’s invitation to construe the management agreements in its favor simply because it took some financial risk in becoming a community-school operator. White Hat bargained for the privilege of engaging in an exclusive money-making enterprise. Yes, White Hat took some risk, but it was a risk White Hat took based on its hope of becoming profitable in the long term. Financial risk taking never has been a means of contract interpretation, and it should not become one here. White Hat is not entitled to favorable legal conclusions merely because it took some financial risk. It is not the role of courts to ensure that a party’s risk was worth taking.

Argument

I. This appeal is not moot because property ownership must be determined to resolve the Schools’ breach-of-contract claims.

White Hat argues that the appeal is moot based on the parties’ actions after this lawsuit began. The claims are not moot, but even if the Court were to conclude they are, that conclusion would not prevent it from deciding this appeal. “[I]f a case involves a matter of public or great

general interest, the court is vested with the jurisdiction to hear the appeal, even though the case is moot.” *In re Appeal of Suspension of Huffer from Circleville High School*, 47 Ohio St.3d 12, 14, 546 N.E.2d 1308 (1989). But it is unnecessary for the Court to invoke this rule here, because the parties still dispute whether White Hat properly titled personal property in its own name.

White Hat first argues that the interim management agreements, which pertain to five of the Schools, nullify their claims related to personal property. This argument mischaracterizes the substance of those agreements, which addressed the terms under which the parties were to operate during the 2012–2013 school year. The agreements expressly preserved the Schools’ claims: the parties “expressly agree[d] that nothing in this agreement in any way prejudices their respective claims and defenses in the Case.” (Interim Management Agreement at § 31) The Schools relinquished their right to *possess* the property at issue but did not release their damage claims. White Hat’s position wrongly assumes that the Schools’ only remedy is replevin.

Furthermore, by citing section 7(b) of the agreements, White Hat misrepresents the significance of that provision in relation to this litigation. Section 7(b) relates to the payment of costs by White Hat during the term of the interim management agreements (i.e., July 2012 through June 2013). During that period, the parties modified their purchasing arrangement to include a grant-funds distinction that was not included in the original management agreements. (*See* Interim Management Agreement at § 4.) Section 7(b) has nothing to do with previously-acquired property, which is the subject of this lawsuit. To accept White Hat’s reading of the agreements, the Court would have to assume the Schools did not intend to preserve their claims, contrary to the express language they used.

White Hat also points to the fact that the remaining schools never “invoked the provisions of the original Management Agreements regarding the purchase of personal property upon their

expiration.” (White Hat Brief at 9) White Hat suggests that the appeal is moot as to these schools because they did not elect to pay White Hat the “remaining cost basis” of property pursuant to section 8.a.i. of the management agreements. This argument ignores the Schools’ claim that they rightfully own the property already and are entitled to damages for White Hat’s breach. That dispute is the very foundation of this appeal.

The appeal is not moot. The parties continue to dispute whether White Hat rightfully titled property in its own name. Although the Schools do not seek to acquire possession of the property itself, they are entitled to damages. White Hat made this same mootness argument to the court of appeals, and that court properly disregarded it. This Court should do the same.

II. Public funds do not immediately lose their public nature once transferred to White Hat because White Hat has to use the funds to carry out a government function and purchase property on behalf of the Schools.

A. In *Oriana House*, the Court recognized that public funds do not immediately lose their public nature.

The issue in *Oriana House, Inc. v. Montgomery*, 108 Ohio St.3d 419, 2006-Ohio-1325, 844 N.E.2d 323, was “whether the State Auditor has authority pursuant to R.C. 117.10 to conduct a special audit of appellant Oriana House, Inc., the entity that controls the day-to-day operations of the Summit County Community-Based Correctional Facility.” *Id.* at ¶ 1. The deeper issue was whether Oriana House, under R.C. 117.10(A)(1), “receive[d] public money for [its] use.” *Id.* at ¶ 14. The Court recognized that Oriana House, as an entity that controlled public funds, had “a duty to account for [its] handling of those funds.” *Id.* at ¶ 13, citing *Linndale*, 18 Ohio St.3d at 229, 480 N.E.2d 777 and *State ex rel. Smith v. Maharry*, 97 Ohio St. 272, 276, 119 N.E. 822 (1918). The Court then held that the State Auditor could audit Oriana House because it “receiv[ed] public funds.” *Id.* at ¶ 15.

