

An Introduction to Judgment Obligation Bonds in California

Financing Tort and Other Involuntary Obligations

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About the Author

Donald S. Field is a Public Finance Partner at Orrick, Herrington & Sutcliffe LLP who has been in the forefront of establishing judgment obligation bond financing solutions for California school districts, cities and counties facing large tort liability obligations resulting from the application of California Assembly Bill Number 218 (Chapter 861, Statutes of 2019) ("AB 218") to claims arising out of childhood sexual assault. These efforts have included working with several local governments on AB 218 judgment obligation bond programs. The programs have included single bond issuances for local governments with a few AB 218 cases that have settled contemporaneously. They have also involved multiple step programs involving interim and long-term financing mechanisms where multiple bond issuances are anticipated over several years due to the substantial number of cases and timing differences. Mr. Field also has assisted the Fiscal Crisis & Management Assistance Team (FCMAT) in developing legislative proposals to make such financing solutions more assessable to local governments. Such proposals were included in FCMAT's report to the Legislature, dated January 31, 2025, entitled *Childhood Sexual Assault: Fiscal Implications for California Public Agencies*.

Members of Orrick's Judgment Obligation Bond Group are shown on the contact list contained in Appendix C to this booklet.

DISCLAIMER: Nothing in this booklet should be construed or relied upon as legal advice. Instead, this booklet is intended to serve as an introduction to the general subject of the use of judgment obligation bonds, from which better informed requests for advice, legal and financial, can be formulated.

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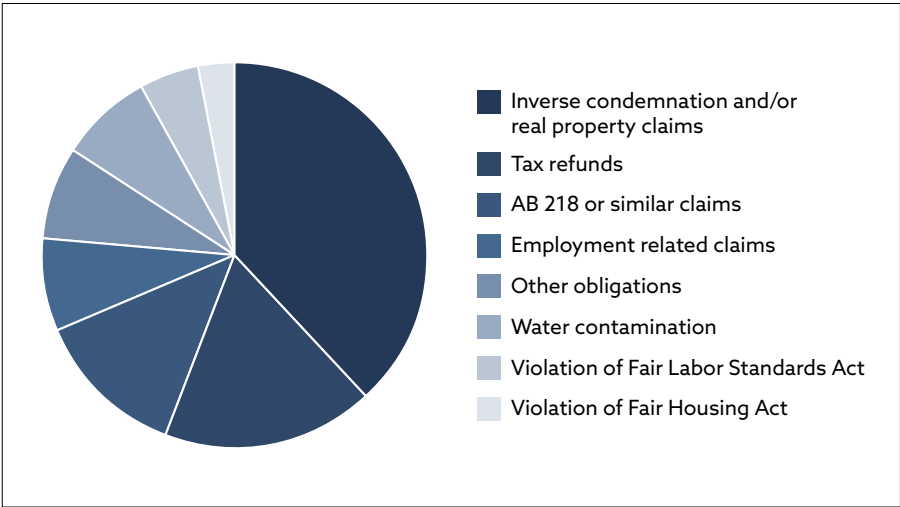
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CHAPTER 1

Introduction

Judgment obligation bonds (“JOBs”) are bonds issued by a state or local government to pay involuntary liabilities arising out of tort or otherwise imposed by law. Presently, JOBs are actively being discussed in the media and issued by local governments as a way to finance and amortize tort liabilities resulting from the application of California Assembly Bill Number 218 (Chapter 861, Statutes of 2019) (*i.e.*, “AB 218”) to claims arising out of childhood sexual assault. The passage of AB 218 has resulted in a flood of litigation against local governments across California and many of them are turning to JOBs to lessen the resulting financial impacts on programs and services. Thus, JOBs have been an increasingly popular and successful way for local governments to mitigate the financial impacts of large tort liabilities.

NATURE OF INVOLUNTARY OBLIGATIONS, 1992-2025



Source: California Debt and Investment Advisory Commission and emma.msrb.org

Historically, JOBs have been issued to finance many types of involuntary obligations, including monetary obligations arising out of inverse condemnation and real property related actions, water contamination claims, federal Fair Housing Act violations, dangerous conditions of public property, various tax refund obligations and wrongful discharge actions. Regardless of the type of

involuntary liability, JOBs give local governments a tool to mitigate the financial impacts of involuntary liabilities. The policy decision for a local government's governing board is whether to finance any such obligations over a term of years or to pay them from funds on hand in a single year, focusing on the impact that any sizable monetary judgment or judgments would have on current programs and services.

The purpose of this booklet is to introduce interested parties to the reasons why JOBs are issued, advantages/disadvantages, structure choices, federal tax issues, and representative programs where JOBs have been used in mass tort situations. For convenience, reference to judgments is made throughout this booklet. However, in most cases, and with some nuances to legal theories, involuntary monetary obligations under settlement agreements should have equal application.

With few exceptions, each year for many years Orrick has been involved as bond counsel in more financings by principal amount than any other law firm in the country. Moreover, Orrick has been ranked number one in total volume as disclosure counsel both nationally and in California nearly every year since such rankings began. In an average year, Orrick handles more than 700 bond issues, aggregating more than \$78.7 billion. Since 1992, Orrick has served as bond counsel to local governments on 50 percent of the judgment obligation financings in California. See Appendix A for detailed JOB and similar debt issuance data.

CHAPTER 2

Why Issue JOBs?

