Mtg.

10/13/62

Memorandum No. 73(1962)

Subject: Study No. 52(L) - Sovereign Immunity (Funding Judgments with Bonds)

Attached as Exhibit I (pink pages) is an extract from the report of the State Bar Committee on Sovereign Immunity. A letter from the office of the Los Angeles County Counsel commenting on the Commission's recommendation relating to funding judgments with bonds is attached as Exhibit II to Memorandum No. 65 (1962).

Attached, also, is a copy of the Commission's tentative recommendation and draft statute.

The Los Angeles County Counsel has made no specific comments with respect to the Commission's recommendation, but has indicated agreement with the Commission on the principle of providing broad authority for local public entities to fund judgments with bonds.

The State Bar Committee has several suggestions and comments to make with respect to the Commission's recommendation:

(1) As indicated in the first paragraph of the attached Exhibit, the State Bar suggests that funding judgments with bonds should be resorted to only in extreme emergencies when no other means are available to the entity to satisfy the indebtedness. Since the statute is intended to grant broad authority to local public entities, the staff suggests that the statute not be limited to the exercise of such authority only in cases of extreme emergency. The statutory provisions for decision by the governing board of the local public entity, an open hearing on the merits of issuing bonds, and

a vote requiring a two-thirds majority of the electorate of the taxing entity are all sufficient protection against abuse of the authority vested in the public entity.

(2) The State Bar Committee suggests that the authority to pay interest on bonds be restricted to a semi-annual interest payment. While most bonding authorizations provide for the payment of interest at a semi-annual rate, the staff suggests that the Commission's statute not be so limited for the reasons indicated above, namely, that the statute is intended to grant broad authority for the issuance of bonds and it is probable that a local public entity will exercise its authority in accord with normal bonding practices. In this regard, it should be noted also that the interest rate of 7 percent provided in the Commission's recommended statute is greater than the normal five or six percent provided in other general bonding authorizations. This lucrative rate of interest might be sufficient to add salability to bonds which provide for interest payment only at an annual rather than a semi-annual rate.

(3) The State Bar Committee suggests that the statute make clear that incidental expenses connected with the bond issue be payable from the proceeds of the bond issue so that the authority to incur indebtedness is not limited to the principal amount of the outstanding judgment. The staff intended to accomplish this same result by omitting the word "principal" in subdivision (c) of Section 742.6. In any event, to make this clear, the staff suggests that the following be added to subdivision (c) of Section 742.6: ", which amount may include legal or other fees incidental to or connected with the authorization, issuance and sale of the bonds, including the costs of printing thereof." This language is adopted from Government Code Section 43610.1.

(4) The State Bar Committee suggests that the statute make clear that the clerk or secretary of the local taxing entity need not personally sign the bond coupons. Although this is the probable effect of the second sentence of Section 742.13 as drafted, the staff suggests in accord with the State Bar Committee that the matter be made clear. Accordingly, the staff suggests that the second sentence of Section 742.13 be revised to read as follows: "All signature on the bonds and the bond coupons, except the countersignature of the clerk or secretary on the bonds, may be printed, lithographed or engraved." (With respect to the specific means of reproduction, several recent statutes have used the language "may be made by facsimile" to avoid restricting the means of reproduction.)

(5) The State Bar Committee questions the distinction between "city" and "municipality" as used in Section 742.6. As the Commission will recall, the second paragraph of this section is a standard boiler plate clause frequently used in many special acts relating to the issuance of bonds. Moreover, it seems clear that "municipality" may have a broader meaning than "city." (See, e.g., Black's Law Dictionary, pages 1212-15, especially "municipality" on page 1215.) Accordingly, the staff suggests no change in this section.

(6) The State Bar Committee recommends that the statute make clear that the legal investment clause in Section 742.6 should not be construed to be in derogation of the prudent investor rule enunciated in Civil Code Section 2261 In this regard, the staff believes that no change is needed in the present statute since the language of Section 2261 clearly overrides any provision in any statute authorizing the investment of trust funds in particular operations. Although prior to 1943, California was among the states adhering

to the "legal list" or "Massachusetts rule" relating to legal investments, it is clear that this is no longer the rule and that the prudent investor criterion would be applicable to any statutory authority relating to legal investment. Accordingly, the staff recommends against the inclusion of this unnecessary provision. (It may be noted also that numerous special acts incorporating the standard boiler plate investment clause as used in the draft statute have been enacted since 1943 without apparent necessity for a clarification of the prudent investor rule as suggested by the State Bar Committee.)

