Proposition 39

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Best Practices Handbook

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INTRODUCTION

On November 7, 2000, California voters reduced the voter approval threshold for school district and community college district general obligation bonds from two-thirds (2/3) voter approval to 55% voter approval. Proposition 39 amends article XVIII A of the California Constitution to allow for the levy of *ad valorem* taxes on real property in excess of the one percent (1%) limit to pay debt service on bonds issued for school construction with the approval of 55% of the votes cast.

The Legislature enacted Assembly Bill 1908 (Lempert), which establishes the issuance procedure for bonds authorized at an election requiring only 55% voter approval. (Ch. 44, Stats. 2000). The statute became operative upon the passage of Proposition 39. AB 1908 sets forth some important restrictions on the issuance of bonds that have been approved pursuant to Proposition 39. Subsequently, AB 2659 (Lempert) was passed by the legislature and signed by the Governor on September 22, 2000. AB 2659 amends certain provisions of AB 1908, as discussed below.

ANALYSIS OF THE INITIATIVE AND LEGISLATION

Proposition 39. Proposition 39 amends portions of the California Constitution to provide for the issuance of general obligation bonds by school districts, community college districts, or county offices of education "for the construction, reconstruction, rehabilitation, or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities" upon approval by 55% of the electorate.

Pursuant to the requirements of Proposition 39, the local ballot measure must: 1) list the specific school facilities projects to be funded, and must certify that the governing board has evaluated safety, class size reduction and information technology needs in developing the list; 2) require that the governing board conduct an annual independent performance audit to ensure that the funds have been expended only on the specific projects listed; and 3) require that the governing board conduct an annual independent financial audit of the bond proceeds until all of the proceeds have been expended.[1] A copy of Proposition 39 is included in Appendix 1.

Education Code. AB 1908, as amended by AB 2659, provides the issuance procedure for bonds approved by a 55% vote. The legislation is set forth in Chapter 1.5 of Title 1, Division 1, Part 10 of the Education Code, commencing with Section 15264. The legislation does not replace existing law that provides for the issuance of general obligation bonds approved by a two-thirds vote, but it allows the governing board to make a choice between existing and new procedures at the time it calls the election. A school board may only proceed under the 55% election process upon a two-thirds vote of the Board members. Once a board decides to utilize the 55% bond option, it may not subsequently opt out of that procedure, even if the proposition ultimately obtains two-thirds voter approval. A copy of AB 1908 is included in Appendix 1.

[1] Proposition 39 also requires every school district to make facilities available to charter schools. This requirement is discussed in more detail later in this handbook.

AB 2659 amends the tax rate limitation contained in AB 1908 by transforming what had been an absolute cap on the tax rate that may be levied to pay debt service on the bonds approved at a particular election. A district may only issue bonds using Proposition 39's 55% voter approval procedure if the district projects, at the time of issuance of the bonds, that the tax rate needed to pay debt service on the bonds will not, taking into account any increases in the tax base allowed under Prop. 13, exceed the applicable limit ($60 per $100,000 for unified school districts, $30 per $100,000 for elementary and high school districts).[2] A copy of AB 2659 is included in Appendix 1.

OPPORTUNITIES AND LIMITATIONS

There are both opportunities and limitations associated with the new 55% bond approval process contained in Proposition 39 and the associated legislation. Members of the Legal Advisory Committee for the Coalition for Adequate School Housing (C.A.S.H.) have prepared this handbook to guide school district personnel through the decisions of whether and how to hold a Proposition 39 bond election.

[2] AB 2659 amends Section 15268 of the Education Code (added by AB 1908), for example, to read, in pertinent part, as follows: "The bonds may only be issued if the tax rate levied ... [to pay debt service on the bonds approved] ... at a single election, would not exceed ... [$30 per $100,000] ... of taxable property when assessed valuation is projected by the district to increase in accordance with ... [Prop. 13].

A Special Thanks To Our Contributors

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The information and materials in this handbook represent the Committee members' current understanding and analysis of Proposition 39. Because this initiative is so recent and complex, the committee members' understanding of the initiative's provisions is still evolving. Future legislation or court decisions may also affect future interpretation of Proposition 39's provisions. In addition, the information in this handbook is necessarily general, and its application to a particular set of facts and circumstances may vary. **For each of these reasons, the information and materials in this handbook do not constitute legal advice and it is recommended that school districts consult with their own legal counsel prior to acting on any of the information in this handbook.**

DETERMINING THE BOND AMOUNT NEEDED

SCOPE OF BOND

2/3 Bonds vs. 55% Bonds

Under the pre-existing law, school districts could already use proceeds of bonds issued with 2/3 voter approval for the "acquisition or improvement of real property." Section 1(b)(2) of Article XIIIA. The proceeds of bonds issued with 55% voter approval ("55% bonds") may be used for a much broader array of property than the proceeds of bonds issued with 2/3 voter approval ("2/3 bonds").

Pursuant to Proposition 39, bonds issued with 55% voter approval pursuant to Proposition 39 may be used for "the construction, reconstruction, rehabilitation or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities." Section 1(b)(3) of Article XIIIA of the California Constitution.[3]

School districts are now faced with the practical dilemma of deciding whether to issue bonds pursuant to the 2/3 or 55% voter approval requirements. In determining whether to utilize a 55% bond, the District must calculate its financial need as well as all costs and limitations of the 55% bond. The total costs of facilities, furnishings, equipment and finance costs must then be compared with the caps created by Proposition 39.

Specific List of Bond Projects

Districts seeking 55% voter approval will have to go through the up-front effort and expense of enumerating the projects to be funded by the bonds (and the additional burden of complying with the new "accountability" standards). Proposition 39 requires the bond proposition to include "a list of the specific school facilities projects to be funded." Section 1(b)(3)(B) of Article XIIIA. Proposition 39 does not define "furnishing and equipping" and does not specify a level of detail required for the project list. We assume the list will need to include any furnishings and equipment to be covered.

In addition, the requirement to list projects on the bond measure may open the door to controversy, as there will be a greater level of detail to be scrutinized by voters, as well as any opponents of the bond measure. Further, the level of specificity included in the project list will need to be balanced against the flexibility necessary to spend bond proceeds. Also, the Citizens' Oversight Committee will need to use the project list to determine whether bond proceeds are spent on projects approved by the voters. Thus, the level of specificity in the bond project list will correlate with the level of interpretation the Citizens' Bond Oversight Committee will be accorded.

[3] All citations herein are to the California Constitution unless specified otherwise.

Charter School Facilities

Proposition 39 also requires school districts to provide public school facilities to charter schools by November 8, 2003, or sooner, if a bond measure is approved before that date. In determining the size of a bond, these new requirements must also be considered. The charter school provisions are described later in this handbook.

DETERMINING THE BOND FINANCE COSTS

Tax Exemption

Two basic types of bonds exist. One is a taxable bond and the other is a tax-exempt bond. The individual or institution that buys a taxable bond must pay taxes on the interest received. In contrast, the interest received by the holder of a tax-exempt bond is not subject to either state or federal income taxes. Only public agencies, i.e., cities, counties, school and community college districts are permitted to issue tax-exempt bonds. Historically, the annual interest rates on tax-exempt bonds are two percentage points lower than taxable bonds. This spread changes from time to time. Current high quality municipal bonds are in the 5.5% range.

School District Finance

A district generally has two types of financing options available to it: a financing backed by the general fund, i.e., a lease transaction; or a financing whose repayment source is some form of property taxes.

The General Fund of the District is the primary operating fund of the District. The primary source of income for the general fund is the state. The state funding is a formula determined by the state to equalize funding, on a per student basis, for each district throughout the state. Some districts are fortunate enough to have enough flexibility in the general fund to be able to make ongoing debt service payments out of the general fund. Many districts do not have this luxury.

The second primary source of funding for district financing is property taxes. Due to Constitutional requirements, a district needs to gain voter approval to access this source of funding. Although this is a difficult task, more and more districts will find it necessary if they wish to access state monies for construction or modernization of their sites. Once approved by the voters the district can then issue general obligation bonds backed by *ad valorem* property taxes.

With Proposition 39 passing, the vote requirement can be reduced from 2/3 to 55% with certain restrictions. One of the primary restrictions is the limit to the amount of the dollar tax. The amount is limited per election to $25 per $100,000 of assessed valuation for community colleges, $30 per $100,000 for elementary as well as high school districts and $60 for a unified school district.

Tax Rate & Assessed Values

The tax rate associated with the debt service on the bonds is a function of the assessed valuation of the District and the required debt repayment due in any given year. Each August the Auditor-Controller of the County will view the assessed value of all taxable property in the District, then look at the required debt service payment for the next year and construct a tax rate. The tax rate for each year may vary depending on what happens to the value of taxable property in the District and the nature of the debt service.

Several assumptions go into the forecast of future tax rates. These factors include: 1) assumptions concerning future growth in assessed values, 2) interest rates, 3) the timing of when each series of bonds is issued, 4) the structure of each bond series, and 5) tax reserves and delinquencies.

The two most important factors are 1) the timing of when each series of bonds are issued and 2) assumptions concerning future growth in assessed values. The timing of the series or issuances is important because the bonds do not appear on the tax rolls until the bonds are sold. The greater the amount and frequency of the bonds sold the greater the tax rate.

The other important issue is assumptions concerning future growth in assessed valuation. The key here is first determining historical rates of growth over the past 5,10 or 20 years. Then you must come up with conservative and defensible assumptions for future growth. Foreknowledge of future construction projects either residential or commercial can be helpful in this regard.

Cost of Issuance

Cost of Issuance (COI) for a general obligation bond is the lowest for any long-term security that can be issued by a public agency. The COI for a General Obligation Bond is the lowest because it is considered the most senior form of debt a public agency can issue. It is considered the most senior because it is backed by an unlimited tax on property owners. The cost of a Proposition 39 Bond (55% vote) versus a “Traditional” General Obligation Bond (2/3 vote) is marginally higher due to the legal and staffing needs of the Citizens’ Bond Oversight Committee.

The typical COI for a General Obligation Bond includes the following:

- **Bond Counsel**: Oversees all legal aspects of the election and the bond sale, including preparation of all the legal documents.

- **Manager/Underwriter**: Structures and sells the bonds to the investors. Guides the District though the issuance process, including the rating of the bonds.

- **Rating Fees**: The cost associated with obtaining a rating from the rating agencies. Moody’s Investor Service, Standard & Poor’s Corporation and Fitch IBCA.

- **Paying Agent**: collects funds from the County and disburses funds to the investors in order to pay debt service. The paying agent can also serve as a Dissemination Agent. The Dissemination Agent assists the district with their obligation under continuing disclosure.

- **Printing**: The costs associated with the printing of the preliminary and final official statements.

- **Data Collection and miscellaneous.**

- **Financial Advisor**: A District may choose to have a Financial Advisor in lieu of, or in addition to, a manager/underwriter. If selected, a financial advisor will either oversee the manager/underwriter or prepare the bonds for a competitive sale.

Bond Counsel, Financial Advisor and Manager/ Underwriter all are employed prior to the election and work on a contingency basis. The other fees are only incurred once the election is successful and the bonds are being prepared for sale. These are third party costs and must be paid once incurred.

LIMITS ON BONDED INDEBTEDNESS

Pursuant to Proposition 39 and implementing legislation, Proposition 39's dollar limits and percentage limits are as follows:

1. $60 per $100,000 of assessed valuation in unified school district at a single election. All outstanding district-wide general obligation bonds subject to a ceiling not to exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located.

2. $30 per $100,000 of assessed valuation in elementary or high school district at a single election. All outstanding district-wide general obligation bonds subject to a ceiling not to exceed 1.25 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located.

3. At the time bonds are issued, they must not require an annual tax projected to exceed $25 per $100,000 of assessed valuation in community college district at a single election. All outstanding district-wide general obligation bonds subject to a ceiling not to exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located.

General obligation bonds approved by a 2/3rds vote may be issued without regard to the tax rate that will result; however, the debt ceilings described above do apply.

FURNISHING AND EQUIPPING SCHOOL FACILITIES

It is clear from Sections 1(b)(2) and 1(b)(3) that proceeds of bonds, whether issued with 55% or 2/3 voter approval, may be used to pay for acquisition or improvement of real property. Now that 55% bonds allow expenditures on furnishings and equipment, we will need to determine what this can include, both in a practical and literal sense.

Whether or not a particular item is "furnishings", "furniture" or "equipment" that may be financed from bonds approved under Proposition 39 depends on a number of factors, including useful life, cost, relationship to the facilities or relationship to the educational program. The California School Accounting Manual requires a distinction to be made between "equipment" and "supplies", "determined on the basis of the length of time the item is serviceable and on its contribution to the value of the Local Educational Agency…"

"Equipment has a relatively permanent value, and its purchase increases the value of the physical properties of the LEA." A series of five questions is offered in Procedure No. 801 for determining whether an item should be characterized as "supplies" or "equipment", and guidance is given that anything with a useful life of less than 2 years is not equipment. Other potentially useful sources of authority may be found in the Education Code sections that follow. However, it should be noted that none of the code sections below are specifically applicable to Proposition 39 bonds, and should ***not*** be considered definitive as to the permitted use of Proposition 39 bond funds.

Proposition 39 only mentions, as permitted uses of bond funds, "construction…of school facilities, including the furnishing and equipping of school facilities" and does not expressly say "furniture and equipment". Most legal advisors believe the language is intended to allow the financing of at least furniture and equipment for the classrooms, and probably extends to what are more properly characterized as "furnishings" such as draperies and blinds, but probably excludes instructional materials and sports equipment.

Although Proposition 39 does not provide guidance on the definitions of "furnishing" or "equipment," we can find some guidance in the Education Code. What follows is a list of related definitions found in the Education Code.

Education Code Section 19962, which relates to the use of state bond funds for the construction and renovation of public libraries, requires that furnishings purchased with grant proceeds shall have an estimated useful life of not less than ten years.[4]

[4] Likewise, Mello-Roos bonds may be used to finance the "purchase, construction, expansion, improvement or rehabilitation of any real or other tangible property with an estimated useful life of five years or longer. . . ." Government Code Section 53313.5.

Education Code Section 19989, which relates to the use of state bond funds for the construction and renovation of public libraries, allows remodeling and rehabilitation projects funded with grants to include “any necessary upgrading of electrical and telecommunications systems to accommodate Internet and similar computer technology [and] procurement or installation, or both, of furnishings and equipment required to make a facility fully operable, if the procurement or installation is part of a construction or remodeling project funded pursuant to this section.”

Education Code Section 17072.35 allows grant money to be spent on “equipment including telecommunication equipment to increase school security, furnishings, and the upgrading of electrical systems or the wiring or cabling of classrooms in order to accommodate educational technology.”

Education Code Section 17173 governs the activities of the California School Finance Authority, and defines "Educational facility" to include “any property, facility, structure, equipment, or furnishings used or operated in conjunction with one or more public schools or community colleges, including, but not limited to, all of the following: (1) Classrooms. (2) Auditoriums. (3) Student centers. (4) Administrative offices. (5) Sports facilities. (6) Maintenance, storage, or utility facilities. (7) All necessary or usual attendant and related facilities and equipment, including streets, parking, and supportive service facilities or structures required or useful for the effective operation of the educational facility.” This is a fairly broad definition of “educational facility” which is useful in determining whether certain items can be considered as relating to “school facilities.”

Education Code Sections 94852 and 94316.2 pertaining to private higher education institutions define "Educational service" to mean “any education, training, or instruction offered by an institution, including any equipment.” The same sections define "Equipment" to include “all textbooks, supplies, materials, implements, tools, machinery, computers, electronic devices, or any other goods related to any education, training, or instruction, or an agreement for educational services or a course of instruction.”

Education Code Sections 17596 and 81644, which deal with contracts, and make a semantic distinction between apparatus and equipment. This distinction could limit the use of 55% bond proceeds for playground apparatus.

Education Code Section 38100 refers to “cafeteria equipment,” which can include vending machines.

Education Code Section 16014(b) allows State Special School Building Aid funds to be used for “necessary desks, tables, chairs and other movable furniture and equipment, as approved by the State Department of Education.”

Proposition 39 gives no definition of furnishings or equipment which may be financed with 55% bond proceeds. Consequently, none of the foregoing references should be considered definitely authoritative or limiting as to the permitted use of bonds following a Proposition 39 55% vote approval; however, any of the foregoing references may be used as guidance. We will not have any definitive parameters unless and until the Legislature enacts clarifying legislation. The courts and the State Department of Education may also weight in with authoritative guidance.

There will also be political parameters to consider. For instance, to what degree will the public tolerate long-term taxation on their homes to pay for furnishing and equipment with a short-term useful life? In addition, if bonds will be issued as federally tax-exempt, the shorter useful life of furnishings and equipment will limit the permitted maturity of such bonds.

ADMINISTRATIVE COSTS

Prior to Proposition 39, the Constitution limited the use of bonds to the "acquisition or improvement of real property." Most advisors believe this permits administrative expenses directly related to the bond program or the facilities construction program. Proposition 39 specifically prohibits the expenditure of bond funds for administrator or teacher salaries. Therefore, for a Proposition 39 bond issue, all such costs must be funded from another source.

ELECTION DATES, CONCURRENT LOCAL ELECTION AND AREA REQUIREMENTS

INTRODUCTION

Proposition 39 provides a new alternative procedure for the authorization of the issuance of general obligation bonds to finance school facilities. This procedure authorizes school districts to submit a proposition to the voters of the school district to authorize the issuance of general obligation bonds by an affirmative vote of 55% of the voters voting on such proposition as opposed to the 2/3rds affirmative vote required under existing law ("2/3 Vote Procedures"). This lower voter approval authorization comes with additional requirements as to election dates and a necessity for a presently unspecified concurrent local election occurring within all of or an unspecified area of the school district. One of the principal questions which C.A.S.H. Legal Advisory Committee has been discussing is when may a Proposition 39 - 55% Local Voter Election be held?

WHEN MAY AN ELECTION BE HELD PURSUANT TO THE 55% VOTE PROCEDURES?