Absent a finding of unreasonable hardship (which may permit a limited installment period for payment of the obligation plus interest), monetary judgments against local governments in California generally are payable in full upon the conclusion of litigation. When tort claims or other involuntary obligations such as AB 218 claims, inverse condemnation claims, and the like, result in large liabilities, payment of such obligations in full upon conclusion of the related litigation may result in significant, negative impacts to a local government's budgetary resources and, therefore, to public programs and services. Such impacts can be mitigated and managed by refunding such obligations through a JOB issuance and amortizing the liability over time. As indicated in Chapter 1, the policy decision for a local government's governing board is whether to finance any monetary judgments over a term of years or to pay them from funds on hand in a single year, focusing on the impact that any sizable monetary judgment or judgments would have on current programs and services.

California courts consistently defer to the judgment of the governing body of a public agency with respect to the determination that a particular action is necessary to the full discharge of its duties. California courts also have recognized the considerable discretion possessed by a local government in the exercise of its powers with respect to its budget, meaning that the policy decision is in the hands of the local government's governing board.

Of course, there are other ways to not pay tort and other involuntary obligations immediately after the relevant judgment is entered. Parties to litigation may settle tort claims and structure an agreement to make monetary payments over time. Moreover, California Government Code section 970.6 currently allows a court to order the payment of a judgment over 10 equal annual installments with interest upon a finding of unreasonable hardship on a local government. However, such terms may provide insufficient financial relief and may be less economical than the local government agreeing to a lump sum payment and refunding and amortizing the liability over time through a financing. Other assistance, like state emergency loans, may be available to some local governments facing large involuntary liabilities.

In some circumstances, a local government also may want to consider whether filing for bankruptcy protection is possible and appropriate. The local government should consider all available options when deciding whether JOBs are appropriate. Expert advice should be sought to ensure all options are understood.

While taking the extraordinary step of filing for bankruptcy protection may in some circumstances make sense, the considerations are highly complex and are beyond the scope of this booklet. Please refer to the Orrick booklet entitled [*Municipal Bankruptcy: Avoiding and Using Chapter 9 in Times of Fiscal Stress*](#). Included as Appendix C is a list of Orrick lawyers, including municipal bankruptcy lawyers, experienced in the decisions local governments must make when considering the issuance of JOBs and other alternatives.

The interplay of various disclosure obligations and annual audit considerations with involuntary liability claims, including the recognition of probable liabilities for accounting purposes under Governmental Accounting Standards Board Statement Nos. 10 and 56, also is beyond the scope of this booklet. However, it is important for local governments to discuss these issues with disclosure counsel and their independent auditor to ensure disclosure obligations are met.

CHAPTER 3

JOB Basics

A. GENERAL

JOBs typically are structured as unsecured obligations payable from the general fund of the issuer. They are not full faith and credit general obligation bonds backed by the issuer's taxing power because the California Constitution's debt limitation requires that type of bonds issued by the State, cities, counties or school districts ("Debt Limit Entities") be approved by two-thirds of the electorate.

Instead, California JOBs issued by Debt Limit Entities generally have been designed to be valid without voter approval under a judicially created exception to the Constitutional debt limitation, which exception generally is referred to as "obligations imposed by law." See discussion in Sections B and C below. Because this exception to the Constitutional debt limitation was and is much less developed in the case law, with few cases directly on point, than the other two principally employed exceptions (for lease financings and for special fund/enterprise revenue bonds), each JOB issue by Debt Limit Entities in California has been validated pursuant to California's validation statute (Code of Civil Procedure §§860 *et seq.*). See discussion in Section E below.

JOBs are considered to have the same legal character as the judgment obligations they refund (*i.e.*, refinance). Accordingly, upon their issuance and refunding of the underlying tort or other involuntary obligation, JOBs are obligations imposed by law and, therefore, are absolute and unconditional obligations, without any right of set-off or counterclaim.

Bonds issued by Debt Limit Entities as obligations imposed by law generally cannot include reserves or capitalized interest because those components of the obligation are not considered to be imposed by law, even on the theory they are essential to marketing the bonds. On the other hand, costs of issuance may be included. The inability to include capitalized interest means that it may be difficult to achieve complete budget relief in the initial period following issuance of the bonds without resort to capital appreciation bonds ("CABs"). See discussion of structure options in Chapter 5B. Some issuers may be able to enter into a lease financing to fund tort or other obligations imposed by

law as an alternative to JOBs (see Chapter 5C), which can include reserves and capitalized interest.

Entities other than Debt Limit Entities, meaning authorities, agencies and districts of various kinds (other than school districts and community college districts), because they are not subject to the Constitutional debt limitation, need not rely on “obligations imposed by law theory” and can simply use the California local agency refunding law as authority for the issuance of JOBs, without a validation action. See discussion in Section D below.

B. CONSTITUTIONAL DEBT LIMIT

The California Constitution, like many state constitutions, restricts the power of local government entities to incur certain debts without the approval of the electorate. Article XVI, section 18 of the California Constitution provides, in pertinent part, that “[n]o 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, voting at an election to be held for that purpose.” In other words, the California Constitution prohibits Debt Limit Entities from entering long-term debt obligations without a vote of the electorate. As described in Section C, though, the courts have recognized a few exceptions to the Constitutional debt limitation and have ruled that debts incurred to satisfy an obligation imposed by law do not violate Article XVI, section 18 of the California Constitution.