The necessary predicate for this holding was that the public funds Oriana House received did not immediately lose their public character upon transfer. Contrary to what the court of appeals held, the funds Oriana House received were not “once public funds,” and Oriana House was not free to “decide how and whether to spend the money.” See *Hope Academy Broadway Campus v. White Hat Mgt., LLC*, 10th Dist. Franklin No. 12AP-496, 2013-Ohio-5036, ¶ 24. This Court made clear that certain duties attach to public funds and remain with them even after they are transferred to a private entity carrying out a government function; Oriana House had “a duty to account for [its] handling of those funds” after it received them. *Oriana House* at ¶ 13.

The Court could not have reached its holding without first concluding that public money remained public even after Oriana House received it. Although the ultimate issue in *Oriana House* was whether a private entity carrying out a government function was subject to state audit, the Court held that an audit was appropriate only because it first determined that the private entity had received and was handling public funds. *Id.* at ¶ 13-15. *Oriana House* provides clear guidance for this Court in determining whether White Hat receives and handles public funds.

White Hat also complains that the Schools did not reference the public-records case involving Oriana House, *State ex rel. Oriana House, Inc. v. Montgomery*, 110 Ohio St.3d 456, 2006-Ohio-4854, 854 N.E.2d 193. The Schools did not discuss that case because it has no bearing on this appeal. The issue in the public-records case was whether Oriana House was a “public office” under the Public Records Act. *Id.* at ¶ 16. The public-records case involved an effort to make Oriana House’s internal records available to the general public and depended on a finding that it was a “public institution” and thus a “public office” under R.C. 149.43(A)(1). The Court adopted the functional-equivalency test, identifying four factors to consider. *Id.* at ¶ 25. One factor is the level of government funding the entity receives, and that factor weighed in

favor of Oriana House being a public institution. *Id.* at ¶ 25, 32. The public-records case did not involve questions about the nature of the funds Oriana House handled, and it did not alter the Court's prior analysis on that issue.

B. The Schools' first proposition narrowly resolves the public-funds question without altering contractual rights or obligations.

Insisting it is just an ordinary service provider, White Hat contends that the Schools' first proposition of law imposes unjustifiable public scrutiny on its use of taxpayer funds. White Hat ignores two limiting factors that narrowly tailor the first proposition. First, the proposition pertains only to "a private entity exercising a government function." White Hat, of course, is not an ordinary service provider, such as a janitorial- or food-service provider. White Hat carries out a government function by operating public schools. In a case involving another community school operated by White Hat, the United States District Court for the Southern District of Ohio found that the White Hat defendants were state actors. *Riester v. Riverside Community Sch.*, 257 F.Supp.2d 968, 972 (S.D. Ohio 2002). The court recognized that "state action is present when government delegates to a private entity functions that are historically and exclusively governmental in nature. The Court agrees with Plaintiff that free, public education, whether provided by public or private actors, is an historical, exclusive, and traditional state function." (Citations omitted.) *Id.* If the Court adopts the Schools' first proposition, it would apply to entities like White Hat that carry out traditional government functions; it would not impact ordinary service providers.

Second, White Hat disregards that the first proposition is tied to an entity's particular contractual obligations. A private entity may earn a profit after it fulfills its contractual and other obligations. In White Hat's case, section 2.b.i. of the management agreements makes it a purchasing agent when the "nature of the funding source" requires it. White Hat must discharge

that duty before it can profit. The agreements earmark the Continuing Fee for certain public purposes. The management agreements require White Hat to expend the Continuing Fee for, among other things, teacher salaries and personal property to be used in the Schools. (Management Agreement at § 8.a.i.) White Hat's complaint that the first proposition would have far-reaching and unintended effects is unfounded because similar contractual obligations would not necessarily exist in every contract. The first proposition accommodates the need for public accountability without imposing new contractual obligations on a private entity.

