SUPERIOR COURT OF CALIFORNIA

COUNTY OF SACRAMENTO

SYNCORA GUARANTEE INC. AND SYNCORA CAPITAL ASSURANCE INC.,

Plaintiffs and Petitioners,

v.

STATE OF CALIFORNIA, et al.,

Defendants and Respondents.

Case No. 34-2012-80001215-CU-WM-GDS

RULING ON SUBMITTED MATTER: PETITION FOR WRIT OF MANDATE AND COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

Introduction

This action presents the issue of whether certain elements of the redevelopment dissolution laws enacted in AB 1X 26 and AB 1484 unconstitutionally impair the contractual rights of redevelopment agency bondholders (and the entities that insure those bonds) or take their property without just compensation.[1]

Syncora Guarantee Inc. and Syncora Capital Assurance Inc. (referred to collectively in this ruling as "Syncora") have filed a First Amended Complaint and Petition for Writ of Mandate (referred to in this ruling as the "Complaint and Petition") alleging that various provisions of the Health and Safety Code enacted in AB 1X 26 and AB 1484, and principally Section 34174, have this effect.[2] Specifically, Syncora alleges that the redevelopment dissolution laws improperly have deprived bondholders and their insurers

[1] In this ruling, AB 1X 26 and AB 1484 will be referred to collectively as the "redevelopment dissolution laws".

[2] Unless otherwise specified, all statutory references in this ruling are to the Health and Safety Code.

of tax increment funds that had been irrevocably pledged as security for the bonds, and have increased the risk that successor agencies, which are now responsible for the debts of former redevelopment agencies, will default on those debts.

On May 3, 2013, the Court held a hearing on the Complaint and Petition. At the close of the hearing, the Court took the matter under submission for issuance of a written ruling. The following shall constitute the Court's ruling.

Summary of Syncora's Claims

In the Complaint and Petition, Syncora alleges that it is "...a financial guaranty insurance company—commonly referred to as a 'monoline insurer' because it does not sell other kinds of insurance such as life, health, or property insurance. Generally, the monoline insurers provide credit enhancement on bonds issued by state and local governments, by insuring against the risk of municipal bankruptcy or default. The insurance specifically protects bond purchasers from the risk that RDAs[3], backed by the irrevocable pledges of the state, will nevertheless fail to make bond payments. Syncora provided bond insurance (and other related insurance policies) for bonds issued by California's RDAs. It is a party to contracts among the RDAs and bondholders relating to the specific RDA bonds covered by the relevant contracts it insures."[4]

Syncora's claims in this action center on the availability and use of so-called "tax increment funding", or "TIF", as security for RDA bonds. Syncora alleges that, prior to the enactment of the redevelopment dissolution laws, Article XVI, Section 16 of the California Constitution, and provisions of the Community Redevelopment Law (specifically, Section 33671), authorized RDAs to irrevocably pledge TIF as security for RDA indebtedness.[5] Respondents do not dispute this allegation.

Syncora alleges: "With the backing of this statutory grant, RDAs issued debt (bonds) containing irrevocable pledges of tax increment revenue. Many RDAs requested credit enhancement from municipal bond insurers, including Syncora, in order to make their debt more attractive to potential bondholders and

[3] RDAs = redevelopment agencies.

[4] See, Complaint and Petition, par. 13.

[5] See, Complaint and Petition, par. 2.

reduce their financing costs. Under the terms of the RDA bonds to which Syncora was a party, security for repayment of RDA debt included a lien on the tax increment revenue allocated to the RDA. Moreover, RDA bond indentures typically included a pledge that the additional tax increment and bond revenue would be used for redevelopment purposes only, thereby enhancing the prospects for future tax increment revenue as additional security for repayment of the bonds in the future. The existence of the irrevocable pledge formed an integral part of the RDA bonds, as well as the insurance policies among RDAs, bondholders, and Syncora, which directly reference, incorporate, and insure those bonds."[6]