(7) The State Bar Committee suggests that the statute make clear that the provisions for the issuance and sale of bonds be restricted to the payment of judgments, that is, restricted to the purpose for which the bonds were issued and sold. The staff believes that this is a valid criticism of the present draft and suggests that the substance of Government Code Section 43628 be added as a second sentence to Section 742.18 in the draft statute to read as follows: "The proceeds from the sale of bonds issued pursuant to the article shall not be used for any purpose other than the purpose stated in the resolution authorizing the issuance of such bonds."

(8) The State Bar Committee recommends the addition of statutory language similar to Government Code Section 43630 with respect to the voiding of unsold bonds. This would seem to be a desirable addition to the statute if only for the reason that it normally appears in bonding statutes similar to that proposed by the Commission. Accordingly, the staff suggests in the alternative either (1) to add the following language to Section 742.10, or (2) to add a new section, Section 742.19, containing the following language:

The board may by two-thirds vote of all its members declare that no part of the bond issue remaining unsold shall be issued or sold. When the resolution takes effect, the bonds described in the resolution which remain unsold are voided.

No other comments on this statute have been received.

Respectfully submitted,

Jon D. Smock
Assistant Counsel

Memo 73(1962)

EXHIBIT I

EXTRACT

from

SECOND REPORT OF

STATE BAR COMMITTEE ON SOVEREIGN IMMUNITY

(Meeting of September 20, 1962)

2. FUNDING JUDGMENTS AGAINST LOCAL PUBLIC ENTITIES WITH BONDS

Because of the frequent improbability of two-thirds of the electorate voting in favor of a bond issue, with its consequent tax increase, to pay an outstanding judgment and because the discretionary authority conferred by the proposed draft statute may militate against public entities providing insurance against tort liabilities, the Section was of the view that funding judgment indebtedness by bonds should be resorted to only in extreme emergencies and when no other means are available to the entity to satisfy the judgment or judgments.

It is noted that the draft statute appears to have been adapted in part from Government Code Sections 43600 et seq and Government Code Sections 43720 et seq. Both of these Acts provide for the payment of interest on bonds semi-annually. The Section questions the advisability in Section 742.6 of authorizing the payment of interest annually.

It should be made clear that the bonded indebtedness to be incurred should be sufficient not only to pay any judgments against the local taxing entity but also to pay legal fees, costs of printing and other expenses incurred in connection with the issuance of the bonds. In this connection see Government Code Section 43610.1.

Section 742.13 provides in part: "all signatures except that of the Clerk or Secretary on the bonds may be printed, lithographed or engraved". Although reference is made therein to bonds it is not clear whether the Clerk or the Secretary would have to personally sign all coupons attached to the bonds. The Section accordingly recommends that there be added after the above quoted sentence the following:

> "The signature of the Clerk or the Secretary on the coupons may be printed, lithographed or engraved".

In the last line of Section 742.16 it is noted that reference is made to the "bonds of cities *** or municipalities of the State". Is there any difference between a city and a municipality?

In the same Section 742.16 where reference is made to the bonds being "legal investments for all trust funds", the Section recommends that the legislative history make it clear that this is not intended as any abrogation of the "prudent man rule" in Civil Code Section 2261.

There should be added to the draft statute a section specifically restricting the use of the proceeds of the sale of such bonds to the purpose expressed in the resolution, (Section 742.6). In this connection attention is invited to Government Code Section 43628 as a convenient form.

It is also recommended that provision be made for the voiding of unsold bonds. In this connection see Government Code Section 43630.