As contrasted with the prior and continuing ability of school districts to hold a two-thirds voter school bond election, generally on any Tuesday, Proposition 39 - 55% Local Voter Elections may be presented to voters only at a primary [March of even numbered years] or general election [November of even numbered years], a regularly scheduled local election or a statewide special election.[5] The determination of primary, general and statewide special elections is straightforward and non-controversial. However, the same cannot be said about the statutory wording "regularly scheduled local election" set forth in AB 1908/AB 2659. There is a range of opinions among attorneys that advise school districts regarding the meaning of this phrase. Some have expressed a broad, less restrictive interpretation of "regularly scheduled local election". It should be noted this relates to the purposes of Education Code Section 15266 as opposed to election determinations of a general nature by a county registrar of voters.

The Legislative Counsel in its Opinion #610 on this subject dated January 16, 2001 on Page 8 stated:

> "In general, we think that any regularly scheduled local election for which all of the electors entitled to vote on the general obligation bond issue are also otherwise entitled to vote at the regularly scheduled local election would avoid creating an election that is in essence a special election and would be an election held 'at a . . . regularly scheduled local election' for the purposes of Section 15266."

[5] Ed. Code § 15266(a)

However, other legal advisors take the position that the term "regularly scheduled local election" should be a restricted interpretation limited to regular local elections.

In this regard, AB 1908/AB 2596 created a requirement not defined in the Elections Code or other applicable law, and did not define what is a "regularly scheduled local election" for the purposes of Education Code Section 15266, as opposed to other elections governed by the Elections Code. As noted, the Legislative Counsel appears to suggest that a special local election held in an area with the same voters voting in a local election and concurrently on a Proposition 39 - 55% Local Voter Election may be a regularly scheduled local election for the purpose of Education Code Section 15266. On a more conservative basis even with coterminous elections with identical voters, others suggest that existing definitions in the Elections Code relating to other election matters and not to Education Code Section 15266 require a contrary conclusion. This position holds that even if the same voters are involved, the Proposition 39 - 55% Local Voter Election must be held concurrent with a local election which is required by statute to be held on a specific day as opposed to being called and held on an election date specified by Elections Code Section 1000. A "local election" is defined as "a municipal, county, or district election."[6] A "regular election" is defined as "an election, the specific time for holding of which is prescribed by law."[7] Since no definition of "regularly scheduled local election" is set forth in the Elections Code, the question is not what the Elections Code does or does not specify, but what facts suffice as to a particular school district to meet the requirements of Education Code Section 15266.

There are certain elections which we can with reasonable certainty conclude are "regularly scheduled local elections" applicable to Proposition 39 - 55% Local Vote Elections. They would include an election of the school district itself at which members of the governing board are standing for election or an election of a county, city, special district or other school district (a) at which one or more members of the legislative body of such agency are standing for election and (b) where the jurisdictional boundaries of the school district in question are either coterminous with or fully encompassed by the jurisdictional boundaries of the such agency.

IS THERE AN IMPLIED COTERMINOUS BOUNDARY REQUIREMENT?

The language of Education Code Section 15266(a) itself does not expressly require that the boundaries of the school district desiring to submit a ballot proposition pursuant to the 55% Vote procedure be coterminous with or entirely contained within the boundaries of the other agency conducting the regularly scheduled local election. Is such a coterminous boundary requirement implied by the language of Education Code Section 15266(a)? As a practical matter, very few school districts are exactly coterminous with another public entity and not always completely contained within a single county. School districts considering an election where boundaries are not coterminous or include voters who would not otherwise be entitled to vote at the regularly scheduled local election should consider factors such as whether the same registrar of voters is conducting both elections on the same date, the percentage of the school district within

[6] El. Code § 328
[7] El. Code § 348

the other agency boundaries, whether the other election is itself a special election and any other facts considered relevant by the district's legal counsel.[8]

THE IMPORTANCE OF JUDICIAL VALIDATION

A school district may bring an action in the superior court to validate bonds of the school district.[9] Therefore, a school district may bring an action to validate its general obligation bonds authorized to be issued pursuant to the 55% Vote Procedures. A final judgment validating the bonds of a school district is forever binding and conclusive as to all matters adjudicated in such action against all other parties.[10] However, as to the validity of any authorized bond, such an action must be brought as to the authorization of the bonds, i.e., as of the date of adoption by the governing board of a resolution authorizing their issuance.[11] This means that the school district will have to wait until after the election to ask a reviewing court if the bonds of the school district were validly authorized at such election. Thus, while a judgment in a validation action may resolve questions regarding whether a specific election is a "regularly scheduled local election," a school district may have expended both monetary resources and time in pursuing an election which might be later invalidated if a reviewing court fails to determine that such election was a "regularly scheduled local election." Furthermore a validation as to any given election will have no value as judicial precedent for any other election.

CONCLUSION

In conclusion, a school district which wants to submit a ballot proposition for a Proposition 39 - 55% Local Voter Election *with certainty* that such election will satisfy the requirements of Ed. Code § 15266(a) may do so at one of the following elections:

- a primary election, i.e., March of even-numbered years;
- a general election, i.e., November of even-numbered years;
- a statewide special election;
- an election of the school district itself at which members of the governing board are standing for election, provided that board members are not elected from trustee areas smaller than the entire district;
- an election of a county, city, special district or other school district (a) at which one or more members of the legislative body of such agency are standing for election and (b) where the jurisdictional boundaries of the school district in question are fully encompassed by the jurisdictional boundaries of such agency, provided that the elected representatives are not elected from districts areas smaller than the entire jurisdiction;

Ultimately, until there is clearer guidance from the Legislature or the courts on this question, any other election dates are a matter to be determined by each school district after consulting with its general counsel and bond counsel.

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[8] The Legislature did address one area requirement issue in SB 1129 (O'Connell), [Chapter 132, Statutes of 2001]. That bill amended Ed. Code Section 15266(b) and related provisions to expressly authorize a 55% vote within a school facilities improvement district.

[9] Code Civ. Proc. § 860 and following

[10] Code Civ. Proc. § 870(a)

[11] Code Civ. Proc. § 864

CITIZENS' OVERSIGHT COMMITTEE

The governing board is required to establish and appoint an independent citizen's oversight committee (the "Committee") within 60 days of the date that the governing board enters in its minutes the election results, pursuant to §15274. [Education Code §15278(a)]

ROLE OF COMMITTEE

Composition of the Committee

The Committee shall consist of at least seven (7) members to serve for a term of two (2) years without compensation and for no more than two (2) consecutive terms. The legislation is silent on how and under what conditions a committee member may be removed prior to expiration of his or her term.

The Committee must include:

- One member who is active in a business organization representing the business community located within the school district;
- One member active in a senior citizens' organization;
- One member who is the parent or guardian of a child enrolled in the school district;
- One member who is both a parent or guardian of a child enrolled in the school district and active in a parent-teacher organization; and
- One member who is active in a bona fide taxpayers' organization.
  [Education Code §15282(a)]

In addition to the above minimum requirements, the Committee may include additional members.

The Committee may not include any employee or official of the school district or any vendor, contractor or consultant of the school district.
[Education Code §15282(b)]

Purpose and Activities of the Committee

The purpose of the Committee shall be to inform the public concerning the expenditure of the bond proceeds. The Committee shall engage in the following activities to carry out this purpose:

- Actively review and report on the proper expenditure of taxpayers' money for school construction;
- Advise the public as to whether the school district is in compliance with the requirements of Article XIIIA, Section 1(b)(3) of the California Constitution; and

- Convene to provide oversight for, but not limited to:
  - Ensuring that bond revenues are expended only for the construction, reconstruction, rehabilitation or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities;

  - Ensuring that no funds are used for any teacher or administrative salaries or other school operating expenses. [Education Code §15278(b)]

It is the express intent of the Legislature that the members of the Committee "promptly alert the public to any waste or improper expenditure of school construction bond money." [Education Code §15264]

The Committee is authorized to engage in any of the following activities in furtherance of its purpose:

- Receive and review copies of the annual independent performance audit required by Article XIIIA, Section 1(b)(3)(C) of the California Constitution;

- Receive and review copies of the annual independent financial audit required by Article XIIIA, Section 1(b)(3)(D) of the California Constitution;

- Inspect school facilities and grounds to ensure bond revenues are expended in compliance with Article XIIIA, Section 1(b)(3) of the California Constitution;

- Receive and review copies of any deferred maintenance proposals or plans developed by the school district including Education Code Section 17584.1; and

- Review efforts by the school district to maximize bond revenues by implementing cost saving measures, including, but not limited to:

  - Mechanisms designed to reduced the cost of professional fees;
  - Mechanisms designed to reduce the costs of site preparation;
  - Recommendations regarding the joint use of core facilities;
  - Mechanisms designed to reduce costs by incorporating efficiencies in school site design; and
  - Recommendations regarding the use of cost-effective and efficient reusable plans. [Education Code §15278(c)]

The Committee shall at least annually issue regular annual reports of the results of its activities. [Education Code §15280(b)]

Governing Board Support of the Committee

The governing board shall provide the Committee with (a) any necessary technical assistance and administrative assistance in furtherance of the Committee's purpose and (b) sufficient resources to publicize the conclusions of the Committee. No bond funds may be used to pay any of these expenses. [Education Code §15280(a)]

Meetings of and Documents Provided to the Committee

All Committee proceedings shall be open to the public and shall be subject to the provisions of the Ralph M. Brown Act. All documents received by the Committee and reports issued by the Committee shall be a matter of public record and be made available on an Internet website maintained by the governing body of the school district. [Education Code §15280(b)]

IMPLEMENTATION ISSUES

Citizens' Oversight Committee Issues

Since the approval of Proposition 39, many school districts have issued bonds with 55% voter approval and implemented the requirements relating to Committees. Currently, the law does not address many of the issues that may arise regarding the conduct of a Committee. In fact, Proposition 39 Committee requirements have raised a number of unanswered questions:

1. Should Districts Adopt Policies and Guidelines?

Although the law does not require school districts to do so, governing boards may want to adopt a board policy and corresponding administrative regulations that outline the fundamental aspects of the Committee's operations. The policy and regulations can address the Committee's purpose, duties, the extent of its authority, member selection and composition, and vacancies. A Committee may also wish to adopt its own set of operational bylaws to assist it in carrying out its functions pursuant to the policy. Adopting its own set of operational bylaws may allow a Committee to perform its functions more efficiently. In no event, however, should the Committee's operational bylaws contradict or provide more authority than the applicable state statutes or the school district's policies and regulations.

2. Who May Serve on the Committee?

Depending on the particular community, a school district may have several or few persons interested in serving on the Committee. The governing board should reserve the right to make Committee selections and appointments, as well as to determine the final size of the Committee. One way to identify potential members is to direct the superintendent or his/her designee to solicit applications for membership. Another is to ask Board members to identify potential members. The school district can limit applicants to persons who live and/or work within the school district's boundaries. If few applications are received, the school district may need to identify members of the particular groups that the Committee must represent to locate applicants who satisfy the minimum statutory requirements for composition of the Committee. On the other hand, if numerous applications are received, the district may choose to interview applicants to make recommendations to the governing board.

While school districts must appoint Committee members from the statutorily-specified community groups, other individuals such as architects, accountants, and attorneys may wish to serve on the Committee. These individuals may bring valuable experience and information relating to construction, financing, and legal process. Their experience may

be in the private sector, however, and they may have as much to learn as other committee members. The governing board may not appoint any employee or official of the school district to the Committee. In addition, the governing board may not appoint persons who have a conflict of interest pursuant to Government Code section 1090 et seq., or hold an office incompatible with serving on the Committee pursuant to Government Code section 1125 et seq.

The governing board may specify that regular attendance at Committee meetings is expected and address removal and replacement of Committee members who fail either to attend a specified number of meetings or to submit a written resignation. The governing board may require a minimum number of meetings per year and require Committee members to be available to attend school district governing board meetings when performance and financial audits are presented. The governing board may also specify that the superintendent or his or her designee shall attend Committee meetings, as well as provide that school district governing board members may attend Committee meetings.

The governing board should also address the situation in which a member ceases to belong to the designated group he or she was appointed to represent. For example, the governing board may allow that member to complete the current term, but not entitle that member to serve a subsequent term as a representative of that group. Committee vacancies should be filled within a specified period of time and new members should be appointed using the same process used to select the original Committee members.

3. What if the Committee Exceeds its Scope of Authority?

In order to ensure that the Committee does not exceed its role, which is to monitor bond expenditures and inform the public about the uses of Proposition 39 bond proceeds, governing boards should set forth the parameters of the Committee's involvement with the projects funded by the Proposition 39 bonds.

For example, the governing board may wish to specify in its policy that the Committee may not participate in specified activities, but may review completed documents relating to those activities. Examples of such limitations include the following:

- The Committee has no authority to participate in the school district's actual bond sale and issuance process, or make decisions regarding the timing, terms, or structure of a bond issuance.

- The Committee does not have the authority, once bonds have been sold and issued, to determine how bond funds shall be spent.

- Committee members do not have the authority to select, or participate, in the negotiation or bid process for contractors or consultants for bond projects.

- The Committee may not inspect job sites or construction projects without prior permission of the school district's superintendent, reserving the right to determine frequency and timing of visits to the superintendent.

- The Committee may not contact school district contractors or consultants without prior permission of the superintendent.

Placing some limitations on the operations of the Committee, while not abridging the authority legally vested in the Committee, may assist in avoiding problems that may arise from Committee members attempting to exceed their scope of authority.

4. What Information must be Posted on the Internet?

A practical problem arises regarding the requirement to post all Committee documents on the school district's website. This can become cumbersome if a school district is required to post every such document, especially if a Committee exists for many years. The law provides no guidance on this issue, and it could have a significant impact on a school district's resources. While the school district must ensure that the Committee has sufficient resources to post documents and minutes on its website, a reasonable argument can be made that this requirement relates only to documents received by the Committee during its meetings. Even then, "receipt" needs to be defined. This provision should not create a requirement that every document submitted to the Committee, in or outside a meeting, must be posted to the District's website, whether or not the Committee considers or takes action regarding the documents. Whether to post only documents that are part of a particular Committee proceeding, or all documents received by the Committee outside the scope of a meeting, may need to be incorporated into District policy or Committee procedures. A school district should work closely with the Committee to develop a reasonable policy for addressing this issue. For example, one reasonable limitation may be to limit posting of documents to those less than six months old and to state that older documents are available from the District on request.

5. Can a School District's Legal Counsel Advise the Committee?

Another question concerns the role the District's legal counsel should play and the extent to which, if any, District legal counsel should advise the Committee. Arguably, the requirement to provide technical and administrative assistance to the Committee may include legal counsel, but it may not be in a school district's best interest to allow the Committee unfettered access to legal counsel at any time and for any matter. Governing boards may wish to retain control of the Committee's access to legal counsel by reserving the discretion to ask school district legal counsel to address the Committee's legal issues. Accordingly, the governing board could direct that the Committee is not entitled to legal representation by school district legal counsel or at school district expense, absent the board's express permission in this regard. One California school district has addressed this issue by creating an annual legal budget for its Committee. The budget establishes a maximum number of hours that the Committee may authorize outside legal counsel to advise it on those matters on which it feels the need to seek legal advice.

In addition, the Committee and the school district could be at odds with one another if, for example, the Committee accuses the school district of improper bond expenditures. This could cause a conflict of interest that would prohibit the school district's legal counsel from advising both the school district and the Committee. These situations

should be addressed on a case-by-case basis and may require conflict waivers or alternative counsel, if applicable.

6. Must the District Insure and Indemnify the Committee?

Committees have asked for liability insurance coverage and indemnification by the District. In order to determine whether these are necessary or advisable, school districts should evaluate their existing insurance policies and discuss their coverage with their insurance advisors to determine whether their current insurance coverage extends to the Committee. Some policies would cover acts of a Committee composed of volunteers such as the Committee. Otherwise, the school district can add the Committee as an additional insured. However, insuring the Committee may cost the District additional premiums. It may also trigger the school district's duty to indemnify the Committee.

A Committee may be concerned about legal exposure as a result of its activities and request that the school district indemnify the Committee from such claims. The law provides little guidance on this issue. As a legal matter, school districts are probably not required to indemnify the Committee and its members against claims arising out of all of its actions, due to the nature of the Committee's charge from the Legislature to oversee school district bond expenditures and report expenditure abuses to the public.

As a practical and policy matter, however, in order not to discourage members of the public from serving on the Committee, a school district may wish to indemnify the Committee against claims arising out of a limited range of conduct. For example, a school district may indemnify and defend the Committee against claims arising only out of acts related to its advisory relationship with the school district and exclude from the agreement claims arising out of the Committee's independent duties to the public and claims that arise out of the willful misconduct of the Committee or its members.

Financial and Performance Audits

As a prerequisite to authorizing a bond by a 55 percent vote, Proposition 39 requires certain "accountability requirements." (Cal.Const., Art. XIIIA, § 1(b)(3).) One of the requirements is that the school district "conduct an annual, independent performance audit to ensure that the funds have been expended only on the specific projects listed." (Cal.Const., Art. XIIIA, § 1(b)(3)(C).) A related requirement is that the school district "conduct an annual, independent financial audit of the proceeds from the sale of the bonds until all of the proceeds have been expended for the school facilities projects." (Cal.Const., Art. XIIIA, § 1(b)(3)(D).)

School districts have sought the services of outside auditors to perform the annual, independent performance and financial audits required by Proposition 39 on a request for proposal basis. Some Committees want to be involved in selection of the auditor(s). The school district should determine the extent to which it wants the Committee involved in this process. Even if the Committee is involved, the district must be the party that selects the auditor(s), and the audits must be prepared for the district.

The audits may be performed by one consultant or by two separate consultants. The financial audit may be performed by the certified public accountant preparing the District's general audit or by a separate certified public accountant. The accountant preparing the financial audit should have a finance and accounting background. The consultant preparing the performance audit should have a construction and finance background. Each should report its findings regarding bond expenditures from an independent perspective. A school district should enter into an agreement with the selected auditor(s) that details the audit services to be provided and the standards to be met in performance of the audit(s).