In the Complaint and Petition, Syncora challenges the constitutionality of several provisions of the redevelopment dissolution laws, specifically, Sections 34172(d), 34174, 34177(d), 34183(a)(4) and 34188, which it collectively terms "the Redistribution Provisions".[7] Syncora describes the effect of these provisions as follows:

"The Redistribution Provisions directly revoke the supposedly irrevocable pledge of tax increment revenues as security for RDA debts. In doing so, they impair the tripartite contracts between the RDAs, the bondholders, and Syncora. First, the Redistribution Provisions eliminate the lien on tax increment revenue, which was established by law and reiterated in the terms of the contracts. Second, the Redistribution Provisions prohibit successor agencies from keeping surplus tax increment revenue for the benefit of potential debt obligations that may become payable more than six months in the future. Third, the Redistribution Provisions require that tax increment revenue not needed for debt service in the next six months be 'distribut[ed] to the taxing entities [as] property tax revenues…', rather than being held by the RDAs or invested in community development projects that strengthen future revenues, and thus security for the bonds. In sum, the Redistribution Provisions take RDA funds previously held for the exclusive purpose of RDA debt service and project area redevelopment and give those funds away to the public coffers."[8]

The effect of this change, Syncora alleges, is the loss of critical security for the bonds in case of

[6] See, Complaint and Petition, par. 3. See also, par. 27.

[7] See, Complaint and Petition, par. 5.

[8] See, Complaint and Petition, par. 6.

default, at the same time that the risk of default has increased significantly. As alleged in the Complaint and Petition, "[t]he Redistribution Provisions interfere with the vitality of critical debt security mechanisms created by the irrevocable pledge of TIF in the bond indentures. Absent the lien on TIF, RDA bondholders are not able to enforce prompt repayment of debt in the event of default. Because TIF revenue constitutes the sole secured source of repayment for bondholders and the Redistribution Provisions limit the successor agencies' authority to hold surplus TIF, the Redistribution Provisions increase the likelihood that debt will default in times of tax revenue shortfall. And the Redistribution Provisions eliminate the main driving force behind future increases in tax increment by prohibiting further redevelopment with TIF funds. Taken together, the Redistribution Provisions severely impair the critical security mechanisms protecting the repayment of RDA debt, in direct contravention of bargained for contractual obligations between the RDAs, the RDA bondholders, and the bond insurers."[9]

Based on these allegations, Syncora has stated causes of action seeking issuance of a writ of mandate under Code of Civil Procedure section 1085, a declaratory judgment under Code of Civil Procedure section 1060, and injunctive relief under Code of Civil Procedure section 526, all based on the theory that the challenged provisions of the redevelopment dissolution laws unconstitutionally impair their contracts. As an alternative to the contractual impairment claims, Syncora also has stated causes of action in inverse condemnation for damages based on a taking of property without just compensation.

The Complaint and Petition names the State of California, the State Controller and the Director of the Department of Finance as respondents (referred to collectively as "the State respondents"). The Complaint and Petition also names Larry Walker, the Auditor-Controller of San Bernardino County, as a respondent on his own behalf and as a representative of all County Auditor-Controllers for counties in the State of California where Syncora has insured RDA bonds.

Preliminary Evidentiary Issues

Prior to the hearing on this matter, the Court issued a minute order granting Syncora's request for leave to present oral testimony. Syncora elected not to present such testimony at the hearing.

[9] See, Complaint and Petition, par. 46.

On April 2, 2013, Syncora filed a request for judicial notice of 48 exhibits. The State respondents filed an objection to Syncora's request as a whole on the ground that it was not filed in a timely manner. Alternatively, the State respondents specifically objected to judicial notice of Exhibits 28-36. The objections are overruled. Although Syncora did not file the request for judicial notice with its opening brief, it nevertheless filed it sufficiently in advance of the hearing to provide the State respondents with sufficient notice of the request to enable them to meet the request as required by Evidence Code section 453. The exhibits the State respondents specifically object to are appropriate subjects for judicial notice as records of this Court (Exhibits 28-33), or as undisputed evidence that certain publications were made by Moody's Investors Service (Exhibits 34-36). Syncora's request for judicial notice is therefore granted. However, the Court will take judicial notice only of the existence of the documents, and not of the truth of statements contained therein. (See, *StorMedia, Inc .v. Superior Court* (1999) 20 Cal. 4th 449, 457, fn. 9.)