C. OBLIGATIONS IMPOSED BY LAW

In particular, the California Supreme Court has recognized that a local government’s liability for involuntary tort claims are obligations of the government imposed by law. The seminal case on this point is *City of Long Beach v. Lisenby*, 180 Cal. 52 (1919), in which the Court held that a predecessor to Article XVI, section 18, *formerly* Article XI, section 18, could “not defeat the asserted right of the city of Long Beach to provide for the payment” of a tort judgment “without regard to the state of its revenues for the year in which such liability arose, and without a vote of the people of said city.” The Court reasoned that the Constitutional debt limitations were confined “to those forms of indebtedness and liability which may have been created by the voluntary action of the officials in charge of the affairs of such city and to have no application to cases of indebtedness or liability imposed by law or arising out of tort.”

Furthermore, the California Supreme Court has concluded that the issuance of bonds to refund obligations imposed by law does not create a liability that is new or different from an already-existing obligation imposed by law. The bonds are only an evidence of the indebtedness and a mere change in the form of the evidence of indebtedness is not the creation of a new indebtedness within the meaning of the Constitution. Accordingly, the issuance of bonds to refund an obligation imposed by law does not violate Article XVI, section 18.

D. CALIFORNIA LOCAL AGENCY REFUNDING LAW

Under the California local agency refunding law (Articles 10 and 11 (commencing with section 53570) of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code), local governments, including school districts, cities and counties, are authorized to issue refunding notes or bonds for the purpose of refunding any evidence of indebtedness of the local government. Therefore, local governments have the power to authorize and issue refunding notes and bonds to satisfy their financial obligations under involuntary tort judgments or other obligations imposed by law. These notes or bonds typically are referred to as judgment obligation notes or bonds.

E. NEED FOR JUDICIAL VALIDATION

Section 860, *et seq.*, of the California Code of Civil Procedure provides a procedure for establishing the validity of notes and bonds and related financing contracts. In certain circumstances, this procedure is necessary to enable notes or bonds to be sold with the level of certainty regarding the validity of the notes or bonds required by the municipal bond market. Because the “obligation imposed by law” exception is much less developed in the case law than other judicially created exceptions, each JOB issue by Debt Limit Entities in California has been validated pursuant to the section 860 *et seq.* procedure.

What is validated in such validation actions is not legal principles, but the bonds and the other principal legal documents approved in a bond resolution. Before the validation action is filed, it is necessary for the local government to first adopt the resolution and authorize the bonds, the principal legal documents, and the initiation of the validation action. The validation action is in the form of a civil complaint for validation filed in the superior court of the county in which the issuer is located, and an order for publication of summons is received. Summons can then be published (usually in a newspaper of general circulation in the city or county in which the issuer is located), which takes a minimum of

21 days. If there is no answer to the complaint filed by the date specified in the summons, which must be at least 10 days after completion of publication, the clerk can enter a default and schedule a hearing before the judge for the default judgment. The timing will depend on the jurisdiction, and may be a day or two or, in some jurisdictions, at least 15 days after the clerk enters the default.

As indicated in the sample validation timeline included in Appendix B, assuming the best case, obtaining a validation judgment takes a minimum of 55 to 65 days (depending on the jurisdiction) after filing the validation complaint. While the validation statute provides that the action is entitled to trial preference over all other civil actions so that the matter may be “speedily” determined, the action is entirely subject to the calendar and assignments of the courthouse, applicable court rules, the judge, and the court clerk. For example, it sometimes takes a week or more to get an order for publication of summons, or longer than 15 days after the clerk enters a default to schedule the hearing. In addition, the judge could take the matter under submission for an indefinite amount of time, or disagree with the proposed default judgment, and decline to validate the transaction. Once granted, the default judgment may be appealed within 30 days, but only on jurisdictional grounds. Therefore, the typical assumption is that the validation action will take approximately 75 to 80 days (not including the appeal period). Usually, JOBs are not sold or issued until after the appeal period has expired.

If someone does answer the complaint, there is true two-party litigation on the merits. While some expedited procedures are available, the timing for resolution of the litigation cannot be predicted and may take many months to proceed through discovery, motion practice, and dismissal or settlement of the answer and its objections. In addition to a dismissal, with or without prejudice to refile, abandonment of the action for validation is a possibility on these facts.

Validation actions can validate not only the JOBs to be issued but also future JOBs, if necessary or desired, or refunding JOBs. See Chapter 7 for a discussion of mass tort situations. Not all validation actions are as inclusive or as flexible as they could be (some leaving out future JOBs or costs of issuance or locking in semiannual interest payment dates, etc.), and must be carefully reviewed before relied on for future JOBs or refunding JOBs. Expert advice should be sought to ensure consideration of the feasible options.

CHAPTER 4

Possible Disadvantages of JOBs

A. TIMING ISSUES

The California local agency refunding law allows local governments to issue bonds for the purpose of refunding “bonds, warrants, notes, or other evidence of indebtedness” of the local government (payable from funds other than the proceeds of *ad valorem* taxes or the proceeds of assessments levied without limitation as to rate or amount by the local agency upon property in the local agency). In short, a local government, including a school district, city, or county, may issue notes or bonds under the California local agency refunding law to refund indebtedness. This prohibits (i) a reimbursement financing (*i.e.*, prohibits a local government from issuing JOBs to refinance a judgment the local government has previously paid as no indebtedness exists to refund after it is paid), and (ii) a local government from issuing JOBs prior to a judgment being entered against the local government.