52(L)

August 1, 1962

CALIFORNIA LAW REVISION COMMISSION
School of Law
Stanford University
Stanford, California

TENTATIVE RECOMMENDATION

of the

CALIFORNIA LAW REVISION COMMISSION

relating to

FUNDING JUDGMENTS AGAINST LOCAL PUBLIC ENTITIES WITH BONDS

NOTE: This is a tentative recommendation prepared by the California Law Revision Commission. It is not a final recommendation and the Commission should not be considered as having made a recommendation on a particular subject until the final recommendation of the Commission on that subject has been submitted to the Legislature. This material is being distributed at this time for the purpose of obtaining suggestions and comments from the recipients and is not to be used for any other purpose.

TENTATIVE RECOMMENDATION

of the

CALIFORNIA LAW REVISION COMMISSION

relating to

FUNDING JUDGMENTS AGAINST LOCAL PUBLIC ENTITIES WITH BONDS

The expansion of tort liability of governmental entities makes it imperative to provide governmental entities with means to minimize the disruptive effect of unexpectedly large judgments. Certain governmental entities in California have long been authorized to issue bonds to raise funds to pay tort judgments. The City of Los Angeles issued bonds to fund a liability of almost six million dollars incurred in the St. Francis Dam disaster of the late 1920's. The City of Long Beach issued bonds to obtain funds to pay judgments in excess of $370,000 that resulted when a platform leading to the entrance to the municipal auditorium collapsed under the weight of a crowd of people in 1914. That these cities were able to fund their tort liabilities with bonds enabled them to meet these obligations without seriously disrupting their financial structures.

The Law Revision Commission recommends that similar authority be extended to all other public entities that levy taxes or assessments and thus have the power to raise the revenues to discharge a bonded indebtedness. Inasmuch as the exercise of this power may result in the imposition of taxes to discharge the bonded indebtedness, the power should be exercised only when two-thirds of the voters, voting at an election called for that purpose, authorize the public entity to issue the bonds.

The Commission's recommendation would be effectuated by enactment of the following measure:

An act to add Article 6 (commencing with Section 742.1) to Chapter 2 of Division 3.5 of Title 1 of the Government Code, relating to funding judgments against local public entities with bonds.

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

SECTION 1. Article 6 (commencing with Section 742.1) is added to Chapter 2 of Division 3.5 of Title 1 of the Government Code, to read:

Article 6. Funding Judgments Against Local Public Entities with Bonds

742.1. As used in this article:

(a) "Board" means the governing body of a local taxing entity.

(b) "Local taxing entity" means a local public entity that has the power to levy ad valorem taxes or assessments upon property within the territory of the entity.

742.2. Whenever the board deems it necessary for the local taxing entity to incur a bonded indebtedness to fund all or any portion of an outstanding judgment against the entity, it shall by resolution state:

(a) The necessity for the indebtedness.

(b) The purpose for which the proposed debt is to be incurred.

(c) The amount of the proposed debt.

(d) The time and place for a hearing by the board on the question whether the local taxing entity should incur a bonded indebtedness to fund all or any portion of an outstanding judgment against the entity.

742.3. Notice of the hearing shall be given by publication of a copy of the resolution pursuant to Section 6066 of this code in a newspaper of general circulation circulated within the local taxing entity. If there is no such newspaper, the resolution shall be posted in three public places in the local taxing entity for two succeeding weeks. No other notice of the hearing need be given.

742.4. The copy of the resolution published or posted shall be accompanied by a notice subscribed by the clerk or secretary of the local taxing entity that:

(a) The hearing referred to in the resolution will be had at the time and place specified in the resolution.

(b) At that time and place, any person interested, including persons owning property within the local taxing entity, will be heard upon the question stated in the resolution.

742.5. At the time and place fixed for the hearing on the resolution or at any time and place to which the hearing is adjourned, the board shall proceed with the hearing. Any person interested, including persons owning property within the local taxing entity, may appear and present any matters material to the question set forth in the resolution. At the conclusion of the hearing, the board shall determine whether it is necessary to incur the bonded indebtedness. The board's determination on the question of necessity is conclusive.

742.6. After the board has made its determination pursuant to Section 742.5 of this article, if it deems it necessary to incur the bonded indebtedness, it shall by resolution state:

(a) That it deems it necessary to incur the bonded indebtedness.

(b) The purpose for which the bonded indebtedness will be incurred.

(c) The amount of the debt to be incurred.

