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IN THE SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF LOS ANGELES

PEOPLE OF THE STATE OF CALIFORNIA, Plaintiff, v. EUGENE SELIVANOV AND TATYANA BERKOVICH, Defendants.	)	CASE NO. BA 372244 **BRIEF OF AMICUS CURIAE** Date: October 4, 2013 Time: 8:30 a.m. Dept.: 102

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I. Introduction

By manufacturing new crimes that heretofore were unknown to charter schools, the prosecution seeks to undermine the cornerstone of what makes charter schools successful—operational freedom to create new dynamic programs and systems that achieve increased academic results and freedom from the rules binding traditional district schools. Accepting the prosecution's theory of criminal liability would nullify Education Code section 47610—what the California Department of Education calls the "mega-waiver"—which exempts charter schools from most laws applicable to district-run schools. Moreover, the prosecution completely ignores the fact that the Legislature has expressly allowed charter schools to be operated by private nonprofit corporations, and that many, if not all, of the complained of actions of the defendants are lawful actions of employees and officers of nonprofit corporations (e.g., ordinary and necessary expenditures on meals, gift cards, flowers, leases with employees and officers of the nonprofit etc.) And, most importantly, the court cases and administrative agency decisions make clear that these private officers and employees of the nonprofit corporation are not subject to Penal Code section 424 – because these nonprofit corporations are private entities, with private employees, expending private moneys (i.e., not "public moneys").

This unprecedented prosecution has sent shock waves throughout the charter school community and has stifled charter school operational freedoms. With no guidelines or set of rules on what is an "allowed" or "disallowed" expenditure, no recognition of the rules and regulations applicable to nonprofit corporations, and district attorneys and courts second guessing nonprofit corporate board's spending decisions years after the fact, charter schools are now forced to forgo their operational flexibility and make only the basic expenditures (e.g., books, salaries etc.) out of fear of future prosecution.

But perhaps more troubling, the prosecution would inject criminal courts unlawfully into the role of public education oversight and policy making—a role specifically reserved by the Legislature for school districts, county offices of education and the State Board of Education through the power to cure and correct nonprofit operators' violations of law and charters via the power to revoke or non-renew the charter school.

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II. Overview of Charter Schools and the Important Role they Play in California Education

Charter schools are a vital, growing part of California's school system. Charter schools are created and operated by parents, educators, nonprofit corporations or community groups to fill an educational need not otherwise fulfilled by traditional district-run public schools. Those parents, educators, nonprofit corporations and community groups start a charter school by initiating a charter petition, which is typically presented to a local school district governing board for approval. (Ed. Code, § 47605, subd. (a).) The law also allows, under certain circumstances, for county boards of education and the State Board of Education to be charter authorizing entities. (Ed. Code, §§ 47605, subd. (j), 47605.5, 47605.6, 47605.8.)

Under the Charter Schools Act, the Legislature originally authorized charter schools as a limited experiment *to establish and maintain schools that operate independently from the existing school district structure* as a method to accomplish the following: (1) improve pupil learning; (2) increase learning opportunities, especially for low achieving students; (3) encourage use of different and innovative teaching methods; (4) create new professional opportunities for teachers; (5) provide parents and students with more choices in the public school system; and (6) hold schools accountable for measurable pupil outcomes and provide a way to change from rule-based to performance-based accountability systems. (See Ed. Code, § 47601, subds. (a)-(f).) The key here is that the charter forms and educational contract binding the nonprofit corporate operator to achieve certain stated academic results in exchange for being freed from the "rule-based" system of accountability.

By 1998, charter schools had sufficiently proven their worth for the Legislature to raise the statutory limit of 100 charter schools to 250, with 100 more to be allowed each year. (Ed. Code §47602.) The Legislature also added an important additional goal to the Charter Schools Act – to create "vigorous competition within the public school system to stimulate continual improvements in all public schools." (Ed. Code, § 47601, subd. (g).) The also Legislature declared that "charter schools are and should become an integral part of the California education system and that establishment of charter schools should be encouraged." (Ed. Code, § 47605, subd. (b).) And importantly, the Legislature expressly allowed charter schools to be operate by nonprofit corporations formed and organized pursuant to the Nonprofit Public Benefit Corporation Law (Corp. Code §5110 et

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seq.) By inviting private entrepreneurs into the world of public education, the California legislature purposely injected the potential for business practices wholly foreign to the normal public education bureaucracy for the purpose of increasing student achievement.

By design, charter schools differ from schools managed by school districts. Charter schools are freed from the "complex tangle of rules sustaining our public school system" which has "the potential to sap creativity and innovation, thwart accountability and undermine the effective education of our children." (*Wilson v. State Bd. of Education* (1999) 75 Cal.App.4th 1125, 1130 (*Wilson*).) As a result, charter schools have unparalleled innovation and flexibility, and are given the autonomy to tailor their educational and operational approaches to meet and respond to the needs of their students and community. That flexibility is primarily outlined in Education Code section 47610 (commonly referred to as the "mega-waiver") that, with the exception of a few laws not applicable to this prosecution, releases the operators of charter schools from having to comply with the "laws governing school districts."

Charter schools are unlike any other organization in the state. They are public schools operated by nonprofit corporate operators; they are a hybrid creature that has only been in existence for twenty years. There is very little guidance to developers of charter schools; there are no start-up manuals or guidelines produced by the state. And there are very limited fiscal resources to assist operators in the development of charter schools. There are only 73 Education Code sections that currently prescribe and proscribe a charter school's functions and operations – and at the time of the creation of Ivy Academia there were only 69 Education Code sections. [1] And, these few controlling Education Code sections clearly give the governing board of the charter school (in most cases a nonprofit corporation board) extensive flexibility in how to spend its moneys in the development and operation of the school (e.g., "funding may be used for any purpose determined by the governing board of the charter school.") (Education Code section 47634.1(f). [2]) The dearth of controlling law over the operation of charter

[1] Over the twenty years of the Charter Schools Act, the Legislature has made a few sections of law outside the Education Code applicable to charter schools (e.g., Govt. Code 3540.1; Govt. Code section 6528). There are only fifteen references to charter schools outside the Education Code.