Although Proposition 39 does not define either performance audit or financial audit, the Government Auditing Standards ("GAS") published by the Comptroller General of the United States provides guidance regarding each type of audit. A financial audit is similar to the annual financial audits required by school districts pursuant to Education Code sections 14503 and 41020. In fact, the California State Controller's Office specifically references the GAS in its publication entitled "Standards and Procedures for Audits of California K-12 Local Educational Agencies." When the Legislature adopted the implementing legislation for Proposition 39, it probably intended that school districts utilize the GAS to define scope and standards when conducting financial audits and performance audits. The GAS is available online at www.gao.gov/govaud/ybook.pdf. Districts may include the following in performance audit scope of work:

- Investigate whether all projects funded by the bond measure are included in the ballot proposition, identifying the projects listed in the ballot measure and bond program that have been performed;

- Prepare and provide to the school district and its governing board a report of the results of the audits and attend meetings of the governing board and the Committee, if requested by the governing board;

- Review the extent of project performance in relation to the expenditure of the bond proceeds.

LIMITS ON COMMITTEE MEMBERS

Members Subject to Prohibitions Regarding Conflict of Financial Interests in Contracts

Under the provisions of Education Code §35233, members of the Committee must abide by the prohibitions contained in Article 4, commencing with §1090, and Article 4.7, commencing with §1125, of Division 4 of Title 1 of the Government Code, which prohibit public officials from having a financial interest in any contracts made in their official capacity. [Education Code §15282(b)]

Committee Members May Be Subject to The Political Reform Act of 1974 and Its Conflict of Interest Provisions

The legislation is silent as to whether members of the Committee are subject to the provisions of The Political Reform Act of 1974 (The "PRA") and the conflict of financial

interest rules and regulations promulgated by the Fair Political Practices Commission ("FPPC"). The FPPC has not issued an opinion on this question as yet.

If the Committee is solely advisory, its members are not likely to be subject to The PRA. On the other hand, if the Committee makes or participates in the making of final decisions, it may be deemed by the FPPC to have decision making authority, and its members would be subject to the provisions of The PRA. At this time, we can only speculate. For information purposes, the FPPC has determined that a board or commission possesses decision-making authority whenever the following occur:

(1) It may make a final governmental decision. (C.C.R., Title 2, §18700(a)(1)(A); see also *In Re Maloney,* No. 76-082, 3 FPPC Ops. 69);

(2) It exerts such influence that its advice is routinely and regularly followed by its recipient board. (C.C.R., title 2, §18700(a)(1)(C); see also *In re Rotman*, No. 86-001, 10 FPPC Ops. 3); see also *Commission on Cal. State Gov. Org. & Econ. v. Fair Political Practices Com.* (1977) 75 Cal.App.3d 716)).

(3) It may compel or prevent the making of a board decision by its action or inaction. (C.C.R., title 2, §18700(a)(1)(B)).

Public officials who make *or participate in the making of final decisions* are covered by the conflict of interest codes adopted pursuant to Government Code sections 87300-87313 of The PRA. Local governmental agencies like school districts are required to include in their conflict of interest codes the positions within the agency which involve the making or participation in the making of final decisions which may foreseeably have a material effect on any private financial interest.

NEW LEGAL ACTIONS TO PREVENT OR RESTRAIN THE EXPENDITURE OF BOND FUNDS

The legislation creates a form of legal action called a "School Bond Waste Prevention Action" which may be brought by a citizen who is assessed and required to pay an *ad valorem* tax to repay bonds issued pursuant to the 55% bond approval option. In order to prevail, the citizen must show that the challenged expenditure of bond funds is not in compliance with the law, that the expenditure will produce waste or great or irreparable injury, or that he governing board has willfully failed to appoint an Oversight Committee. This legal remedy supplements existing remedies to challenge school bond elections and expenditures.

CHARTER SCHOOL PROVISIONS
Education Code Section 47614

As an integral, but less publicized part of Proposition 39, the initiative amended Education Code Section 47614 regarding the obligations of a school district to provide facilities to charter schools. The intent of this amendment to Section 47614 is to provide that public school facilities are shared fairly among all public school pupils, including those in charter schools. The effective application date of this amendment is either three (3) years after the effective date of Proposition 39, (November 8, 2003), or if a school district passes a school bond, prior to that time, the next July 1 after the measure passes. In determining the amount of a bond, school districts should also be aware of the new obligations of Section 47614.

Prior to the passage of Proposition 39, Section 47614 required that a school district in which a charter school operates merely permit such a charter school to use, at no charge, facilities not currently being used by the school district for instructional or administrative purposes or that have not been historically used for rental purposes provided the charter school is responsible for maintenance of such facilities. A school district did not otherwise have a responsibility to provide or make facilities available for charter schools. As amended by Proposition 39, Section 47614 now requires each school district to make available, to each charter school operating in the school district, facilities sufficient to accommodate all of the charter school's in-district students. A charter school is deemed to be "operating" within a school district if such charter school is currently providing public education to in-district students or has identified at least 80 in-district students who are meaningfully interested in enrolling in the charter school for the following year. If the projected average daily attendance (ADA) is less than eighty (80) for an operating charter school or the projected attendance for a charter school, the school district may deny the facilities request.

STATE DEPARTMENT OF EDUCATION
PROPOSITION 39 REGULATIONS

On August 30, 2002, the State Department of Education's final Proposition 39 Regulations became effective. The Regulations define many of the terms used in the statute and also set forth the procedures for the request and reimbursement for, and provision of, facilities to charter schools.

Requirements for Facilities

Proposition 39 requires that "[e]ach school district shall make available, to each charter school *operating in the school district*, facilities sufficient for the charter school to accommodate all of the charter school's *in-district students* in *conditions reasonably equivalent* to those in which the students would be accommodated if they were attending other public schools of the district. Facilities provided shall be *contiguous, furnished and equipped*, and shall remain the property of the school district. The school district shall make reasonable efforts to provide the charter school with facilities near to where the charter school wishes to locate, and shall not move the charter school

unnecessarily." (Emphasis Added) The Regulations define each of the italicized terms above.

Operating in the School District: Regulation section 11969.2(b) provides that a charter school is deemed to be "'operating in the school district' if the charter school meets the requirements of Education Code section 47614(b)(5) regardless of whether the school district is or is proposed to be the authorizing entity for the charter school and whether the charter school has a facility inside the school district's boundaries." Education Code section 47614(b)(5) defines the terms "operating" as "either currently providing public education to in-district students, or having identified at least 80 in-district students who are meaningfully interested in enrolling in the charter school for the following year." Therefore, the provisions of Proposition 39 only apply to districts to the extent that the charter school enrolls more than 80 in-district students.

It is important to note that Proposition 39 does not make any distinction between charter schools operating in the district with charters granted by the home district, as opposed to those granted by another district, a county board of education, or the State Board of Education. Therefore, a district is obligated to provide facilities to a charter school operating in its enrollment area even if the charter is granted by another district, a county office, or the State Board, as long as that charter school has more than 80 in-district students enrolled or has identified more than 80 in-district students who are meaningfully interested in enrolling in the charter school for the following year.

In-District Students: Regulation section 11969.2 defines "in-district students" as charter school students who are "entitled to attend the schools of the school district and could attend a school district-operated school, except that a student eligible to attend the schools of the school district based on interdistrict attendance [pursuant to an interdistrict attendance agreement between two districts] or based on parental employment... shall be considered a student of the school district where he or she resides."

Conditions Reasonably Equivalent: The Regulations also set forth detailed criteria for what constitutes "conditions reasonably equivalent" to those enjoyed by other students attending public schools in the district. Regulation section 11969.3 identifies three factors in determining whether facilities are in conditions reasonably equivalent to those provided to district students: comparison group, capacity and condition.

Comparison Group: Regulation section 11969.3(a)(1) requires a comparison group of district schools with similar grade levels to the facilities provided to the charter school. "The comparison group shall be the school district-operated schools with similar grade levels that serve students living in the high school attendance area... in which the largest number of students of the charter school reside." For districts not serving high school students, the comparison group shall be three (or all, if a district has less than three) district schools "with similar grade levels that the largest number of students of the charter school would otherwise attend." (Regulation Section 11969.3(a)(3)).

Capacity: Regulation section 11969.3(b) requires districts to provide charter school facilities "in the same ratio of teaching stations to ADA as those provided to students in the school district attending comparison group schools," based on the fiscal year and grade levels for which facilities are requested. Regulation section 11969.3(b)(2)

requires districts to allow charter schools to share "specialized classroom space, such as science laboratories," as well as "non-teaching station space," including but not limited to "administrative space, kitchen, multi-purpose room, and play area space," in proportion to the in-district classroom ADA of the charter school.

Condition: Regulation section 11969.3(c) lists the following factors to determine whether charter school facilities are in reasonably equivalent condition to those of public schools: site size, condition of interior and exterior surfaces, condition of mechanical, plumbing, electrical and fire alarm systems, the conformity of those systems to applicable codes, the availability and condition of technology infrastructure, the suitability of the facility as a learning environment, and the manner in which the facility is furnished and equipped.

For conversion charter schools, the condition of the facility of the previously existing public school shall be considered to be reasonably equivalent during the first year of the charter school's occupation.

Contiguous, Furnished and Equipped: The draft regulations describe "contiguous" as contained within or immediately adjacent to a school site. (Regulations, 11969.2(d)). However, where a district cannot accommodate all of a charter school's in-district students in one site, "contiguous facilities also includes facilities located at more than one site, provided that the school district shall minimize the number of sites assigned and shall consider student safety." (Regulations, 11969.2(d)).

Under Regulations, 11969.2(e), "a facility is 'furnished and equipped' if it includes all the furnishings and equipment necessary to conduct classroom-based instruction (i.e., at a minimum, desks, chairs and blackboards)."

Charges for Facilities Costs

The school district may charge the charter school a pro-rata share of the school district's facilities costs that it pays for with its unrestricted general fund revenues. (Regulations section 11969.7). The maximum amount of this prorated share is to be calculated as follows: the per-square-foot amount the district pays for facilities costs paid out of unrestricted general fund revenues, divided by the total space of the school district, multiplied by the amount of space allocated by the school district to the charter school, including the charter school's pro-rata share of shared space. (Regulations section 11969.7, 11969.7(c))).

The draft regulations define "facilities costs" as "costs associated with facilities acquisition and construction, and facilities rents and leases," as well as "the contribution from unrestricted general fund revenues to the district deferred maintenance fund, costs from unrestricted general fund revenues for projects eligible for funding but not funded from the deferred maintenance fund, and costs from unrestricted general fund revenue for replacement of furnishings and equipment according to district schedules and practices." (Regulations section 11969.7(a)). Costs of facilities financed with debt also include debt financing costs. (Regulations section 11969.7(b)). The school district shall not otherwise charge the charter school for the facility, but also shall not be required to use unrestricted general fund revenues to rent, buy or lease facilities for the charter school.

Procedures and Timelines for Requesting and Providing Facilities

The Regulations set forth the procedure and timelines under which charter schools may request facilities.

Eligibility: A new or proposed charter school can only request facilities for a fiscal year if it submitted its petition to a district before November 15 of the fiscal year preceding the fiscal year for which facilities are sought. (Regulation section 11969.9(a)). A new charter school is only eligible to receive facilities if its charter is approved before March 1 of the fiscal year preceding the fiscal year for which facilities are sought. (Regulation section 11969.9(a)).

The charter school's written request for facilities must be submitted to the District by October 1 of the fiscal year preceding the fiscal year for which facilities are sought. (Regulation section 11969.9(b)). A new charter school (i.e., a charter school that did not receive funds in the fiscal year preceding the fiscal year for which facilities are sought) must submit its request by January 1 of the fiscal year preceding the fiscal year for which facilities are sought. (Regulation section 11969.9(b)).

Requirements for Written Facilities Request

Regulation section 11969.9(c)(1) requires the charter school's written facilities request to include the following: reasonable projections for in-district and total ADA and in-district and total classroom ADA, broken down by grade level and school that the student would attend if not attending the charter school; the methodology for the projections; documentation of the number of in-district students meaningfully interested in attending the charter school; the charter school's instructional calendar; information regarding the geographical area where the school wants to locate; and information regarding the school's education program to the extent that it is relevant to the assignment of facilities. Districts may require charter schools to submit their written requests on forms from the State Department of Education or the district, and may require the charter school to distribute the written request to interested parties. (Regulations section 11969.9(c)(3)).

Requirements for District Response

Regulation section 11969.9(d) requires the district to provide the charter school an opportunity to respond to district concerns over the projections. The district must prepare a preliminary proposal for review and comment by the charter school, and provide a final notification of the facilities to be provided to the school by April 1 preceding the fiscal year for which facilities are sought. The district's response must include the following: identification of the teaching and non-teaching space to be offered to the charter school for exclusive or shared use; sharing arrangements, if any; ADA assumptions on which the facility allocation is based; the pro rata share amount, and the payment schedule therefore.

No later than May 1 in the fiscal year prior to the fiscal year for which facilities are sought, or within 30 days of the district's notification (whichever is later), the charter school must notify the district whether it intends to use the proposed facilities. (Regulation section 11969.9(f)). A charter school's notification of intent to use the

space obligates the school to pay its pro rata share once the deadline for responding has passed. (Regulation section 11969.9(f)). The charter school's failure to notify the district of its acceptance by the deadline will entitle the district to use the offered space for school district programs during the following fiscal year. (Regulation section 11969.9(f)).

Use of Space by Charter School

Once the charter school notifies the district of its intent to use the space, the district must make the space furnished, equipped and available for use no later than seven days prior to the first day of instruction. (Regulation section 11969.9(g)).

Regulation section 11969.9(h) also requires the district and charter school to negotiate an agreement regarding use of the space. The agreement must include at least the information contained in the District's final notification of availability of facilities, and also address the charter school's payment of facilities costs. The district can also require that the charter school maintain liability insurance with the district as an additional insured and comply with district policy regarding operations and maintenance of the facilities and furnishings.

Regulation section 11969.9(k) allows a district and a charter school to negotiate different timelines and procedures than those set forth in the regulations. The district may establish timelines up to two months earlier than those provided in the regulations if it notifies the charter school of the changes and offers the charter school the same amount of time to respond to the district's offer of facilities. The parties cannot change the date for submission of facilities requests. (Regulation section 11969.9(k)).

Reimbursement for Over-Allocation of Space

The regulations provide the district the right to reimbursement in the event that it over-allocates space based on the charter school's over projection of ADA. Regulation 11969.8(a) states that "[s]pace is considered to be over-allocated if (1) the charter school's actual in-district classroom ADA is less than the projected in-district classroom ADA upon which the facility allocation was based and (2) the difference is greater than or equal to a threshold ADA amount of 25 ADA or 10 percent of projected in-district classroom ADA, whichever is greater." The rate of reimbursement is the statewide average cost avoided per pupil under Education Code section 42263. The reimbursement amount shall be calculated as follows: the reimbursement rate multiplied by the difference between the charter school's projected ADA and actual ADA, less the reimbursement rate multiplied by one-half the threshold ADA. (Regulation section 11969.8(a)).

A charter school must notify the district if it anticipates over-allocation of space. (Regulation section 11969.8(b)). If the district elects to use the over-allocated space for school district programs, it must so notify the charter school within 30 days, and the charter school's payments for over-allocated space shall be reduced accordingly. (Regulation section 11969.8(b)). If the district does not use the over-allocated space, the charter school must continue to make its reimbursement payments for over-allocation and its pro rata share payments. (Regulation section 11969.8(b)).

CONDUCTING AN ELECTION

ASSEMBLING A TEAM

Successful passage of school bond elections and the subsequent issuance of bonds authorized by the voters requires legal, financial and political effort and expertise. The process is a melding of these areas of expertise. The legal and financial expertise is essential and the political expertise is highly recommended.

Bond Counsel

The election, campaign and bond issuance process is controlled by various constitutional provisions, statues and case law. In addition, the interest paid on school general obligation bonds is exempt from state and federal income taxation. The federal government has burdened such bonds with a substantial amount of law and regulation in order to limit the amount and purposes of bond issuance. Additionally, the Internal Revenue Service has recently embarked on what The Bond Buyer (December 28, 2000) describes as "virtual fishing expeditions" into areas that may or may not have any problems or concerns.

Bond Counsel is the designation given lawyers who specialize in the legal aspects of the authorization and issuance of tax exempt debt issued by public agencies. The function of the bond counsel is to assist the District in understanding the alternatives available for debt financing, make sure that all procedures and actions are properly taken and documented so that the bonds are legally issued and are tax exempt, and to render an approving opinion to that fact. Additionally bond counsel will frequently assist the District in regard to understanding what it can and cannot do during the election process.

Districts may additionally seek legal advise from their general counsels regarding campaign legalities and such matters as providing for the citizens oversight committee required in order to use Proposition 39.

Financial Expertise — Financial Advisor and/or Underwriter

Bond transactions are as much financial transactions as legal, and financial expertise is mandatory, both in the planning needed to put the bond proposition on the ballot and for the eventual sale of the bonds in the bond market. The District has a choice to make as to whether it will hire an independent financial advisor or an underwriting firm to provide financial assistance. Financial advisors do not buy the bonds, but underwriters do.

If the District determines to hire a financial advisor the bonds will often be sold by competitive sale conducted to receive interest rate bids from underwriters. The lowest interest rate wins. Alternatively the financial advisor may advise that a negotiated sale pursuant to a Bond Purchase Agreement to a particular underwriter is preferable in the particular circumstances.

The District may determine to hire an underwriting firm directly and negotiate the sale of the bonds directly with that firm. In such cases, the chosen underwriter should provide the financial assistance needed to determine the size of the requested bond authorization, estimated tax rates, and the estimated sequence of bond sales.

Appendix 2 entitled Overview of Debt Financing was produced by the California Debt and Investment Advisory Commission as a part of its California Debt Issuance Primer (April, 1998) and provides helpful information regarding the overall process and the roles of the team, including financial advisors, underwriters and bond counsel.

Political Expertise

In recent years the presence of political consultants in the bond authorization process has become increasingly common. The exact function of such consultants can vary considerably from district to district. Many Districts contract with public opinion survey consultants to conduct telephone polling to assist in the determination to call a bond election. It is generally permissible for the District to pay for such services rendered prior to the adoption of the resolution calling the election.