The Court should not follow *State ex rel. Yovich v. Bd. of Edn. of Cuyahoga Falls City School Dist.*, 10th Dist. Franklin No. 91AP-1325, 1992 Ohio App. LEXIS 3323 (June 23, 1992), because it is factually distinguishable, and its holding forestalls contractual accountability in this case. In *Yovich*, public funds were transferred to a private entity to provide "auxiliary educational services" at a nonpublic school. *Id.* at *1-2. The private entity then hired and paid Yovich to provide psychological services at the school. *Id.* Based on his belief that he was paid with public funds, Yovich argued that the public board of education for the district in which the private school operated was required to make employer contributions to the State Teachers Retirement System. *Id.* at *1, 6-7. Unlike White Hat (which operates all functions of numerous public schools), the private entity in *Yovich* provided a discrete service to a private school. In fact, White Hat must use the Continuing Fee to make contributions to the public retirement systems on behalf of teachers and staff. (See Management Agreement at § 3.e.)

Application of the *Yovich* holding here not only ignores its factual differences but also disregards the contractual, statutory, and fiduciary obligations that accompanied White Hat's receipt of the Continuing Fee. The Continuing Fee does not constitute earned compensation immediately upon transfer; the fee consists of the operational funds White Hat uses to carry out

its duties. The fee must be used for specified public purposes before any part of it can belong to White Hat. The court of appeals disregarded this by applying *Yovich*'s bright-line rule, which allows White Hat to "decide how and whether to spend the money." *Hope Academy*, 2013-Ohio-5036, at ¶ 24. That holding eviscerates White Hat's contractual, statutory, and fiduciary duties.

Regardless of whether White Hat is accountable to the State Auditor or parents, White Hat must remain directly accountable to the parties with whom it contracts. With no sense of irony, two amici argue that the first proposition is unnecessary because the Schools can sue White Hat if it discovers White Hat has breached its duties. (Brief of Summit Academy at 11; Brief of Leadingage Ohio, et al., at 9) They disregard the fact that the Schools did just that and have been disarmed in their efforts to hold White Hat accountable.

C. The Schools' first proposition is not "unworkable."

White Hat also argues that the Schools' first proposition of law is unworkable because, according to White Hat, the Schools then can arbitrarily decide "when (if ever) White Hat may earn the fees for the services it provided." (White Hat Brief at 14) This argument ignores the context in which the public-funds question arises and misconstrues the Schools' proposition.

The court of appeals held that the entire Continuing Fee loses its public nature immediately on transfer to White Hat. The Schools' first proposition addresses this holding by clarifying that the nature of public funds—when paid to a private entity exercising a government function—does not change *immediately* upon transfer. The Schools have explained that the caselaw on which the court of appeals relied is inapplicable, and the better approach is to account for the specific contractual duties undertaken by the private entity and the scope of its public role in general. The second sentence of the first proposition merely accounts for the fact that a private

entity may at some point profit from its undertaking. It clarifies that a community-school operator *can* earn a profit.

The first proposition does not address *when* a private entity earns a profit, because such a rule is unnecessary to resolve this appeal. The dispute here requires the Court to determine the nature of Ohio Department of Education money as a funding source. The Court must decide whether the funds immediately become private once they are transferred, irrespective of the contractual, statutory, and fiduciary obligations attached to the funds. The Schools do not suggest that the Court should—or even could—craft a rule that dictates precisely *when* public funds become private earnings. The Schools certainly do not suggest that they have the right to deem funds to be earned profit or to “claw back” justly earned compensation for services.

These questions will arise just as they have in this case—in the context of a lawsuit where a public entity alleges that a private entity has not fulfilled its contractual, statutory, and fiduciary obligations. A private entity exercising a government function ordinarily will earn its fee when it has money left over after fulfilling its obligations. But if the private entity does not fulfill its obligations (by, for example, failing to use the funds as a purchasing agent on behalf of the public entity), in all likelihood it will be sued, and a court or jury will decide whether it properly used the funds. White Hat’s concern that the first proposition gives the Schools unfettered discretion to dictate White Hat’s earnings rings hollow. Questions of misuse will be decided judicially. The first proposition aims to ensure that private entities exercising a government function are not relieved of their contractual, statutory, and fiduciary obligations simply because they are private.

