Attachment E

BILL LOCKYER
Attorney General

State of California
DEPARTMENT OF JUSTICE

1300 I STREET, SUITE 125
P.O. BOX 944255
SACRAMENTO, CA 94244-2550

Telephone: (916) 323-5344
Facsimile: (916) 324-8835

February 8, 2006

Mr. Frank Furtek
Chief Counsel
California Health and Human Services
1600 Ninth Street
Sacramento, CA 95814

RE: Securitization of Revenues from Proposition 63 (Mental Health Services Act) Through the California Housing Finance Agency Service Contracts

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Dear Mr. Furtek:

This informal advice letter addresses the question as to whether the model proposed by the California Housing Finance Agency (CalHFA) for securitizing funding from Proposition 63, the Mental Health Services Act[1] ("MHSA"), to issue bonds for housing mentally ill homeless is consistent with the intent of Proposition 63. We also address whether proposed State long-term contracts to secure these housing bonds would create an unconstitutional debt.

We conclude that strong arguments would support a finding by a court that the securitization of funding from Proposition 63 to issue housing bonds for mentally ill homeless individuals is inconsistent with the intent of Proposition 63 and that any state contract to secure these bonds would create an unconstitutional debt.

Background

In November 2004, California voters approved Proposition 63, which imposed a new state income tax surcharge to finance the expansion of mental health services in the state. This initiative did not originate in the Legislature, but rather was legislation approved directly by the voters through the initiative process. Sherman Russell Selix, Jr., the Executive Director of the Community Mental Health Agencies, and former Assemblymember Darrell Steinberg submitted the initiative for voter approval.

[1] Initiative Measure Proposition 63, approved November 2, 2004, effective January 1, 2005.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Courts consider the information provided in the ballot pamphlet for an initiative as indicia of the voters' intent.[2] The Analysis by the Legislative Analyst in the Ballot Pamphlet for Proposition 63 described the initiative, in part, as follows:

> "**PROPOSAL**
>
> This proposition establishes a state personal income tax surcharge of 1 percent on taxpayers with annual taxable incomes of more than $1 million. Funds resulting from the surcharge would be used to expand county mental health programs.
>
> ***New Revenues Generated under the Measure.*** This measure establishes a surcharge of 1 percent on the portion of a taxpayer's taxable income that exceeded $1 million. The surcharge would be levied on all such tax filers beginning January 1, 2005...
>
> Under this measure, beginning in 2004-05, the State Controller would transfer specified amounts of state funding on a monthly basis into a new state fund named the Mental Health Services Fund. The amounts transferred would be based on an estimate of the revenues to be received from the surcharge. The amounts deposited into the fund would be adjusted later to reflect the revenues actually received from the tax surcharge.
>
> ***How This Funding Would Be Spent.*** Beginning in 2004-05, revenues deposited in the Mental Health Services Fund would be used to create new county mental health programs and to expand some existing programs. These funds would not be provided through the annual state budget act and thus amounts would not be subject to change by actions of the Legislature and the Governor. Specifically, the funds could be used for the following activities:
>
> - ***Children's System of Care.*** Expansion of existing county system of care services for children who lack other public or private health coverage to pay for mental health treatment.
> - ***Adult System of Care.*** Expansion of existing county system of care services for adults with serious mental disorders or who are at serious risk of such disorders if they do not receive treatment.
> - ***Prevention and Early Intervention.*** New county prevention and early intervention programs to get persons showing early signs of a mental illness into treatment quickly before their illness becomes more severe.
> - ***"Wraparound" services for Families.*** A new program to provide state assistance to counties, where feasible, to establish various types of medical and social services for families (for example, family counseling) where the children are at risk of being placed in foster care.
> - ***"Innovation" Programs.*** New county programs to experiment with ways to improve access to mental health services, including for underserved groups, to improve program quality, or to promote interagency collaboration in the delivery of services to clients.
> - ***Mental Health Workforce: Education and Training.*** Stipends, loan forgiveness, scholarship programs, and other new efforts to (1) address existing shortages of mental health staffing in county programs and (2) help provide the additional staffing that would be needed to carry out the program expansions proposed in this measure.

---

[2] *People v Canty* (2004) 32 Cal.4th 1266, 1281; *Kaufman & Broad Communities, Inc. v Performance Plastering, Inc.* (2005) 133 Cal.App.4th 26, 31.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

- ***Capital Facilities and Technology.*** A new program to allocate funding to counties for technology improvements and capital facilities needed to provide mental health services.

This measure specifies the portions of funds that would be devoted to particular activities. In 2004-05, most of the funding would be provided for expanding the mental health care workforce and for capital facility and technology improvements. In subsequent years, most funding would be used for new prevention and early intervention programs and various expansions of the existing types of services provided by counties directly to mental health clients.

Oversight and Administration. Under the terms of the proposition, each county would draft and submit for state review and approval a three-year plan for the delivery of mental health services within its jurisdiction. Counties would also be required to prepare annual updates and expenditure plans for the provision of mental health services.

The Department of Mental Health, in coordination with certain other state agencies, would have the lead state role in implementing most of the programs specified in the measure and allocating the funds through contracts with counties. In addition, a new Mental Health Services Oversight and Accountability Commission would be established to review county plans for mental health services and to approve expenditures for certain programs…

The measure permits up to 5 percent of the funding transferred into the Mental Health Services Fund to be used to offset state costs for implementation of the measure. Up to an additional 5 percent could be used annually for county planning and other administrative activities to implement this measure.

Other Fiscal Provisions. The proposition specifies that the revenues generated from the tax surcharge must be used to expand mental health services and could not be used for other purposes. In addition, the state and counties would be prohibited from redirecting funds now used for mental health services to other purposes. The state would specifically be barred from reducing General Fund support, entitlements to services and formula distribution of funds now dedicated for mental health services below the levels provided in 2003-04.

The state would also be prohibited from changing mental health programs to increase the share of their cost borne by a county or to increase the financial risk to a county for the provision of such services unless the state provided adequate funding to fully compensate for the additional costs or financial risk…

Partially Offsetting Savings. State and national studies have indicated that mental health programs similar to some of those expanded by this measure generate significant savings to state and local governments that partly offset their additional cost. Studies of such programs in California to date suggest that much of the savings would probably accrue to local government. The expansion of county mental health services as proposed in this measure would probably result in savings on state prison and county jail operations, medical care, homeless shelters, and social services programs…"[3]

Recently, various options have been proposed to commit part of the Proposition 63 revenue available for capital facilities to support the issuance of bonds for supportive housing projects. Proponents of this approach, including Darrell Steinberg, one of the authors of

[3] Ballot Pamp., Gen. Elec. (Nov. 2, 2004) Analysis by the Legislative Analyst of Prop. 63, pp 33-35.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Proposition 63, contend that providing services in conjunction with housing represents the most effective and efficient service delivery system for mentally ill clients who are homeless.