[2] Formerly, Education Code section 47634.1(h).

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schools is by Legislative design – it is in keeping with the old adage that "one cannot hold someone accountable for the outcomes if one dictates the means." Hence, the Charter Schools Act allows all 1000+ operators of charter schools in the state to create their own framework for operational design that best meets that school's and their students' needs. As a consequence, no two charter schools' charters, bylaw, policies and procedures and operational design are the same.

III. The Operators of Charter Schools are Closely Supervised and Monitored by Multiple Levels of State and Local Government with the Power to Cure and Correct Violations of Law and Charter and Fiscal Mismanagement

The operational flexibility outlined above is not without its bounds or oversight; the Charter Schools Act establishes a strong framework of oversight, supervision, and accountability by the granting school district, county board of education, and the State Board of Education. In addition, for those nonprofit operators of charter schools, the nonprofit is also subject to supervision by the California Attorney General and its actions are further circumscribed by the Nonprofit Integrity Act and the applicable provisions of the Corporations Code. (Ed. Code §47604(a); Corp. Code §§5250; Govt. Code §12588, and 12598; Govt. Code §§12580 –12599.7.)

The supervision and oversight of charter schools by the state's education organizations differs at each level of government. The granting agency has the greatest degree of responsibility. Granting agencies must: (1) designate a charter school oversight employee; (2) visit the school at least annually; (3) review a multitude of reports produced by the charter school (both operational, academic and fiscal); (4) monitor the fiscal condition of the school; (5) monitor the charter school's compliance with the law, its charter, its proposed academic outcomes, and the school's compliance with generally accepted accounting principles. (Education Code section 47604.32, 47604.33, 47607.) The operator of a charter school must produce an annual fiscal audit, conducted by a certified public accountant that has been screened and approved by the State Controller. (Ed. Code §47605(m) and §41020(f).) The annual fiscal audit, conducted in accordance with Government Auditing Standards, must be sent by the charter schools to its granting agency, the county superintendent of schools, the California Department of Education and that State Controller. (Ed. Code §47605(m).) All operators of charter schools must cooperate with its granting agency in the monitoring and investigation of the school's operations. (Education Code §47604.3.) In addition to its statutorily prescribed lawful obligation to oversee and

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supervise the charter schools the school districts have an incentive to monitor the charter schools closely because if they fail to properly monitor and oversee the charter school they can be liable for the debts and obligations of the charter school even if operated by a nonprofit corporation. (Education Code section 47604(c).)

The operators of charter schools are also overseen and monitored by, and must be responsive to, the county boards of education and the county superintendents of schools. (Ed. Code §47604.4.) This same section grants the county superintendent of schools the right to investigate the operator of a charter schools in the county. County superintendents also have the authority to begin an extraordinary audit of charter schools if it believes "that fraud, misappropriation of funds, or other illegal fiscal practices have occurred…" (Ed. Code §1241.5.) Any such audits must be provided to the governing board of the charter school and to the granting agency; and the governing board of the charter school must report to the county superintendent within fifteen days its response to the county superintendent's recommendations. (Ed. Code §1241.5(c).)

Charter schools are also overseen and monitored by the State Board of Education. The State Board of Education, whether or not it is the granting agency of the charter school, based upon the recommendation from the State Superintendent, may revoke a charter school for "gross fiscal mismanagement" or "illegal or substantially improper use of charter school funds" or "substantial and sustained departure from measurably successful practices." (Ed. Code §47604.5.) However, much like a granting agency's ability to revoke a charter outlined below, the State Board of Education must provide the charter school notice and an opportunity to cure the alleged basis for the revocation. (5 CCR §§11968.5 and 11968.5.1.)

The entire framework of flexibly in operation is backed up against a detailed mechanism and process for the granting agency and that state to enforce an operator's compliance with its charter, the applicable law, its proposed outcomes, and fiscally prudent operations. It is through the power of charter revocation or nonrenewal that the granting agency (and the state) enforces compliance. But before a granting agency (or the state) may exercise this power it must give the operator of a charter school *notice* of the alleged violation and a *reasonable opportunity to cure* the alleged violation—unless the granting agency determines the violation constitutes a "severe and imminent threat to the

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health or safety of the pupils." (Ed. Code §47607(c) and 5 CCR 11965, 11968.5.2, and 11968.5.3.)

For the last twenty years operators of charter schools have relied upon the annual fiscal audit process with its multiple layers of governmental review and/or the granting agency's cure and correct authority to define the outside boundaries of its operational flexibility. Where, as is the case herein, the actions taken by the employees of nonprofit operator were reviewed by the outside auditors and the fiscal operations of the charter school were reviewed annually by the granting agency with no notice to cure and correct the operators, like all other operators in the state, rightfully believed that their actions comported with the flexibility expressly stated in the law (as well as the lawful practices of nonprofit corporations.) Because LAUSD and its Office of Inspector General believed that the actions the underlie this prosecution violated the law and the charter school's charter they had a *statutory duty* to bring these allegations to the attention of the operator of the charter school and allow the operator a chance to conform its behavior through the notice and opportunity to cure process outlined in the Charter Schools Act. (*California School Bds. Assn. v. State Bd. of Education* (2010) 186 Cal.App.4th 1298, 1326)(the court of appeal held that a granting agency can be forced through writ of mandate to begin the revocation process if a charter school violates the law.) For whatever reason, the record is clear in this matter that LAUSD did not follow its statutory duties to give notice and a time to cure any alleged noncompliance and instead elected to press for the prosecution of the nonprofit operators of this charter school instead of following the framework the Legislature specifically set forth to resolve these types of disputes.