Similarly unavailing is the argument that the rule would prove unworkable for nonprofit private entities. An amicus argues it never would be able to expend funds because it never would

“earn a profit” as a nonprofit entity. This argument, too, misunderstands the first proposition. As an initial matter, the first proposition does not mandate that any management company—whether for-profit or nonprofit—actually make a profit. It merely acknowledges that profits could result. What is more, the first proposition does not hamstring companies from carrying out contractual obligations; it requires them to fulfill their duties. The amicus argues it never would be able to use funds to purchase assets because it never earns a profit. But under the first proposition, if its agreement required it to acquire property with the funds it receives, it would be permitted (indeed, *required*) to do so. The first proposition expressly requires private entities—including nonprofit ones—to carry out their contractual, statutory, and fiduciary obligations.

D. The Schools did not waive the arguments presented in their first proposition.

White Hat argues that the Schools waived their first proposition because it was not raised as an assignment of error below. This argument ignores the fact that the Schools had no reason to assert error concerning the public nature of the funds because the trial court agreed with the Schools on that issue. (Appendix at A-73.) (“There is no dispute that the personal property at issue was purchased with public funds.”) The Schools’ first proposition responds to the court of appeals holding that Ohio Department of Education funds lost their public character immediately upon transfer to White Hat. In any event, *Queen City Terminals, Inc. v. Gen. Am. Transp. Corp.*, 73 Ohio St.3d 609, 617, 653 N.E.2d 661 (1995), does not support White Hat’s waiver argument because the court of appeals did address the issue.

III. Funding from the Ohio Department of Education, by its nature, requires personal property to be titled in the name of a public school.

A. The management agreements determine ownership of personal property based on “the nature of the funding source.”

Section 2 of the management agreements sets out services White Hat must provide the Schools. Subsection 2.b.i. (subtitled “Equipment”) requires White Hat to serve as the Schools’

purchasing agent, providing that White Hat “shall purchase on behalf of the School any furniture, computers, software, equipment, and other personal property which, by the nature of the funding source, must be titled in the School’s name.” Section 8.a. provides for payment of fees and defines the Continuing Fee as 95 or 96 percent “of the revenue per student received by the School from the State of Ohio Department of Education.” Section 8.a.i. then provides that the Continuing Fee will be used to purchase books, computers, equipment, and other property for use in the Schools. Because 8.a.i. is a subsection of Section 8, it is reasonable to conclude that property used for the operation of the Schools would be purchased with public dollars—i.e., the Continuing Fee. Reading the contract as a whole, the most reasonable interpretation is that White Hat would purchase the property to be used in the operation of the Schools with the Continuing Fee and title the property in the Schools’ name because the public nature of the Continuing Fee requires it. *See Seringetti Constr. Co. v. Cincinnati*, 51 Ohio App.3d 1, 553 N.E.2d 1371 (1st Dist. 1988), paragraph three of the syllabus. (recognizing that contract provisions must be read together to determine the intent of the parties); *Hartong v. Makary*, 106 Ohio App.3d 145, 149, 665 N.E.2d 704 (9th Dist. 1995) (recognizing that contracts must be examined in their entirety).

The management agreements, when read in their entirety, contemplate that funds designated by the Ohio Department of Education for the education of public-school students will be used for the benefit of public schools and not their private operators. This is the most rational interpretation of the agreements. The notion that the Schools would knowingly transfer most of their funds to White Hat so White Hat could buy property for itself (and then later require the Schools to buy the property back with additional public funds) is absurd. The Schools’ interpretation also is consistent with Ohio law. Because the funds are public, “the rights of the public, as beneficiaries, are paramount to those of any private person or corporation.” *Maharry*,

97 Ohio St. at 276, 119 N.E. 822. The Court should apply the terms of 2.b.i.—not in a vacuum as White Hat suggests—but in keeping with *Maharry* and in conjunction with the other provisions in the management agreements.

