

## OREGONS CERTIFICATES OF PARTICIPATION (COP's)

**QUESTION -- Is a Certificate of Participation (COP) in truth a long term obligation that has been crafted to look like a short term (aka two-year) obligation to avoid violating the constitutional debt limit of \$50,000 without a vote of the people?**

**ANSWER -- Effectively, yes. COP's have been used to circumvent the Constitution's limit on borrowing.**

A COP is a form of revenue borrowing in which the obligation is secured by the real or personal property financed and payable from available funds, which is a defined term. For purposes of state-issued COPs, ORS 283.085 defines "available funds" to include "funds appropriated or otherwise made available by the Legislative Assembly to pay amounts due under a financing agreement for the fiscal period in which the payments are due." So, each Legislative Assembly must decide whether to appropriate funds in each biennium in which COP payments become due.

The Oregon Supreme Court found COPs to be constitutional in *State ex rel Kane v. Goldschmidt*, 308 Or. 573, 583 (1989).

### DISCUSSION

Generally, public borrowing can be parsed into two broad categories. General obligation borrowing is a full faith and credit obligation for which the unlimited taxing power of government is pledged to secure payment. If existing funds are insufficient to pay the obligation, the lender can compel the government through legal process to levy additional taxes sufficient to pay the obligation. Revenue-based borrowing is an obligation for which only specific revenue, income or property is pledged to secure payment. If the pledged revenue, income or property is insufficient to pay the obligation, the lender has no other legal recourse to compel the government to pay the obligation.

COP's are an out-growth of ORS 271.390.

Historically, ORS 271.390 was a narrow authorization for cities and counties to lease, rent or purchase real property. Through the amendment process, beginning in 1995, the authority to finance real property has grown far beyond its original scope. What began as a modest alternative for cities and counties to supplement the issuance of bonds in the specific instance of taking a leasehold on real property has grown to become authority for public bodies to issue certificates of participation as a substantial alternative to the issuance of bonds for the purpose of contracting to make payments for real or personal property.

ORS 271.390 and 283.085 to 283.092 authorize a public body to enter into “contracts for the leasing, rental or financing of any real or personal property” and the contracts may provide for the “issuance of certificates of participation in the payment obligations of the public body.” To secure the payment obligations, a public body may grant a security interest in the leased, rented, purchased or financed property and may pledge all or a portion of the lawfully “available funds” of the public body.<sup>11</sup> Certificates of participation are not full faith and credit obligations. For purposes of state issued certificates of participation, “available funds” means “funds appropriated or otherwise made available by the Legislative Assembly to pay amounts due under a financing agreement for the fiscal period in which the payments are due, together with any unexpended proceeds of the financing agreement, and any reserves or other amounts which have been deposited in trust to pay amounts due under the financing agreement.”

In *State ex rel Kane v. Goldschmidt*, 308 Or. 573, 583 (1989), the Oregon Supreme Court considered the use of COPs as a financing tool and found them to be constitutional. The Supreme Court in *Kane* concluded: “The drafters of the constitution intended that the state pay as it goes. An unconditional promise to pay is invalid if payment is to be made, in whole or in part, from future appropriations out of the general tax fund.”

The decision in *Kane* reflects an evolution in the jurisprudence concerning public debt. One of the earliest decisions defining the term “debt or liabilities” is *Salem Water Co. v. City of Salem*, in which the Oregon Supreme Court stated: “The words ‘any debt or liabilities,’ . . . are general and may include any kind of debt or liability, either absolute or contingent, express or implied.”<sup>4</sup> However, in *Kane*, the Supreme Court stated:

Over the last century, as public bodies have devised various methods of avoiding constitutional or charter prohibitions, the definition of “debt or liabilities” has gained precision beyond that stated in *Salem Water Co.* This court has looked at not less than two basic characteristics in deciding whether action violates [a constitutional debt limit]: (1) the fund from which payments on the obligation are made; and (2) the degree to which the public body is liable for repayment of the loan.

If the revenues generated from a particular project being financed are pledged for repayment, rather than revenues from general taxation, no “debt” or “indebtedness” is thereby created. Often referred to as the “special fund” cases, this line of decisions upholds the plan if the promise by the state is to make installment payments only from a “special [revenue] fund.” Such a promise does not create a “debt” or “liabilities,” within the meaning of Article XI, section 7, because general tax revenues have not been pledged.

A second line of cases classifies debt based on the degree to which the public body is liable for

the repayment of the obligation. *Rorick v. Dalles City*, 140 Or. 342, 12 P.2d 762 (1932), involved the issuance and sale of Columbia River bridge bonds by Dalles City. The authorizing statute contained a debt limitation provision similar to Article XI, section 7. Although principal on the bonds was payable only from the tolls and revenues of the bridge, the city was absolutely liable for the interest on future installments if the “special fund” was insufficient to meet the obligation. (Citations omitted.)<sup>5</sup>

The court in *Kane* found in regard to COPs:

**[A] future legislature is bound only by its collective conscience. .... if the legislature makes an unenforceable promise to replenish the source from which repayments are made, "it is at most based upon a moral obligation which the members of future legislatures might feel to meet the deficiency. We do not interpret Article XI, section 7, as prohibiting such a moral and therefore unenforceable pledge." Nor does the fact that the legislature may feel compelled to make payments in a future biennium out of the fiscal concern to protect its credit rating convert the state's "obligation" into a legal one subject to Article XI. The economic and fiscal consequences of either continuing the agreements or allowing them to terminate by failing to appropriate money merely becomes a factor in the public policy calculus of a political system that automatically "subjects the economic wisdom of such projects to [biennial] review by future taxpayers and their elected representatives." .... These consequences are of no constitutional significance.**