Frequently, the citizens campaign committee will hire and pay for assistance with the advocacy campaign, which it can, but the District cannot, run. As discussed in the next section Districts may legally and arguably, should, provide information regarding the bond measure to citizens and voters. Informational, as opposed to advocacy, activities may be supported by District resources and this may include engaging the services of experts.

LEGALITIES OF SCHOOL BOND ELECTION CAMPAIGNING USE OF DISTRICT RESOURCES

Permissible Campaign Activities of District Trustees and Employees

California law prohibits the use of District funds, services, supplies or equipment for the purpose of urging the passage or defeat of any school measure of the District, including school bond measures ("Bond Measure"). However, the law does permit board members, officers, and employees to take certain actions within prescribed limitations during the campaign period associated with school bond elections. The California law setting forth permissible campaign activities of school districts, governing boards and employees is found in sections of the Education Code and in California case law developed over time. (All section references below are to the Education Code unless otherwise noted.)

The Legislature passed Senate Bill 82 in 1995 to clarify school district responsibilities and liability during campaigns. This measure made it a misdemeanor or felony for a school district to use its funds, services, supplies or equipment for the purpose of supporting or defeating any ballot measure or candidate. Punishment for violations of these restrictions may include jail time and fines. This law demonstrates the degree of scrutiny being placed by the Legislature on campaign activities associated with local school bond elections. It is therefore more important than ever that school districts

considering a bond campaign are thoroughly familiar with all applicable rules and regulations.

Prohibition Against Use of District Funds

Section 35160 of the Education Code, which is part of the general provisions in the Education Code regarding powers and duties of a school district's governing board, provides the governing board of a school district with the authority to initiate and carry out a program that is not otherwise inconsistent with, or preempted by, another law and not in conflict with school district purposes. Section 7054, contained in the general provisions regarding public school personnel, is such another law and specifically prohibits the use of school district funds, services, supplies or equipment "for the purpose of urging the passage or defeat of any ballot measure." Section 7054 specifically provides that public resources may only be used to provide information to the public about a ballot measure if:

a. The informational activities are otherwise authorized by the Constitution or laws of California; and

b. The information provided constitutes a fair and impartial presentation of relevant facts to aid the electorate in reaching an informed judgment regarding the ballot measure.

Thus, under no circumstances may the District use District money or property to advocate the passage or defeat of the Bond Measure in the election. This prohibition includes indirect uses of funds or property, such as use of an administrator's or other employee's time, or the use of District vehicles or drivers to transport District Board Members to meetings, rallies, etc., to present partisan views. Case law also mandates this rule. The decision in Mines v. Del Valle (1927) 201 Cal. 273, 257 P. 530, held that it was illegal for the City Council of Los Angeles to provide City funds to advocate the passage of a public utility bond issue. In Stanson v. Mott (1976) 17 Cal.3d. 206, 130 Cal.Rptr. 697, the California Supreme Court determined that the Director of the California Department of Parks and Recreation could not use Department funds to advocate electorate approval of a State park bond issue.

Although the District may not spend District funds to hire campaign consultants, pursuant to the Political Reform Act, independent recipient committees may be organized to campaign on behalf of the Bond Measure. However, these committees may not have free use of District equipment or services, including the services of District staff during business hours. However, in some situations, further discussed below, an independent recipient committee may utilize District facilities.

Permitted Use of District Funds

As long as the expenditure of District funds is not made for the purpose of advocating the passage or defeat of a Bond Measure there are a number of items that the District can spend its money on which are closely related to the need for facilities. For instance, the District may pay for a voter survey prior to making the determination whether an election should be called. The money is being spent to assist the District in making a

decision which it is authorized to make. Surveys conducted after the calling of the election would generally not be a permissible use of District funds.

As always, the District has the authority to expend funds in order to determine the current state of its facilities and to better understand the current and predicted needs and demands which will be placed upon District facilities.

Additionally, as discussed herein, the District is authorized to provide written communications to citizens on a wide variety of subject matters involving facilities, facility needs, the existence of a pending ballot measure, and the use to which the revenues from a ballot measure would be put. Such communications must be factual, neutral and should include, at a minimum, the tax impact of any proposed bond measure.

In making determinations regarding permissible expenditures it is advisable to consult with the District's legal counsel before committing to a plan of expenditure.

Activities of District Trustees and Employees

School district trustees have typically enjoyed more freedom than other school personnel to engage in activities which may be construed as urging the passage of a bond measure, and the passage of SB 82 did not affect that freedom. SB 82 specifically provides that it is not the intent of the Legislature to prohibit the ability of a governing board of a school district or a member thereof from "preparing or disseminating information or making private or public appearances or statements for the purpose of urging the support or defeat of any ballot measure by means of, or in circumstances that do not involve the use of public funds." Therefore, any information prepared and disseminated by a board member, and any other campaign-related activities engaged in by such board member must not advocate the passage of the Bond Measure if District funds, services, supplies, etc., are involved, but must in this situation be factual and unbiased.

District employees may also not engage in activities for the purpose of urging the passage of the Bond Measure, if the activity involves District funds, services or supplies as well. For example, the District may include an unbiased, informational item explaining the Bond Measure in the school newspaper or parent newsletter. A message contained in regular District publications reminding constituents to vote on the Bond Measure would also be permissible, as long as the message was simply a reminder to "vote" and not to "vote yes."

In preparing and providing unbiased and neutral information materials, the District should be cautious not to cross the line into unauthorized campaign expenditures. The court acknowledged in Stanson that "frequently. . . the line between unauthorized campaign expenditures and authorized informational activities is not so clear." (Id. at 708.) The court further discussed that "while past cases indicate that public agencies may generally publish a 'fair presentation of facts relevant to an election matter, in a number of instances publicly financed brochures or newspaper advertisements which have purported to contain only relevant factual information, and which have refrained from exhorting voters to "Vote Yes," have nevertheless been found to constitute improper campaign literature." The court in Stanson concluded that "the determination

of the propriety or impropriety of the expenditure depends upon a careful consideration of such factors as the style, tenor and timing of the publication; no hard and fast rule governs every case." (See Id.)

Under Section 7054.1 and case law, District trustees may also give speeches, or attend events, for the purpose of urging the passage or defeat of the Bond Measure. This type of campaign activity is permitted because of the guarantee of freedom of speech and assembly under the First Amendment of the United States Constitution and Article I, Section 2, of the California Constitution. However, the right is limited by the prohibition that the trustees cannot expend public funds to advocate a partisan viewpoint. If a trustee travels in a District-owned vehicle or is driven by a District employee to speak at a gathering or organization regarding the Bond Measure the trustee may not advocate approval of the Bond Measure, but must restrict his or her role to that of disseminating information, e.g. a discussion of the terms of the Bond Measure, why the election was called and the cost to the electorate.

Section 7054.1 also recognizes that school district administrators and board members may appear before citizens groups which request an appearance, to discuss and explain an election proposition and to answer questions about the fiscal impact of the election proposition. During business hours, however, District administrators are restricted to making requested appearances only, and may not advocate, but only explain the Bond Measure. However, First Amendment rights also guarantee District administrators and employees the right to undertake campaign appearances and activities during non-business hours to advocate as long as no District funds are directly or indirectly used for the appearance or activity.

Fund Raising and Campaign Committee Activities

Although the District may not use public funds to advocate approval of the Bond Measure, Board Members and employees are not prohibited from raising money to pay for campaign expenses. However, they must raise money on behalf of an independent recipient committee and not on behalf of the District. Fund raising activities should be strictly confined to after-business hours and no District funds may be used in the course of such fund raising.

However, District facilities may be utilized after school hours by an independent recipient committee if used in conformity with the Civic Center Act. (Education Code Sections 40040-40048). The Civic Center Act allows the citizens of a school district to use school facilities to meet and discuss "educational, political, economic, artistic, and moral" subjects of interest to the community. Under that authority, a district may allow a forum for discussion of any measure or candidate on the ballot. Care should be given, however, to make equal time available to opposing views. That does not mean that every use of school facilities must be a balanced presentation; it simply means that the facilities should be equally available to both sides of a ballot issue. (See Stanson v. Mott, supra, at p. 219.)

District Board Members and employees are free to contribute their own personal time and funds to any independent recipient committees that are formed to aid the passage or defeat of the Bond Measure. Board Members and employees should not be required by the District to make contributions of their own time or money to independent recipient committees.

School Bond Election Requirements

In 1995, the California Legislature enacted Senate Bill 82 (Kopp). Senate Bill did not alter existing restrictions on campaigning as much as it clarified guidelines that have been gleaned from California case law over time do specifically apply to school bond elections. The major effect of SB 82 is to set forth the penalties for violating campaign laws. In summary, the relevant campaigning portions of SB 82 are as follows:

- Explicitly prohibits members of a school board from preparing and disseminating information or making appearances or statements for the purpose of urging the passage or defeat of a school measure unless no public funds or resources are used.

- Makes clear that public resources may only be used to provide information to the public about the possible effects of any ballot measure as long as (a) the information activities are otherwise authorized by the Constitution or laws of this state; and (b) the information provided "constitutes a fair and impartial presentation of relevant facts to aid the electorate in reaching an informed judgment regarding the ballot measure."

- Makes clear that a forum under the control of the governing board of a school district may be used if the forum is made available to all sides on an equitable basis.

- Makes violations of said provisions a misdemeanor or felony punishable by imprisonment in the county jail, not exceeding one year or by a fine not exceeding $1,000, or by both, or imprisonment in a state prison for 16 months, two, or three years.

General Recommendations

We recommend that District Board Members, officers, and employees do not use District funds for any purpose that might be interpreted as advocating the passage or defeat of the Bond Measure. This should be given a broad interpretation to include use of District money, use of District equipment (i.e., automobiles, copy machines), use of District supplies (i.e., postage), and use of District property (posting signs on the lawn advocating for the measure). If employees are invited to speak at local organizations during business hours, they should be careful not to advocate a particular position on the Bond Measure, but merely give information on the Bond Measure and election information.

Should the District decide to provide unbiased and neutral informational material regarding the Bond Measure, it should be closely scrutinized to ensure that the presentation of the material is fair. The material must not urge recipients to take a

position concerning the election since this would constitute improper campaigning. In order to ensure that the District acts within the confines of the law, we recommend that the District provide any informational material pertaining to the election to its Counsel for review prior to its distribution. Public and legislative scrutiny will likely continue, and school districts are well advised to be cautious in the campaigning arena.

CAMPAIGN COMMITTEE DISCLOSURE REQUIREMENTS

If a Campaign Committee is to be formed to advocate for the Bond Measure, the Committee will have to become familiar with the regulations of the California Fair Political Practices Commission ("FPPC"). The FPPC requires that certain forms be filed with the state when an independent recipient committee is formed in relation to a school measure. The requirements, forms, and related instructions can be found in the FPPC's "Information Manual D."

The basic forms required are the Statement of Organization (Form 410), and the Recipient Committee Campaign Disclosure Statement (Form 460). The following is an overview of the requirements for each of these forms in regards to a committee formed to support the District's Bond Measure (the "Committee").

Statement of Organization (Form 410)

Filing Date: No later than ten days after the Committee has received contributions totaling $1,000.

Any person who receives contributions totaling $1,000 within any calendar year "qualifies" as a recipient committee and within ten days of qualifying must file Form 410 with the Secretary of State. This suggests that the ten-day filing period begins once the committee has accumulated $l,000 in contributions. However, the Committee may file this form before it has received $1,000. The Committee need only note on the form that it is "not yet qualified" where the form requests the date of qualification. When $1,000 has been received, the committee must file an amended Form 410 indicating the date qualified. Once this form has been filed, the Secretary of State will assign the committee a number, which must be included on all subsequent forms.

If the Committee never raises $1,000 or more, the Committee does not need to file anything with the FPPC and is not required to file any more paperwork.

The original plus one copy of Form 410 must be filed with the Secretary of State and a copy must also be filed with the City Clerk of the City if the District boundaries are contained within the City, or the County Clerk if they are not. The address for the Secretary of State is:

Secretary of State, Political Reform Division
P. O. Box 1467,
1500 11th Street
Sacramento, California 95812-1467

Recipient Committee Campaign Disclosure Statement (Form 460)

Filing Dates:

a) Pre-election statements due forty days prior to election and twelve days prior to election.
b) semi-annual statements due every six months for the life of the Committee (but see discussion below).
c) Quarterly statements due every three months, but most likely not necessary for the usual school bond election (see discussion below).

The Political Reform Act requires committees that support or oppose passage of state or local ballot measures to file periodic campaign statements that disclose contributions received, expenditures made, unpaid bills and any miscellaneous increases to C.A.S.H., such as bank interest. Form 460 must be filed by ballot measure committees if they have:

a) received an itemizable contribution (a cumulative amount of $100 or more from a single source);
b) received any other itemizable receipt; or
c) have outstanding loans (made or received) or outstanding unpaid bills.

Form 460 serves multiple purposes; it acts as a "pre-election statement," a "semi-annual statement," and a "quarterly statement," and the Committee must file these on several occasions.

Pre-Election Statements. The schedule specifies that Form 460 be filed twice before the election in the form of a pre-election statement, once forty days preceding the election and once twelve days preceding the election. The second pre-election statement must be sent by guaranteed overnight mail or delivered in person on the day the form is due.

Semi-Annual Statements. The "semi-annual statement," due on July 31 and January 31 of each year, represents a six-month period of expenditure, and there are two reporting periods for any given year: January 1 through June 30, and July I through December 31.

Quarterly Statements. In addition, the FPPC requires a local ballot committee to file a "quarterly statement" on or before April 30 and October 31 of each year. The quarterly statement represents a three-month period of expenditure, but there are only two relevant periods to be reported on in any given year: January 1 through March 31, and July 1 through September 30. This statement need not be filed during any semi-annual period in which the ballot measure is being voted upon.

The Committee must file the original plus one copy of each form discussed above with the City Clerk of the City if the District boundaries are entirely within city limits, or the County Clerk if they are not. **Detailed record keeping on contributions is required, including non-monetary contributions**.

Additional Information

There are some helpful resources available to the District with regard to campaign reporting including the FPPC's Information Manual "D". We recommend that at the appropriate time copies of the manual be distributed to everyone on the Committee and that the Treasurer of the Committee review it thoroughly before attempting to complete any forms.

Information and copies of forms can be obtained at the FPPC's website: www.fppc.ca.gov.

APPENDIX 1

PROPOSITION 39
AND IMPLEMENTING LEGISLATION

APPENDIX 2

OVERVIEW OF DEBT FINANCING

Proposition 39: Text of Proposed Law

This initiative measure is submitted to the people of California in accordance with the provisions of Section 8 of Article II of the California Constitution.

This initiative measure amends provisions of the California Constitution and the Education Code; therefore, existing provisions proposed to be deleted are printed in ~~strikeout type~~ and new provisions proposed to be added are printed in *italic type* to indicate that they are new.

PROPOSED LAW
SMALLER CLASSES, SAFER SCHOOLS AND FINANCIAL ACCOUNTABILITY ACT

SECTION ONE. TITLE

This act shall be known as the Smaller Classes, Safer Schools and Financial Accountability Act.

SECTION TWO. FINDINGS AND DECLARATIONS

The people of the State of California find and declare as follows:

(a) Investing in education is crucial if we are to prepare our children for the 21st Century.

(b) We need to make sure our children have access to the learning tools of the 21st Century like computers and the Internet, but most California classrooms do not have access to these technologies.

(c) We need to build new classrooms to facilitate class size reduction, so our children can learn basic skills like reading and mathematics in an environment that ensures that California's commitment to class size reduction does not become an empty promise.

(d) We need to repair and rebuild our dilapidated schools to ensure that our children learn in a safe and secure environment.

(e) Students in public charter schools should be entitled to reasonable access to a safe and secure learning environment.

(f) We need to give local citizens and local parents the ability to build those classrooms by a 55 percent vote in local elections so each community can decide what is best for its children.

(g) We need to ensure accountability so that funds are spent prudently and only as directed by citizens of the community.

SECTION THREE. PURPOSE AND INTENT

In order to prepare our children for the 21st Century, to implement class size reduction, to ensure that our children learn in a secure and safe environment, and to ensure that school districts are accountable for prudent and responsible spending for school facilities, the people of the State of California do hereby enact the Smaller Classes, Safer Schools and Financial Accountability Act. This measure is intended to accomplish its purposes by amending the California Constitution and the California Education Code:

(a) To provide an exception to the limitation on ad valorem property taxes and the two-thirds vote requirement to allow school districts, community college districts, and county offices of education to equip our schools for the 21st Century, to provide our children with smaller classes, and to ensure our children's safety by repairing, building, furnishing and equipping school facilities;

(b) To require school district boards, community college boards, and county offices of education to evaluate safety, class size reduction, and information technology needs in developing a list of specific projects to present to the voters;

(c) To ensure that before they vote, voters will be given a list of specific projects their bond money will be used for;

(d) To require an annual, independent financial audit of the proceeds from the sale of the school facilities bonds until all of the proceeds have been expended for the specified school facilities projects; and

(e) To ensure that the proceeds from the sale of school facilities bonds are used for specified school facilities projects only, and not for teacher and administrator salaries and other school operating expenses, by requiring an annual, independent performance audit to ensure that the funds have been expended on specific projects only.

SECTION FOUR

Section 1 of Article XIII A of the California Constitution is amended to read:

SEC. 1. (a) The maximum amount of any ad valorem tax on real property shall not exceed One percent (1%) of the full cash value of such property. The one percent (1%) tax to be collected by the counties and apportioned according to law to the districts within the counties.

(b) The limitation provided for in subdivision (a) shall not apply to ad valorem taxes or special assessments to pay the interest and redemption charges on ~~(1)~~ any ~~indebtedness~~ *of the following:*

(1) Indebtedness approved by the voters prior to July 1, 1978. ~~, or (2) any bonded~~

(2) Bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978, by two-thirds of the votes cast by the voters voting on the proposition.