Although White Hat alleges the Schools seek to rewrite the management agreements and avoid their terms, White Hat itself cannot point to language that supports its reading of section 2.b.i. White Hat contends that the second sentence of 2.b.i. refers only to grant funds, but White Hat cannot show a source for that claim or show how grant funds differ in nature from state funds. White Hat refers to federal Title I and IDEA grants, but section 2.b.i. does not make that distinction. No evidence shows the “terms” of any grant requiring property to be titled in the names of the Schools, and even if evidence did exist, the agreements do not reference “terms” but instead refer to the “nature” of the funds. The grant-funds distinction is a false one.

Grant funds and funds deriving from the Ohio Department of Education have the same “nature.” Both are public. All the public funds are designated for the benefit of public schools. White Hat concedes that property purchased with grant funds must be titled in the names of the Schools because the public nature of those funds demands it. White Hat fails to explain why state funds should not be treated the same.

B. The Schools’ second proposition is not overly broad.

White Hat also argues that it cannot be required to act as purchasing agent for the Schools when using Ohio Department of Education funds because that result would cause “the exception” to “swallow the rule.” (White Hat Brief at 16) White Hat contends that *all* the property it purchases then would be titled in the Schools’ names. This argument misapprehends the scope of the purchasing-agent component of section 2.b.i. and ignores the fact that White Hat may earn a profit (with which it could purchase property in its own name).

Section 2.b.i. does not set forth a “rule” and an “exception,” because it does not provide—or even suggest—that most of White Hat’s purchases should be in White Hat’s own name. White Hat’s ownership of personal property used in the Schools is not the “rule,” and public policy dictates that it should not be the rule. Indeed, R.C. 3314.074 suggests that the opposite is true. That statute provides that if a community school closes, property purchased with state funding would be distributed to other public schools. This is consistent with R.C. 3314.08(C), which provides that funding for community schools comes from public school districts. The General Assembly certainly expected that community schools would own substantial property.

An amicus similarly argues that the Schools’ position would have “no logical limit.” The amicus suggests that the rule would cause a school to own the buses of a transportation provider and the pots and pans of a food vendor. This argument fails to recognize that White Hat expressly agreed to serve as the Schools’ purchasing agent. To use the amicus’s example, a school could acquire pots and pans if a contract provided that a food-service provider would purchase pots and pans on the school’s behalf. The amicus’s analogy falters because this case involves contracts that expressly provide for the service provider to act as purchasing agent. The logical limit is found in the contracts themselves.

IV. White Hat owes a fiduciary duty to the Schools because it is a public official that operates the Schools as their duly authorized representative and agent.

A. White Hat became an agent and fiduciary based on the nature of its undertaking.

A court determines whether a party is a fiduciary by examining the nature of the party’s undertaking; a party is a fiduciary if it agreed to act “primarily for the benefit of another in matters connected with [its] undertaking.” (Emphasis deleted.) *Strock*, 38 Ohio St.3d at 216, 527 N.E.2d 1235, quoting *Haluka v. Baker*, 66 Ohio App. 308, 312, 34 N.E.2d 68 (9th Dist. 1941).

An agency relationship is fiduciary in nature. See *Cincinnati Golf Management v. Testa*, 132 Ohio St.3d 299, 2012-Ohio-2846, 971 N.E.2d 929, ¶ 20; Restatement of the Law 3d, Agency, Section 8.01 (2006). To determine whether agency exists, courts examine the agent’s power to bind the principal, the principal’s right to control the actions of the agent, and the fiduciary nature of the relationship. *Cincinnati Golf* at ¶ 20.