On April 8, 2013, the State respondents filed a request for judicial notice of four exhibits, consisting of documents related to Recognized Obligation Payment Schedules filed for the period January 1, 2013 to June 30, 2013 by the City of Hesperia, as successor agency to the Hesperia Community Redevelopment Agency, and by the City of Victorville, as successor agency to the Victorville Redevelopment Agency, and letters from the Department of Finance to those cities approving certain bond-related items in the ROPS. Syncora has not objected to the request. The exhibits are proper subjects for judicial notice as acts of public agencies. The State respondents' request for judicial notice is therefore granted.

On March 19, 2013 and April 18, 2013, Syncora filed declarations of Erica P. Taggart with attached exhibits, primarily consisting of copies of bond-related documents. The State respondents filed objections to the declarations on April 8, 2013 and April 29, 2013, and Syncora filed a response on April 18, 2013. The Court has reviewed the declarations, the objections, and the response. The objections are overruled. The declarations and the attaehed exhibits are admitted into evidence for purposes of this proceeding.

Discussion

Syncora's Impairment of Contracts Claims:

It is important to note at the outset that Syncora has not established that the redevelopment dissolution laws effected an outright repudiation of the indebtedness of former redevelopment agencies to bondholders. Indeed, although Section 34174(a) provides, as Syncora asserts, that "[s]olely for the purposes of Section 16 of Article XVI of the California Constitution…", all agency indebtedness and interest thereon "…shall be deemed extinguished and paid…", the same statute explicitly provides that "…nothing herein is intended to absolve the successor agency of payment or other obligations due or imposed pursuant to the enforceable obligations…".

Moreover, Section 34175(a) states: "It is the intent of this part that all pledges of revenues associated with enforceable obligations of the former redevelopment agencies are to be honored. It is intended that the cessation of any redevelopment agency shall not affect either the pledge, the legal existence of that pledge, or the stream of revenues available to meet the requirements of the pledge."

Similarly, Section 34172(d) states: "Revenues equivalent to those that would have been allocated pursuant to subdivision (b) of Section 16 of Article XVI of the California Constitution shall be allocated to the Redevelopment Property Tax Trust Fund of each successor agency for making payments on the principal and interest on loans, and moneys advanced to or indebtedness incurred by the dissolved redevelopment agencies."

Instead, as discussed above, Syncora's impairment of contracts claims are based on the contentions that certain provisions of the redevelopment dissolution laws deprived bondholders (and bond insurers) of their irrevocably pledged security interest in tax increment revenues, and changed the distribution of tax increment revenues in such a manner as to increase the risk of default by the successor agencies.

In the recent case of *California Redevelopment Association v. Matosantos* (2013) 212 Cal. App. 4th 1457, the Third District Court of Appeal addressed similar claims arising out of the Legislature's enactment of AB 4X 26, which required redevelopment agencies throughout the state to contribute

portions of their property tax increment funding for the 2009-2010 and 2010-2011 fiscal years to supplemental educational revenue augmentation funds (SERAF's) to be used for financing K-12 education in redevelopment areas.

The plaintiffs, certain redevelopment agencies suing on behalf of themselves and all other California redevelopment agencies (referred to in the court's opinion as "the CRA plaintiffs"), advanced the claim that AB 4X 26 effected an unconstitutional impairment of contract and a taking of bondholders' contractual rights to tax increment funds. Their argument was virtually identical to Syncora's contentions here: that the Legislative enactment had resulted in the loss of security and an increased risk of default.