It is only if the cure and correct process of the Charter Schools Act is followed by granting agencies will charter schools have the comfort to be able to experiment and create new ways to operate and manage charter schools—knowing that disagreements can be worked out in the civil context. The Legislature did not intend the criminal courts to be the arbiter of "allowable" and "disallowable" expenses in a charter schools' operations. Overlaying the threat of a felony conviction where the granting agency and an operator disagree over allowable expenditures is not only inconsistent with the statutory structure the legislature put in place to remedy these disputes it will immediately immobilize the state's charter school's substantial gains that have been achieved over the last twenty years.

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And lastly, it would seem to be reversible error to not provide a copy of the Charter Schools Act or instruct the jury on the Charter Schools Act's express operational flexibility for nonprofit operators (including the "mega-waiver"), the rules and regulations circumscribing nonprofit corporations, the broad grant of spending flexibility expressing granted to charter school operators (Ed. Code §47633(c) and 47634.1(h), and the Charter Schools Act's mandatory process of notice, cure and correct. (Ed. Code §47607(c) and 5 CCR 11965, 11968.5.2, and 11968.5.3.)

IV. The Employees of a Nonprofit Corporation Operating a Charter School are not Subject to Penal Code §424

A. The Charter Schools Act Authorizes Charter Schools to be Operated by Nonprofit Public Benefit Corporations

The Charter Schools Act specifically authorizes a charter school to be operated by or as a nonprofit public benefit corporation, formed and organized pursuant to the Nonprofit Public Benefit Corporation Law (commencing with Corp. Code §5110.) (Ed. Code §47604(a).) The intent of the Legislature in allowing nonprofit corporations to operate charter schools is to insulate school districts from the debts and liabilities of charter schools. (Ed. Code §47604(c).) This was necessary because some school districts were not approving charter schools because they feared assuming liability for the debts and obligations of the charter school should it fail. However, because the nonprofit corporation operator has perpetual existence, the nonprofit corporation will remain responsible for the debts and liabilities of the charter school after the charter school is revoked, non-renewed or surrender. On multiple occasions throughout the Act's twenty year history, the nonprofit corporation operators have remained in place after the charter school it operated was closed (by revocation or non-renewal) to handle the closure of the charter school (i.e., conduct a final audit, transfer student records, redirect students to new schools, perform and account of assets and liabilities, and proceed through bankruptcy if necessary. Examples include, Liberty Family Academy (in North Monterey Unified School District), Promise Charter School (in San Diego Unified School District), Urban Pioneer Charter School (in San Francisco Unified School District), Crescendo Charter School (Los Angeles Unified School District). [3] (See Exhibit A attached to the Request for Judicial Notice for a sample Voluntary

[3] Indeed, Ivy Academia's original charter, operative during the period of time forming the basis of this prosecution, states in the Governance Section that: "The nonprofit will continue its existence notwithstanding any withdrawal of charter status." (Ivy Charter, Oct. 2003, p. 42.)

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Notice of Bankruptcy of the nonprofit operator of the Prosser Creek Charter School.)

The separateness of the nonprofit corporation operator from the charter school it operates is easier to appreciate where the nonprofit corporation's specific purpose is broader than just operating a charter school. For example, the East Bay Conservation Corps and the San Jose Conservation Corps each operate a charter school in addition to conservation corps activities and responsibility.

It must be noted that, as would be consistent with a private employer, the employment practices of a nonprofit corporation operator of a charter school are not controlled by state law or regulations. Indeed, the operator of the charter school will define certain employee rights in the charter itself (e.g., qualifications for employment, retirement benefits, return rights to the school district etc.)[(Ed. Code §47605(b)(5)(E), (K) and (M)] but the bulk of employee rights are defined in the nonprofit corporation's employee handbook, policies, and individual employment contracts.

The nonprofit operator plays an important role in the wind up and closure of charter schools. The Charter Schools Act requires that each charter outline the "closure procedures" and how the nonprofit operator will dispose of "all assets and liabilities of the charter school, including any plans for disposing of any net assets[.]" (Ed. Code §47605(b)(5)(P).) After paying or adequately providing for all known debts and liabilities, a California nonprofit corporation can dispose of net assets upon dissolution in conformity with its articles of incorporation. (Corp. Code §6716.) Under California law a nonprofit corporation can dispose of net assets upon dissolution by distributing those assets to another nonprofit corporation upon approval by the Attorney General. (See Exhibit B attached to the Request for Judicial Notice for a sample Attorney General approval of distribution of a nonprofit's net assets after closure of the charter school it operated.)

Ivy Academia charter school has always been operated by Alternative Schools, Inc., a California nonprofit corporation. The Articles of Incorporation of Alternative Schools, Inc. provide that upon dissolution the assets of this entity shall be distributed to an organization that is organized and operated exclusively for charitable, religious, scientific, testing for public safety, literary, or educational purposes, fostering national or international amateur sports competition or for the prevention of cruelty to children or animals that has established its tax-exempt status under section 501(c)(3) of the Internal Revenue Code and section 23701d of the California Revenue and Taxation

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Code. As such, the Education Code, Corporations Code and the Articles of Incorporation of Alternative Schools, Inc. permit the distribution of assets, upon dissolution, to a private organization.[4]

The ability of a nonprofit corporation operator to distribute the net assets of a closed charter school to a private organization proves that these assets are not "public moneys"; if the moneys (i.e., net assets) of the charter school were public moneys these moneys would have to be returned to the state because the allocation of those funds outside the public school system would be a gift of public funds in violation of the California Constitution. (Cal. Cons. Art. XVI, Sec. 6.)("The Legislature shall have no power…to make any gift or authorize the making of any gift, of any public money or thing of value to any individual, municipal or other corporation whatever[.]".)