(3) Bonded indebtedness incurred by a school district, community college district, or county office of education for the construction, reconstruction, rehabilitation, or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities, approved by 55 percent of the voters of the district or county, as appropriate, voting on the proposition on or after the effective date of the measure adding this paragraph. This paragraph shall apply only if the proposition approved by the voters and resulting in the bonded indebtedness includes all of the following accountability requirements:

(A) A requirement that the proceeds from the sale of the bonds be used only for the purposes specified in Article XIII A, Section 1(b)(3), and not for any other purpose, including teacher and administrator salaries and other school operating expenses.

(B) A list of the specific school facilities projects to be funded and certification that the school district board, community college

board, or county office of education has evaluated safety, class size reduction, and information technology needs in developing that list.

(C) A requirement that the school district board, community college board, or county office of education conduct an annual, independent performance audit to ensure that the funds have been expended only on the specific projects listed.

(D) A requirement that the school district board, community college board, or county office of education conduct an annual, independent financial audit of the proceeds from the sale of the bonds until all of those proceeds have been expended for the school facilities projects.

(c) Notwithstanding any other provisions of law or of this Constitution, school districts, community college districts, and county offices of education may levy a 55 percent vote ad valorem tax pursuant to subdivision (b).

SECTION FIVE

Section 18 of Article XVI of the California Constitution is amended to read:

SEC. 18. *(a)* No county, city, town, township, board of education, or school district, shall incur any indebtedness or liability in any manner or for any purpose exceeding in any year the income and revenue provided for such year, without the assent of two-thirds of the ~~qualified electors thereof,~~ *voters of the public entity* voting at an election to be held for that purpose, except that with respect to any such public entity which is authorized to incur indebtedness for public school purposes, any proposition for the incurrence of indebtedness in the form of general obligation bonds for the purpose of repairing, reconstructing or replacing public school buildings determined, in the manner prescribed by law, to be structurally unsafe for school use, shall be adopted upon the approval of a majority of the ~~qualified electors~~ *voters* of the public entity voting on the proposition at such election; nor unless before or at the time of incurring such indebtedness provision shall be made for the collection of an annual tax sufficient to pay the interest on such indebtedness as it falls due, and ~~also provision~~ to ~~constitute~~ *provide for* a sinking fund for the payment of the principal thereof, on or before maturity, which shall not exceed forty years from the time of contracting the ~~same; provided, however, anything to the contrary herein notwithstanding, when~~ *indebtedness.*

(b) Notwithstanding subdivision (a), on or after the effective date of the measure adding this subdivision, in the case of any school district, community college district, or county office of education, any proposition for the incurrence of indebtedness in the form of general obligation bonds for the construction, reconstruction, rehabilitation, or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities, shall be adopted upon the approval of 55 percent of the voters of the district or county, as appropriate, voting on the proposition at an election. This subdivision shall apply only to a proposition for the incurrence of indebtedness in the form of general obligation bonds for the purposes specified in this subdivision if the proposition meets all of the accountability requirements of paragraph (3) of subdivision (b) of Section 1 of Article XIII A.

(c) When two or more propositions for incurring any indebtedness or liability are submitted at the same election, the votes cast for and against each proposition shall be counted separately, and when two-thirds or a majority *or 55 percent* of the ~~qualified electors~~ *voters*, as the case may be, voting on any one of ~~such~~ *those* propositions, vote in favor thereof, ~~such~~ *the* proposition shall be deemed adopted.

SECTION SIX

Section 47614 of the Education Code is amended to read:

47614. ~~A school district in which a charter school operates shall permit a charter school to use, at no charge, facilities not currently being used by the school district for instructional or administrative purposes, or that have not been historically used for rental purposes provided the charter school shall be responsible for reasonable maintenance of those facilities.~~

(a) The intent of the people in amending Section 47614 is that public school facilities should be shared fairly among all public school pupils, including those in charter schools.

(b) Each school district shall make available, to each charter school operating in the school district, facilities sufficient for the charter school to accommodate all of the charter school's in-district students in conditions reasonably equivalent to those in which the students would be accommodated if they were attending other public schools of the district. Facilities provided shall be contiguous, furnished, and equipped, and shall remain the property of the school district. The school district shall make reasonable efforts to provide the charter school with facilities near to where the charter school wishes to locate, and shall not move the charter school unnecessarily.

(1) The school district may charge the charter school a pro rata share (based on the ratio of space allocated by the school district to the charter school divided by the total space of the district) of those school district facilities costs which the school district pays for with unrestricted general fund revenues. The charter school shall not be otherwise charged for use of the facilities. No school district shall be required to use unrestricted general fund revenues to rent, buy, or lease facilities for charter school students.

(2) Each year each charter school desiring facilities from a school district in which it is operating shall provide the school district with a reasonable projection of the charter school's average daily classroom attendance by in-district students for the following year. The district shall allocate facilities to the charter school for that following year based upon this projection. If the charter school, during that following year, generates less average daily classroom attendance by in-district students than it projected, the charter school shall reimburse the district for the over-allocated space at rates to be set by the State Board of Education.

(3) Each school district's responsibilities under this section shall take effect three years from the effective date of the measure which added this subparagraph, or if the school district passes a school bond measure prior to that time on the first day of July next following such passage.

(4) Facilities requests based upon projections of fewer than 80 units of average daily classroom attendance for the year may be denied by the school district.

(5) The term "operating," as used in this section, shall mean either currently providing public education to in-district students, or having identified at least 80 in-district students who are meaningfully interested in enrolling in the charter school for the following year.

(6) The State Department of Education shall propose, and the State Board of Education may adopt, regulations implementing this subdivision, including but not limited to defining the terms "average daily classroom attendance," "conditions reasonably equivalent," "in-district students," "facilities costs," as well as defining the procedures and establishing timelines for the request for, reimbursement for, and provision of, facilities.

SECTION SEVEN. CONFORMITY

The Legislature shall conform all applicable laws to this act. Until the Legislature has done so, any statutes that would be affected by this act shall be deemed to have been conformed with the 55 percent vote requirements of this act.

SECTION EIGHT. SEVERABILITY

If any of the provisions of this measure or the applicability of any provision of this measure to any person or circumstances shall be found to be unconstitutional or otherwise invalid, such finding shall not affect the remaining provisions or applications of this measure to other persons or circumstances, and to that extent the provisions of this measure are deemed to be severable.

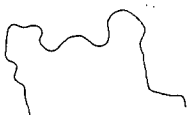
SECTION NINE. AMENDMENT

Section 6 of this measure may be amended to further its purpose by a bill passed by a majority of the membership of both houses of the Legislature and signed by the Governor, provided that at least 14 days prior to passage in each house, copies of the bill in final form shall be made available by the clerk of each house to the public and the news media.

SECTION TEN. LIBERAL CONSTRUCTION

The provisions of this act shall be liberally construed to effectuate its purposes.

Assembly Bill No. 1908



CHAPTER 44

An act to amend Sections 15102, 15106, 35233, and 72533 of, and to add Chapter 1.5 (commencing with Section 15264) to Part 10 of, the Education Code, relating to school bonds.

[Approved by Governor June 27, 2000. Filed with Secretary of State June 27, 2000.]

LEGISLATIVE COUNSEL'S DIGEST

AB 1908, Lempert. School bonds.

Existing law authorizes the governing board of any school district or community college to order an election and submit to the electors of the district the question of whether the bonds of the district shall be issued and sold to raise money for specified purposes. Existing law generally requires $^2/_3$ of the votes cast on the proposition of issuing bonds to be in favor of issuing the bonds to pass the measure.

This bill would provide that, contingent upon the passage of the "Smaller Classes, Safer Schools and Financial Accountability Act" at the November 7, 2000, general election, as an alternative, the governing board of a school district or community college district, may, pursuant to a $^2/_3$ vote of the governing board, pursue the authorization and issuance of bonds by a 55% vote of the electorate, at a primary or general election, a regularly scheduled local election, or a statewide special election, subject to certain additional requirements.

The bill would require the ballot to be printed with a statement that the governing board will appoint a citizens' oversight committee and conduct annual independent audits to assure that funds are spent only on school and classroom improvements and for no other purposes. The bill would require that after a successful election, the board appoint an independent citizens' oversight committee, as specified. The bill would state that the purpose of the citizens' oversight committee is to inform the public concerning the expenditure of bond revenues.

The bill would authorize, as specified, an action to be maintained to restrain and prevent expenditures of bond funds under certain circumstances.

The people of the State of California do enact as follows:

SECTION 1. Section 15102 of the Education Code is amended to read:

15102. The total amount of bonds issued pursuant to this chapter and Chapter 1.5 (commencing with Section 15264) shall not exceed 1.25 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the county in which the district is located for the 1987–88 fiscal year, and multiplying that result by the gross assessed value of all unitary and operating nonunitary property of the county on the last equalized assessment roll.

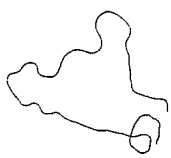
SEC. 2. Section 15106 of the Education Code is amended to read:

15106. Any unified school district or community college district may issue bonds that, in aggregation with bonds issued pursuant to Section 15270, may not exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located.

In computing the outstanding bonded indebtedness of any unified school district or community college district for all purposes of this section, any outstanding bonds shall be deemed to have been issued for elementary school purposes, high school purposes, and community college purposes, respectively, in the respective amounts that the proceeds of the sale of those outstanding bonds, excluding any premium and accrued interest received on that sale, were or have been allocated by the governing board of the unified school district or community college district to each of those purposes respectively.

(a) For the purposes of the State School Building Aid Law of 1952 (Chapter 6 (commencing with Section 16000) of Part 10) with respect to applications for apportionments and apportionments filed or made prior to September 15, 1961, and to the repayment thereof, Chapter 6 (commencing with Section 15700) of this part, inclusive, only, any unified school district shall be considered to have a bonding capacity in the amount permitted by law for an elementary school district and a bonding capacity in the amount permitted by law for a high school district.

(b) For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the



county in which the district is located for the 1987–88 fiscal year, and multiplying the result by the gross assessed value of all unitary and operating nonunitary property of the county on the last equalized assessment roll. In the event of the unification of two or more school districts or community college districts subsequent to the 1987–88 fiscal year, the assessed value of all unitary and operating nonunitary property of the unified district or community college district shall be deemed to be the total of the assessed value of the taxable property of each of the unifying districts as that assessed value would be determined under Section 15102.

SEC. 3. Chapter 1.5 (commencing with Section 15264) is added to Part 10 of the Education Code, to read:

CHAPTER 1.5. STRICT ACCOUNTABILITY IN LOCAL SCHOOL CONSTRUCTION BONDS ACT OF 2000

Article 1. General Provisions

15264. It is the intent of the Legislature that all of the following are realized:

(a) Vigorous efforts are undertaken to ensure that the expenditure of bond measures, including those authorized pursuant to paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution, are in strict conformity with the law.

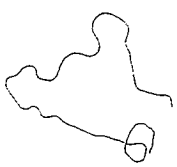
(b) Taxpayers directly participate in the oversight of bond expenditures.

(c) The members of the oversight committees appointed pursuant to this chapter promptly alert the public to any waste or improper expenditure of school construction bond money.

(d) That unauthorized expenditures of school construction bond revenues are vigorously investigated, prosecuted, and that the courts act swiftly to restrain any improper expenditures.

15266. (a) As an alternative to authorizing and issuing bonds pursuant to Chapter 1 (commencing with Section 15100), the governing board of a school district or community college district may decide, pursuant to a two-thirds vote and subject to Section 15100, to pursue the authorization and issuance of bonds pursuant to paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution and subdivision (b) of Section 18 of Article XVI of the California Constitution. An election may only be ordered on the question of whether bonds of a school district or community college district shall be issued and sold pursuant to subdivision (b) of Section 18 of Article XVI of the California Constitution at a primary or general election, a regularly scheduled local election, or a statewide special election.

(b) Upon adopting a resolution to incur bonded indebtedness pursuant to subdivision (b) of Section 18 of Article XVI of the

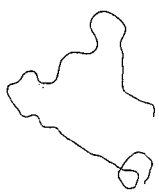


California Constitution and after the question has been submitted to the voters, if approved at the election, the bonds shall be issued pursuant to paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution and this chapter, and the governing board may not, regardless of the number of votes cast in favor of the bond, subsequently proceed exclusively under Chapter 1 (commencing with Section 15100). Where not inconsistent, the provisions of Chapter 1 (commencing with Section 15100) shall apply to this chapter.

15268. The total amount of bonds issued pursuant to this section and Section 15102 shall not exceed 1.25 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred by a school district pursuant to this chapter, at a single election, shall not exceed thirty dollars ($30) per one hundred thousand dollars ($100,000) of taxable property. For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the county in which the district is located for the 1987–88 fiscal year, and multiplying that result by the gross assessed value of all unitary and operating nonunitary property of the county on the last equalized assessment roll.

15270. (a) Notwithstanding Sections 15102 and 15268, any unified school district may issue bonds pursuant to this article that, in aggregation with bonds issued pursuant to Section 15106, may not exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred pursuant to this chapter at a single election, by a unified school district, shall not exceed sixty dollars ($60) per one hundred thousand dollars ($100,000) of taxable property.

(b) Notwithstanding Sections 15102 and 15268, any community college district may issue bonds pursuant to this article that, in aggregation with bonds issued pursuant to Section 15106, may not exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred pursuant to this chapter at a single election, by a community college district, shall not exceed twenty-five dollars



($25) per one hundred thousand dollars ($100,000) of taxable property.

(c) In computing the outstanding bonded indebtedness of any unified school district or community college district for all purposes of this section, any outstanding bonds shall be deemed to have been issued for elementary school purposes, high school purposes, and community college purposes, respectively, in the respective amounts that the proceeds of the sale of those outstanding bonds, excluding any premium and accrued interest received on that sale, were or have been allocated by the governing board of the unified school district or community college district to each of those purposes respectively.

(d) For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the county in which the district is located for the 1987–88 fiscal year, and multiplying the result by the gross assessed value of all unitary and operating nonunitary property of the county on the last equalized assessment roll. In the event of the unification of two or more school districts subsequent to the 1987–88 fiscal year, the assessed value of all unitary and operating nonunitary property of the unified district shall be deemed to be the total of the assessed value of the taxable property of each of the unifying districts as that assessed value would be determined under Section 15268.

15272. In addition to the ballot requirements of Section 15122 and the ballot provisions of this code applicable to governing board member elections, for bond measures pursuant to this chapter, the ballot shall also be printed with a statement that the board will appoint a citizens' oversight committee and conduct annual independent audits to assure that funds are spent only on school and classroom improvements and for no other purposes.

15274. If it appears from the certificate of election results that 55 percent of the votes cast on the proposition of issuing bonds pursuant to subdivision (b) of Section 18 of Article XVI of the California Constitution are in favor of issuing bonds, the governing board shall cause an entry of that fact to be made upon its minutes. The governing board shall then certify to the board of supervisors of the county whose superintendent of schools has jurisdiction over the district, all proceedings had in the premises. The county superintendent of schools shall send a copy of the certificate of election results to the board of supervisors of the county.

15276. Notwithstanding any other provision of law, a county board of education may not order an election to determine whether

bonds may be issued under this article to raise funds for a county office of education.

Article 2. Citizens' Oversight Committee

15278. (a) If a bond measure authorized pursuant to paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution and subdivision (b) of Section 18 of Article XVI of the California Constitution is approved, the governing board of the school district or community college shall establish and appoint members to an independent citizens' oversight committee, pursuant to Section 15282, within 60 days of the date that the governing board enters the election results on its minutes pursuant to Section 15274.

(b) The purpose of the citizens' oversight committee shall be to inform the public concerning the expenditure of bond revenues. The citizens' oversight committee shall actively review and report on the proper expenditure of taxpayers' money for school construction. The citizens' oversight committee shall advise the public as to whether a school district or community college district is in compliance with the requirements of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution. The citizens' oversight committee shall convene to provide oversight for, but not be limited to, both of the following:

(1) Ensuring that bond revenues are expended only for the purposes described in paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(2) Ensuring that, as prohibited by subparagraph (A) of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution, no funds are used for any teacher or administrative salaries or other school operating expenses.

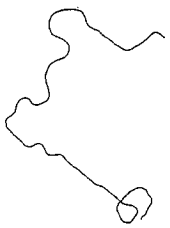
(c) In furtherance of its purpose, the citizens' oversight committee may engage in any of the following activities:

(1) Receiving and reviewing copies of the annual, independent performance audit required by subparagraph (C) of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(2) Receiving and reviewing copies of the annual, independent financial audit required by subparagraph (C) of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(3) Inspecting school facilities and grounds to ensure that bond revenues are expended in compliance with the requirements of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(4) Receiving and reviewing copies of any deferred maintenance proposals or plans developed by a school district or community college district, including any reports required by Section 17584.1.



(5) Reviewing efforts by the school district or community college district to maximize bond revenues by implementing cost-saving measures, including, but not limited to, all of the following:

(A) Mechanisms designed to reduce the costs of professional fees.

(B) Mechanisms designed to reduce the costs of site preparation.

(C) Recommendations regarding the joint use of core facilities.

(D) Mechanisms designed to reduce costs by incorporating efficiencies in schoolsite design.

(E) Recommendations regarding the use of cost-effective and efficient reusable facility plans.

15280. (a) The governing board of the district shall, without expending bond funds, provide the citizens' oversight committee with any necessary technical assistance and shall provide administrative assistance in furtherance of its purpose and sufficient resources to publicize the conclusions of the citizens' oversight committee.

(b) All committee proceedings shall be open to the public and notice to the public shall be provided in the same manner as the proceedings of the governing board. The citizens' oversight committee shall issue regular reports on the results of its activities. A report shall be issued at least once a year. Minutes of the proceedings of the citizens' oversight committee and all documents received and reports issued shall be a matter of public record and be made available on an Internet website maintained by the governing board.

15282. (a) The citizens' oversight committee shall consist of at least seven members to serve for a term of two years without compensation and for no more than two consecutive terms. While consisting of a minimum of at least seven members, the citizens' oversight committee shall be comprised, as follows:

(1) One member shall be active in a business organization representing the business community located within the district.

(2) One member shall be active in a senior citizens' organization.

(3) One member shall be active in a bona fide taxpayers' organization.