The appellate court found that the CRA plaintiffs' claims were premature. The court stated:

> The CRA Plaintiffs next point out that, as a result of Assembly Bill 4X 26, redevelopment bondholders have lost $2.05 billion in irrevocably pledged security. They argue the $2.05 billion lost through Assembly Bill 4X 26 cannot be recouped and will force agencies to borrow with no means of repayment. This claim...is premature. The CRA Plaintiffs provide no basis for assuming the loss of $2.05 billion in 2010 and 2011 will make it impossible for successor agencies to meet redevelopment obligations. It is not enough simply that money has been taken away. That takeaway must cause an inability to otherwise meet obligations in order for there to be an impairment of contract.
>
> The CRA Plaintiffs next take issue with the redefinition in Assembly Bill 4X 26 of 'existing indebtedness' from the entire amount of indebtedness owed by the redevelopment agency to merely the amount due in the current fiscal year. They argue this change ignores the multiyear nature of such obligations. However, the CRA Plaintiffs fail to explain how this will result in an impairment of contractual obligations. On this record, there is no basis for concluding such change will prevent the successor agencies from ultimately paying all redevelopment obligations. Hence, this claim too is premature.[10]

In this case, Syncora has alleged that the redevelopment dissolution laws have taken away money, in the form of tax increment funding, irrevocably pledged as security for redevelopment agency bonds, and that the redevelopment dissolution laws effectively have changed the amount of tax increment funds available as security for bondholders from the entire amount available in a given fiscal year to merely the amount due in the next ROPS period, which is used to make debt service payments rather than held as

[10] 212 Cal. App. 4th at 1493.

security. The result, Syncora alleges, is the loss of security and an increased risk of default.

Even if this is true, however, Syncora has not demonstrated, through evidence, that the takeaway of security has caused an inability on the part of successor agencies to meet their obligations to bondholders as those obligations become due, or that successor agencies will be prevented from ultimately paying all redevelopment obligations. Syncora has presented no evidence that any redevelopment agency bonds it insures are in default, or that any redevelopment agency bonds are in default at all. The Moody's Investors Service reports Syncora has offered through its request for judicial notice may demonstrate that certain analysts have concluded that the risk of default on some redevelopment agency bonds may be greater than it was, but such reports do not establish that defaults actually have occurred, or that defaults inevitably will occur.

In the absence of any evidence that successor agencies actually are unable to meet their obligations as they become due, or that successor agencies will be prevented from ultimately paying all redevelopment obligations, the Court follows the reasoning and holding of the Third District Court of Appeal in *California Redevelopment Association v. Matosantos* and concludes that Syncora's claim of impairment of contracts is premature.[11]

The Court accordingly denies Syncora any form of relief requested in the Complaint and Petition on its impairment of contracts claims, solely on the ground that those claims are premature. The judgment in this matter shall contain a provision denying such relief.

Syncora's Takings Claims:

In *California Redevelopment Association v. Matosantos, supra,* 212 Cal. App. 4th at 1949, the Third District Court of Appeal also found that the CRA Plaintiffs' takings claims were premature. The court stated: "Because we find no impairment of contract under the circumstances of this matter, we likewise dispose of the CRA Plaintiffs' takings claim, which relies on the same arguments [as their

[11] At the hearing, Syncora's counsel argued that *California Redevelopment Association v. Matosantos* was distinguishable from the present case because it involved changes to redevelopment laws that were within the contractual expectations of the bondholders and thus would not impair their contracts. The Court disagrees that the case is distinguishable on this basis. Analysis of the contractual expectations of the bondholders formed no part of the appellate court's discussion of the impairment issue, and would have been necessary only if the court had addressed the merits of the impairment issue, which it did not.

impairments claim]. Furthermore, there has been no taking of any property of the redevelopment agencies, because they never had an irrevocable right to the tax increment funds required to be paid to the SERAF's."

Based on this statement, the Court concludes that Syncora's takings claims would be premature to the extent that they are based on the same arguments and evidence as its impairment claims. At the hearing on this matter, however, Syncora's counsel argued that Syncora could present evidence that would show that the challenged provisions of the redevelopment dissolution laws have caused Syncora to suffer compensable damages and losses that already have accrued even though there have been no actual defaults on the redevelopment bonds Syncora insures.