If the Debt Limit Entity desires to finance a judgment, it generally must anticipate and incorporate the timing necessary to complete a validation proceeding and market and sell JOBs into any scheduled payment of the judgment. The local government should discuss timing and strategy with bond counsel experienced with JOBs and validation actions promptly when litigation has been threatened or filed such that payment of claims is being considered, would require any express payment commitment, and particularly where substantial liability may result. The local government’s litigation counsel should also participate in these discussions to ensure there are no missteps in timing. As indicated above, a typical, uncontested section 860 *et seq.* validation proceeding could take 75 to 80 days (sometimes more) to complete (not including the 30-day appeal period). See Chapter 3E for discussion of section 860 *et seq.* validation proceedings and Appendix B for a sample validation timeline.

B. BARGAINING POSITION

In some instances, the issuance of JOBs to finance monetary judgments over a period of years will be an invaluable fiscal tool for local governments. For example, plaintiffs/claimants and their counsel likely want to be paid immediately rather than over time in installments, regardless of whether such installments are pursuant to a settlement agreement or required under California Government Code section 970.6 hardship provisions. Agreeing to a lump sum payment and refunding and amortizing the liability over time through a financing can be beneficial for all parties because plaintiffs/claimants may be willing to accept a smaller amount in return for the prompt payment. However, the availability of JOBs may be seen by some plaintiffs/claimants and their counsel as an additional source of funds to increase settlement offers rather than a fiscal tool for local governments to manage the impacts of large monetary obligations. Because JOBs as a source of funding for tort claims and other involuntary obligations have been widely discussed recently in the news media, local governments should expect the option to be known and understood when negotiating settlements.

C. TAX-EXEMPT JOBS HAVE ONGOING COMPLIANCE OBLIGATIONS THAT TAXABLE JOBS DO NOT

Both tax-exempt and taxable JOBs have been issued. In July 2016, final Treasury Regulations were released governing long-term tax-exempt JOBs, including clarification of the existing rules and adding a post-issuance ongoing compliance scheme that requires an issuer to review its annual available funds. Tax rules also limit the amount of tax-exempt JOBs that may be issued, factoring in any reasonable reserves for the liability. See Chapter 6 for a discussion of when JOBs may be issued as tax-exempt. Consequently, some issuers may choose to issue taxable JOBs even if they are eligible to issue those obligations on a tax-exempt basis.

On the other hand, taxable JOBs with fixed interest rates generally are sold as noncallable bonds or with “make-whole” calls. Adding a redemption feature will ordinarily result in a materially higher interest rate cost than the same redemption feature in tax-exempt bonds. Therefore, taxable noncallable bonds may be expensive to refund or defease, although there have been a number of successful tender offer refundings of similar taxable bonds (that is, a tender offer was made for the prior bonds and the tender price was paid with proceeds of new refunding bonds). Another way to address this concern is by

using variable rate bonds, which may contain redemption provisions without additional interest rate cost, and may be accompanied by a floating-to-fixed interest rate swap if a fixed rate obligation is desired. See Chapter 5B for a discussion of variable rate JOBs.

CHAPTER 5

JOB Structures and Other Matters

Once it is determined that the issuance of JOBs is appropriate, the local government will need to decide how and to whom the JOBs will be sold and how the JOBs will be structured.

A. HOW AND TO WHOM WILL THE JOBS BE SOLD?

The two basic methods of sale for local government debt are negotiated sale and competitive sale. The two types of sales involve different processes, players and roles, and present different sets of advantages and disadvantages. The best choice for a given debt offering depends upon the facts and circumstances of the financing and the importance placed by the local government on the different inherent attributes of the choices.

Local governments also are constrained by debt management policies, some of which may require consideration and/or amendment to provide for the issuance of JOBs or consideration of a judgment obligation refunding program as described herein.

1. NEGOTIATED SALE

In a negotiated sale, the local government selects an underwriter to underwrite the bonds (by purchasing the bonds from the local government for resale to investors) on terms to be negotiated between the local government and the underwriter. The local government works with the underwriter, bond counsel and its municipal advisor to structure the transaction. The local government enters into a purchase contract with the underwriter providing for the purchase of the bonds by the underwriter from the local government on agreed terms and conditions. Having the underwriter as an integral part of the structuring process in a negotiated sale may allow the bond structure to be better tailored to what the underwriter perceives as the demands of the marketplace.

Negotiated sales allow the underwriter to work with potential investors before the actual offering date of the bonds to provide information and otherwise

generate interest in the issue. If the JOBs are financing socially sensitive obligations, as with AB 218, there might be a need to generate investor interest and seek additional advice on disclosure and debt profile.

A negotiated sale also allows flexibility to make last minute adjustments to debt structure or sale timing, allowing the local government to respond to investor needs and market fluctuations. Flexibility is of particular value for unusual borrowings, volatile markets or financings involving a number of independent variables.

2. COMPETITIVE SALE

In a competitive sale, the local government works with its municipal advisor and bond counsel to structure the transaction. A notice of sale is published inviting bids for the bonds to participating municipal bond broker-dealers specifying the terms of the offering and detailing the basis for the award of the bonds (generally the lowest “true interest cost”). The bonds are sold to the winning bidder. The winning bidder underwrites the bonds by purchasing the issue from the local government and reselling them to investors but does not play an active role in structuring the transaction. A competitive sale results in a competitive pricing of the bonds – the best bid (in terms of lowest debt service cost to the local government) wins the bonds.