CalHFA has proposed one model for developing supportive housing, which contains the following key elements:

- A fixed amount of Proposition 63 revenues ($75 million per year for 20 years) would be committed to support the issuance of bonds for supportive housing projects.
- Counties would sign 20-year contracts with the California Department of Mental Health ("Department") in which the counties agree to provide supportive housing in exchange for the $75 million per year of Proposition 63 revenues from the Department.
- Counties would assign the right to this annual $75 million payment to CalHFA, who would issue bonds using the Proposition 63 funds in conjunction with other existing CalHFA fund sources. In this way, the Proposition 63 funding could be "leveraged" to create immediate opportunities for housing.
- Based on this assignment, the Department would allocate $75 million in Proposition 63 funding to CalHFA on an annual basis to pay the debt service on the housing bonds.
- CalHFA would provide loans to designated housing owners and operators who have agreements with the counties to provide supportive housing for homeless mentally ill clients.

In this approach, the bonds would finance the capital costs associated with the construction and development or the acquisition and rehabilitation of supportive housing facilities. Although the amount of housing potentially created by this approach depends on numerous variables, one CalHFA estimate concludes that approximately 10,700 units of housing would be created over the next 20 years.

CalHFA intends to pursue legislation amending the codified portions of the MHSA to explicitly allow for this type of securitization model. The MHSA may be amended by a two-thirds vote of the Legislature "so long as such amendments are consistent with and further the intent of this act."[4] Your office has requested that the Attorney General's Office (AGO) review the CalHFA model and evaluate whether it can be implemented by legislation that a court would conclude is "consistent with and furthers the intent of" Proposition 63. You have also requested that we evaluate whether the proposed contract(s) between the Department and counties to commit $75 million per year for 20 years would create an unconstitutional debt in violation of Article XVI, section 1 of the California Constitution.

[4] Prop. 63, Section 18 (uncodified). Section 18 also allows the Legislature to "add provisions to clarify procedures and terms including the procedures for the collection of the tax surcharge imposed by Section 12 of this act" by a majority vote. We assume that since Proposition 63 does not specifically provide for bonds of any nature, any amendment providing for bonding authority would not be viewed as a "clarification" of an existing procedure.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Analysis

A. Legislation Enacting The Proposed CalHFA Service Contract Model Would Exceed The Legislature's Authority Under Article II, Section 10(c) Of The California Constitution And Section 18 Of Proposition 63.

The MHSA was enacted through the initiative process pursuant to Section 8, Article II of the California Constitution. Section 10 (c) of Article II states that the electorate must approve any Legislative amendments to an initiative statute unless the initiative statute permits amendment or repeal without their approval. Courts have interpreted this provision as providing the electorate with an absolute power to place limits and conditions on the Legislature's ability to amend an initiative statute.[5] The purpose of this limitation on the Legislature's authority is to "protect the people's initiative powers by precluding the Legislature from undoing what the people have done, without the electorate's consent."[6]

As noted above, Proposition 63 states that the Legislature may amend the provisions of the MHSA by a two-thirds vote so long as the amendments are "consistent with and further the intent of" the act. In reviewing any proposed amendments, courts generally strictly construe this type of limitation on the Legislature, but they also must ensure that the voter's restrictions are given the effect that the voters intended them to have.[7] As the California Supreme Court noted in *Amwest Surety Insurance Company v. Wilson,* adopting a highly deferential standard when reviewing proposed amendments to initiative statutes might have the "ironic and unfortunate consequence of causing the drafters of future initiatives to hesitate to grant even a limited authority to the Legislature to amend those statutes."[8]

In *Amwest Surety*, the Supreme Court considered whether a legislative amendment to Proposition 103, the Insurance Rate Reduction and Reform Act, was valid pursuant to the terms of the initiative. In Proposition 103 Section 8(b), the electorate had limited the Legislature's ability to amend the initiative to those amendments that "furthered its purposes."[9] The Supreme Court determined that it would uphold the validity of the challenged amendment if "by any reasonable construction, it can be said that the statute furthers the purposes of Proposition 103."[10]

---

[5] *Amwest Surety Ins.Co. v Wilson* (1995) 11 Cal.4th 1243, 1251 (citations omitted).

[6] *Proposition 103 Enforcement Project v. Charles Quackenbush* (1998) 64 Cal.App.4th 1473, 1484 (citations omitted).

[7] *Amwest Surety Ins Co., supra,* 11 Cal.4th at 1255.

[8] *Ibid.*

[9] Stats. 1988, p A-290.

[10] *Amwest Surety Ins Co., supra,* 11 Cal.4th at 1256. We note that the restrictions in Proposition 63 represent a more rigorous test than the court considered in *Amwest Surety.* Proposition 63 requires a two-prong evaluation as to

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

In order to determine the purposes of Proposition 103, the Supreme Court was "guided by, but not limited to, the general statement of purpose found the initiative."[11] The Court also looked at context within which Proposition 103 was passed as instructive in evaluating the Proposition's purposes.

After *Amwest Surety*, other courts have expanded the discussion regarding the interpretation of initiatives, noting that the principles governing the construction and interpretation of statutes also apply when interpreting a voter initiative. Courts begin by examining the language of the initiative statute itself, giving the words their usual and ordinary meaning, viewed in the context of the statute as a whole and the overall statutory scheme. If the terms of the statute are unambiguous, courts will presume that the lawmakers meant what they said, and the plain meaning of the language governs.[12]

In evaluating the context in which Proposition 63 was passed, it is again instructive to consider the information provided by the Legislative Analyst in the ballot materials presented to the voters for Proposition 63. Under the heading of "Background", the Legislative Analyst stated, in part, as follows:

> "***County Mental Health Services***. Counties are the primary providers of mental health care in California communities for persons who lack private coverage for such care. Both children and adults are eligible to receive such assistance. Counties provide a range of psychiatric, counseling, hospitalization, and other treatment services to patients. In addition, some counties arrange other types of assistance, such as housing, substance abuse treatment and employment services to help their clients. A number of counties have established so called "systems of care" to coordinate the provision of both medical and nonmedical services for persons with mental health problems. County mental health services are paid for with a mix of state, local and federal funds. As part of a prior transfer of mental health program responsibilities from the state to counties, some state revenues are automatically set aside for the support of county mental health programs and thus are not provided through the annual state budget act. Other state support for county mental health programs is provided through the annual state budget act and thus is subject to change by actions of the Legislature and the Governor."[13]

This description clearly communicated to voters that, regardless of the funding source, counties are the primary providers of mental health services in California. It also indicates that all counties provide a range of individual treatment services to both adults and children, such as

---

whether the amendment is both consistent with and furthers the intent of the Act, whereas Proposition 103 requires only that the amendment "further its purposes."

[11] *Id. At 1257.*

[12] *Knight v. Superior Court* (2005) 128 Cal.App.4th 14, 23 (citations omitted); *See also People v Canty, supra,* 32 Cal.4th at 1276.

[13] Ballot Pamp., Gen. Elec. (Nov. 2, 2004) Analysis by the Legislative Analyst of Prop. 63, p 32.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

psychiatric, counseling and hospitalization treatment, but that some counties also arrange other types of assistance, including housing and substance abuse treatment. Finally, it makes the distinction for voters that moneys provided for through the annual state budget act are subject to change by actions of the Governor and the Legislature, but that, under some circumstances, funding can be set aside to avoid the requirement for annual state budget act approval.