(4) For a school district, one member shall be the parent or guardian of a child enrolled in the district. For a community college district, one member shall be a student who is both currently enrolled in the district and active in a community college group, such as student government. The community college student member may, at the discretion of the board, serve up to six months after his or her graduation.

(5) For a school district, one member shall be both a parent or guardian of a child enrolled in the district and active in a parent-teacher organization, such as the Parent Teacher Association or schoolsite council. For a community college district, one member shall be active in the support and organization of a community

college or the community colleges of the district, such as a member of an advisory council or foundation.

(b) No employee or official of the district shall be appointed to the citizens' oversight committee. No vendor, contractor, or consultant of the district shall be appointed to the citizens' oversight committee. Members of the citizens' oversight committee shall, pursuant to Sections 35233 and 72533, abide by the prohibitions contained in Article 4 (commencing with Section 1090) and Article 4.7 (commencing with Section 1125) of Division 4 of Title 1 of the Government Code.

Article 3. Bond Accountability

15284. (a) An action to obtain an order restraining and preventing any expenditure of funds received by a school district or community college district through the sale of bonds authorized by this chapter pursuant to paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution and subdivision (b) of Section 18 of Article XVI of the California Constitution may be maintained against any officer, agent, or other person acting on behalf of, that school district or community college district, by a citizen residing in the school or community college district who is assessed and is liable to pay an ad valorem tax on real property within the school or community college district, or who has paid an ad valorem tax on real property within the school or community college district within one year before the commencement of the action if it appears by the complaint or affidavits that any of the following conditions are present:

(1) An expenditure of funds received by a school district or community college district through the sale of bonds authorized by this chapter is for purposes other than those specified in paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(2) The expenditure is not in compliance with paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution.

(3) That an expenditure in violation of paragraph (3) of subdivision (b) of Section 1 of Article XIII A of the California Constitution will be made or will continue to be made during the litigation that would produce waste or great or irreparable injury.

(4) The governing board of a school district or community college has willfully failed to appoint the citizens' oversight committee in violation of the requirements of Section 15278.

(b) An action brought pursuant to this section shall take special precedence over all civil matters on the calendar of the court except those matters granted equal precedence by law.

(c) The rights, remedies, or penalties established by this section are cumulative to the rights, remedies, or penalties established under other laws, including subdivision (a) of Section 526 of Chapter 3 of Title 7 of Part 2 of the Code of Civil Procedure.

(d) If an order is obtained to restrain and prevent an expenditure of funds pursuant to subdivision (a), a court may award attorneys' fees pursuant to Chapter 6 (commencing with Section 1021.5) of Title 14 of Part 2 of the Code of Civil Procedure.

(e) The action authorized by this section shall be known as a "School Bond Waste Prevention Action."

15288. It is the intent of the Legislature that upon receipt of allegations of waste or misuse of bond funds authorized in this chapter, appropriate law enforcement officials shall expeditiously pursue the investigation and prosecution of any violation of law associated with the expenditure of those funds.

SEC. 4. Section 35233 of the Education Code is amended to read:

35233. The prohibitions contained in Article 4 (commencing with Section 1090) and Article 4.7 (commencing with Section 1125) of Division 4 of Title 1 of the Government Code are applicable to members of governing boards of school districts and to members of citizens' oversight committees appointed by those governing boards pursuant to Chapter 1.5 (commencing with Section 15264) of Part 10.

SEC. 5. Section 72533 of the Education Code is amended to read:

72533. The prohibitions contained in Article 4 (commencing with Section 1090) and Article 4.7 (commencing with Section 1125) of Division 4 of Title 1 of the Government Code are applicable to members of governing boards of community college districts and to members of citizens' oversight committees appointed by those governing boards pursuant to Chapter 1.5 (commencing with Section 15264) of Part 10.

SEC. 6. This act shall only become operative upon the passage of the "Smaller Classes, Safer Schools and Financial Accountability Act" which is contained in a proposition at the November 7, 2000, general election.

O

Assembly Bill No. 2659

CHAPTER 580

An act to amend Sections 15268, 15270, and 47605 of the Education Code, relating to education.

[Approved by Governor September 22, 2000. Filed with Secretary of State September 23, 2000.]

LEGISLATIVE COUNSEL'S DIGEST

AB 2659, Lempert. Education.

(1) Existing law, if the "Smaller Classes, Safer Schools and Financial Accountability Act" is passed at the November 7, 2000, general election, authorizes a school district or community college district to pursue the authorization and issuance of bonds by a 55% vote of the electorate and restricts the rate at which property taxes may be levied to service the debt incurred.

This bill would instead prohibit the issuance of the bonds unless the tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of an indebtedness incurred by a school district, unified school district, or community college district at a single election would not exceed a specified amount per year per $100,000 of taxable property when assessed valuation is projected by the district to increase in accordance with Article XIII A of the California Constitution. The bill would define, for specified purposes, a "general obligation bond."

(2) Existing law prohibits the governing board of a school district or county board of education from denying a petition for the establishment of a charter school unless it sets forth specific findings, including findings that the petition does not contain reasonably comprehensive descriptions of certain criteria. Existing law authorizes the State Board of Education to grant a petition for the establishment of a charter school when the petition has been submitted to and denied by the governing board of a school district or a county board of education.

This bill would require the State Board of Education to develop criteria to be used for review and approval of charter school petitions presented to the board. The bill would require the board to adopt the criteria on or before June 30, 2001.

The people of the State of California do enact as follows:

SECTION 1. (a) The Legislature hereby finds and declares all of the following:

(1) Paragraph (1) of subdivision (j) of Section 47605 of the Education Code allows a charter school petitioner to submit a petition for the establishment of a charter school directly to the State Board of Education if the governing board of a school district denies the petition.

(2) Under current law, the governing board of a school district or county board of education is prohibited from denying a petition for the establishment of a charter school unless it sets forth specific findings, including findings that the petition does not contain reasonably comprehensive descriptions of certain criteria. Use of the term "reasonably comprehensive" is somewhat subjective and should be defined, consistent with the intent of existing charter school law, and within the context of a rubric that will be used for the evaluation of charter school petitions under review by the State Board of Education.

(3) In order to ensure implementation of the appeal process established in law, clear criteria must be established for the review and approval of charter petitions.

(b) It is the intent of the Legislature that the State Board of Education shall review a petition for the establishment of a charter school pursuant to subdivision (b) of Section 47605 of the Education Code, which prescribes the reasons why a charter can be denied, provided it makes written factual findings, specific to the particular petition.

SEC. 2. Section 15268, as added by Chapter 44 of the Statutes of 2000 is amended to read:

15268. The total amount of bonds issued, including bonds issued pursuant to Chapter 1 (commencing with Section 15100), shall not exceed 1.25 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The bonds may only be issued if the tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred by a school district pursuant to this chapter, at a single election, would not exceed thirty dollars ($30) per year per one hundred thousand dollars ($100,000) of taxable property when assessed valuation is projected by the district to increase in accordance with Article XIII A of the California Constitution. For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the county in which the district is located for the 1987–88 fiscal year, and multiplying that result by the gross assessed

value of all unitary and operating nonunitary property of the county on the last equalized assessment roll.

SEC. 3. Section 15270, as added by Chapter 44 of the Statutes of 2000, is amended to read:

15270. (a) Notwithstanding Sections 15102 and 15268, any unified school district may issue bonds pursuant to this article that, in aggregation with bonds issued pursuant to Chapter 1 (commencing with Section 15100), may not exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The bonds may only be issued if the tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred pursuant to this chapter at a single election, by a unified school district, would not exceed sixty dollars ($60) per year per one hundred thousand dollars ($100,000) of taxable property when assessed valuation is projected by the district to increase in accordance with Article XIII A of the California Constitution.

(b) Notwithstanding Sections 15102 and 15268, any community college district may issue bonds pursuant to this article that, in aggregation with bonds issued pursuant to Chapter 1 (commencing with Section 15100), may not exceed 2.5 percent of the taxable property of the district as shown by the last equalized assessment of the county or counties in which the district is located. The bonds may only be issued if the tax rate levied to meet the requirements of Section 18 of Article XVI of the California Constitution in the case of indebtedness incurred pursuant to this chapter at a single election, by a community college district, would not exceed twenty-five dollars ($25) per year per one hundred thousand dollars ($100,000) of taxable property when assessed valuation is projected by the district to increase in accordance with Article XIII A of the California Constitution.

(c) In computing the outstanding bonded indebtedness of any unified school district or community college district for all purposes of this section, any outstanding bonds shall be deemed to have been issued for elementary school purposes, high school purposes, and community college purposes, respectively, in the respective amounts that the proceeds of the sale of those outstanding bonds, excluding any premium and accrued interest received on that sale, were or have been allocated by the governing board of the unified school district or community college district to each of those purposes respectively.

(d) For purposes of this section, the taxable property of a district for any fiscal year shall be calculated to include, but not be limited to, the assessed value of all unitary and operating nonunitary property of the district, which shall be derived by dividing the gross assessed value of the unitary and operating nonunitary property



within the district for the 1987–88 fiscal year by the gross assessed value of all unitary and operating nonunitary property within the county in which the district is located for the 1987–88 fiscal year, and multiplying the result by the gross assessed value of all unitary and operating nonunitary property of the county on the last equalized assessment roll. In the event of the unification of two or more school districts subsequent to the 1987–88 fiscal year, the assessed value of all unitary and operating nonunitary property of the unified district shall be deemed to be the total of the assessed value of the taxable property of each of the unifying districts as that assessed value would be determined under Section 15268.

(e) For the purposes of this article, "general obligation bonds," as that term is used in Section 18 of Article XVI of the California Constitution, means bonds of a school district or community college district the repayment of which is provided for by this chapter and Chapter 1 (commencing with Section 15100) of Part 10.

SEC. 4. Section 47605 of the Education Code is amended to read:

47605. (a) (1) Except as set forth in paragraph (2), a petition for the establishment of a charter school within any school district may be circulated by any one or more persons seeking to establish the charter school. The petition may be submitted to the governing board of the school district for review after either of the following conditions are met:

(A) The petition has been signed by a number of parents or guardians of pupils that is equivalent to at least one-half of the number of pupils that the charter school estimates will enroll in the school for its first year of operation.

(B) The petition has been signed by a number of teachers that is equivalent to at least one-half of the number of teachers that the charter school estimates will be employed at the school during its first year of operation.

(2) In the case of a petition for the establishment of a charter school through the conversion of an existing public school, that would not be eligible for a loan pursuant to subdivision (b) of Section 41365, the petition may be circulated by any one or more persons seeking to establish the converted charter school. The petition may be submitted to the governing board of the school district for review after the petition has been signed by not less than 50 percent of the permanent status teachers currently employed at the public school to be converted.

(3) A petition shall include a prominent statement that a signature on the petition means that the parent or guardian is meaningfully interested in having his or her child, or ward, attend the charter school, or in the case of a teacher's signature, means that the teacher is meaningfully interested in teaching at the charter school. The proposed charter shall be attached to the petition.

(b) No later than 30 days after receiving a petition, in accordance with subdivision (a), the governing board of the school district shall hold a public hearing on the provisions of the charter, at which time the governing board of the school district shall consider the level of support for the petition by teachers employed by the district, other employees of the district, and parents. Following review of the petition and the public hearing, the governing board of the school district shall either grant or deny the charter within 60 days of receipt of the petition, provided, however, that the date may be extended by an additional 30 days if both parties agree to the extension. In reviewing petitions for the establishment of charter schools pursuant to this section, the chartering authority shall be guided by the intent of the Legislature that charter schools are and should become an integral part of the California educational system and that establishment of charter schools should be encouraged. A school district governing board shall grant a charter for the operation of a school under this part if it is satisfied that granting the charter is consistent with sound educational practice. The governing board of the school district shall not deny a petition for the establishment of a charter school unless it makes written factual findings, specific to the particular petition, setting forth specific facts to support one or more of the following findings:

(1) The charter school presents an unsound educational program for the pupils to be enrolled in the charter school.

(2) The petitioners are demonstrably unlikely to successfully implement the program set forth in the petition.

(3) The petition does not contain the number of signatures required by subdivision (a).

(4) The petition does not contain an affirmation of each of the conditions described in subdivision (d).

(5) The petition does not contain reasonably comprehensive descriptions of all of the following:

(A) A description of the educational program of the school, designed, among other things, to identify those whom the school is attempting to educate, what it means to be an "educated person" in the 21st century, and how learning best occurs. The goals identified in that program shall include the objective of enabling pupils to become self-motivated, competent, and lifelong learners.

(B) The measurable pupil outcomes identified for use by the charter school. "Pupil outcomes," for purposes of this part, means the extent to which all pupils of the school demonstrate that they have attained the skills, knowledge, and attitudes specified as goals in the school's educational program.

(C) The method by which pupil progress in meeting those pupil outcomes is to be measured.

(D) The governance structure of the school, including, but not limited to, the process to be followed by the school to ensure parental involvement.

(E) The qualifications to be met by individuals to be employed by the school.

(F) The procedures that the school will follow to ensure the health and safety of pupils and staff. These procedures shall include the requirement that each employee of the school furnish the school with a criminal record summary as described in Section 44237.

(G) The means by which the school will achieve a racial and ethnic balance among its pupils that is reflective of the general population residing within the territorial jurisdiction of the school district to which the charter petition is submitted.

(H) Admission requirements, if applicable.

(I) The manner in which annual, independent, financial audits shall be conducted, which shall employ generally accepted accounting principles, and the manner in which audit exceptions and deficiencies shall be resolved to the satisfaction of the chartering authority.

(J) The procedures by which pupils can be suspended or expelled.

(K) The manner by which staff members of the charter schools will be covered by the State Teachers' Retirement System, the Public Employees' Retirement System, or federal social security.

(L) The public school attendance alternatives for pupils residing within the school district who choose not to attend charter schools.

(M) A description of the rights of any employee of the school district upon leaving the employment of the school district to work in a charter school, and of any rights of return to the school district after employment at a charter school.

(N) The procedures to be followed by the charter school and the entity granting the charter to resolve disputes relating to provisions of the charter.

(O) A declaration whether or not the charter school shall be deemed the exclusive public school employer of the employees of the charter school for the purposes of the Educational Employment Relations Act (Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code).

(c) (1) Charter schools shall meet all statewide standards and conduct the pupil assessments required pursuant to Section 60605 and any other statewide standards authorized in statute or pupil assessments applicable to pupils in noncharter public schools.

(2) Charter schools shall on a regular basis consult with their parents and teachers regarding the school's educational programs.

(d) (1) In addition to any other requirement imposed under this part, a charter school shall be nonsectarian in its programs, admission policies, employment practices, and all other operations, shall not charge tuition, and shall not discriminate against any pupil on the

basis of ethnicity, national origin, gender, or disability. Except as provided in paragraph (2), 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 guardian, within this state, except that any existing public school converting partially or entirely to a charter school under this part shall adopt and maintain a policy giving admission preference to pupils who reside within the former attendance area of that public school.

(2) (A) A charter school shall admit all pupils who wish to attend the school.

(B) However, if the number of pupils who wish to attend the charter school exceeds the school's capacity, attendance, except for existing pupils of the charter school, shall be determined by a public random drawing. Preference shall be extended to pupils currently attending the charter school and pupils who reside in the district. Other preferences may be permitted by the chartering authority on an individual school basis and only if consistent with the law.

(C) In the event of a drawing, the chartering authority shall make reasonable efforts to accommodate the growth of the charter school and, in no event, shall take any action to impede the charter school from expanding enrollment to meet pupil demand.

(e) No governing board of a school district shall require any employee of the school district to be employed in a charter school.

(f) No governing board of a school district shall require any pupil enrolled in the school district to attend a charter school.

(g) The governing board of a school district shall require that the petitioner or petitioners provide information regarding the proposed operation and potential effects of the school, including, but not limited to, the facilities to be utilized by the school, the manner in which administrative services of the school are to be provided, and potential civil liability effects, if any, upon the school and upon the school district. The petitioner or petitioners shall also be required to provide financial statements that include a proposed first-year operational budget, including startup costs, and cash-flow and financial projections for the first three years of operation.

(h) In reviewing petitions for the establishment of charter schools within the school district, the school district governing board shall give preference to petitions that demonstrate the capability to provide comprehensive learning experiences to pupils identified by the petitioner or petitioners as academically low achieving pursuant to the standards established by the State Department of Education under Section 54032.

(i) Upon the approval of the petition by the governing board of the school district, the petitioner or petitioners shall provide written notice of that approval, including a copy of the petition, to the State Board of Education.

(j) (1) If the governing board of a school district denies a petition, the petitioner may elect to submit the petition for the establishment of a charter school to either the county board of education or directly to the State Board of Education. The county board of education or the State Board of Education, as the case may be, shall review the petition pursuant to subdivision (b). If the petitioner elects to submit a petition for establishment of a charter school to the county board of education and the county board of education denies the petition, the petitioner may file a petition for establishment of a charter school with the State Board of Education.

(2) In assuming its role as a chartering agency, the State Board of Education shall develop criteria to be used for the review and approval of charter school petitions presented to the State Board of Education. The criteria shall address all elements required for charter approval, as identified in subdivision (b) of Section 47605 and shall define "reasonably comprehensive" as used in paragraph (5) of subdivision (b) of Section 47605 in a way that is consistent with the intent of the Charter Schools Act of 1992. Upon satisfactory completion of the criteria, the State Board of Education shall adopt the criteria on or before June 30, 2001.

(3) A charter school for which a charter is granted by either the county board of education or the State Board of Education pursuant to this subdivision shall qualify fully as a charter school for all funding and other purposes of this part.

(4) If either the county board of education or the State Board of Education fails to act on a petition within 120 days of receipt, the decision of the governing board of the school district, to deny a petition shall, thereafter, be subject to judicial review.

(5) The State Board of Education shall adopt regulations implementing this subdivision.

(6) Upon the approval of the petition by the county board of education, the petitioner or petitioners shall provide written notice of that approval, including a copy of the petition to the State Board of Education.

(k) (1) The State Board of Education may, by mutual agreement, designate its supervisorial and oversight responsibilities for a charter school approved by the State Board of Education to any local education agency in the county in which the charter school is located or to the governing board of the school district that first denied the petition.