Based on this argument, which amounts to an offer of proof, the Court concludes that Syncora's takings claims are not necessarily premature. An evidentiary hearing should be held at which the parties may present evidence on the issues raised by Syncora's taking claims as asserted in the Sixth and Seventh Causes of Action of its Complaint and Petition. Counsel for the parties are directed to meet and confer regarding the scheduling of the evidentiary hearing and file separate written status reports with the Court within seven days of the date of this ruling, which shall address the following: 1) the need for discovery; 2) the need for pre-hearing motions on evidentiary or other issues; 3) whether evidence will be submitted in the form of declarations and documentary exhibits (as in a writ of mandate hearing), or whether oral testimony and cross-examination of witnesses will be necessary; 4) the parties' estimates of the earliest date the hearing could be held; and 5) the parties' estimates of the length of the hearing. The Court may thereafter calendar a status and scheduling conference, or contact counsel regarding available dates for the hearing.

Syncora's Class Certification Issues:

Syncora's Complaint and Petition names Larry Walker, the County Auditor-Controller of San Bernardino County, both in his individual capacity and as a representative of all other County Auditor-Controllers in California under Code of Civil Procedure section 382.[12] In essence, Syncora seeks to certify

[12] See, Complaint and Petition, par. 17.

a class of County Auditor-Controllers as respondents, although no proceedings have been held regarding the certification of such a class.

On March 21, 2013, the Office of the County Counsel, County of Santa Clara, filed a letter with the Court on behalf of County of Santa Clara Auditor-Controller Vinod K. Sharma opposing the representative or class action aspect of the Complaint and Petition. On April 5, 2013, counsel for Syncora filed a letter of response stating, among other things, that the Court "...should consider class certification in due course, but need not take any action now, although Syncora stands ready to fully brief this issue at the Court's convenience". None of the parties addressed the class action aspect of this case at the May 3, 2013 hearing.

Having reviewed the above-referenced letters and the allegations of the Complaint and Petition, the Court concludes that the potential certification of a class of County Auditor-Controllers is relevant only to Syncora's impairment of contract claims. The letter submitted by Syncora's counsel makes it clear that Syncora named the class of County Auditor-Controllers as respondents because those officials perform the ministerial function of distributing tax revenues that have been pledged by a redevelopment agency to secure bonded indebtedness, and Syncora wanted to insure that all of them would be immediately required to follow the Court's decision on the ultimate question of the constitutionality of the challenged laws. It is only Syncora's impairment of contracts claims that implicate the duties of the County Auditor-Controllers, because only those claims seek to declare the so-called Redistribution Provisions invalid.

Syncora's takings claims, on the other hand, assert causes of action for damages as compensation for the alleged unconstitutional takings. The County Auditor-Controllers have no role or duty in connection with the alleged takings or in providing compensation for those takings. The Court therefore concludes that its ruling denying relief on Syncora's impairment of contract claims as premature renders any class certification issues moot, and makes no ruling on the certification of a class of County Auditor-Controllers in this case.

Conclusion

The Court denies relief on Syncora's claims that the challenged provisions of the redevelopment dissolution laws unconstitutionally impaired its contracts on the ground that those claims are premature, following the reasoning and the holding of the Third District Court of Appeal in *California Redevelopment Association v. Matosantos, supra,* 212 Cal. App. 4th 1457, 1494. The Court concludes that Syncora's takings claims are not necessarily premature, and that an evidentiary hearing should be conducted to address such claims. Finally, the Court concludes that the possible certification of a class of County Auditor-Controllers is now moot.

DATED: May 29, 2013

MICHAEL KENNY

Judge MICHAEL P. KENNY
Superior Court of California,
County of Sacramento

CERTIFICATE OF SERVICE BY MAILING
(C.C.P. Sec. 1013a(4))

I, the undersigned deputy clerk of the Superior Court of California, County of Sacramento, do declare under penalty of perjury that I did this date place a copy of the above-entitled **RULING ON SUBMITTED MATTER** in envelopes addressed to each of the parties, or their counsel of record as stated below, with sufficient postage affixed thereto and deposited the same in the United States Post Office at 720 9th Street, Sacramento, California.

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Superior Court of California,
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Dated: May 29, 2013

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