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MEMORANDUM

DATE: April 7, 2015

TO: Margaret S. Van Vliet, Director
Housing and Community Services Dept.

FROM: Cynthia C. Byrnes, Senior Assistant Attorney General
Tax & Finance Section

SUBJECT: Financing with Article XI-Q Bond Proceeds
DOJ File No. 914200-GT0186-15

You asked several questions regarding the financing of housing projects for the Housing and Community Service Department through the issuance of general obligation bonds authorized under Article XI-Q of the Oregon Constitution. That article of the Oregon Constitution provides that general obligation bonds may be issued to finance the costs of:

> (a) Acquiring, constructing, remodeling, repairing, equipping or furnishing real or personal property that is or will be owned or operated by the State of Oregon, including, without limitation, facilities and systems;
> (b) Infrastructure related to the real or personal property; or
> (c) Indebtedness incurred under this subsection.

Your questions generally involve various ways in which agencies of the State of Oregon, if authorized by their enabling statutes, may own property, or an interest in property that meets the constitutional requirement that property financed under Article XI-Q must be owned or operated by the State of Oregon. We have grouped your questions into several categories and answered them below.

1. INDIRECT COSTS:

You asked whether certain costs that are not part of the materials and labor that go into the construction or remodeling of a real property asset may be financed as an allowable "cost" of "acquiring, constructing, remodeling, repairing equipping or furnishing real or personal property." We understand from the information that you have provided to us that such costs are often treated for accounting purposes as part of the costs attributable to a capital asset. For instance, GASB 62 provides that costs should be capitalized if all of the following conditions are met:

> The costs are directly identifiable with the specific property;
> The costs would be capitalized if the property already were acquired;
> Acquisition of the property or of an option to acquire the property is probable (defined as likely to occur); and
> The prospective purchaser is actively seeking to acquire the property and there is no indication that the property is not available for sale.

Article XI-Q was adopted by Oregon voters in the general election on November 2, 2010. *See* Ballot Measure 72 (2010) (containing Article XI-Q (then designated as XI-P)). It was submitted to the people through legislative referral. SJR 48 (2010) (creating the provision for referral to the people). The interpretive methodology that applies to initiated Oregon constitutional provisions applies to provisions adopted by the voters pursuant to legislative referral. ***State v. Harrell***, 353 Or 247, 254-255, 297 P3d 461(2013) (so stating, citing ***Stranahan v. Fred Meyer, Inc.***, 331 Or 38, 56, 11 P3d 228 (2000)).

Under that framework, our task is to discern the intent of the voters. *Id.* The best evidence of the voters' intent is the text and context of the provision itself and, if the intent is clear, "the court does not look further. ***Ecumenical Ministries v. Oregon State Lottery Comm.***, 318 Or 551, 559, 871 P2d 106 (1994). Nevertheless, "caution must be used before ending the analysis at the first level, *viz.*, without considering the history of the constitutional provision at issue." ***Stranahan***, 331 Or at 57. The history includes "sources of information that were available to the voters at the time the measure was adopted and that disclose the public's understanding of the measure, such as the ballot title and materials in the voters' pamphlet. ***Ecumenical Ministries***, 318 Or at 560 n 8.

The text of Article XI-Q refers to the "costs of acquiring, constructing, remodeling, repairing, equipping or furnishing real or personal property." The costs that may be financed are connected to the activities financed through use of the preposition "of." Using the court's interpretive methodology, to discern the scope and meaning of the word "of" we turn first to the dictionary. *Oregon Telecommunications Assoc. v. Oregon Dept. of Transportation*, 314 Or 418, 144 P3d 935 (2006) (interpreting "of" within Oregon Constitution, Article IX, Section 3a, regarding revenues used for the construction, ***, operation and use of public highways); citing *Flavorland Foods v. Washington County Assessor*, 334 Or. 562, 568, 54 P.3d 582 (2002). Like the highway funds at issue in the *Oregon Telecommunications* case, the costs at issue in Article XI-Q relate to a list of activities that are related to real and personal property. Relying on the dictionary, the *Oregon Telecomm.* court concluded that "[i]n context, the term "of" requires that the process or activity be "with reference to," "relating to," or "about" the public highway." *Webster's Third New Int'l Dictionary* 1565 (unabridged ed 2002). We believe an Oregon court would reach a similar conclusion here and hold that the costs financed under Article XI-Q must be "with reference to," "relating to" or "about" the ownership or operation of real or personal property that is the subject of the financing.