3. BANK DIRECT PURCHASE

One variation on the foregoing is a “bank direct purchase,” in which bonds are sold by the local government directly to a bank. Depending on market conditions, banks may offer more favorable interest rates than what is available in the public market. Moreover, a bank direct purchase, which would not involve disclosure in a public offering, may offer a local government a less public sale of socially sensitive obligations. Banks, however, traditionally offer shorter maturity dates than those obtainable in the public market – typically under 20 years. Moreover, it may be difficult to find a bank willing to purchase large sized bonds. When issuing JOBs, a local government should seek advice on whether its bond terms and size would be of interest to a bank. Please refer to the Orrick booklet entitled [*Tax-Exempt Lending to Governments and Nonprofits; Bank Loans and Direct Purchases of Municipal Securities*](#) for more information regarding bank direct purchases.

B. STRUCTURES

Because JOBs are typically payable directly from the general fund of the local governmental issuer, the structure of the bond issue is usually simple and straightforward, varying primarily in interest rate mode, using one or a combination of the following:

1. FIXED RATE BONDS

Most JOBs are issued as fixed rate bonds. The advantages are the same as fixed rate bonds generally; namely, they lock in interest cost, and with interest rates at relative historic lows, this is an attractive prospect in itself. A disadvantage is that if the JOBs are issued as taxable, most fixed rate taxable bonds are sold as noncallable or with “make-whole” calls, so they cannot be easily refunded or defeased if rates drop or circumstances change. See Chapter 6 for a discussion of tax issues related to JOBs.

2. VARIABLE RATE DEMAND BONDS

Variable rate demand bonds are bonds bearing interest at variable rates, subject to reset over time, the holders of which may tender them back to the issuer or its agent upon short notice (usually seven days, but may be one day, one month or other periods), for a purchase price equal to par plus accrued interest. As a result, they bear interest at rates like, and have some other characteristics of, short term obligations. Variable rate demand bonds generally require a bank letter of credit, standby purchase agreement or other facility to assure liquidity in the event bonds are tendered and cannot be remarketed. Unless the issuer is highly rated, variable rate demand bonds are typically also credit enhanced with either bond insurance or a bank letter of credit or other credit facility. The advantages of variable rate demand JOBs are that (a) their interest rates generally are lower than fixed rate bonds, and (b) they usually are subject to redemption at any time without premium and at no extra interest rate cost for the right to redeem. However, while the interest rate usually starts out lower than fixed rate bonds, the rate is variable and subjects the issuer to interest rate exposure. Interest rates may be affected not only by market conditions but also by the financial condition of the issuer or the credit provider or liquidity provider. In addition, there are risks, costs and aggravation associated with renewal of any bank liquidity or credit facilities, which usually have a term of one to five years, compared to JOBs which typically have a term of 10 to 15 years. By separate agreement, the interest rate on variable rate bonds may be swapped to fixed rates but

the use of swap agreements comes with additional risks to issuers. See swap discussion in Section B5 below.

3. INDEXED BONDS

Indexed bonds are variable rate bonds that are not subject to tender back to the issuer and, therefore, do not require a bank liquidity facility, and bear interest at a fixed spread over a market index (currently either the SOFR Index or the SIFMA Index) reset at the end of each accrual period. The SOFR Index refers to the Secured Overnight Financing Rate Index and is published daily by various news and information services. The SIFMA Index refers to the SIFMA Municipal Swap Index, which is a weekly, high-grade market index comprised of tax-exempt variable rate demand obligations published by Securities Industry and Financial Markets Association. Index rate bond documents may refer to one or both benchmark rates.

Index bonds may be subject to redemption without penalty. However, like variable rate bonds, there is no assurance that indexed rates will not increase to exceed the fixed rate at which the JOBs could have been originally issued. Unlike variable rate bonds, indexed bonds are not affected by events affecting the JOBs issuer or the JOBs (although the spread over the index will be impacted by these). By separate agreement, the interest rate on index bonds also may be swapped to fixed rates but the use of swap agreements comes with additional risks to issuers. See swap discussion in Section B5 below.

4. CAPITAL APPRECIATION BONDS

Capital appreciation bonds (CABs) are bonds that bear no current interest, which instead is accrued, compounded (usually semiannually) and paid at the maturity of the bonds. They are used primarily to reduce debt service in the early years. A variation is convertible CABs, that function as CABs for several years and then convert on a certain date to current interest bonds (with interest paid on the then accrued value of the bonds, being the original principal amount plus the amount of accrued, compounded interest up to the conversion date). The disadvantage of CABs is that higher rates of interest are required to market them.

5. SWAPS

If variable rate or index bonds are used, the resulting interest rate exposure may be swapped to a fixed rate, in whole or in part, using a floating-to-fixed

interest rate swap. While swaps are often considered to make financial sense in this context, they are complex financial investments and beyond the scope of this booklet. Please refer to Orrick's booklet entitled [Interest Rate Swaps: Application to Tax-Exempt Financing](#) (much of which is applicable even though JOBs might be issued as taxable) for more information about swaps and to inform a conversation with a municipal advisor. It is important to make sure that if a swap is to be used, it is consistent with the issuer's objectives and does not itself expose the issuer to risks or consequences the issuer does not fully understand. For example, if the purpose of using variable rate JOBs is to allow for refunding or early redemption if rates drop or other circumstances change, the termination payment that may be due on early termination of the swap may offset the benefit of and effectively prevent refunding or redemption. There also are other circumstances in which a substantial termination payment may be due from a local government, such as default of the swap provider or downrating of either party, as well as other terms that can be modified to suit the state or local government's objectives. Expert advice should be sought before entering into any swap.