(2) The designated local education agency shall have all monitoring and supervising authority of a chartering agency, including, but not limited to, powers and duties set forth in Section 47607, except the power of revocation, which shall remain with the State Board of Education.

(3) A charter school that has been granted its charter by the State Board of Education and elects to seek renewal of its charter shall,

prior to expiration of the charter, submit its petition for renewal to the governing board of the school district that initially denied the charter. If the governing board of the school district denies the school's petition for renewal, the school may petition the State Board of Education for renewal of its charter.

(*l*) Teachers in charter schools shall be required to hold a Commission on Teacher Credentialing certificate, permit, or other document equivalent to that which a teacher in other public schools would be required to hold. These documents shall be maintained on file at the charter school and shall be subject to periodic inspection by the chartering authority. It is the intent of the Legislature that charter schools be given flexibility with regard to noncore, noncollege preparatory courses.

O

Overview of a Debt Financing

This chapter provides an overview of a debt financing and outlines the roles and responsibilities of the major participants and various problems that may arise in connection with the financing. As one might imagine, the issuer is the central actor and major focus of most debt financings. In the case of a conduit financing, the borrower is in many cases the central actor, although the issuer still retains most of its functions and responsibilities. Included in this section is a discussion of the roles of bond counsel, financial advisors, underwriters and their counsel, disclosure counsel, credit rating agencies, investment advisors and investors among others. This section also summarizes the steps involved in developing a request for proposals to hire members of the financing team and considerations applicable to workouts and troubled transactions. Finally, this section contains a description of most of the basic legal documents encountered in public finance transactions.

The process of issuing bonds is the process of borrowing money. A bond (which may be a note or other form of obligation) is simply evidence of the issuer's debt, i.e., its obligation to pay (either from its funds generally or from specified resources) a stated amount of money (principal) at a given time (maturity) with interest, payable either periodically or at maturity.

Conceptually, the initial buyer of a bond is "lending" money to the issuer in return for the issuer's obligation to pay (repay) money in the future with interest. Customarily, the owner of a bond may freely sell it to another buyer in the secondary market, resulting in the issuer being obligated to pay the new owner. Building over the years in many ways on each of these simple themes has resulted in today's highly sophisticated municipal bond market, with a myriad of financing techniques available to provide capital to issuers in amounts ranging up to billions of dollars.

The purpose of this chapter of the *Primer* is to provide an introduction to the process of issuing bonds by describing the functions of each of the principal participants in the process and discussing one of the ways of selecting them – the request for proposal. Also, because the incidence of bond defaults and challenges from government regulators has increased over the past several years, this part of the *Primer* explains the roles of the various participants in resolving problems that may arise in the issuance and repayment of bonds. In addition, a brief discussion of the legal documents encountered in a typical financing is provided, which defines and describes the most common documents generated during debt issuance, who drafts the documents, the most critical sections of the documents, and the documents' purposes.

We have made an attempt to describe the principal participants without using too much undefined jargon. For example, "bonds" is used to mean all types of debt instruments,

including long-term bonds, short-term notes, Certificates of Participation in financing leases, commercial paper, and so on. However, the reader may find unfamiliar terms explained below in this chapter or in "***Appendix C – Debt Financing Terms and Concepts***." Additional participants are also described in that Appendix (including remarketing agent, yield verification consultant, special tax counsel, escrow agent and feasibility consultant) and in "***Appendix A – Working with State Agencies***" (including the California Debt and Investment Advisory Commission, the California Debt Limit Allocation Committee and the California Industrial Development Financing Advisory Committee). Finally, ***"Appendix B – Resources and Contacts"*** contains listings of agencies and associations which may be useful to the reader.

ROLES AND RESPONSIBILITIES OF PRINCIPAL PARTICIPANTS

THE ISSUER

The Issuer as the Central Actor. The issuer is the legal entity that is borrowing money by issuing bonds and is customarily the central actor in the process. The financing is being accomplished by and for the issuer and, even in the case of a financing for a nongovernmental borrower, should be designed to serve the objectives of the issuer.

In some instances the issuer may be controlled by another governmental entity. For example, redevelopment agencies, housing authorities, joint powers authorities and industrial development authorities may be formed by cities and counties and the city council or board of supervisors may sit as the governing body of the agency or authority. Similarly, nonprofit corporations have been created by governmental entities to issue bonds on behalf of the governmental entities to accomplish financings that may not be specifically authorized for governmental entities. Other sections of this *Primer* will clearly distinguish between the issuer and any entity that controls the issuer, but in this more general discussion, the two will be treated as "the issuer."

Legal Authorization. Issuers are authorized by state law to borrow money (issue bonds) for many different specific purposes, and in some cases for their "general corporate purposes." For the most part, these purposes are limited to those that in one respect or another benefit the public welfare, so-called "public purposes." In the case of chartered cities, debt may be issued for purposes which constitute "municipal affairs." See ***"State Constitutional Limitations – Charter Cities and Home Rule"*** for a discussion of the municipal affairs doctrine. Within these statutory and constitutional guidelines, an issuer determines its own capital improvement program (including the parameters of any lending program), determines the resources that it has available (legally and financially) for the payment of capital expenditures (including the repayment of any debt) and is in ultimate control of the process of issuing bonds as a part of that capital improvement program. In addition, in certain limited circumstances, an issuer may determine to issue debt to finance non-capital items. See ***"Types of Financing Instruments – Tax and Revenue Anticipation Notes; Grant Anticipation Notes" "—Pension Obligation Bonds" and "—Teeter Financings"*** for examples of non-capital borrowing programs.

Similarly, some issuers are authorized by law to issue notes to borrow for short-term cash flow ("working capital") needs and are in ultimate control of the decisions concerning how those cash flow needs will be met.

"Types of Financing Instruments" contains a more complete discussion of the constitutional and statutory authorization for a variety of different types of debt financing programs.

Selecting the Financing Team. One of the first decisions to be made by an issuer is the selection of the initial members of its debt financing team, including bond counsel (and perhaps disclosure counsel) and either a financial advisor or underwriter or both. Team members may be selected on the basis of a request for proposals, long standing relationship with the issuer, reputation or recommendation by others. (See below in this chapter – "Using a Request for Proposals to Select Financing Team Members.")

The nature of the team members may depend upon several factors, including the type of debt being issued, procedural requirements for that type of debt and the level of in-house sophistication of the issuer. For example, in a situation in which bonds are to be sold at competitive (or "public") sale (the opening of bids from prospective underwriters at a time and place specified in a published notice of sale), an issuer will typically hire a financial advisor. On the other hand, in cases in which bonds are to be sold in a negotiated (or "private") sale, an issuer will customarily select an underwriter or an underwriting team and may also select a financial advisor. (See below – "Financial Advisor" and "Underwriter/Placement Agent/Purchaser").

The Issuer's Responsibilities. Having selected its team, an issuer then works with its team to issue debt to finance the capital improvement or working capital program. Subject to legal constraints and considering the recommendations of its team members, an issuer retains ultimate control and responsibility over the overall financing plan and the details of the financing structure. The issuer's staff must consider itself responsible for reviewing all aspects of the financing plan, including all documents which determine or describe aspects of the financing. The issuer's staff (including its general counsel) is in the best position to be aware of the impact of aspects of the financing on other aspects of the issuer's finances and operations.

Also, the issuer will be involved in any legal action that may arise with respect to issuance of the bonds. In circumstances where there may be legal uncertainty about some aspect of a proposed bond transaction, the issuer may pursue a validation action to obtain judicial approval before the bonds are issued. If a bond transaction is controversial and gives rise to a reverse validation action, the issuer will find itself a party to that litigation. Furthermore, after the bonds are issued, the issuer will be ultimately responsible for long-term management and trouble-shooting, including:

- Supervising, investing and administering the expenditure of bond proceeds
- Collecting, or monitoring the collection of, revenues
- Use of revenues to pay operating expenses and debt service

- Compliance with all undertakings, covenants and agreements
- Management of any enterprise funded by the debt
- Filing of any reports required with various governmental regulators, a bond insurer or other credit enhancement provider, if any, and the credit rating agencies
- Addressing any problem that may arise with respect to the bonds, such as a shortfall in revenues, a tax audit or a regulatory issue
- Preparing, reviewing and filing Annual Reports and Listed Event Notices under SEC Rule 15c2-12

The degree to which members of the issuer's debt financing team are capable of looking out for the issuer's long-term interests, or are motivated to do so, will vary, depending on the relationship that each team member has with the issuer. Ultimately, the issuer must bear responsibility for looking out for its own interests. For this reason, the issuer must be an active participant in the debt financing process and not leave it all to the consultants. Even if the issuer selects its consultants with an eye toward providing the services that cannot be provided in-house, the issuer must be prepared to examine the consultants' work and ask the questions necessary to assure the issuer that the end result is appropriate given the issuer's objectives.

Workouts. In the event that a problem arises with respect to the bonds, such as a shortfall in revenues needed to repay the bonds, a tax audit that reveals irregularities, or an investigation by a regulatory agency, the issuer will likely find itself thrown into the middle of the problem. The issuer should be aware of this possibility. The issuer is the participant most likely to be called upon to provide information and coordinate a workout strategy. Because of this, throughout the debt financing process the issuer should remain alert for any potential problem, as prompt remedial efforts may avoid a larger problem later on.

Issuers should be aware that there can be substantial costs involved in dealing with a troubled bond transaction, including legal and litigation costs, obtaining appraisals and hiring financial advisors and other consultants. In addition, significant staff time can be spent on these matters. Finally, political fallout can result if a transaction goes bad in a way which reflects badly on elected officials. Although a thorough discussion of defaults and workout situations is beyond the scope of this book, issuers are encouraged to be aware of the potential for such events and structure their debt issues prudently so as to avoid such problems.

BOND COUNSEL

The Bond Opinion. Bond counsel is the attorney or firm of attorneys that gives the legal opinion delivered with the bonds confirming that the bonds are valid and binding obligations of the issuer and, customarily, also that interest on the bonds is exempt from federal and state income taxes. In relatively rare cases, bonds designed to be taxable for federal income tax purposes are issued. In such cases, the tax opinion may be nonexistent, or may run only to exemption for state income tax purposes.

The Source of the Need for Bond Counsel. Historically, the requirement for such an opinion began in the second half of the 19th century when a number of issuers of railroad bonds disclaimed liability on their bonds on the basis of their own errors made in the process of issuing the bonds. Buyers of bonds began to require that an independent lawyer or law firm have rendered an opinion that the bonds were validly issued and binding. The issuer of that legal opinion, bond counsel, was and is required by market standards to be nationally recognized for expertise in municipal finance.

The Independence of Bond Counsel. Originally, bond counsel rendered the legal opinion very late in the process, sometimes after the bonds had been issued. Over time, however, to avoid the risk of a negative opinion, bond counsel was hired earlier and earlier in the issuing process. One result of the early engagement of bond counsel has been a shift in the role and the independence of bond counsel. Originally, bond counsel was required to be "independent" of the issuer and sometimes was even hired by the bond buyers (a practice occasionally seen even today).

Today, however, bond counsel, though not an employee of the issuer, is no longer necessarily required to be "independent" of the issuer. Rather, the standard, as reflected in the National Association of Bond Lawyers' guidelines concerning the function and professional responsibilities of bond counsel, is that the bond lawyer should be "objective," but nevertheless may be the lawyer for, responsible to and compensated by the issuer. The guidelines retain part of the "independence" concept by stating that bond counsel should not give their customary bond opinion unless it would be unreasonable for a court to conclude otherwise as to the law upon which the opinion depends.

The bond counsel final opinion thus meets a much more rigorous standard than is customary for most legal opinions. Under certain circumstances, where the law on a point is not entirely free from doubt, counsel may render an opinion to the effect that, if the matter were properly briefed and argued to a court of competent jurisdiction, the court "should" or "would" hold as described in the opinion. This is the standard that many non-bond legal opinions are measured against. It requires the reader to understand and appreciate the limitations of the authorities cited in the opinion and to understand that counsel is making some assumptions about the way a court would interpret these authorities if presented with the facts described in the opinion. While these "should hold" or "would hold" opinions may be used in a municipal finance transaction to address collateral matters from time to time, it would not generally be possible to successfully issue and sell bonds the validity or tax exemption of which was covered only by an opinion couched in such terms.

The Responsibilities of Bond Counsel. Originally, the bond opinion covered only the concept that the bonds were legal, valid and binding, and were issued in accordance with the law. In the last 30 to 40 years the statement that interest on the bonds is exempt from federal and state income taxes has become a very crucial part of the bond opinion. The legal work that goes into many bond issues is dominated by tax issues, in part because of the constant change in the tax laws relating to tax-exempt bonds. The bond opinion may also cover the validity of one or more of the legal documents under which revenues are made available to pay the bonds, such as a lease or loan agreement.

Disclosure. The bond opinion does not make financial recommendations or represent a financial judgment as to the acceptability of the bond for the Investor, is not intended to be a disclosure document and does not in and of itself represent a judgment that the disclosure available with respect to the bond is adequate under federal or state securities laws. However, in bond counsel's expanding role, bond counsel sometimes agrees to a separate component of responsibility for advising the issuer concerning compliance with federal and state securities laws in the course of the debt issuance process. This is often stated as a separate item in the issuer's agreement with bond counsel for legal services or is stated to be the primary responsibility of some other lawyer participating in the transaction, such as disclosure counsel.

Legal Team. The legal team for a bond issue sold on a negotiated basis generally will include bond counsel, issuer's counsel, underwriter's counsel and/or disclosure counsel, counsel for the company or other nongovernmental borrower, if any, and trustee's counsel. Bond counsel's role in these cases will customarily be as special counsel to the issuer for the financing and not as counsel to the investor. In a negotiated sale, the interests of the investor are indirectly represented by the underwriter and underwriter's counsel.

Bond Counsel May NOT be Underwriter's Counsel. Historically, when an issue was to be sold on a negotiated basis and was too small to afford several attorneys, with the consent of the issuer and the underwriter, bond counsel occasionally also acted as underwriter's counsel. In 1985, Section 53593 was added to the Government Code prohibiting bond counsel with respect to an issue of bonds from also being counsel with respect to that issue to the underwriter or other initial purchaser of the bonds. Bond counsel may render opinions to the underwriter or purchaser, but only as bond counsel and not as counsel to the underwriter or purchaser. As described below under "underwriter's counsel," a recent development is the increasing use of disclosure counsel, or counsel to the issuer with respect to disclosure and bond sale matters. This type of relationship is not prohibited by Government Code Section 53593.

In the case of bonds sold at competitive sale, no underwriter or underwriter's counsel is involved in the transaction until the financial structure has been determined, the proceedings are basically final and the bonds are offered at the sale. In that situation, bond counsel and the financial advisor work with the issuer to design a bond issue that will be acceptable to investors. The format of such transactions is usually relatively standard.

Whether the bonds are sold at negotiated or competitive sale, bond counsel is customarily responsible for preparation or review of the legal proceedings for the issuance of the bonds, including election proceedings if an election is required, resolutions of the governing body of the issuer authorizing the issuance of the bonds and otherwise relating to the bond issue, and the documents under which the bonds will be issued and secured. In the case of certain types of lending programs, bond counsel may also prepare loan agreements, origination and servicing agreements, lease agreements, deeds of trust and other similar documents relating to the sources of revenues with which the issuer will pay debt service on the bonds.

Finally, bond counsel may address a wide variety of legal issues relating to the financing. In circumstances where there may be legal uncertainty about some aspect of a proposed bond transaction, bond counsel may pursue a validation action to obtain judicial approval before the bonds are issued. If a bond transaction is controversial and gives rise to a

reverse validation action, bond counsel will likely be asked to represent the issuer in the litigation or to assist the issuer's general counsel or outside litigation counsel.

Bond counsel is not ordinarily general counsel to the issuer. However, in some cases (especially where the issuer's general counsel is hired on a "contract" basis rather than as a regular employee), if the issuer's counsel has the requisite expertise, he or she may serve as bond counsel as well. Where the issuer's regular counsel also serves as bond counsel, special attention should be paid to conflicts of interest, particularly where a contingent fee for the bond counsel services is involved.

If the issuer's regular counsel is not bond counsel, the issuer's counsel (e.g. the City Attorney) will nevertheless play an important role, typically with respect to conforming the procedures and documents to the special needs of the issuer. In addition, issuer's counsel will often be required to render an opinion with respect to the issue, typically limited to the organization and existence of the issuer, the due approval, execution and delivery of documents, the absence of litigation and similar matters.

Because of the complexities of bond financing, there are several roles that bond counsel may play. It is very important that a clear relationship between the issuer and bond counsel be established early in the transaction and that the issuer establish who bond counsel represents and the purposes for which bond counsel is engaged.

Bond counsel may be compensated on a variety of bases, including an hourly rate, proportional to the size of the issue (customarily on a sliding scale representing a smaller percentage of larger issues), a fixed dollar amount and others. Bond counsel's fee may be payable whether or not the bonds are issued or may be contingent upon the issuance of the bonds. In addition, even if the fee is contingent, reimbursement for bond counsel's out-of-pocket expenses may be payable without regard to whether the bonds are issued.

Workouts. Bond counsel is often involved in resolving any problem that arises after the bonds are issued. Such problems may include a shortfall in revenues needed to repay the bonds, irregularities revealed by a tax audit, or regulatory concerns such as a disclosure issue. Where the problem is serious, such as a payment or significant covenant default, the issuer may wish to hire new counsel to provide a fresh perspective.

FINANCIAL ADVISOR

The Scope of the Financial Advisory Relationship. A financial advisor is a professional consultant retained (customarily by the issuer) to advise and assist the issuer in formulating and/or executing a debt financing plan to accomplish the public purposes chosen by the issuer. A financial advisor may be a consulting firm, an investment banking firm or a commercial bank. Some financial advisors identify themselves as "Independent Financial Advisors," being firms that do not engage in underwriting or trading of municipal securities.

