Bond Case Briefs

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BONDS - KENTUCKY

Bluegrass Equine and Tourism Foundation; and KHPWESLUX, LLC v. Commonwealth of Kentucky

Court of Appeals of Kentucky - May 10, 2013 - S.W.3d - 2013 WL 1919567

Developers entered into a series of agreements with state entities to develop a luxury hotel at a Kentucky horse park. The project was to be financed by tax-exempt bonds.

As a result of developer's inability to market the bonds, the state terminated the agreement. Developer filed a complaint against the state for breach of contract, seeking monetary damages and alleging that months of efforts and millions of dollars had been expended toward the project.

The court of appeals identified three issues: 1) Whether a "contract for construction services" existed as that term is contemplated by the RFP; 2) If so, whether developers diligently advanced work on the project under the contract; and 3) What form of notice of termination and opportunity to cure the state was required to provide, and whether or not it effectively complied.

The court first determined that a "contract for construction services" was formed. Consequently, the agreement between the parties clearly indicated that the failure to diligently advance work under the contract was an event default. The court concluded that the developer's failure to obtain financing was indeed an act of default. The court also found that the state had provided developers with proper notice of termination and an opportunity to cure.

Pursuant to the underlying agreement, the developers had a contractual obligation to reimburse the state for its costs in relocation of public utilities. However, the court concluded that a mistake occurred in this instance. "As our law makes clear, mutual mistake occurs when both parties participate in the transaction and each labors under the same conception of the alleged agreement."

Both parties were mistaken as to the availability of bond financing, and the state's belief that financing would be available was the primary reason it completed the utility projects prior to the completion of financing. The state did so with clear and full knowledge that financing had not yet been obtained and, thus, assumed the risk that the project could still fail for lack of financing. Moreover, the improvements made by the state still inure to the benefit of the commonwealth, and will facilitate any future efforts to develop the site.

The appeals court concluded that principles of equity dictate that the state should have to assume the costs of the improvements, particularly in light of the fact that it will continue to realize the economic benefits of same. The state cannot simultaneously recover from a breach of contract, and at the same time, recover for initiating a utility project at a time when it now argues it was clear that financing for the project would ultimately not be obtained.