As discussed in Chapter 3E, not all validation actions are as inclusive or as flexible as they could be. Moreover, what is validated in validation actions is not legal principles, but the bonds and the other principal legal documents approved in a bond resolution. If a local government desires flexibility, the validated bond documents may include alternative interest rate modes and other features. Expert advice should be sought to ensure consideration of the feasible options.

C. ALTERNATIVES TO JOBS

To finance their tort or other involuntary obligations, some local governments may choose to pursue a lease financing, which would not require a section 860 *et seq.* validation proceeding. The structure avoids the delay of the validation proceeding and potential legal challenges to the financing that may result from such a proceeding. Moreover, the timing issues under the California local agency refunding law relating to refunding indebtedness do not apply to a lease financing, which may add flexibility to the financing. On the other hand, lease financing requires a leased asset. Utilizing a lease option, therefore, ties up local government assets that could otherwise be available for future capital financings. Thus, each local government would need to compare the advantages and disadvantages of

a lease financing when deciding to pursue a financing of involuntary liabilities arising out of tort or otherwise imposed by law.

Note that current California law prohibits school districts from using the proceeds of a lease financing for general operating purposes, which would generally prohibit school districts from lease financing tort liabilities and other similar involuntary obligations. Moreover, some debt management policies and some city charters may similarly restrict utilization of lease financing.

CHAPTER 6

Tax Issues

In most situations, tax-exempt bonds are used to finance capital costs. The use of tax-exempt proceeds to pay judgments or legal liabilities generally is viewed as financing a working capital expenditure, instead of a capital one. There are limited situations where tax-exempt bonds may be issued for working capital purposes.

Issuers may be familiar with using tax-exempt short-term borrowings, such as tax and revenue anticipation notes ("TRANs") or tax anticipation notes ("TANs"), to finance current operating expenses on a short-term (that is, current year) basis. Such use is premised on the issuer experiencing a cash deficit or shortfall in the current year's operations. The tax focus is on the issuer's reasonable expectations as to the deficit, based on the funds the tax law treats as "available," in order to determine the size of the issuance.

A subset of working capital expenditures that may be financed with tax-exempt JOBs is an 'extraordinary' item. An 'extraordinary' working capital expenditure is an expenditure that is non-recurring and not customarily payable from current revenues. The Treasury Regulations list, as an example of such expenditure, an extraordinary legal judgment in excess of reasonable insurance coverage or applicable reserves.

Financing an extraordinary working capital item does not require an issuer to expect a deficit in its available amounts, only that the issuance amount is not already covered by applicable insurance or reserves. The term of this type of tax-exempt JOBs often spans multiple years, that is, long-term. The tax focus becomes how long the term may be to avoid leaving the bonds outstanding too long and creating replacement proceeds. In that regard, final Treasury Regulations were released on July 18, 2016, setting out a post-issuance compliance scheme to neutralize the burden that this type of debt places on the tax-exempt market.

After issuance, an issuer of long-term tax-exempt JOBs, generally, must undertake a review of available, unrestricted cash on an annual basis. The amount of available cash above a "working capital reserve" on each annual testing date is considered replacement proceeds of an issue that are burdening the tax-exempt market.

The amount of the working capital reserve is five percent of the issuer's working capital expenditures and capital expenditures paid from current revenues in the year prior to the testing date. Upon such annual review, any excess above the working capital reserve must be invested in specific investments, either eligible tax-exempt bonds or Demand Deposit U.S. Treasury State and Local Government Series ("SLGs") or used to redeem tax-exempt working capital bonds.

The final Regulations released in 2016, by generally requiring an issuer to review and address, on an annual basis, any available amounts, provided more certainty about the term of long-term JOBs. Some issuers find compliance onerous and less flexible than prior to the rule issuance. However, in unique circumstances, as demonstrated in a private ruling, an issuer may be exempt from the post-issuance compliance scheme.

CHAPTER 7

Mass Tort Situations

Historically, JOB validation actions have involved underlying tort or other actions that have already reached judgment. Thus, a local government typically would issue bonds to refund a single judgment or a handful of judgments on an as-needed basis following the completion of a section 860 *et seq.* validation proceeding. However, given the sheer number of lawsuits and the magnitude of potential aggregate involuntary tort liability against some local governments in certain mass tort situations, like the thousands of claims filed against local governments after the enactment of AB 218, the process of issuing bonds following judicial validation thereof on a case-by-case, piecemeal basis would be costly in terms of time and monetary costs and significantly burden judicial resources.

Case Study – AB 218

AB 218 impacts local government liability exposure because it extended the statute of limitations periods and revived certain claims for which applicable statute of limitations periods had otherwise expired for claims of childhood sexual assault.

Extension of Statute of Limitations – Pursuant to AB 218, a plaintiff now has 22 years from the age of majority (*i.e.*, 40 years of age) instead of the previous eight years (*i.e.*, 26 years of age) or five years after the plaintiff discovered or reasonably should have discovered psychological injury or illness occurring after the age of majority caused by the alleged childhood sexual assault to bring an action, with certain actions being barred from commencement after the plaintiff's 40th birthday.

Revival of Certain Claims – AB 218 also revived certain claims for which applicable statute of limitations periods had otherwise already expired if brought within three years of January 1, 2020.