The fundamental elements of agency are the same whether the Court follows the Second Restatement on agency, as many Ohio courts have done, or the Third Restatement. One Ohio court cited both versions in the same opinion, describing a section of the Third Restatement as “[a] more succinct statement” containing the same substantive principles as the second. *Abrams v. Worthington*, 169 Ohio App.3d 94, 2006-Ohio-5516, 861 N.E.2d 920, ¶ 13 (10th Dist.). Like its predecessor, the Third Restatement focuses on the fiduciary nature of the relationship, the agent’s power, and the principal’s right to control. See Restatement 3d, Section 1.01. In any event, a court must “look beyond the agreement to the reality of the relationship between the parties.” *Eyerman v. May Kay Cosmetics, Inc.*, 967 F.2d 213, 219 (6th Cir. 1992). Accord *Grigsby v. O.K. Travel*, 118 Ohio App.3d 671, 675, 693 N.E.2d 1142 (1st. Dist. 1997); Restatement 2d, Section 13, Comment c (“The name which the parties give to the relation is not determinative”); Restatement 3d, Section 1.02, Comment a (“[H]ow the parties to any given relationship label it is not dispositive”).

But White Hat responds by avoiding the reality of the relationship and resting on the label it used. White Hat first misconstrues the Schools’ position by arguing that the Schools cannot unilaterally create a fiduciary relationship. Indeed, an amicus misrepresents the Schools’ position entirely by claiming that the Schools wish to do away with the mutuality requirement altogether. (Ohio Coalition for Quality Education Brief at 19) The Schools argue that “the parties

subjective understandings are irrelevant when an express fiduciary relationship is at issue,” not that the fiduciary relationship need not be mutual. (Emphasis added.) (Schools’ Brief at 18) The Schools never argued that White Hat is a fiduciary based on the Schools’ unilateral understanding of their relationship. The case on which the amicus relies, *Paterson v. Equity Trust Co.*, 11th Dist. Lorain No. 11CA009993, 2012-Ohio-860, actually supports the Schools’ position that the parties’ agreement governs whether they intended a fiduciary relationship. In *Paterson*, the court analyzed the parties’ contract and found it twice disclaimed fiduciary status. *Id.* at ¶ 16. In contrast, the management agreements include no such disclaimer. Although the agreements disclaim a partnership or joint venture, they do not disclaim fiduciary duties. (See Management Agreement at § 14.) Recognizing a fiduciary duty would not impose upon White Hat any obligations to which it has not already expressly agreed.

Similarly, the fact that White Hat labeled itself an independent contractor is meaningless. White Hat cites that language and argues the Court’s analysis should end there. Yet White Hat fails to rebut the Schools’ showing that the agreements empower White Hat to act as the Schools’ agent while also giving the Schools oversight of White Hat’s conduct. White Hat’s undertaking is inherently fiduciary in nature notwithstanding White Hat’s status as “independent contractor.” And contrary to White Hat’s argument, *Guth v. Allied Home Mtge. Capital Corp.*, 12th Dist. Clermont No. CA2007-02-029, 2008-Ohio-3386, directly supports the Schools’ position. Although the court noted “current legislation” that codified the common law concerning mortgage brokers, its holding did not depend on that legislation. *See id.* at ¶ 63. An independent-contractor label does not foreclose a fiduciary relationship. *Id. Accord Berge v. Columbus Community Cable Access*, 136 Ohio App.3d 281, 301, 736 N.E.2d 517 (10th Dist. 1999). Indeed, an independent-contractor label is so unhelpful that the Third Restatement does

not use the term, describing it as “equivocal in meaning and confusing in usage.” Restatement 3d, Section 1.01, Comment c.

White Hat relies heavily on *Cincinnati Golf*, 132 Ohio St.3d 299, 2012-Ohio-2846, 971 N.E.2d 929, noting that the Court should focus on whether White Hat had actual authority to bind the Schools as purchaser. *See id.* at ¶ 20. To be sure, the Court focused on the agent’s power as the primary factor, suggesting that the principal’s right to control is less significant here because control relates only to vicarious-liability tort claims. *See id.* at ¶ 21. But the Court rejected Cincinnati Golf’s agency claim because the contract at issue expressly disclaimed agency and did not authorize Cincinnati Golf to make purchases on behalf of the city. *Id.* at ¶ 25. The Court held that “the management contract’s way of defining the relationship between CGMI and the city does not appear to be consistent with imputing purchasing-agent status on CGMI.” *Id.* at ¶ 26. In stark contrast here, the management agreements expressly authorize White Hat to make purchases for the Schools when the nature of the funding source requires it.