B. The Nonprofit Corporations Operating Charter Schools Are Deemed to be Private Entities under the law of California

A number of court cases in California (both state and federal) addressing the "private" v. "public" nature of the nonprofit operator of a charter school and a growing body of administrative decisions have concluded that the nonprofit operators of charter schools are "private" entities and not a public entity.

Of particular import to this prosecution is the California Supreme Court's holding in the matter of *Joey Wells v. One2One Learning Foundation* (2006) 39 Cal.4th 1164 ("*Joey Wells*"). This case is important to this court's consideration for two reasons. First, the Supreme Court concluded that the nonprofit operators of a charter school are private "persons" and thus, unlike "public" school districts, are subject to lawsuits under the California False Claims Act (Govt. Code §12650 et seq.)("CFCA"). And second, one of the reasons the Supreme Court concluded that the nonprofit operators of charter schools are "private" persons is that the funds held by the nonprofit corporation that would be used to satisfy any false claims are not public funds—and as a consequence exposing nonprofit charter school operators to CFCA liability (i.e., treble damages, and fines) would not have a negative impact on the

[4] The California Department of Education website states the following regarding Charter School Closure Requirements and Recommendations: "If the charter school is a nonprofit corporation and the corporation does not have any other functions than operation of the charter school, the corporation should be dissolved according to its bylaws. The corporation's bylaws should address how assets are to be distributed at the closure of the corporation." (http://www.cde.ca.gov/sp/cs/lr/csclosurerules.asp)

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public fisc.

In *Joey Wells* the Supreme Court, looking at the types of entities that could be liable for CFCA claims, concluded that the term "person" under the CFCA does not include "school districts, or for that matter, any other public entities or governmental entities." (Joey Wells, supra, at p.1190.) By concluding that nonprofit operators of charter schools can be liable for CFCA claims, the Supreme Court concluded that the nonprofit operators are not "public entities or governmental entities."

As further support for its conclusion that school districts should not be liable for CFCA claims the Court stated:

> "School districts must use the limited funds at their disposal to carry out the state's constitutionally mandated duty to provide a system of public education…We note that '[t]he ultimate purpose of the [CFCA] is to protect the public fisc. [citations omitted.] Given that school district finances are largely dependent on and intertwined with state financial aid [citations omitted] the assessment of double and treble damages, as well as other penalties, to school districts would not advance that purpose." (*Joey Wells*, supra, p. 196.)

Hence, the Court concluded that exposing school districts to CFCA claims would harm the public fisc where exposing nonprofit operators of charter schools to the same claims would not harm the public fisc. Indeed, in concluding that the nonprofit operators are not public entities nor do the moneys used to operate the charter schools make up part of the public fisc, the Court stated about these nonprofit operators that "there can be little doubt the CFCA applies generally to nongovernmental entities that <u>*contract*</u> with state and local governments to provide services on their behalf." (*Joey Wells*, supra, p. 1201.)(Emphasis added.) Thus, the Court recognized that nonprofit operators are <u>*contractors*</u> that provide services to the state through local educational entities (such as school districts).

Following the *Joey Wells* decision the Second District Court of Appeal, in *Knapp v. Palisades Charter High School* (2007) 146 Cal.App.4th 708, also concluded that a nonprofit operator of a charter school is not a "public entity" for purposes of the Government Tort Claims Act (Govt. Code §900 et seq.)(*Knapp, supra*, 146 Cal.App.4th at p. 716-717.) In addition, the Court held that a nonprofit corporate operator of a charter school was not a "public entity" for purposes of the State's Roster of Public Agencies. (Govt. Code §53050.)(*Knapp, supra*, 146 Cal.App.4th at p. 718.) In reaching its conclusions, the *Knapp* court used similar reasoning as the *Wells* court in finding that a charter is a

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"*contract*" detailing the school's educational programs, goals, students served, measurable pupil outcomes and measurement methods, and the school's governance structure. (*Knapp, supra*, 146 Cal.App.4th at p. 714.) As further support, the court stated:

> "Focusing on the corporate structure of these charter schools, the court reasoned that the charter schools in question were '*operated*, not by the public school system, but by distinct outside entities—which the parties characterize as nonprofit corporations—that are *given substantial freedom* to achieve academic results free of interference by the public educational bureaucracy. The sole relationship between the charter school operators and the chartering districts is through the charters governing the schools' operations.'" (*Knapp, supra*, 146 Cal.App.4th at p. 716.)

The federal courts have reached the same conclusions as the courts *Wells* and Knapp--that nonprofit corporate operators of charter schools are private entities under contract with state and local governments and the employees of said private entities, as private employees, are not subject to lawsuits applicable only to public employees (e.g., civil rights lawsuits under 42 U.S.C §1983.) The Ninth Circuit Court of Appeal in *Caviness v. Horizon Community Learning Center* (2009) 590 F.3d 806, concluded that under Arizona law (which is substantially similar to California's Charter Schools Act) the nonprofit corporation's "actions and personnel decisions were 'made by concededly private parties, and turn[ed] on judgments made by private parties without standards established by the State." (*Caviness, supra*, 590 F.3d at p. 818.) In arriving at this conclusion the Court rejected arguments made by the plaintiff (that are similar to arguments made by the prosecution herein) that the nonprofit operator should be found to be a "state actor" because: (1) the state law defines charter schools as "public schools"; (2) operating a public school is an exclusive function of the state; and (3) employees working at the charter school are permitted to participate in the state teachers retirement system. In rejecting each of plaintiff's arguments, the Court relied upon the United States Supreme Court case of *Rendell-Baker v. Kohn*, 47 U.S. 830 (1982) in holding that just "because [the nonprofit operator] is a 'private entity perform[ing] a function which serves the public does not make its acts state action." (*Rendell-Baker v. Kohn, supra*, 47 U.S. at p. 842.)