Financial Impact of AB 218 – With the enactment of AB 218 and, in particular, the revival window provisions thereof, thousands of claims against local governments, some alleging claims dating back to the 1940s, have been filed. In its report to the California Legislature, dated January 31, 2025, entitled *Childhood Sexual Assault: Fiscal Implications for California Public Agencies*, the Fiscal Crisis & Management Assistance Team (FCMAT), which was created in 1991 by the California Legislature to help California’s TK-14 local education agencies avoid fiscal insolvency, made the following assessment of AB 218:

Even with missing details, we can conclude that the fiscal impact is and will continue to be significant and will affect programs and services. The best estimate of the dollar value of claims brought to date because of AB 218 is \$2-\$3 billion for local educational agencies. Other local public agencies’ costs will exceed that value by a multiplier, with one county government alone estimating their claim value at \$3 billion. The dollar estimate increases further for total childhood sexual assault claims when considering claims outside of the time frame covered by AB 218. The fiscal impact is not limited to local educational and public agencies with claims but affects all public agencies, because it includes increased insurance premiums and special assessments based on the joint and several liability of current and past members of public entity risk pools.

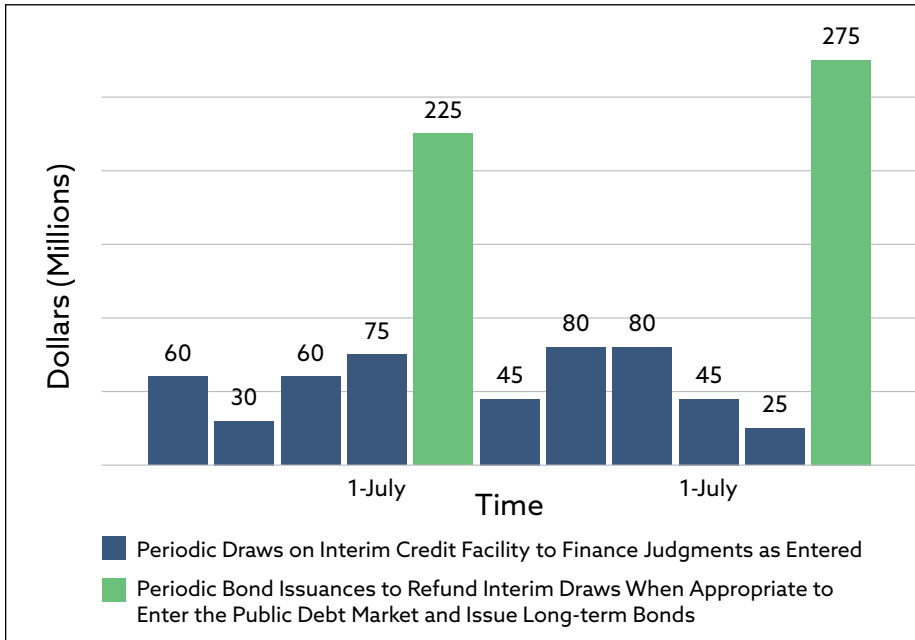
Accordingly, many local governments are facing multiple claims brought either by application of AB 218 or because of similar childhood sexual assault claims for tort liability. In some instances, several local governments have reported facing dozens, hundreds and even thousands of such claims.

One solution is for a local government to bring one section 860 *et seq.* validation proceeding relating to the refunding of all prospective judgments that could potentially be entered against the local government.

As discussed in Chapter 3E, a typical, uncontested section 860 *et seq.* validation proceeding takes approximately 75 to 80 days (not including the 30-day appeal period) to complete. It is easy to see that pursuing a separate validation proceeding for the refunding of each judgment entered against a local government (or even for multiple judgments that happen to be contemporaneously entered against the local government) when the local government has dozens or possibly hundreds or thousands of pending cases against it would be significantly more costly in terms of time, legal fees and judicial resources. Moreover, a validation proceeding involving all prospective claims would allow the local government to more efficiently and effectively manage the financing of multiple claims, both in terms of developing a program to aggregate the liability on an interim basis and to periodically enter the public debt market to amortize the liability on a long-term basis.

To address this issue, Orrick has developed, and certain local governments have approved, forms of AB 218 judgment obligation refunding programs involving both interim financing methods and long-term financing mechanisms. Interim financing methods allow a local government to refund tort judgments falling within the program as they are entered against the local government. Long-term financing mechanisms allow the refinancing of outstanding amounts under interim financings into long-term obligations from time to time when appropriate to enter the public debt market and sell long-term bonds.

USE OF INTERIM AND LONG-TERM FINANCING MECHANISMS



Whether privately placed or publicly offered, bringing a long-term debt offering to market is time consuming. If a local government is dealing with dozens, hundreds or even thousands of tort claims, it will not want to be repeatedly in the market with several series of long-term JOB offerings. An interim financing mechanism, which can involve short-term fixed or variable rate notes issued under a line of credit or pursuant to direct purchase agreements, can provide efficient financing of judgments as and when the judgments are entered against the local government. This preserves the obligation as “indebtedness,” helping solve some of the timing issues discussed in Chapter 4A. When the outstanding amount of interim debt and the timing is otherwise periodically appropriate to enter the public debt market and issue long-term obligations, the local government would then issue its long-term JOBs to refund the interim obligations under the long-term funding mechanism.

Conclusion

JOBs give local governments a tool to mitigate the financial impacts of involuntary liabilities by amortizing payments on the monetary liability over time. The various components of a judgment obligation refunding program and the approach taken for a section 860 *et seq.* validation proceeding will vary based on many factors, including the number and timing of the underlying tort cases or other involuntary obligations as well as the local government's litigation strategy. The various options should be thoroughly discussed and considered with bond counsel promptly when litigation has been threatened or filed such that payment of claims is being considered, would require any express payment commitment, and particularly where substantial liability may result. We hope this booklet provides some initial guidance and promotes a disciplined and thoughtful approach to developing JOB programs that mitigate the negative impacts of involuntary liabilities to public programs and services.