Issuers have in some cases retained financial advisors for the sole purpose of assessing bond market conditions at the time of sale of the bonds to determine the appropriateness of the interest rate and other terms of the offer by the underwriter to buy the

bonds. On the other hand, a financial advisor may be retained to perform a broad variety of functions for the issuer, including surveying the issuer's existing debt structure and capital financing program and designing and assisting in executing a total financing plan for the issuer.

The role of or necessity for the financial advisor may depend upon the financial sophistication of the issuer and its staff, the workload capacity of the issuer's staff and the division of labor among the staff and other participants in the debt financing. For example, in the case of a negotiated sale of bonds, the underwriter is often selected by the issuer early in the process and may be the principal "advisor" of the issuer as to the best manner of accomplishing the issuer's ultimate financial objectives. In such cases, the issuer may not select any financial advisor, or the role of the financial advisor may be limited to assessing the appropriateness of the underwriter's recommendations. In other cases, a financial advisor may be selected initially, regardless of the method of sale, and play a key role in assisting the issuer.

Issuers should be aware that whether they initially hire and rely on the advice of an underwriter or a financial advisor, they are going to receive such advice subject to the biases inherent in the position of these participants. The only true objectivity is that of the informed staff of the issuer keeping in mind the goals and policies to which they are committed.

The Traditional Services of a Financial Advisor. For example, in a public facilities capital improvement program to be financed by general obligation or revenue bonds required to be sold at competitive sale, the financial advisor will customarily do each of the following:

- Review the financial feasibility of the capital projects
- Assess the available sources of revenue
- Recommend a financing structure (including the nature of the security for the bonds, excess revenue coverage requirements, debt service reserve account requirements, facilities insurance requirements, liability insurance requirements and the need for credit enhancement)
- Recommend a maturity schedule, redemption terms and other terms of the notice of sale
- Prepare on behalf of the issuer an Official Statement for distribution to potential underwriters and investors and describing the issuer, the bonds, the security for repayment of the bonds and any other matters that would be material to an investor
- Be the primary spokesperson on behalf of the issuer with the credit rating agencies
- Recommend the timing of sale of the bonds

- Arrange for and direct the mailing of the Official Statement and the official notice of sale to potential underwriters and investors
- Contact and answer the questions of potential underwriters and investors
- Analyze bids received at the competitive sale
- Recommend whether to accept or reject such bids
- Assist bond counsel in organizing the closing, i.e., the delivery of the bonds in return for payment for the bonds
- Recommend appropriate investments for the proceeds of the bonds

Other possible responsibilities include recommending, where the options are available, competitive sale, negotiated sale or a private placement of the bonds and, in the case of a negotiated sale or private placement, negotiating bond terms on behalf of the issuer.

Workouts. In the event that any problem arises with respect to the repayment of the bonds, such as a shortfall in revenues, a financial advisor typically gets involved in the efforts to resolve the problem. Issuers facing repayment and other problems sometimes turn to the financial advisor who assisted with the original transaction, or bring in a new financial advisor to provide a fresh perspective. Some financial advisors have acquired substantial expertise in restructuring bond transactions, negotiating with bondholders and trustees, and carrying out other necessary or appropriate workout steps.

Conflicts of Interest. The relationship between the issuer and the financial advisor should be one of confidence and trust, and is in the nature of a fiduciary relationship. The law emphasizes this by prohibiting certain actions that might create a conflict of interest. Section 53591 of the Government Code prohibits a financial advisor with respect to an issue of bonds from acquiring the bonds from the issuer as principal either alone or as a participant in a syndicate or other similar account unless the issue is sold by the issuer at competitive public sale and the issuer has, prior to the bid, expressly consented in writing. Section 53592 of the Government Code requires each financial advisory relationship to be evidenced by a written document executed prior to or promptly after the inception of the relationship, or promptly after the creation or selection of the issuer if the issuer does not exist or has not been determined at the time the relationship commences. The document must describe the basis of compensation for the services to be rendered. With certain limited exceptions the compensation must be on a basis other than a percentage of the amount of the bonds to be issued. Section 1090 of the Government Code also regulates conflict of interest. The full text of these Government Code sections is set out in ***"Appendix D – Legal References."***

Rule G-23 of the Municipal Securities Rulemaking Board contains requirements that are similar to, although not quite as stringent as, the requirements of Government Code Sections 53591 and 53592 relating to financial advisory relationships. Rule G-23 includes an express additional requirement that prior to purchasing from an issuer bonds with respect to

which a financial advisor has provided advisory services, the financial advisor must terminate its financial advisory relationship with the issuer with respect to that issue.

Neither state law nor the MSRB rules prohibit a financial advisor from purchasing bonds in the secondary market, either for the financial advisor's own trading account or for the account of customers, except to the extent that such purchase is made to contravene the purpose and intent of the above-described requirements.

As these rules emphasize, the financial advisor's professional duty is to the issuer, and the advisor must advance the financial interests of the issuer on the issuer's chosen course.

UNDERWRITER/PLACEMENT AGENT/PURCHASER

Underwriter vs. Placement Agent. An Underwriter purchases bonds from an issuer with the intent to resell the bonds to investors. In contrast, a placement agent acts as agent for the issuer in selling bonds to a private placement purchaser, and, as such, does not purchase the bonds. The responsibilities and functions of the underwriter will depend primarily on whether the bonds are to be sold at competitive sale or at negotiated sale.

Services in a Negotiated Sale. In the case of a negotiated sale, the issuer will customarily select the underwriter (or the underwriting team) early in the process and the underwriter may perform many of the services described above for financial advisors. If the issuer has not retained a separate financial advisor, the underwriter may assist the issuer in determining what is to be financed, the method of financing and the financing structure. The underwriting firm performing these functions is often called the managing underwriter or, where there is more than one member of the initial underwriting team, the "lead managing underwriter" or "senior managing underwriter." In such cases the underwriter will customarily hire its own counsel and the underwriter and underwriter's counsel will take the lead in coordinating preparation of the Official Statement for the bonds. Alternatively, as discussed above, the issuer may elect to retain disclosure counsel for the purpose of preparing the Official Statement and related sale documents. However, regardless of who takes primary drafting responsibility, the issuer remains responsible for full disclosure in the Official Statement.

After the design of the financing and the preparation of the Official Statement, the underwriter in a negotiated sale will ordinarily do the following:

- Mail the Official Statement to potential bond buyers and underwriting syndicate members
- Assess bond market conditions to recommend timing and pricing of the bond sale
- Form an underwriting syndicate in the case of larger issues
- Obtain the agreement of the underwriting syndicate to the interest rates and terms of sale for the bonds

- Sign a bond purchase agreement on behalf of itself or the underwriting syndicate, as the case may be

- Ensure that appropriate continuing disclosure undertakings are entered into by the issuer to show compliance with SEC Rule 15c2-12

As an alternative to forming a syndicate, an underwriter may form a selling group. When a syndicate is formed, each syndicate member has, through the agreement among underwriters and the bond purchase agreement, a direct obligation to the issuer to buy the bonds. A selling group member has no such obligation, and in such cases only the managing underwriter has a direct obligation to the issuer to buy the bonds. A selling group member receives only the bonds the managing underwriter agrees to sell to it (in response to its order for such bonds).

An issuer selling bonds at negotiated sale has the flexibility of advancing or delaying the sale date to respond to market conditions in an effort to obtain the best possible financing terms. In the case of complex or unusual debt financings, the negotiated sale process also permits direct input from the buyer of the bonds as to the desirability of various financing structures or features. Finally, in a negotiated sale, the underwriting syndicate can do a substantial amount of preselling of bonds, thus lowering the underwriting risk and, presumably, lowering the need for compensation for taking underwriting risk.

Services in a Competitive Sale. On the other hand, in a competitive sale, at the time and place specified by the official notice of sale, competing underwriters deliver sealed bids to the issuer, and the issuer selects the underwriter (alone or as representative of an underwriting syndicate or selling group) offering the best terms at that time and place. Customarily, bidders are permitted to specify, within the limits specified by the notice of sale, the interest rate for each maturity of the bonds and the price (including premium or discount) at which they will buy the bonds. The notice of sale also specifies the method of determining the best bid, which is customarily either the net interest cost method or the "net effective interest rate" method (sometimes called the true interest cost method). See "***Appendix C –Debt Financing Terms and Concepts.***" Because the underwriters in a competitive sale have not been independently involved in the design of the financing structure and only have available to them the Official Statement and other readily accessible information concerning the issuer, bonds sold at competitive sale are customarily relatively standard in design and security. In addition, the potential investors in such bonds are relatively identifiable.

Legal requirements respecting published notice for a competitive sale may sometimes make it difficult for an issuer to remain flexible concerning the timing, terms and amount of the sale. (See "Types of Financing Instruments" for discussion of requirements relating to the process for sale for various debt instruments.) On the other hand, a properly conducted competitive sale gives an issuer reasonable comfort that on the date of sale, given the financial structure chosen, the issuer has received the best possible bid for its bonds. Recently, issuers have begun including a provision in the notice of sale in a competitive offering which allows the issuer to postpone the sale date for up to a limited number of days or weeks (usually on 24 hours notice by Munifacts[SM] wire service). This gives the issuer some flexibility to postpone a sale if the market on the sale date does not appear favorable.

Compensation - The Underwriter's Gross Spread. In both negotiated and competitive sales, the underwriters are primarily compensated by the difference between the price they pay the issuer for the bonds and the price at which they resell the bonds to investors (the "spread"). When a managing underwriter and syndicate members determine the amount to be bid for the bonds and the expected amount of the spread, they take into account a number of factors, including:

- **Management Fee** - a fee paid to the managing underwriter for handling the affairs of the syndicate, including, in the case of a negotiated sale, structuring the issue and negotiating with the issuer

- **Expenses** - any advertising and printing costs to the underwriter, fees and expenses of underwriter's counsel, Blue Sky fees and expenses, computer expenses, travel expenses, MSRB fees, CDIAC fees, and other similar expenses

- **Takedown** - normally the largest component of the spread, similar to a commission, which represents the income derived by the selling broker or dealer from the sale of the bonds; if bonds are sold by a member of a syndicate, the seller is entitled to the full takedown (also called the "total takedown"); if bonds are sold by a dealer which is not a member of the syndicate, such seller receives only that portion of the takedown known as the concession or dealers allowance, with the balance (often termed the "additional takedown") retained by the syndicate

- **Risk** - the amount of compensation for risks incurred by the underwriter in underwriting the bond issue, relating to the difficulty of marketing the issue, bond market conditions, and the amount of bonds remaining to be resold after the execution of the bond purchase agreement. It is very uncommon for there to be any risk component in the spread

Underwriting spreads have tended to decline over the last 5 to 10 years due to competition and market factors. It is not possible to state a "rule of thumb" for what an underwriting spread should be or what the components should be relative to each other, because it depends on many factors including the type of financing, the credit quality of the debt, the scope of services to be provided by the underwriter, and other factors. In the process of the final pricing of the bonds, the issuer should request from the underwriter information as to the elements of the expected spread and data on comparable spreads from other recent pricings. Issuers should remember that all of the elements of a spread are negotiable. If a financial advisor is involved in the transaction, the financial advisor should be prepared to analyze the proposed spread and ensure that it is reasonable under all of the circumstances.

Rule G-37 of the Municipal Securities Rulemaking Board generally prohibits underwriters which have made political contributions to elected officials of an agency from conducting any underwriting business with that agency for a period of two years after the contribution is made. In some cases, state law or local ordinances may impose similar limitations or exclusions.

Workout. The role of the underwriter varies in workout situations. If new bonds are being issued as part of solving the problem, the original underwriter, or a new underwriter, may be closely involved with the financial advisor and bond counsel in the workout effort. Nonetheless, because many underwriters are concerned about the viability of bonds in which they were involved, if asked to do so they will attempt to identify the bondholders and help to facilitate contact with them as part of the workout effort.

UNDERWRITER'S COUNSEL AND DISCLOSURE COUNSEL

Selection and Need. Underwriter's counsel is customarily selected by the underwriter to represent the underwriter and its interests in a negotiated sale. Normally, no underwriter's counsel is retained in a competitive sale. Underwriter's counsel will customarily review, from the underwriter's perspective, the documents prepared by bond counsel and will negotiate matters relating to those documents on behalf of the underwriter.

Disclosure and Securities Laws Compliance. Underwriter's counsel will also often coordinate preparation of the Official Statement with input provided by other financing team members, including the issuer, issuer's general counsel, the underwriter, bond counsel, the financial advisor, if any, the credit enhancement provider, if any, and the nongovernmental borrower, if any. In addition, underwriter's counsel will often prepare the continuing disclosure agreement or Certificate to evidence the undertakings of the issuer and other obligated persons with respect to SEC Rule 15c2-12. In so doing, underwriter's counsel will make recommendations concerning the disclosure requirements of federal and state securities laws. Upon the issuance of the bonds, underwriter's counsel will give to the underwriters what is commonly called a "10b5 opinion" concerning compliance with the disclosure requirements of federal law.

In order to give a "10b5 opinion" underwriter's counsel will need to conduct "due diligence" concerning the issuer, the securities and their sources for repayment. Due diligence is the inquiry made to reveal or confirm facts about the issuer, the issue and the security for the issue that would be material to a prudent investor in making a decision to purchase the issue. Due diligence inquiries are made by underwriters and lawyers to determine, for example, whether the issue follows the purpose and scope outlined by the enabling legislation, statutes, and resolutions of the issuer and whether all material facts have been accurately disclosed in the Official Statement. This exercise varies depending upon the type of debt being issued and the issuer involved, but typically involves review of documents including financial statements, minutes of meetings, major contracts, licenses, permits and real estate documents and other items relevant to the credit involved. Counsel will typically start this process with a request that specific documents be made available for inspection in the issuer's offices on a particular day. After review of the documents, counsel may need to follow up with interviews or requests for additional information.

Underwriter's counsel also will advise the underwriter concerning the registration requirements, if any, of federal and state securities laws (so-called "Blue-Sky Laws") for sale of the bonds in various jurisdictions.

Compensation of Underwriter's Counsel. Underwriter's counsel is customarily paid by the underwriter from the underwriting expense portion of the spread.

Disclosure Counsel. Recently, some issuers have started using disclosure counsel in connection with bond issues. Disclosure counsel handles many, if not all, of the tasks traditionally handled by underwriter's counsel, except when it is clear that the disclosure counsel's client is the issuer and not the underwriter. If underwriter's counsel has been retained, it may not be necessary to retain disclosure counsel.

Disclosure counsel may prepare the draft Official Statement, the Bond Purchase Contract (or, in the case of a competitive sale, the Official Notice of Sale), the Continuing Disclosure Agreement and any Blue Sky Memoranda. In addition, disclosure counsel may render a "10b5 opinion" to the underwriter for the transaction. In doing this work, the disclosure counsel is representing the issuer and not the underwriter, and all parties must be aware of this role and of the duties disclosure counsel owes to its client, the issuer. If structured in this way, disclosure counsel may be the same lawyer or firm as bond counsel on a particular transaction since the client in both cases is most likely the issuer. Occasionally where disclosure counsel is used, the underwriter will also have its own counsel, but typically that counsel's role is limited to advising the underwriter on negotiation of the purchase contract and on regulatory compliance issues.

Compensation of Disclosure Counsel. Because disclosure counsel works for the issuer, typically disclosure counsel is paid by the issuer from the proceeds of the bonds. As with bond counsel, compensation arrangements may include hourly rates, fixed or percentage fees or a combination of methods, and may be contingent upon issuance of the bonds or payable regardless of the success of the transaction.

CREDIT RATING AGENCIES

The credit rating agencies (principally Moody's Investors Service, Inc., Standard & Poor's Corporation and Fitch Investors Service, Inc.) provide, for a fee customarily paid by the issuer, an independent appraisal of the credit quality and likelihood of timely repayment of a bond issue. Normally, when the financing structure is designed and the documents are in reasonably final form, the financial advisor or underwriter will provide all of the documents to the rating agency or agencies selected by the issuer (with advice from the financial advisor or underwriter) and will provide any other additional information (such as cash-flows or other financial calculations) requested by the rating agency. Representatives of the rating agency may also visit the issuer or the project being financed. In the alternative, a financial advisor or underwriter may recommend that representatives of the issuer meet with the rating agency in their offices in San Francisco or New York.

Underwriters and investors rely upon the credit quality judgment made by the rating agencies (expressed as a credit rating). Some mutual funds, institutions and investment trusts are restricted by law or by the terms of their organizational documents to buying securities at or above specified credit rating levels. Other investors may apply such criteria informally. Investors generally demand higher interest rates with respect to lower-rated bonds. Generally speaking, the credit rating is the most important factor in determining the interest rate on bonds

relative to other issues sold at the same time. Tables 1-1 and 1-2 below describe the various credit ratings for Moody's, Standard & Poor's and Fitch.

Bonds are generally not legally required to be rated. However, in most cases issuers find it to their advantage to obtain bond ratings because of the difficulty of selling unrated bonds. One important exception is in the case of land-secured financings such as assessment or Mello-Roos Bonds for districts where development has not been completed at the time of the issuance of the bonds, which are commonly issued as unrated bonds. Some conduit issuers require a minimum rating in order to issue bonds as a matter of policy. For example, the State's Educational Facilities and Health Facilities Financing Authorities require a minimum "A" rating – either through credit enhancement or on a "stand-alone" basis, although on a case-by-case basis will permit a "BBB" or "Baa" rating if additional collateral (such as a deed of trust) is posted.

Each major rating agency maintains separate rating scales for long-term debt (generally debt with a maturity of greater than 1 year) and short-term debt (generally debt with a maturity of less than one year). It is possible for an issuer's short-term rating to be of a different category than its long-term rating.

Ratings are reviewed periodically by the rating agencies whether or not requested by the issuer. Such a review may result in upgrading or downgrading of an existing rating. To perform such a review, the rating agencies expect periodic financial and other reports relating to the status of a bond issue, and may, in the absence of such reports, suspend the rating of an issue.

Finally, although ratings are generally assigned only in response to a request from the issuer, the rating agencies reserve the right to assign a rating without such a request. The following tables are condensed from the rating descriptions published by each rating agency. More detailed descriptions of the ratings categories for each major rating agency are available on the rating agencies' web sites. See ***"Appendix B – Resources and Contacts."***