White Hat argues that recognizing a fiduciary relationship in this case would upset every service contract a public entity makes, turning ordinary business relationships into fiduciary ones. This argument ignores the nature of White Hat’s undertaking. White Hat is not providing just janitorial or food services but provides the *entire* educational process, a government function. *See Riester*, 257 F.Supp.2d at 972. White Hat’s primary obligation must be to act on the Schools’ behalf to help them succeed as educational institutions. That is what it agreed to do.

B. White Hat is a public official.

A “duly authorized representative of a community school is a public official pursuant to R.C. 117.01(E).” *Cordray v. Internatl. Preparatory Sch.*, 128 Ohio St.3d 50, 2010-Ohio-6136, 941 N.E.2d 1170, ¶ 24. White Hat is a public official because it is the Schools’ duly authorized

representative and agent. As a public official, White Hat owes a fiduciary duty to the public. *State v. McKelvey*, 12 Ohio St.2d 92, 232 N.E.2d 391 (1967), paragraph one of the syllabus.

White Hat's primary response is that the fiduciary duty that prevents a public official from taking unlawful profits does not attach unless the public official engaged in financial misconduct. White Hat relies on *Cristino v. Bur. of Workers' Comp.*, 10th Dist. Franklin No. 12AP-60, 2012-Ohio-4420, which held that the bureau of workers' compensation does not owe a fiduciary duty to a workers' compensation claimant. *Id.* at ¶ 19. White Hat's argument does not really answer the question here, because the Schools have alleged financial misconduct on the part of White Hat. White Hat's argument that it does not owe a fiduciary duty because it has not breached a fiduciary duty is inherently circular, and this Court should reject it.

Although not raised by White Hat itself, an amicus argues that White Hat cannot be a public official because that status would conflict with R.C. 3314.024. The argument is that the General Assembly would not create redundancy by subjecting management companies to "general audits by the State Auditor" in two different statutes. As an initial matter, this argument fails to account for the types of audits the State Auditor may conduct. The State Auditor must audit all "public offices" and has discretion to audit private entities "receiving public money." R.C. 117.10(A). The auditor is required to audit the Schools as public offices. The auditor may audit White Hat as a private entity that receives public money.

Two fallacies are evident with the amicus's understanding of the State Auditor's authority. First, R.C. 3314.024 does not subject management companies to audit. The "detailed accounting," which may be subject to audit during an audit *of the Schools*, is not an audit of White Hat itself. The purpose of the detailed accounting is to allow a school to prepare a footnote for the auditor's review. It is not an independent evaluation of how a management company is

using resources. Second, management companies such as White Hat are subject to nonmandatory state audits under R.C. 117.10(A) because they “receiv[e] public money for their use,” not because they are “public officials.” R.C. 3314.024 does not preclude White Hat from being recognized as a public official under the framework used in *Cordray*.

And there is no merit to the amicus’s argument that *Cordray* should not be applied in this case. The amicus points out that no statute expressly calls community-school operators “public officials” yet disregards that the General Assembly did not intend to enumerate every conceivable person or entity that might qualify as a public official. In crafting R.C. 117.01, the legislature set out criteria for determining who qualifies as a public official. In *Cordray*, the Court showed it is capable of applying that statutory language.

The amicus further argues that the Court should not use the statutory definition of “public official” found in R.C. 117.01 because the Schools’ claims do not arise under R.C. Chapter 117. The amicus points out that R.C. Chapter 3314 does not incorporate the R.C. 117.01 definition. This argument lacks merit for two reasons. First, White Hat’s public-official status relates primarily to the Schools’ common-law fiduciary claims. The Schools do not assert a statutory cause of action under R.C. Chapter 3314, so there is no significance to the fact that that chapter does not expressly incorporate the R.C. 117.01 definition. Second, this Court has held that “statutory definitions can serve as a helpful guide” even when they are not binding. *First Bank of Marietta v. Mascrote*, 79 Ohio St.3d 503, 506, 684 N.E.2d 38 (1997). The fact that the Court already applied the R.C. 117.01 definition in the community-school context should make it a particularly useful guide in determining White Hat’s status as a public official in this case.