And then just **two months** ago the United Stated District Court for the Northern District of California, following *Joey Wells*, *Knapp*, and *Caviness*, while specifically *reviewing California law*,

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concluded that the California law regarding charter schools is very similar to the Arizona law reviewed by the Ninth Circuit in *Caviness* and under the Charter Schools Act in California the private employees of the nonprofit operators of charter schools are not subject to suit as "state actors" under 42 U.S.C §1983. (*Sufi v. Leadership High School* (2013 U.S. Dist. Lexis 94232.) In *Sufi* the District Court rejected all of the same arguments made in Caviness, and concluded, as did the court in Caviness, that "the personnel decisions at issue…turned on judgments made by private parties that were not governed by state-established standards." (*Sufi v. Leadership High School, supra*, at p. 16.)

California State agencies are adopting the same position as the court opinions noted above—that nonprofit corporations that operate charter schools are not "public entities." For example, in the employment context the Labor Commissioner has twice denied charter schools' efforts to utilize the exemptions of Labor Code section 220(b) applicable to employees that are "employed by any county, incorporated city, or town or other municipal corporation." (See, Exhibit D attached the Request for Judicial Notice in Support of Amicus Brief) In addition, the California Public Employees Retirement System (PERS) has begun rejecting applications by the nonprofit corporation operators of charter schools claiming that these entities are not "an agency or instrumentality of the state or a political subdivision of the state" and therefore cannot be a participant in the CalPERS system. (See Exhibit E attached to the Request for Judicial Notice.) In concluding the nonprofit operators of charter schools are not entitled to participate in this state retirement program CalPERS is concluding, consistent with IRS guidelines, that nonprofit operators do not meet the following "public agency" criteria: (1) the entity's governing board is not controlled by the state or a political subdivision; (2) the governing board is not publicly elected; (3) the state or a political subdivision is not liable for the debts and obligations of the entity; (4) the entity's employees are not entitled to the same statutory rights as state or political subdivision employees; and (5) the entity does not have any of the powers of a political subdivision (the power of taxation, eminent domain, and police power). (See Exhibit E attached to the Request for Judicial Notice.)[5]

[5] CCSA notes that CalPERS actions are contrary to Ed. Code §47605(b)(5)(K) that requires a charter school to describe in its charter how employees of the charter school will participate in CalPERS. In addition, CalPERS actions also contravene other California statutory provisions that authorize the participation of charter schools.

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C. Employees of the Nonprofit Corporation Operating a Charter School are Not Public Employees (i.e., Not Officers of the State, or Any County, City, Town or District)

Penal Code section 424 by its express terms only applies to two categories of people: (1) an officer of this state, or of any county, city, town, or district of this state; or (2) every other person charged with the receipt, safekeeping, transfer or disbursement of public moneys. (Penal Code §424(a).) As the court cases clearly articulate above, the nonprofit operator of a charter school is not the state, nor a county, nor a city or town, nor a "district" of this state – indeed, the nonprofit operator of a charter school is not any of these public agencies of the state; the nonprofit operator of a charter school is a private entity under contract to provide educational services. Consequently, the employees and officers of the nonprofit operator of a charter school are private employees not subject to prosecution under Penal Code §424's first category applicable people.

The Second District Court of Appeal, in reviewing the definition of "public officer" under Penal Code §424 stated that it is a "well recognized requirement that to constitute an officer of the state, or any subdivision thereof, in his official capacity he must exercise some portion of the sovereign functions of government[.]" (*People v. Showalter* (1932) 126 Cal.App. 665, 666.) Further, the Court said that "a public office is the right, authority and duty, created and conferred by law, by which for a given period, either fixed or by law or enduring at the pleasure of the creating power, an individual is vested with some portion of the sovereign functions of government[.]"(*People v. Showalter* (1932) 126 Cal.App. 665, 667.) In concluding that a receiver appointed by the court is not a "public officer" and therefore not subject to prosecution under Penal Code §424 the court found the following facts to be dispositive: (1) the receiver was appointed by and removable by the court; (2) he is responsible to no one but the court; (3) his compensation is fixed by the court; (4) his authority comes from the court; and (5) he exercises none of the powers of civil government.

In the matter before the court, it is clear that the defendants did not "exercise some portion of the sovereign functions of government" (this much was concluded by the *Joey Wells*, *Knapp*, *Caviness* and *Sufi* courts); that the defendants were employees of the nonprofit corporation and removable by the nonprofit corporation board only; that the defendants were responsive to no one but the nonprofit corporation board; that the defendants' compensation was fixed by the nonprofit corporation board;

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that the defendant's duties and authority came from the nonprofit (and not any applicable statute or regulations); and that defendants' employment with the nonprofit was not controlled by any public agency. Hence, defendants are not "officers" of a "district" under Penal Code §424—they were employees and officers of a private nonprofit corporation, that under contract, provided educational services through a charter school.

Further, in a recent Second District Court of Appeal decision in *People v. Christiansen* (2013) 216 Cal.App.4th 1181, the court held that "a [criminal] statute must be construed in light of the common law unless the legislature clearly and unequivocally indicates otherwise." (*Christiansen, supra*, 216 Cal.App.4th at page 1188.) There is, obviously no "clear and unequivocal" intent by the Legislature to define "district" under Penal Code §424 to include the nonprofit operators of charter schools. Consequently, this court should look to common law to determine the definition of "district" for purposes of this case. While amicus was unable to find any specific court case defining the term "district" the courts will in that case turn to dictionary definitions of the word. The American Heritage Dictionary, Second College Edition 1982, defines "district" as "a division of an area or geographic unit marked out by law for a particular purpose—a school district." Under this definition a charter school, unlike a school district, is not a "district" – charter schools do not have legally defined boundaries and are considered a system of state-wide schools. A charter school can locate in the boundaries of its granting agency or an adjacent school district (or in some cases in any school district in the county or adjacent county). (Ed. Code §47605.1(d). [6]) Charter schools do not need boundaries because their boards are not elected by the public and by law a charter school must "admit all pupils who wish to attend the school" and admission to a charter school "shall not be determined according to the place of residence of the pupil, or of his or her parent or legal guardian, within this state[.]" (Ed. Code §47605(d)(1).) Consequently, under *Christiansen* and the common law it was error or the court to instruct the jury that a charter school is a "district" for purposes of Penal Code §424.