The plain language of the MHSA, which was described in general terms to the voters by the Legislative Analyst (see excerpts from LAO's Analysis, "Proposal" above) reflects these same themes of county responsibility, an emphasis on individual treatment services, and the insulation of Proposition 63 funding from diversion by the Governor and the Legislature. As noted above, the initiative specifies that the funding shall be used to expand the existing county services for adults[14] and children[15] and to create new programs including services for children with severe mental illnesses,[16] county services for prevention and early intervention,[17] innovative county programs, [18] and a new program with dedicating funding for human resources, education and training to remedy the shortage of qualified service providers.[19] Clearly, the initiative's emphasis was on increased county services and training for service providers.

In addition, the initiative clearly reflects an intent to isolate the Proposition 63 revenue, designate the specified uses for the revenue, eliminate the ability of the Legislature and the Governor from diverting the funds to non-specified uses and make counties and local stakeholders responsible for both developing and implementing the specified programs. For example, the Mental Health Services Fund (MHS Fund) is continuously appropriated by the initiative for the designated purposes described above, which means that the Legislature and the Governor do not control the expenditure of the funds through the annual state budget. [20] The initiative specifies that the act shall not be construed to "modify or reduce" the existing authority or responsibility of the Department.[21] The initiative then states, in part, as follows:

> "The funding established pursuant to this act shall be utilized to expand mental health services. These funds shall not be used to supplant existing state or county funds utilized to provide mental

---

[14] Welfare and Institutions Code sections 5813.5, 5847, 5892 and 5897.

[15] Welfare and Institutions Code sections 5847, 5892 and 5897.

[16] Welfare and Institutions Code sections 5878.1-5878.3.

[17] Welfare and Institutions Code sections 5840-5840.2, 5847, 5892 and 5897.

[18] Welfare and Institutions Code sections 5830, 5847, 5892 and 5897.

[19] Welfare and Institutions Code sections 5820-5822, 5892 and 5897.

[20] Welfare and Institutions Code section 5890.

[21] *Id.*

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

> health services...These funds shall only be used to pay for the programs authorized in Section 5892 [allocation of funding for designated programs]. These funds may not be used to pay for any other program. These funds may not be loaned to the General Fund or any other fund of the state, or county general fund or any county fund for any purpose other than those authorized in Section 5892." (emphasis added).[22]

To the extent that the initiative establishes broad categories of programs to be funded, the development and implementation of the programs rest primarily at the local level. Counties are required to develop three-year plans for expenditure of Proposition 63 funding on the designated program areas, with the plan to be updated at least annually.[23] Each plan and update must be developed with local stakeholders, including circulation of a draft, a notice and comment period, and a public hearing.[24]

The draft three-year plans are reviewed by the Department and a new Commission created by the initiative, entitled the "Mental Health Services Oversight and Accountability Commission" (Commission). According to the initiative, the Commission "oversees" all of the Proposition 63 programs with the exception of the taxation provisions, and it reviews and comments on all of the three-year plans. The Commission is composed of 16 voting members, but only four represent the State. The remaining twelve members are to be members of the public, including two individuals with severe mental illnesses, family members of adults and children with mental illnesses and representatives from a variety of other interests, including a physician, a county sheriff, a mental health professional and a representative from a labor organization.[25] The Department is not a member of the Commission.

Although the Department ultimately approves the three-year plans and allocates the funding to counties, the Commission reviews and comments on all of the three-year plans and it approves the county programs for innovation and prevention and early intervention. The initiative limits the Department's review and approval of the prevention and early intervention, adult services, children's services and innovation portions of the three-year plans as "limited to ensuring the consistency of such programs with the other portions of the plan and providing review and comment to the Mental Health Services Oversight and Accountability Commission."[26]

---

[22] Welfare and Institutions Code section 5891.

[23] Welfare and Institutions Code section 5847.

[24] Welfare and Institutions Code section 5848.

[25] Welfare and Institutions Code section 5845.

[26] Welfare and Institutions Code section 5846, 5847.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Having reviewed the context and plain language of the initiative, the issues and concerns with CalHFA's model become apparent. The primary concerns consist of the following:

1. Use Of Proposition 63 Funding As Security For Long-Term Bond Funding Is Not Listed As An Approved Use And Is Inconsistent With The Dynamic Nature Of The Three-Year Plans.

When voters approve the issuance of bonds, courts view the law under which the bonds are issued as a contract between the issuing authority and the bondholders, which cannot be impaired by subsequent legislation.[27] Section 1 of Article XVI of the California Constitution states that a bond law approved by voters cannot be repealed until the principal and the interest are paid. Thus, when the electorate approves public bonds, they must be informed that the law creating the bonding authority cannot be impaired or repealed for the duration of the bonds.

In this case, neither the plain language nor the ballot information mentions use of the proposed revenue as security for long-term debt. Thus, the voters were not put on notice that they would be prohibited from significantly changing or repealing the programs being approved for a minimum of 20 years. This notice is critical for programs funded through tax revenues, because the electorate's right to repeal or suspend a tax cannot be surrendered or suspended by a grant or contract under the Constitution.[28]

Under Proposition 63, the program is structured to allow flexibility over time. Counties are required to develop three-year plans that are updated on at least an annual basis. This dynamic feature of the proposal was touted as evidence that Proposition 63 "requires strict accountability" because "to ensure accountability, they can cut off programs that aren't effective."[29] This type of accountability is identified as one of the purposes and intentions of the MHSA in the Proposition itself.[30]

CalHFA has indicated that any contracts formed and bonds sold would be subject to an explicit statement that the voters could repeal the program and the tax at any time. Obviously, the actual contract language and the disclosure language would have to be evaluated in its totality to ensure that the State was not otherwise obligated should the voters repeal or amend the tax or the program. In addition, while this approach might

---

[27] *Veterans of Foreign Wars v. State of California* (1974) 36 Cal.App.3d 688, 692.

[28] California Constitution, article XIII, section 31.

[29] Ballot Pamp., Gen. Elec. (Nov. 2, 2004) Rebuttal to Argument Against Prop. 63, p 37

[30] Proposition 63, Section 3 Purpose and Intent, subsection (e): "(e) To ensure that all funds are expended in the most cost effective manner and services are provided in accordance with recommended best practices subject to local and state oversight to ensure accountability to the taxpayers and to the public."

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

satisfy the need to make the obligation "repealable" by a statewide initiative, it does not address the notion that voters were told that the oversight panel could administratively cut off programs that were not effective.

In addition, Section 5847(e) states as follows:

> "The department shall evaluate each proposed [county three-year] expenditure plan and determine the extent to which each county has the capacity to serve the proposed number of children, adults and seniors pursuant to Part 3 (commencing with Section 5800), and Part 4 (commencing with Section 5850) of this division; the extent to which there is an unmet need to serve that number of children, adults and seniors; and determine the amount of available funds; and provide each county with an allocation from the funds available. The department shall give greater weight for a county or a population which has been significantly underserved for several years." (emphasis added.)