The extent, however, to which certain costs are "with reference or related to" owning or operating the real or personal property asset is a factual inquiry that will not always have a clear answer. The test that you have provided in relation to whether certain costs are sufficiently connected to a capital asset to be included in the cost of the capital asset appears to require a

connection that is sufficiently close that an Oregon court would be likely to conclude that costs meeting the GASB test would also be sufficiently related to the asset to be a cost "of" the financed project. The GASB standards are not the only measure, however, of whether a cost is sufficiently related to the asset to be considered a cost "of" the activity it is financing. A cost that met only the first requirement in the GASB test, that the costs "are directly identifiable with the [ownership or operation of] specific property" could still be sufficiently related to the property to be within the court's requirement that the cost be "with reference to" or "related to" the activity being financed for the property. The focus of the text in Article XI-Q is on the connection between the listed activity and the cost at issue. See *Oregon Telecommunications*, 314 Or at 429 ("the focus of the text is on the connection between the process or activity and the public highway").

For further guidance, we may turn to the legislative history related to Article XI-Q. As discussed, Article IX-Q was submitted to the voters in 2010 as Ballot Measure 72. Voters' Pamphlet materials concerning that measure are pertinent sources of legislative history. *Ecumenical*, 318 Or at 560 n 8. Ballot Measure 72 does not contain any discussion about the meaning of the phrase "costs of". The ballot title itself simply refers to borrowing for the "state's real and personal property projects." Voters' Pamphlet, November 2, 2010, General Election at 68. The Explanatory Statement informs voters that:

> Ballot Measure 72 would amend the state constitution to add a new exception to allow the state to issue general obligation bonds to finance acquisition, construction, remodeling, repair, equipping or furnishing of state owned or operated property. Currently, the state constitution forbids lending the state's credit or borrowing in excess of $50,000, with some exceptions. General obligation bonds are the cheapest method of borrowing the state may use and would cost less than the certificates of participation the state currently uses.

Id. at *69* (emphasis added). The voters were told that Article XI-Q was necessary to provide a cheaper method of financing state projects than the certificates of participation that the state was currently using to finance those projects. It would be reasonable for the voters to have understood that Article XI-Q bonds would be available to fund the same types of projects relating to real or personal property that were funded with certificates of participation.

The relevant statute governing certificates of participation, ORS 283.085, provided in 2010 for certificate of participation financing "[t]*o finance real or personal property that is or will be owned and operated by the state or any of its agencies."* Pursuant to that statute, at the time Ballot Measure 72 was submitted to voters, certificate of participation financing was available only to pay the cost of financing agreements for facilities owned *and* operated by the state and projects related to those facilities. While the materials in the Voters' Pamphlet suggest that Article XI-Q was intended to authorize financing of the projects that were then being financed with certificates of participation, the *language* of Article XI-Q is more expansive - authorizing financing for real property owned *or* operated by the state. We must give effect to the language that the voters approved. For that reason, the history is not helpful; although it appears to affirm that at the least, projects or costs that were financeable with certificates of participation would be financeable with Article XI-Q bonds. The state has historically used

certificates of participation to finance projects that were considered capital assets under accounting principles. See e.g. Chapter 904 Oregon Laws 2009 (listing capital projects financed with certificates of participation). Therefore, costs that are sufficiently connected to be considered part of the cost of a capital asset under the governmental accounting standards used by the state are likely to be considered a cost of the asset that is also financeable with Article XI-Q bonds.