The prosecution's sole reliance on *Wilson v. State Board of Education* (1999) 75 Cal.App.4th 1125 to support the applicability of Penal Code 424 is misplaced. In *Wilson*, the court's focus was on

[6] Certain types of charter schools can be located anywhere in the state. (Ed. Code §47605.8 and 47605.1(g).)

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the nature of the charter school itself and the control exercised over charter schools by officers of the public school system (e.g., the school district, county office of education, and the State Superintendent and Board of Education)– not on the nature of the different types of charter school operators (here a nonprofit corporation.[7]) The court ultimately finds the Charter Schools Act constitutional because "charter schools are under the jurisdiction of chartering authorities…and chartering authorities are authorities 'within the Public School System[.]"(*Wilson, supra*, 75 Cal.App.4th at p. 1142.) The Court only concludes that a charter school is a "district" for a very limited purpose – two statutory funding sections of the Charter Schools Act. The court did not make a broad proclamation that a charter school is a governmental "district" just like a public school district for all purposes; had the court done so it would have vested charter schools with the sovereign powers of government (i.e., the powers held by school districts -- the power to tax, issues laws/police power, and the authority to condemn property for public use.[8]) Charter schools clearly do not have these sovereign powers and are therefore not "districts" for any purpose other than the specified funding sections on the Education Code.

D. <u>The Nonprofit Corporation Moneys are Not "Public Moneys"</u>

While the second category of people subject to prosecution under Penal Code §424 is much broader in scope it is still only limited to those people responsible for handling "public money." And the phrase "public moneys" as used in Penal Code §424 is defined in Penal Code §426 to "all moneys belonging to the state, or any county, town, district, or public agency therein, and all moneys, bonds, and evidence of indebtedness received or held by state, county, district, city, town, or public agency officers in their official capacity." Again, the court cases and other arguments cited above make it abundantly clear that the nonprofit operators of charter schools are private entities under <u>*contract*</u> with local school districts and are not the state, nor a county, nor a city, nor a town, nor a district, nor any

[7] Prosecution's statement in the People's Opposition to Defendants' Motion for New Trial on page 10, lines 15-16 that "charter schools…remain very much a public-sector creature…" is not a quote from the Court – it is quote from a private sector organization (the Little Hoover Commission.) In any event, as noted herein, the quote speaks to the nature of a charter school being a public school (as opposed to a private school) and not to the nature of the private operator of that charter school under contract with the school district.

[8] The California Supreme Court stated in *Wells*, that "…that charter schools act assigns no [] sovereign significance to charter schools or their operators." (*Wells, supra*, 39 Cal.4th at p. 1201.)

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other "public agency" of the state. Moreover, if the money held by the nonprofit operator was "public money" it could not be gifted over to any private party upon the closure of the charter schools—but as demonstrated above the nonprofit operator of the charter school is required to resolve all liabilities of the school it operates as well as retain the right to distribute net assets upon dissolution to another private entity. Consequently, "public moneys" were not involved in the actions of the defendants as defined in Penal Code §426.

As the court cases demonstrate, the law treats the nonprofit operator of a charter school as a private "contractor" of local government for the provision of educational services (similar to other vendors to the state that provide other services like correctional facilities or legal services etc.). As noted in *Caviness* just because a private entity is performing a function under contract which services the public does not make this entity a public entity. (*Caviness, supra*, 590 F. 3d 806, 815.)

E. Any Vagueness or Doubt in the Application of Criminal Statutes Should Be Interpreted in Favor of Defendants

Even if we assumed for the sake of argument that the case law on this matter was not 100% clear—that nonprofit operators of charter schools are private entities under contract to operate a charter school—"when the language employed is ambiguous or doubtful in its intent, a construction of the statute should always be favorable, rather than unfavorable, to any person accused of a violation of the law. (*People v. Showalter* (1932) 126 Cal.App. 665, 669.) "The defendant is entitled to the benefit of every reasonable doubt as to the true interpretation of words or the construction of language in a statute." (*People v. Holtzendorff* (1960) 177 Cal.App.2d 788, 795.) This proposition addresses Rule number One – that there be a bright line.

Penal Code §424 was added to the code in 1872, and while there has been a number of minor revisions over the years, there has not been a major revision or reassessment of Penal Code §424's applicability to newly emerging organizations such as the unusual nature of charter schools. What is clear is that "section 424 has to do solely with protection and safeguarding public moneys defined in Section 426 of the Penal Code, and with the duties of public officers charged with their custody and control and no other kind of public property." (*People v. Dillon* (1926) 199 Cal. 1)(Emphasis added.) And what is clear from the current legal analyses by the California Supreme Court and the Ninth

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Circuit Court of Appeal is that nonprofit operators of charter schools are not public agencies and their offices and employees are not public employees and that as contractors for the provision of education services their moneys are not "public moneys." And even if these conclusions were not clear the court was required to give the benefit of the doubt to the defendants.

V. The Jury Instructions on Penal Code §424 and §504 Violate the Fundamental Rules of Our Criminal Justice System

This case touches upon the fundamental rules of our criminal justice system. It involves violations of the three most important rules in our jurisprudence. Rule One, if someone is going to be deprived of life or liberty, that person needs to have been convicted of crossing a bright line of behavior, in which the State has clearly described the prohibited behavior. Vague laws violate due process because they "fail to give adequate guidance to those who would be law-abiding, to advise defendants of the nature of the offense with which they are charged, or to guide courts in trying those who are accused." *Musser v. Utah*, 333 U.S. 95, 97 (1948). Rule Two, the crossing of that bright line has to be intentional, with knowledge of the prohibition. And Rule Three, the architecture of the trial process requires the judge to be the finder of law, and the jury the finder of fact. Due to the unique nature of charter schools, the jury instructions in this prosecution on Penal Code §424 and §504 violate all three of the fundamental rules of our criminal justice system.