Clearly the statute intends the Department to evaluate each year, for each county, the county's capacity to serve, relative to its unmet need, in the context of the amount of funding available and whether or not the county has been underserved for several years. All of these indices will change for each county and for the State on an annual basis. A long-term commitment for bonds may limit the Commission's ability to comply with the statute's mandate to be responsive to counties whose unmet needs change over time and who become underserved as funding and capacity lag behind.

Thus, in the early years while bonds proceeds are being allocated, the needs of those counties with high unmet needs relative to housing homeless mentally ill individuals will take precedent over the needs of those counties whose unmet needs increase and become underserved in later years, since $75 million each year for 20 years will be spent to address the initial unmet needs for housing in the counties with bond-funded projects.

2. The Creation Of A New, Unproven State Bond Program Was Never Proposed To Voters And Is Inconsistent With The Initiative's Emphasis On The Expansion Of Proven County Services Programs And The Prohibition Against State Diversion For Unspecified Purposes.

   As described above, the focus of Proposition 63 based on the context of the initiative and its plain language is an increase in funding of designated county mental health services, as proposed and implemented at the local level, and restrictions on the ability of the state to alter the priorities specified in the law. Both Proposition 63 and

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

the Ballot Pamphlet emphasize the notion that the funding would be used to expand community-based programs that have already demonstrated success.[31]

The Rebuttal to Argument Against Proposition 63 in the Ballot Pamphlet makes a forceful statement regarding these points. It stated, in part, as follows:

> "...PROPOSITION 63 EXPANDS A PROGRAM THAT WORKS.
>
> After decades of neglecting mental illness, California began an experimental, community-based mental health program five years ago. It helps teenagers and adults get the care they need from one place. Special community teams offer treatment, medicines, housing, job training and other assistance.
>
> The program has been studied extensively. (See www.AB34.org.)...
>
> PROPOSITION 63 REQUIRES STRICT ACCOUNTABILITY.
>
> Under Proposition 63:
> 1. Funding goes only to these proven, new programs.
> 2. Bureaucrats can't redirect the funding.
> 3. An oversight panel of independent, unpaid members supervises expenditures.
> 4. To ensure accountability, they can cut off programs that aren't effective."[32] (emphasis added).

Homelessness and housing for the mentally ill are mentioned in both the initiative and the Ballot Pamphlet as an issue for California. However, the "proven, new" programs being promoted are generally described as a "community-based" programs which provide a variety of integrated services, one of which is housing. Even a casual review of the

---

[31] Proposition 63, Section 2, Findings and Declarations: "...(e) With effective treatment and support, recovery from mental illness is feasible for most people. The State of California has developed effective models of providing services to children, adults, and seniors with serious mental illness. A recent innovative approach, begun under Assembly Bill 34 in 1999, was recognized in 2003 as a model program by the President's Commission on Mental Health. This program combines prevention services with a full range of integrated services to treat the whole person, with the goal of self-sufficiency for those who may have otherwise faced homelessness or dependence on the state for years to come. Other innovations address services to other underserved populations such as traumatized youth and isolated seniors. These successful programs, including prevention, emphasize client-centered, family focused and community-based services that are culturally and linguistically competent and are provided in an integrated services setting. (f) By expanding programs that have demonstrated their effectiveness, California can save lives and money..."

Section 3, Purpose and Intent. "The people of the State of California hereby declare their purposes and intent in enacting this act to be as follows:...(c) To expand the kind of successful, innovative service programs for children, adults and seniors begun in California, including culturally and linguistically competent approaches for underserved populations. These programs have already demonstrated their effectiveness in providing outreach and integrated services, including medically necessary psychiatric services, and other services to individuals most severely affected by or at risk of serious mental illness."

[32] Ballot Pamp., Gen. Elec. (Nov. 2, 2004) Rebuttal to Argument Against Prop. 63, p 37

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

website referenced in the Ballot Pamphlet indicates, at most, city or county programs which construct housing for homeless mentally ill individuals in order to deliver services. Our review of the website, although brief, gave no indication that these programs required bond funding nor that the state had any control other than the provision of funding to the local community-based programs.

As noted above, the MHSA has numerous controls on the use of the revenue, including a continuous appropriation of the fund to avoid state diversion, a detailed inventory of the activities to be funded, and an explicit statement that the funding can only be used for those specifically designate purposes. In addition, the MHSA has strict limits on the use of funds for administrative purposes at both the state and local levels. For state administrative costs, the MHSA states as follows, in part:

> "...the department shall also provide funds for the costs of itself, the California Mental Health Planning Council and the Mental Health Services Oversight and Accountability Commission to implement all duties pursuant to the programs set forth in this section. Such costs shall not exceed 5 percent of the total annual revenues received for the fund. The administrative costs shall include funds to assist consumers and family members to ensure the appropriate state and county agencies give full consideration to concerns about quality, structure of service delivery or access to services. The amounts allocated for administration shall include amounts sufficient to ensure adequate research and evaluation regarding the effectiveness of services being provided and achievement of the outcome measures set forth in Part 3 (commencing with Section 5800), Part 3.6 (commencing with 5840) and Part 4 (commencing with Section 5850) of this division..." (Emphasis added).[33]

From the plain language of the initiative, it is clear that state administrative costs are intended to be limited. All of the oversight costs of the Department, the Commission, and other state advisory committees must be covered within this allocation. In addition, within its allocation, the State must provide funding to ensure that consumers and family members have access to participate in the process and it must also fund research and evaluation processes to ensure the effectiveness of the program.

Given these limitations on the state's administrative allocation, it is not clear whether the costs of issuance, including the costs of CalHFA staff, underwriters and bond counsel, could reasonably be paid within the state allocation without sacrificing other specified duties. These costs of issuance might be particularly expansive given the complexity of CalHFA's model, which represents a new model for the State involving numerous agreements and funding sources.[34] Again, the plain language of the initiative restricts the

[33] Welfare and Institutions Code section 5892(d).

[34] CalHFA has indicated that its work with the Bay Area Housing Plan, in conjunction with the Department of Development Services, represents an example of an existing program comparable to the proposed Proposition 63

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

State's ability to divert funds for unspecified programs and limits the State's administrative expenses. There is no indication that the voters contemplated the creation of a new, complex, state-controlled bond program which would divert funding from the specified priorities for a 20-year period, particularly with MHSA language indicating that the initiative was not intended to modify the existing authority or responsibility of the Department.[35]

3. Housing Is Not Explicitly Designated As A Key Priority For Funding, And The Commitment Of Funding To Long-Term Debt Service For Housing Effectively Makes It A Priority Over Other Designated Service Programs.