APPENDIX A

Judgment Obligation Bond & Similar Debt Issuance Data

Issuer	Sale Date	Principal Amount	Nature of Underlying Obligation
Los Angeles Unified School District	7/1/25	\$308,150,000	AB 218 or similar claims
Los Angeles Unified School District*	3/27/25	\$14,026,453	AB 218 or similar claims
Los Angeles Unified School District*	1/30/25	\$1,362,476	AB 218 or similar claims
Bellevue Union School District	11/27/24	\$4,650,000	AB 218 or similar claims
Los Angeles Unified School District*	11/22/24	\$54,563,613	AB 218 or similar claims
City of Fullerton	3/9/21	\$5,010,000	Inverse condemnation and/or real property related claims
Hermosa Beach Public Financing Authority**	10/13/20	\$8,150,000	Other obligations
County of Tuolumne	6/28/18	\$4,900,000	Water contamination
Town of Mammoth Lakes	10/11/17	\$23,995,000	Other obligations
City of Indio	5/18/17	\$16,300,000	Inverse condemnation and/or real property related claims
San Bernardino County Flood Control District	2/23/16	\$27,870,000	Inverse condemnation and/or real property related claims
Hermosa Beach Public Financing Authority**	7/23/15	\$11,600,000	Other obligations
City of Fullerton	8/23/13	\$7,250,000	Inverse condemnation and/or real property related claims
City of San Juan Capistrano	6/14/11	\$11,140,000	Inverse condemnation and/or real property related claims
City of Los Angeles	6/10/10	\$50,875,000	Employment, physical injury and inverse condemnation claims
City of Half Moon Bay	7/14/09	\$16,680,000	Inverse condemnation and/or real property related claims
City of Los Angeles	6/23/09	\$20,600,000	Employment related claims
San Bernardino County Flood Control District	4/15/08	\$37,295,000	Inverse condemnation and/or real property related claims

Issuer	Sale Date	Principal Amount	Nature of Underlying Obligation
San Bernardino County Flood Control District	5/25/07	\$103,780,000	Inverse condemnation and/or real property related claims
County of Tuolumne	11/7/06	\$6,195,000	Water contamination
City of Desert Hot Springs	10/14/04	\$9,725,000	Violation of the Fair Housing Act
City of Huntington Beach	9/8/04	\$12,500,000	Tax Refunds
County of Monterey	6/17/04	\$7,470,000	Inverse condemnation and/or real property related claims
County of Santa Cruz**	6/17/04	\$23,000,000	Inverse condemnation and/or real property related claims
City & County of San Francisco	11/19/03	\$44,275,000	Tax Refunds
City of Fresno	4/25/02	\$5,370,000	Inverse condemnation and/or real property related claims
City & County of San Francisco	8/14/01	\$60,755,000	Tax Refunds
City of Los Angeles	8/15/00	\$13,995,000	Violation of Fair Labor Standards Act
City of Los Angeles	4/12/00	\$25,000,000	Violation of Fair Labor Standards Act
City of Concord	9/1/99	\$4,620,000	Employment related claims
City of Fresno	6/12/98	\$3,205,000	Inverse condemnation and/or real property related claims
City of Los Angeles	6/2/98	\$25,000,000	Tax Refunds
City of Fresno	8/15/96	\$3,045,000	Inverse condemnation and/or real property related claims
City of Pico Rivera	6/19/95	\$2,960,000	Tax Refunds
City of Fresno	5/27/94	\$8,295,000	Inverse condemnation and/or real property related claims
City of Los Angeles	2/23/93	\$15,415,000	Tax Refunds
City of Los Angeles	7/28/92	\$198,320,000	Tax Refunds

Key: Orrick served as bond counsel

Refunding in whole or in part

Source: California Debt and Investment Advisory Commission and emma.msrb.org

* Tax and revenue anticipation note interim financing of judgments

** Lease revenue bond or certificates of participation issuance

APPENDIX B

Judgment Obligation Bonds Validation Timeline

The following is an estimated timeline for filing a validation action in the Superior Court for the State of California and, assuming the action is uncontested, obtaining a final judgment.

Event	Best Case	Worst Case
File validation action in the Superior Court	Day 1	Day 4
File application for order for publication of summons	Day 1	Day 5
Obtain order for publication of summons	Day 1	Day 15
Post summons in public places, mail summons (if applicable)	Day 2	Day 16
Begin publication in newspaper for three consecutive weeks	Day 10 ¹	Day 19
Final publication in newspaper	Day 24 ²	Day 33 ²
Deadline for interested persons to respond	Day 41 ²	Day 50 ²
File Notice of Default	Day 42	Day 51
Obtain Clerk's Default	Day 43	Day 56
File application for entry of judgment	Day 44	Day 60
Obtain entry of judgment	Day 55-65	Day 75-80
Appeal period expires	Day 85-95	Day 105-110

Notes

¹ Even in the best case, publication likely will not start for approximately ten days after filing because the firm "last response date" must be included in the summons submitted to the court. Therefore, several additional days should be included to allow time to receive the order back from the judge and still meet the newspaper's printing deadline.

² "Publication" does not end until 21 days from the first publication, even though the final publication is 15 days later. Then the ten days is added to the 21 days, making the total notice period 31 days. Such notice cannot be shortened.

APPENDIX C

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