(d) The maximum term the bonds to be issued shall run before maturity, which term shall not exceed 40 years.

(e) The annual rate of interest to be paid, which rate shall not exceed 7 percent, payable annually or semiannually, or in part annually and in part semiannually.

(f) The proposition to be submitted to the voters.

(g) The date of the special election of the local taxing entity (which may be consolidated with a general election of the local taxing entity) at which such proposition shall be submitted to the voters; the manner of holding the election and the procedure for voting for or against the proposition.

742.7. The resolution made pursuant to Section 742.6 of this article shall constitute the notice of such election and such resolution shall be published pursuant to Section 6066 of this code in a newspaper of general circulation circulated within the local taxing entity. If there is no such newspaper, the resolution shall be posted in three public places in the local taxing entity for two succeeding weeks. No other notice of the election need be given.

742.8. The board shall provide for holding the election in the same manner as provided by law in respect to general elections of the local taxing entity ~~so far as applicable, except as otherwise provided~~ in this article.

742.9. Every elector authorized to vote in general elections of the local taxing entity may vote on the proposition to authorize the bonds.

742.10. If two-thirds or more of the votes cast upon the proposition at the election are in favor of incurring the bonded indebtedness, the board may issue the bonds at the time or times it deems proper.

742.11. The board shall prescribe the form of the bonds. The bonds may be issued in denominations not to exceed $1,000 and not less than $100. The board shall fix, and designate in the bonds, a time and place for payment of the bonds.

742.12. The board may provide for the redemption of bonds issued under this article before maturity at prices determined by it. A bond shall not be subject to call or redemption prior to maturity unless it contains a recital to that effect.

742.13. The bonds shall be signed by the presiding officer of the board and countersigned by the clerk or secretary of the local taxing entity, and the coupons shall be signed by the clerk or secretary. All signatures except that of the clerk or secretary on the bonds may be printed, lithographed or engraved. If any officer whose signature appears on the bonds or coupons ceases to be such officer before the delivery of the bonds, his signature is as effective as if he had remained in office.

742.14. The local taxing entity may sell the bonds at the times or in the manner the board deems to be to the public interest. The bonds shall be sold on sealed proposals to the highest bidder after advertising for bids by publication of notice of sale pursuant to Section 6061, not less than 10 days prior to the date of sale, in a newspaper of general circulation circulating in the local taxing entity. If there is no such newspaper, the notice of sale shall be posted in three places in the local public entity for two succeeding weeks ending not less than 10 days prior to the sale. If satisfactory bids are received, the bonds offered for sale shall be awarded to the highest responsible bidder. If no bids are received or if the board determines that the bids received are not satisfactory as to price or responsibility of the bidders, the board may reject all bids received, if any, and either readvertise or sell the bonds at private sale.

742.15. An action to determine the validity of bonds may be brought pursuant to Chapter 9 (commencing with Section 860) of Title 10 of Part 2 of the Code of Civil Procedure.

742.16. Any bonds issued by any local public entity under the provisions of this article have the same force, value and use as bonds issued by any municipality and are exempt from all taxation within the State.

Such bonds are legal investments for all trust funds, for the funds of all insurance companies, banks (both commercial and savings) and trust companies, for the state school funds, and for any funds which may be invested in bonds of cities, counties, school districts, or municipalities in the State.

742.17 Bonds issued under this article constitute general obligations of the local taxing entity for the payment of both principal and interest of which all property in the local taxing entity subject to taxation by the local taxing entity or subject to ad valorem assessment by the local taxing entity shall be taxed or assessed without limitation of rate or amount.

The board shall, at the time and in the manner provided by law for levying taxes or assessments, fix an ad valorem rate of tax or assessment sufficient to pay the principal of and interest on all bonds issued under this article as they become due. Such ad valorem taxes or assessments shall be in addition to all other taxes or assessments levied by the local taxing entity, and when collected shall be used for no purpose other than the payment of such bonds and the interest thereon.

Nothing in this section shall be construed to prohibit the use of other revenues of the local taxing entity for the payment of principal and interest on bonds issued under this article.

742.18. The authority provided in this article is in addition and supplementary to any other law authorizing public entities to issue bonds to fund an outstanding indebtedness.