2. LESS THAN FEE INTEREST IN REAL PROPERTY

You also asked whether the proceeds of Article XI-Q bonds may be used to finance the acquisition, construction, remodel, repair, equipping or furnishing of an in interest in real or personal property that is less than the full fee simple interest in the property. For instance, could the State finance the acquisition of a long term ground lease or easement, or the construction, remodel etc. of improvements on a ground lease or an easement?

As discussed above, Article XI-Q does not define any of the terms that it uses. We give words of common usage their plain, natural and ordinary meanings. ***Ecumenical Ministries***, 318 Or at 567. The dictionary that is most often used by Oregon courts in determining plain meanings, WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY (unabridged 2002), contains no definition of the phrase "real property" so we parse the terms. The pertinent definition of "real" is "of or relating to things (as lands, tenements) that are fixed, permanent, or immovable; *specifically*: of or relating to real estate <*real* property>[[.]" WEBSTER'S at 1890. These applicable definitions of "property" are "**2** *a*: something that is or may be owned or possessed: WEALTH, GOODS; *specifically*: a piece of real estate * * * *b*: the exclusive right to possess, enjoy, and dispose of a thing: a valuable right or interest primarily a source or element of wealth: OWNERSHIP * * * *c*: something to which a person has a legal title: an estate in tangible assets (as lands, goods, money) or intangible rights (as copyrights, patents) in which or to which a person has a right protected by law [.]" WEBSTER'S at 1818, *see also*, BLACK'S LAW DICTIONARY at 1252 (defining "property" as "[t]he right to possess, use, and enjoy a determinate thing (either a tract of land or a chattel); the right of ownership * * *. Also termed *bundle of rights.")* (8th ed 1999).

"Real property" is used as a term of art in the law. The legal definition is "[l]and and anything growing on, attached to, or erected on it, excluding anything that may be severed without injury to the land. Real property can be either corporeal (soil and buildings) or incorporeal (easements)." *Id.* at 1254. "Incorporeal" in this context means "of, relating to, or constituting a right that has no physical existence but that issues out of corporate property which has a physical existence and that concerns or is annexed to or exercisable in relation to such property[.]" WEBSTER'S at 1145.

In both its plain and legal senses "real property" encompasses land, buildings, and other fixtures erected on or growing from the land as well as rights in those things. It also incorporates the incorporeal or intangible rights in the property, such as a right to possess, as is conferred in a lease, or an incorporeal right to use the property as is conferred in an easement. Similarly, the meaning of personal property includes both tangible and intangible elements in the property. Therefore, we conclude that the term "real property" as used in Article XI-Q includes any or all

of the rights and estates in the real property, and is not limited to only the fee simple, or entire "bundle of sticks" attributable to the property, but include the tangible assets attached to land and incorporeal or intangible elements that also attach to the property, such as long term leases or easements.[1]

3. CONDOMINIUM OWNERSHIP

The State might seek to acquire a portion of a larger project by financing the acquisition of condominium ownership interest. A condominium unit owner's rights in the unit are similar to those of an owner of independent real property: "[A] unit may be individually conveyed and encumbered and may be the subject of ownership, possession or sale and of all types of juridic acts inter vivos or mortis causa, as if it were sole and entirely independent of the other units." ORS 100.505(1). Consequently, "[e]ach unit owner shall be entitled to the exclusive ownership and possession" of his unit. ORS 100.505(2). Additionally, each condominium unit owner has "an undivided interest in the common elements" of the condominium, apportioned based on the allocation in the condominium declaration. ORS 100.515(1). This undivided interest cannot be "separated from the unit" and must be "conveyed or encumbered with the unit." ORS 100.515(3).

As discussed above, the owner of a condominium unit has, with respect to that unit, the sole right to convey, possess, encumber and sell the unit. Therefore, if the state acquires a condominium interest, it acquires most, if not all, of the incidents of ownership described in the portion of the real property that constitutes that condominium interest, and so the state "owns" the real property comprised of that unit for purposes of Article XI-Q. In addition, the State acquires an undivided interest in the common elements of other real property elements that comprise the entire condominium interest subject to the condominium declaration. Such interest appears closely related to the condominium interest being acquired and so would properly financeable as a cost "of" the condominium.