Proposition 63 mandates a complicated formula for allocating percentages of the revenue to be used for the various specified programs, and some of these percentages change over time. MHSA does not designate housing for the homeless mentally ill as an approved use of the funds, although it provides funding for "capital facilities." In the first three years (2005-06, 2006-07 and 2007-08), 10 percent of the funding shall be used for "capital facilities and technological needs distributed to counties in accordance with a formula developed in consultation with the California Mental Health Directors Association to implement plans developed pursuant to Section 5847 [three-year plans]."[36] During that same period, approximately 50 percent of the funding is to be distributed to counties for services to adults and children.[37]

After 2007-08, the allocation for funding distributed to counties for services to adults and children increases to approximately 70 percent. Within this allocation, programs for services "may include funds for technological needs and capital facilities, human resources needs and a prudent reserve to ensure services do not have to be significantly reduced in years in which revenues are below the average of previous years. The total allocation for purposes authorized by this subdivision shall not exceed 20 percent of the average amount of funds allocated to that county for the previous five years pursuant to this section." (emphasis added.)[38]

---

model. The extent to which the existing BAHP framework may be used is unclear; however, we note that BAHP involves contracts between a non-state entity (Regional Centers) and the housing developer based on a legislatively created statutory program, where the funding comes primarily from the General Fund and is subject to appropriation through the annual budget act. With Proposition 63, the state itself (the Department) would be contracting with local counties pursuant to a statute enacted through initiative in which the underlying fund source is a tax which is continuously appropriated.

[35] Welfare and Institutions Code section 5890 (c). We note that the Department currently does not have the statutory authority to enter 20-year contracts.

[36] Welfare and Institutions Code section 5892(a)(2).

[37] Welfare and Institutions Code section 5892(a)(5).

[38] Welfare and Institutions Code section 5892(b).

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

It may be reasonable to assume that housing for homeless could be included in the types of "capital facilities" to be funded. However, the funding for all of the listed purposes, including (but not limited to) capital facilities, is limited to 20 percent of the average amount of funds allocated to each county for the previous five years. Thus, the amount of funding for these purposes must be established on a county-by-county basis and will vary over time.

This accounting becomes more complex upon consideration of how the tax revenue itself is calculated. In simplistic terms, each month the Controller deposits an amount into the MHS Fund (probably from the General Fund) which is an estimate of the amount of revenue which will be generated from the tax.[39] On an annual basis, State makes an adjustment to the MHS Fund to reconcile the true receipts with the estimated deposits in the fund. If the estimate was high (too much money was transferred to MHS Fund), then the Controller will suspend monthly transfers until the overage is corrected. If the estimate was low (not enough money was transferred into the MHS Fund), then the Controller must transfer funds from the General Fund into the MHS Fund to reconcile the accounts. However, this annual accounting and reconciliation appears to occur two years in arrears. That is, the reconciliation between deposits based on estimates and actual receipts for any given year will not take place until at least two years after the funding was estimated and allocated.[40]

In short, in any year after 2007-08, each county submits a three-year plan and receives an annual allocation which is based, in part, on the overall estimated amount of revenues to be generated throughout the State by an income tax during the applicable period. As a subset of this allocation, each county may use a portion of its individual allocation for adult and children services (approximately 70 percent of its individual allocation) to fund capital facilities, technological needs, human resource needs or to fund a prudent reserve. However, the total allocation for these purposes also "shall not exceed 20 percent of the average amount of funds allocated to that county for the previous five years pursuant to this section."[41] In addition, the funding in the MHS Fund to be allocated will vary from year to year because of changes in the tax base and the annual adjustment to reconcile for prior years.

With this complicated, county-specific formulation and a variable revenue stream, it seems problematic for the State to prospectively demonstrate compliance with an explicit limit on capital funding through a fixed-dollar commitment at the State level for 20 or more years. If 20-year contracts are signed by the State as security for long-term bonds,

---

[39] Revenue and Taxation Code section 19602.5(a)-(b).

[40] Revenue and Taxation Code section 19602.5(c).

[41] Welfare and Institutions Code section 5892(b).

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

the State must allocate this fixed amount of revenue to CalHFA, regardless of whether any of the counties with housing projects exceed the 20 percent limit. Therefore, a 20-year State commitment to fund bonds for housing might eliminate the State's ability to control compliance with the 20 percent limitation. In addition, if overall revenues fall below this fixed amount in any one year, it is unclear whether the General Fund would be required to make up the shortfall. Finally, this 20-year commitment would elevate housing as a priority over other designated activities, including a prudent reserve for services for adults and children in those years in which the revenues fall below the average of previous years.

4. Proponents' Arguments In Support Of The Model Do Not Appear Persuasive.

Proponents of the CalHFA model assert various arguments supporting a conclusion that the model is "consistent with and furthers the intent of" the initiative. Many of the arguments address the merits of the approach. We note, however, that our role is not to opine as to whether the CalHFA model furthers the public good, but whether the proposed model furthers the purposes of initiative as specified by Proposition 63 and required by Article II, Section 10 (c) of the Constitution.[42] Therefore, we address only those arguments involving consistency with the MHSA:

- *Proponent Argument: Housing was always intended as one of the uses for Proposition 63 funding.*

  Response:

  Darrell Steinberg, one of the proponents of Proposition 63, supports the CalHFA model, and has stated that permanent housing was always intended as one of the uses for Proposition 63 funding. While this statement might lend public credibility to the model, courts generally do not recognize a declaration by one of the drafters regarding an initiative's intended purpose as valid extrinsic evidence for determining the voters' intent.[43] In addition, the initiative mentions homelessness and housing as an issue in its preamble but it does not list permanent housing for homeless mentally ill clients as a one of the listed designated services to be funded by Proposition 63. If an initiative's language is clear, courts will assume that the drafters said what they meant

[42] *See Amwest Surety Ins Co, supra,* 11 Cal.4th at 1265.

[43] *See Knight v Superior Court, supra,* 128 Cal App. 4th at 25; *Kaufman & Broad Communities, Inc., supra,* 133 Cal.App.4th at 37.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

and meant what they said. If the drafters wanted permanent housing to be a priority, they could have made this intent clear and explicit. They did not.[44]

- *Proponent Argument: Proposition 63 funding is not "county" funding. The State has discretion as to whether it allocates to counties because it approves the 3-year plans.*

  Response:

  Throughout the statute, the plain language indicates that the Department shall distribute or allocate funds to counties, counties shall provide services and the Department shall contract with counties for the provision of those services. In particular, under Welfare and Institutions Code section 5847, each county shall prepare and submit a three-year plan to be updated annually for the provision of services provided for in MHSA.[45] In turn, the Department shall inform counties of the amounts available for services for adults and children, shall evaluate each proposed expenditure plan, and shall provide each county with an allocation of funds available, based on a determination of the county's capacity to serve, the county's unmet need and the amount of available funds.[46]

  Likewise, under Welfare and Institutions Code section 5897, the Department shall implement the services provided to adults and children, as well as the contracts for innovative programs and early intervention, through annual county mental health performance contracts.[47] These requirements, together with provisions limiting the Department's scope of review of the three-year plans[48], suggest that the Department's role is intended to consist primarily of oversight as to how and where the funding is distributed to counties. Other than development of the five-year education and training development plan under Part 3.1 of the initiative, there is no indication from the plain language of the statute that voters intended to provide the State with the discretion to create and/or mandate its own state-wide bond program and withhold a fixed amount of funding over a 20-year period in lieu of allocating the funding directly to the counties for the provision of services.