A. There was No Crime Here; Defendant's Conduct Did Not Constitute Misappropriation of Public Funds under Penal Code §424

The starting point for discussion must be the existence *vel non* of some specific regulations, guidelines, or rules governing the employee actions or business practices that these defendants allegedly violated; otherwise their broad operational discretion outlined in the Charter Schools Act is within the "authority of law". Which leads us inexorably to a discussion of *Stark v. Superior Court of Sutter County* (2011) 52 Cal.4th 368 ("*Stark*").

1. Stark Was Misinterpreted by this Court

Stark is not simply a discussion of Penal Code §424. It involves Rules One and Rule Two discussed above. Rule One goes back to the Enlightenment and the causes of the American and French revolutions. Locke and Rousseau's notion of a social contract inspired the drafters of our Declaration

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of Independence and Constitution. They tossed aside the notion of a divinely inspired monarch in favor of a government where the people are supreme. The concept of a bright line in criminal jurisprudence, coupled with the requirement of a *mens rea* element in all prosecutions for serious crimes, derives from our notions of a constitutional democracy in which the governed agree to be governed only so long as the mandates of government are fair, clear, understandable and just.

In the last century, however, the concept of strict liability began to creep over from civil law into criminal law, as industrialization made life complex and the risks inherent in modern life multiplied. The *Stark* Court was faced with a vaguely written 1872 statute that appeared, at least on its face, to permit prosecution for a general intent only – that is, a misappropriation that occurred without knowledge of the criminal nature of the act. Moreover, the statute was so vaguely worded that it was not clear what specific conduct was prohibited. We know in our gut that a common law thief is a criminal--the mayor who puts his brother on the payroll and tells him he need not show up–but what about a stubborn bureaucrat like Stark who is not necessarily motivated by venality, but is on some kind of personal power trip designed to get everyone ticked off? In order to preserve Stark's prosecution and nevertheless honor our founding fathers, the Supreme Court of California narrowed Penal Code §424 prosecutions in two important ways, which thus avoided a Rule One and Rule Two violation.

a. <u>Rule Number One: The Bright line</u>

Let's start with Rule One, the requirement of a "bright line". The *Stark* Court focused on the element of Penal Code §424 that criminalized conduct "without authority of law":

> "As the statutory language provides, it is not simply appropriation of public money, or the failure to transfer or disburse public funds, that is criminalized. Criminal liability attaches when those particular actions or omissions are contrary to laws governing the handling of public money. *Unlike many statutory provisions, these provisions make the presence or absence of legal authority part of the definition of the offense. The People must prove that legal authority was present or absent.*" (*Stark, supra*, 52 Cal.4th at 395) (emphasis supplied).

In order to elaborate upon the People's burden of proving the presence or absence of legal authority, the Supreme Court undertook a detailed examination of the regulatory context in which

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Stark operated. It turns out that Stark's supervising authorities had specifically instructed him to perform his legal duty in several instances, and Stark stubbornly refused to obey those clear mandates. By contrast, defendants in this case were not allowed to supply the few rules that actually govern the actions of a nonprofit operator of a charter school. Rules like the Charter Schools Act's spending provisions, the mega-waiver, the California Corporations Code and the entrepreneurial business practices of running a charter school. The wide business discretion given the nonprofit operator of a charter school is a direct product of the public policy of allowing charter schools to be a laboratory of experimentation. In other words, to analyze the appropriateness of a Penal Code §424 prosecution in this case, the authorizing rules that bind the business conduct of the defendants needed to be understood. In *Stark*, the California Supreme Court called these authorizing rules "non-penal laws."

Using the subject of administrator or teacher compensation and perquisites as an example, the Supreme Court would have the prosecutor meet its burden by producing rules and regulations governing the setting of compensation. If there is a regulation binding a charter school operator that forbids the provision of morale-building perquisites (such as lunches or a holiday party) these are the kinds of "non-penal laws" that would rescue Penal Code §424 from a due process attack based on a lack of bright line specificity. "Vague laws may trap the innocent by not providing fair warnings. Second, if arbitrary and discriminatory enforcement is to be prevented, laws must provide explicit standards for those who apply them. A vague law impermissibly delegates basic policy matters to policemen, judges, and juries for resolution on an *ad hoc* and subjective basis, with the attendant dangers of arbitrary and discriminatory applications." (*Grayned v. City of Rockford*, 408 U.S. 104, 108-09(1972), quoted in *Village of Hoffman Estates v. The Flipside*, 455 U.S. 489,498(1982).)

The final jury instructions are examples of perfectly circular reasoning– Penal Code §424 says do not steal; so does the school's charter. Penal Code §424 says do not steal; so do the corporate by-laws. Penal Code §424 says do not steal; so does the Education Code. In other words, the alleged non-penal laws provide no greater specificity than Penal Code §424 itself. In *Stark*, the Supreme Court held that Penal Code §424 alone, without the specificity of non-penal laws, would render the prosecution unconstitutional. *To repeat, to satisfy the Constitution and the rule in Stark, the non-penal law or laws have to specifically require or prohibit the defendant's conduct*. (Id. At 30.)