White Hat’s public-official status would not make a private entity a public official just because it provides services to a public entity. Contrary to the arguments that have been raised,

the Schools' reasoning is limited by the language of R.C. 117.01 and *Cordray*, which accord public-official status only to an "officer, employee, or duly authorized representative or agent of a public office." It is hard to imagine a janitorial- or food-service provider satisfying this standard. White Hat, on the other hand, is a public official because it operates "all functions" of the Schools on their behalf.

Conclusion

The holding of the court of appeals contravenes Ohio law concerning the nature and use of public funds. It also disregards White Hat's undertaking as a public-school operator, which is fiduciary in nature. The Court should give meaning to the parties' agreements and hold that White Hat must purchase personal property on the Schools' behalf when it uses funding from the Ohio Department of Education. The judgment of the court of appeals should be reversed, and the case should be remanded to the trial court.

Respectfully submitted,



Karen S. Hockstad (0061308)

(Counsel of Record)

Gregory P. Mathews (0078276)

DINSMORE & SHOHL LLP

191 W. Nationwide Blvd., Suite 300

Columbus, Ohio 43215

(614) 628-6930 (telephone)

(614) 628-6890 (facsimile)

karen.hockstad@dinsmore.com

gregory.mathews@dinsmore.com

James D. Colner (0012376)
Adam M. Galat (0081068)
SHUMAKER, LOOP & KENDRICK, LLP
41 South High Street, Suite 2400
Columbus, Ohio 43215
(614) 628-4459 (telephone)
(614) 463-1108 (facsimile)
jcolner@slk-law.com
agalat@slk-law.com
*Counsel for Appellants Hope Academy Broadway
Campus, et al.*

Proof of Service

It is hereby certified that a copy of the foregoing was served via U.S. mail this 25th day of August, 2014, on:

C. David Paragas
Kevin R. McDermott
Amy Ruth Ita
BARNES & THORNBURG, LLP
41 South High Street, Suite 3300
Columbus, Ohio 43215
Counsel for Appellees White Hat Management, LLC, et al.

Todd Marti, Esq.
Assistant Attorney General
30 East Broad Street, 17th Floor
Columbus, Ohio 43215
Counsel for Ohio Department of Educ.

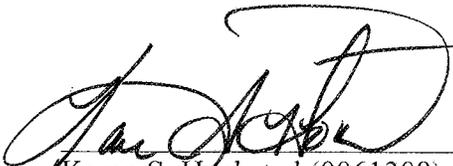
Donald J. Mooney, Jr.
ULMER & BERNE LLP
600 Vine Street, Suite 2800
Cincinnati, Ohio 45202
Counsel for Amicus Curiae Ohio School Boards Association

Martha J. Sweterlitsch
BENESCH, FRIEDLANDER, COPLAN &
ARONOFF LLP
41 South High Street, Suite 2600
Columbus, Ohio 43215
Counsel for Amici Curiae LeadingAge Ohio, et al.

Katherine Frech
BENESCH, FRIEDLANDER, COPLAN & ARONOFF
LLP
200 Public Square, Suite 2300
Cleveland, Ohio 44114
Counsel for Amici Curiae LeadingAge Ohio, et al.

Robert J. McBride
Maria L. Markakis
Kristen S. Moore
DAY KETTERER LTD.
Millennium Centre, Suite 300
200 Market Avenue North
Canton, Ohio 44702
Counsel for Amicus Curiae Summit Academy Management, LLC

Chad A. Readler
Kenneth M. Grose
JONES DAY
325 John H. McConnell Blvd., Suite 600
P.O. Box 165017
Columbus, Ohio 43216-5017
Counsel for Amicus Curiae Ohio Coalition for Quality Education



Karen S. Hockstad (0061308)