---

[44] *See, e.g., Knight v. Superior Court, supra,* 128 Cal. App.4th at 24 (Court holds that statute providing rights to domestic partners not invalid when initiative could have easily and effectively stated an intent to repeal or regulate domestic partnerships, but plain language of Proposition 22 regarding marriage does not state such an intent.)

[45] Welfare and Institutions Code section 5847(a).

[46] Welfare and Institutions Code section 5847(d), (e).

[47] Welfare and Institutions Code section 5897(a), (c).

[48] Welfare and Institutions Code section 5847(b).

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

- *Proponent Argument: The CalHFA model is consistent with the general intent and purpose of Proposition 63, and is the most effective means of providing services for mentally ill individuals that are homeless.*

  Response:

  As noted previously, a court's role in evaluating legislation amending a voter-approved statute is not whether the legislation addresses the same concerns and is good public policy, but whether it conforms to the restrictions on amendments imposed by the voters in the initiative itself.[49] In this case, the legislation implementing the CalHFA model would have to be consistent with and further the intent of Proposition 63.

  Section 18 of Proposition 63 states "This act shall be broadly construed to accomplish its purposes." This directive, along with the Supreme Court's test of "reasonable construction" in *Amwest Surety*, could be interpreted to provide the State with substantial discretion to propose a variety of procedural mechanisms for "allocating" funding to counties to enable them to provide services to mentally ill individuals. [50] These general declarations, however, cannot be used to negate specific directives when the language of the statute is plain.

  In *Foundation for Taxpayer and Consumer Rights v. Garamendi*[51] *("Foundation for Taxpayer")* the Court of Appeal considered whether a statute amending Proposition 103 was invalid because it did not further the purposes of and undermined one of the major purposes of the initiative. As noted above, in Section 8(b) of the initiative, the electorate had limited the Legislature's ability to amend the initiative to those amendments that "furthered its purposes."[52]

  In *Foundation for Taxpayer*, the amending statute allowed automobile insurers to grant a discount on the basis of whether an applicant was previously insured by any insurer. Plaintiffs claimed that this provision was inconsistent with and undermined one of the purposes of Proposition 103, which was to eliminate discrimination against previously uninsured drivers.

---

[49] *See Amwest Surety Ins Co., supra,* 11 Cal.4th at 1265.

[50] However, as noted above, the Proposition 63 limitations on amendments are more rigorous than those considered by the court in *Amwest Surety*. (See footnote 10.)

[51] *Foundation for Taxpayer and Consumer Rights v. Garamendi,* (2005) 132 Cal.App.4th 1354.

[52] Stats. 1988, p A-290.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

> Although proponents of the amending statute disagreed on this characterization of Proposition 103's purpose, the Court noted that "[a] valid amendment to Proposition 103 must not only further its purposes in general, but it cannot do violence to specific provisions of Proposition 103. So even if an amendment can be shown to further its purposes, it may nonetheless be invalid if it violates a specific primary mandate."[53] The court held that the statute violated the specific Proposition 103 mandate that prohibited insurers from using the absence of prior insurance, in and of itself, as a criterion in determining eligibility for discounts, rates, premiums or insurability.[54]
>
> In this case, the plain language of the statute mandates that the Department shall allocate the funds to each county to provide services on an annual basis based on each county's capacity and unmet needs, the amount of funding available for that year, and whether the county has a history of being underserved. The statute also identifies specific uses and percentages for the funding and indicates that the funds may not be used to pay for any program other than those specified. The State's long-term commitment of funds for a state bond program for housing homeless mentally ill individuals would appear to violate the Proposition's specific mandates. The Proposition contains no mention of bonds and debt service, and it does not designate permanent housing as a priority use for the funds. The State would not be allocating the available funding to the counties each year based on consideration of the current needs of all counties and could not "give 'greater weight' to counties which have been significantly underserved" because a portion of the funding would have been committed on a 20-year basis to previously identified needs of specific counties.

In summary, when voters approved Proposition 63, they were told that counties are the providers of services, and that the funds generated by this tax could only be used for specified new county service programs and the expansion of existing, proven community programs. The funds could not be diverted by the State and local stakeholders had an ongoing role in determining the use of funds, which were allocated to counties each year based on their current needs and capacity. Fiscal accountability was incorporated into the proposal because programs could be stopped if they were not effective. The State had a limited role in oversight of the

---

[53] *Foundation for Taxpayer and Consumer Rights, supra,* 132 Cal.App.4th at 1370.

[54] *Id.* In the *Foundation for Taxpayer* case, the proposition language read: "The absence of prior automobile insurance coverage, in and of itself, shall not be a criterion for determining eligibility for a Good Driver Discount policy, or generally for automobile rates, premiums or insurability. " (Insurance Code section 1861.02(c).) The amending statute added the following language to section 1861.02(c): "However, notwithstanding subdivision (a), an insurer may use persistency of automobile insurance coverage with the insurer, an affiliate, or another insurer as an optional rating factor. The Legislature hereby finds and declares that it furthers the purpose of Proposition 103 to encourage competition among carriers so that coverage overall will be priced competitively. The Legislature further finds and declares that competition is furthered when insureds are able to claim a discount…"

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

program and there were limits on the amount of funding that could be used for State administrative costs.

In contrast, the CalHFA model represents an unproven state program involving a commitment for 20+ years for bonds, which were not contemplated by the statute, for a use that was not designated as a priority. The State would be bound through contract to not eliminate the program for the duration of bonds unless the voters repealed the program and/or the tax in a statewide initiative. The State could not use the committed funds for any other purpose for the duration of the bonds, even if counties without bond projects demonstrated unmet needs that had been significantly underserved for a period of years. Payment for these bonds will take priority over any other program specified in the proposition, because all other payments would be annual commitments. State administrative costs would increase significantly as a result of this program, and it is unclear whether, over time, the designated uses for both the program and administrative funds would be sacrificed to pay for the State's long-term bond commitment.

In conclusion, we believe that strong arguments exist to support a finding by a court that legislation adopting the CalHFA model would be invalid as inconsistent with Proposition 63 because the State would be functionally prohibited from complying with specific primary mandates within the MHSA.

B. Twenty-Year Contracts Committing Revenue To Secure Bonds Under CalHFA's Service Contract Model Would Constitute A "State Debt" In Violation Of The Constitution. These Contracts Cannot Be Made Sufficiently Conditional To Withstand A Challenge Based On The Current Status Of The Constitutional Debt Limit Jurisprudence.

1. Service Contract Exception

It has been suggested that a long-term contract would be permissible under the debt limit under the "service contract" model. This longstanding exception to the local debt limit has significant amount of case law approving and controlling its use. In general, to employ the service contract model the contract only requires each payment for the consideration actually furnished.[55] The Supreme Court has "repeatedly applied this principle to uphold multiyear contracts in which the local government agrees to pay in each successive year for land, goods, or services provided during that year."[56] Certain long-term contracts pass muster under the debt limit because the obligation to pay in future goods is contingent upon first receiving something such as goods, services or the use of real property in that year. [57] Therefore, in order for the

[55] *McBean v. City of Fresno* (1896) 112 Cal.159.