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In defendant's case, despite the Court's disapproval of the prosecution's reliance on the biblical admonition "Thou shalt not steal", the Court nonetheless permitted the case to go to the jury on a similarly vague basis. *Stark* held that to pass constitutional muster the applicable non-penal law must specifically prohibit the conduct of accused. Prosecutions of the type demonstrated in defendant's case risk violating that important concept.

b. Rule Number Two: The *Mens Rea* Requirement

The second way the *Stark* court narrowed Penal Code §424 and preserved it from constitutional failure is Rule Two – the imposition of a distinct *mens rea* requirement. The Court held that "[s]trong public policy supports a rule requiring either actual knowledge or criminal negligence in failing to know the legal requirements underlying the section 424 charges. . . .The negligence must be aggravated, culpable, gross, or reckless." (*Id.* at 32.) Of course, Rule One and Rule Two act together. That is, the "bright line" has to be truly bright for the transgression of it to be truly reckless. What if, instead of going to the prosecutor, LAUSD Office of Inspector General ("OIG") staff had followed LAUSD's statutory obligation (as discussed in Section III) and called for a meeting with the charter school operators? Assume that at that meeting the OIG expressed the opinion that some of the expenditures and reimbursements appeared to be, in their view, unlawful. Of course we do not agree that any such expenditures were unlawful (see above), but let us assume for the sake of argument that there is a written prohibition somewhere, applicable to charter schools, against taking teachers out to lunch and paying with a school credit card. Despite such notice, let us assume that the conduct (as in *Stark*) persisted. In that case the jury would be free to examine the conduct of the defendants to determine if the notice from the OIG was sufficient to make the defendants' conduct criminally negligent or reckless. But nothing of the sort occurred here. In fact, just the opposite occurred. Every supervisory agency or individual who had the opportunity to examine the defendant's finances gave approval. The defendants' accountants, the defendants' auditors, the defendants' Board of Directors, the defendants' authorizer, the County Board of Education, the State Controller and the California Department of Education, all either specifically approved the financial documents or were silent on the issues. The credit card bills were neatly stacked and available, along with backup receipts. Reimbursement was neatly logged. The books were, for the most part, clearly understandable and

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open. The leases were specifically approved by the Board of Directors in an open public meeting and captured in the public minutes. Given all this, how could this Court possibly allow the case to go to the jury on the issue of criminal negligence?

The imposition of a *mens rea* requirement is linked to the fair warning requirement. In *Stark*, defendant violated specific legal instructions from supervisors (bright line: Rule One), and admitted, in some instances, that he understood that his legal obligation required him to obey. As defendant's case demonstrates, nonprofit operators of charter schools function in a much different environment. Instead of the clear non-penal law warning Stark received, defendants had to contend with the prosecution's conviction that the obligation is plainly obvious, without that belief being evidenced by non-penal laws and proof of knowledge of such non-penal laws. This is precisely the evil addressed by the U.S. Supreme Court in *Grayned*, *supra*: prosecution without specific non-penal laws "impermissibly delegates basic policy matters to policemen, judges, and juries for resolution on an *ad hoc* and subjective basis, with the attendant dangers of arbitrary and discriminatory applications."

It really does not matter here what the defendants' (or Stark's) motivation for their conduct was. Rules One and Rule Two require an objective standard, skewed in favor of the accused. That standard requires the burden to always be on the prosecution to demonstrate the bright line and the mental element of the defendant who is alleged to have crossed it. That burden was never met here, nor as a matter of law, could it have been met; which leads us to Rule Three.

c. Rule Number Three: The Judge Must be the Finder of Law and the Jury the Finder of Fact

Using the teacher lunch example, instead of guiding the jury to determine whether in fact the defendants took a teacher out to lunch and paid for it with a school credit card in violation of a specific non-penal law and that they took this action knowing that it was illegal, or with such criminal negligence as to equate to knowledge of illegality, the Court permitted the jury to determine, generally, whether a non-penal law was in fact broken. Now, if Rule One had been satisfied and there were a non-penal law specifically prohibiting teacher lunches, there would be no error. Finally, even though there was no non-penal laws that clearly prohibited defendant's conduct, the jury was permitted to speculate whether the school's charter, by-laws, or non-applicable provisions of the Education Code

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were violated, with no direction as to what the vague terms contained in these documents –terms such as "fiscal mismanagement" or "misuse of school property" or "fiduciary responsibility" -- actually mean.

As argued earlier, to comply with *Stark* the non-penal laws have to closely track and prohibit the specific conduct alleged. In other words, the Court in defendant's case passed on its charging authority to the jury, allowing the jury to decide if one or more of a variety of vaguely-worded proscriptions should be applied. The Court never evaluated the proffered non-penal laws in order to decide if they met the *Stark* standards of specificity. It is not for the jury to rummage among a group of non-penal laws, pick one that they think applies and then keep it a secret. "Men of common intelligence cannot be required to guess at the meaning of [an] enactment." (*Winters v. New York*, 333 U.S. 507, 515-16 (1948). As the California Supreme Court recently said "it is a fundamental and historic precept of our judicial system that jurors are restricted solely to the determination of factual questions and are bound by the law as given them by the court. They are not allowed either to determine what the law is or what the law should be." (*People v. Williams* (2001), 25 Cal. 4th 441, 455.) Prosecutions of the type exhibited in defendant's case open the door to such a scenario.

B. <u>Penal Code §504 Counts Suffer the Same Disability</u>

With regard to embezzlement, Penal Code §504 contains an element nearly identical to the "authority of law" element of Penal Code §424--It is "not in the due and lawful execution of that person's trust". The identical analysis undertaken by the *Stark* Court is required here. To understand the range of these defendants' lawful execution of their trust, the Court must undertake an examination of the business and regulatory context in which the alleged acts occurred. In a Penal Code §504 prosecution the prosecution faces the identical burden as in *Stark*; that is, to show that the defendants lacked lawful authority. How should that have been done? ***Specific non-penal laws*** **–** otherwise the law suffers from a Rule One violation – no bright line. Every charge in this case requires the same missing specificity, or is derivative of the Penal Code §424 and Penal Code §504 charges.

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VI. CONCLUSION

For the forgoing reasons, amicus curiae respectfully requests the court grant a new trial consistent with the reasoning outlined herein.

Respectfully Submitted,

Dated: September 30, 2013

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