[56] *Rider v. San Diego* (1998) 77 Cal.Rptr.2d 189, 196.

[57] *See Dean v. Kuchel* (1950) 35 Cal.2d 444, 447 (Supreme Court concludes that long term contracts may be upheld "but only where no liability or indebtedness came into existence until the consideration was actually furnished.")

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

proposed 20-year contracts to be exempt from the current debt limit the Department would have to receive a service/consideration prior to any obligation to make a payment.

This office has opined that:

> According to its common definition, the term 'service' extends to any act performed for the benefit of another under some arrangement or agreement whereby such act was to have been performed.[58]

As discussed above, counties are the primary providers of mental health services to individuals in the community. Therefore, Proposition 63 provides funding for obligations which are inherent to local governments rather than the State. It has been proposed that the Department enter into 20-year "service" contracts with counties to provide funds for the county to operate a supportive housing program. However, since the localities, rather than the State, have the primary obligation to serve the mentally ill population, the State would receive no "services" under a contract in which the State pays the counties to provide services for the mentally ill.

Proponents of the service contract model suggest that the conditions or contingencies placed on the grant recipients in order for them to receive money are the "services" or "consideration" rendered to the State such that this type of long-term contract would not violate the debt limit. However, such conditions do not transform a grant[59] contract into a contract where services are being provided to the State. Instead the conditions imposed on the grant recipients "serve primarily to ensure that all grant funds will be properly spent and the projects will be duly monitored and completed." [60] This office has opined that such grant contracts do not constitute a contract for goods or services "even if, as here, the grants are made pursuant to an

---

[58] 74 Ops. Cal. Atty. Gen 10 (1991). We note that Opinions of the Attorney General, while not binding on the courts, are entitled to great weight. (*Napa Valley Educators' Assn.* v. *Napa Valley Unified School District* (1987) 194 Cal.App.3rd 243, 251.)

[59] This office views the proposed Department contracts with counties to be grant contracts for several reasons. First, as described above the programs involved are essentially county programs for which the State is simply providing resources for the counties to carry out their programs. (*See* Welfare and Institution Code section 17000 and Ballot Pamp., Gen. Elec. (Nov. 2, 2004) analysis by the Legislative Analyst pp. 32-34.) Thus, these contracts comport with the description of grant contracts described in formal Attorney General Opinions as described more fully below, in that they do not provide services for the benefit of the Department rather they provide funds for the accomplishment of a specified project. (58 Ops. Cal. Atty. Gen. 586, 590-591 (1975).) Secondly, the statutory language also supports this view. For example one of the areas for funding is the Adult and Older Adult System of Care Act which provides that "the department shall provide annual oversight of grants issued pursuant to this part for compliance. . . ." (Welfare and Institution Code section 5806.)

[60] 88 Ops. Cal. Atty. Gen 56 (2005) (citing 74 Ops. Cal. Atty. Gen. 10, 15 (1991) and 58 Ops. Cal. Atty. Gen. (1975) 586, 590-591)

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

executed agreement." [61] Additionally grants are viewed as "furthering the purposes of the grantee not the Department, subject to the powers of the Department to provide administrative assistance relating to the programs for which it funnels funds." [62] Importantly, this office has opined that under such circumstances "the Department receive[s] no consideration from the grantee pursuant to the grant documents." [63] Simply stated, such grants are not "'procurement contracts' through which a state agency acquires goods or services, but are instead awards of assistance to others...to support projects undertaken by the grantees in the public interest"[64]

Since this office has found that no case law running counter to these formal Attorney General Opinions, we are of the view that such a 20-year contract would violate the state's debt limit as it is currently understood because the Department would not be receiving consideration in any year when payment is due.[65]

2. Revenue-Lease

It has been suggested that analyzing the grant contract under the revenue lease or Offner-Dean[66] exceptions could provide the State with an exception to the debt limit. For the reasons stated below, this office does not believe that this exception applies to the proposed Department contract.

---

[61] 88 Ops. Cal. Atty. Gen 56 (2005) (citing 74 Ops. Cal. Atty. Gen. at 151 (1991) and 63 Ops. Cal. Atty. Gen. 290 (1980).)

[62] 63 Ops. Cal. Atty. Gen. 290, 292 (1980).

[63] *Ibid. See also* 74 Ops. Cal. Atty. Gen. 10 (1991).

[64] 88 Ops. Cal. Atty. Gen 56 (2005).

[65] It may be argued that consideration is not actually necessary if sufficient contingencies are put in place. There is language is some cases that could be used to frame such an argument to a court. Additionally, it can be argued that the term "service contract" is broad enough to include what this office describes as "grant contracts." However, this office could not find any cases so holding. Without such case law, this office believes it prudent to not reach conclusions on such a radically different view in this arena. This view certainly does not foreclose this office from bringing such an argument before a court to determine its validity.

[66] California uses an abatement lease structure known as the "Offner-Dean" exception. (*City of Los Angeles v. Offner* (1942) 19 Cal.2d 483; *Dean v. Kuchel* (1950) 35 Cal.2d 444, 446.) This approach was restated and confirmed in *Rider v. City of San Diego* (1996) 47 Cal.App.4th 1473. In these financings, the payment of the lease obligation is subject to abatement, use and occupancy has to be tendered to the user during each lease period, and the lease cannot be accelerated due to default. For example, SPWB abatement lease financings (the typical SPWB bond financing structure) are supported by a continuous appropriation (See Government Code section 15848), which is not improper in that context because there is a legal obligation to make the lease payment in the abatement lease structure if use and occupancy has been provided and no abatement event has occurred.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

A lease "creates no immediate indebtedness for the aggregate installments, confines liability to each installment as it falls due and each year's payments is for the consideration actually furnished that year, and there is no right to acceleration." [67] However, as discussed above, the Department would not be receiving any consideration and thus its payments do not satisfy the Offner-Dean financing. In fact, as we understand the proposed model, any leases would be between a county and an operator of a facility. Therefore, this exception, while being available to the county with its operator, would not be available to the Department and the county.

Additionally, even if we were to assume for the sake of argument, that there was some type of consideration given to the Department, we have been informed that these payments would be required to be made prior to the use and occupancy of the building involved and even if the buildings ceased being used for the contracted purpose.

It has been held generally in the numerous cases that have come before this court involving leases and agreements containing options to purchase that if the lease or other agreement is entered into in good faith and creates no immediate indebtedness for the aggregate installments therein provided for but, on the contrary, confines liability to each installment as it falls due and each year's payment is for the consideration actually furnished that year, no violence is done to the constitutional provision.[68]

3. Appropriations Exception

The final debt limit exception that has been suggested for this contract is seldomly used appropriations exception.[69] In order to qualify under the appropriations exception to the debt limit, there can be no legally enforceable obligation against the State's general fund or taxing power[70] and the "obligation" of the State must be subject to annual discretionary appropriation by the Legislature. The appellate court has explained, "since there is no legal obligation to appropriate money for payments in future years there is no violation of the debt limitation provision [Article XVI, Section 1] of the California Constitution." [71]

---

[67] *Dean v. Kuchel* (1950) 35 Cal.2d 444, 446 (quoting *City of Los Angeles v. Offner* (1942) 19 Cal.2d 483, 486)

[68] *Los Angeles County v. Nesvig* (1965) 231 Cal.App.2d 603, 609.

[69] While this exception is widely used for lease financings in other jurisdictions, California has favored the abatement lease structure under the "Offner-Dean" exception.

[70] *California Housing Finance Agency v. Elliott* (1976) 17 Cal.3d 575 (citing *California Educational Facilities Authority v. Priest* (1974) 12 Cal.3d 593).

[71] *Mayhew Tech Center, Phase II v. County of Sacramento* (1992) 4 Cal.App.4th 497, 515; *See also Board of Supervisors of the City and County of San Francisco v. Dolan* (1975) 45 Cal.App.3d 237 (a discretionary appropriation does not constitute a legally enforceable obligation).

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

Under Proposition 63, the funding at issue is continuously appropriated.[72] The voters placed this continuous appropriation for all funds in the Mental Health Service Fund and it may not be eliminated by the Legislature. In fact, as noted above, ballot materials for Proposition 63 stated that "bureaucrats can't redirect the funding."[73] Based on that continuous appropriation, bondholders could reasonably expect that they have an appropriation for payment of principal and interest on their bonds. A court would likely determine that this reliance created a contractual right of the bondholder to obtain payment regardless of the desire of the Legislature to not appropriate, especially since the Legislature has no power to eliminate the appropriation.[74] Therefore, since there is a continuous appropriation in this case, reliance on a debt limit exception that is premised on the annual legislative discretion to refuse payment appears misplaced.

It has been argued that since Department annually "allocates" the money, this would satisfy the requirements of the appropriations exception.[75] However, as discussed above, the appropriation exception is premised on legislative discretion - not executive discretion. A look at the practical consideration helps illustrate why an executive duty to annually allocate cannot be viewed as identical with the legislative prerogative of whether or not to appropriate. A court cannot issue a writ compelling the Legislature to appropriate money as this violates the separation of powers.[76] However, the courts can issue a writ against the executive branch to compel them to exercise a duty. [77] Thus, Department could be compelled to allocate funds and its actions can be reviewed by a court. In contrast, the Legislature could never be compelled to appropriate funds. Simply stated, the choice to appropriate is not intrinsically the same as the requirement to allocate funds continuously appropriated.[78] Therefore, the appropriations exception to the debt limit is not available here.

---

[72] Welfare and Institutions Code section 5890 (a).

[73] Ballot Pamp., Gen. Elec. (Nov. 2, 2004) Rebuttal to Argument Against Prop. 63, p 37

[74] *See Walsh v. Board of Administration PERS* (1992) 4 Cal.App.4th 682.

[75] Welfare and Institutions Code section 5892 (a).

[76] *City of Sacramento v. Legislature* (1986) 187 Cal.App.3d 393.

[77] *South of Dakota v. Brown* (1978) 20 Cal.3d 765 (Governor can be compelled by writ of mandate to consider whether or not to extradite a fugitive.)

[78] Again, arguments can be framed that allocating and appropriating funds are sufficiently analogous that the appropriations exception to the debt limit should extend to decisions to allocate. However, there is no case law or secondary source material to support this conclusion. Without such case law, this office believes it prudent to not reach conclusions on such a radically different view in this arena. This view certainly does not foreclose this office from bringing such an argument before a court to determine its validity.

ATTORNEY-CLIENT PRIVILEGED COMMUNICATION

4. Additional Considerations - Opinion Standard

As stated above, it is our view that under the current state of the law, a guaranteed 20-year grant contract is not consistent with Proposition 63 nor does it comport with the State's debt limit. Even if reasonable arguments can be made to assert that such a contract is permissible, it is not conceivable that these arguments would permit the Attorney General could give a "clean opinion" that such a 20 year contract was legal, valid, and binding on the State. This issue is raised because the Attorney General has been asked to opine in bond settings on the question of whether or not contracts which sold the income stream designated for the repayment of bonds was legal, valid and binding (e.g. tobacco bonds, and planned tribal gaming bonds.) Therefore a brief discussion of the opinion standard may be helpful for the Department of Finance.

Pursuant to bond market custom and practice, the Attorney General's opinion covers not only ground typically covered by issuer's counsel (contracts are binding on counsel's client, etc.), but also the validity of the contracts upon which bonds are based and state bonds. In fact, the Attorney General's opinion mirrors bond counsel's unqualified validity opinion. Consequently, the standard imposed upon bond counsel is applicable. The Board of Directors of the National Association of Bond Lawyers (NABL) has endorsed and articulated the standard for rendering of bond counsel opinions as follows:

> The opinion should be based upon a reasonably sufficient examination of material, legal and factual sources and reasonable certainty as to the subjects addressed therein. As to subjects about which the opinion is unqualified, bond counsel should have concluded that it would be unreasonable for a court to hold to the contrary. [79]

Given the foregoing analysis, were we to render an opinion that the proposed contracts were valid, we would be liable, even under a negligence standard, for any damages incurred by third party bond buyers and banks making investment decisions in reliance upon our opinion.

> "[T]he issuance of a legal opinion intended to secure benefit for the client, either monetary or otherwise, must be issued with due care, or the attorneys who do not act carefully will have breached a

[79] NABL Bond Attorneys Workshop 2000 publication, p. BAW 553. This is a simpler statement than that of the federal district court in *City of Cleveland v. Cleveland Electric Illuminating Company* (1977) 440 F.Supp 193, 199. "Meticulous attention to detail, exactness and veracity coupled with sagacious pedantic legal acumen are the hallmark of successful bond counsel in an astutely discriminating financial community. Eminence is not achieved by accepting, at face value, the presentements of the subscriber, nor does perfunctory approbation effectuate and maintain probity."

> duty owed to those they attempted or expected to influence on behalf of their clients."[80]

Since it would not be unreasonable for a court to determine that the proposed contract is inconsistent with Proposition 63 nor that it violates the State's debt limit, a clean validity opinion could not be provided for the proposed contract by this office.

Conclusion

Although it is difficult to predict with certainty how a court would view contracts under the proposed CalHFA model, we believe a court would have strong arguments to support a finding that the securitization of funding from Proposition 63 to issue housing bonds for mentally ill homeless individuals is inconsistent with the intent of Proposition 63 and that any state contract to secure these bonds would create an unconstitutional debt. Based on this conclusion, our office could not provide, if asked, a clean validity opinion on the proposed state contract as security for the bonds unless a court had validated the action under state law or voters in a statewide election had approved the contract and the bonds.

Please feel to call our office if you have any questions.

Sincerely,

JENNIFER K. ROCKWELL
Deputy Attorney General

and

KATHLEEN S. CHOVAN
Deputy Attorney General

For BILL LOCKYER
Attorney General

---

[80] *Roberts v. Ball, Hunt, Brown & Baerwitz* (1976) 57 Cal.App.3d 104, 111; *See also Goodman v. Kennedy* (1976) 18 Cal.3d 335, 344, n. 4 (citing *Roberts).*