4. JOINT OWNERSHIP

Article XI-Q requires that the property being financed is "owned or operated" by the State of Oregon. The pertinent definition of the verb "own" is "to have or hold as property or appurtenance: have a rightful title to: whether legal or natural: POSSESS." WEBSTER'S at 1612. The applicable definition of "possess" is similar: "to have and hold as property: have a just right to: be master of "OWN <*possessing* lands and money>." WEBSTER'S at 1770. The concepts of "property" and "ownership" are intertwined and sometimes difficult to separate. For instance, "property" is also defined as "the exclusive right to possess, enjoy, and dispose of a thing: a valuable right or interest primarily a source or element of wealth: OWNERSHIP" or "something to which a person has a legal title: an estate in tangible assets (as land, goods money)[.]" *Id.* at 1818, *see also*, BLACK'S LAW DICTIONARY at 1252 (defining "property" as *"*[t]he right to possess, use, and enjoy a determinate thing (either a tract of land or a chattel); the

[1] We note also that such assets are often treated as capital assets for State accounting functions and under the Internal Revenue Code, and that capital leases are financeable under the State's certificates of participation program (though at increased cost), if the property is also operated by the State.

right of ownership * * *. Also termed bundle of rights*")* (8th ed 1999). The pertinent definitions of "title" are "**2** *a*: the union of all the elements constituting legal ownership and being divided in common law into possession, right of possession, and right of property *b*: something that constitutes a legally just cause of exclusive possession: the body of facts or events that give rise to the ownership of real or personal property." WEBSTER'S at 2400.

Tenants in Common.

Under Oregon law property may be held in several forms of joint ownership. The state may be a tenant "in common" with other owners. A tenancy in common is created when "[a] conveyance [] of real property, or an interest in real property, [] is made to two or more persons," so long as that conveyance does not expressly grant a right to survivorship. ORS 93.180. Unless evidence of the parties' intent indicates otherwise, each tenant's interest in the property is proportionate to his contribution to the property's purchase price. *See Glaster v. State Const. Co.*, 196 Or 625, 640-41, 251 P2d 441 (1952). With respect to his share in the property, a tenant has all the same rights as an individual owner, except the right of sole possession. *Shea v. Peters*, 126 Or 76, 82, 268 P 989 (1928). Therefore, each tenant "may manage his part of the [property] as he pleases, provided he does not injure his cotenant in so doing." *Id. See also Le Vee v. Le Vee*, 93 Or 370, 382, 183 P 773 (1919) ("Tenants in common hold their interest in realty independent of each other. Neither one can do an act respecting the title which will bind the others.") Generally, a tenant does not incur liability to his cotenants by occupying or using the property. *Hanns v. Hanns*, 246 Or 282, 310, 423 P2d 499 (1967). However, if the tenant's use or occupation of the property "excludes the others from enjoyment of their interest, the occupying cotenant will be required to reimburse the others for the rental value of their interest." *Palmer v. Protrka*, 257 Or 23, 33 n 12, 476 P2d 185 (1970).

Article XI-Q refers simply to "owning" or "operating" property. The plain language contains no modifiers as to whether the ownership or operation of the property must be solely by the State of Oregon, or may be shared with other entities. As previously discussed, our goal is to discern the intent of the voters through the text used, without the use of additional words or failing to give effect to the words used. A co-tenancy creates a shared ownership of the property. Therefore, if the State of Oregon acquires property as a co-tenant along with another legal entity, it will acquire an ownership interest in the entirety of the property. As discussed above, the term "own" means, according the dictionary most often cited by the Oregon courts, "to have or hold as property or appurtenance: have a rightful title to: whether legal or natural: POSSESS." The interest acquired in a co-tenancy is the same as an individual owner, except the right of sole possession. Included in the concept of property "ownership" is a legally protected right to use and occupy property, even if it is subject to some restrictions, the interest of a co-tenant to possess and use the property is a protected legal right under Oregon law and so may fall within the scope of property that may be "owned" as the term is used in Article XI-Q.

A co-tenancy that is created, however, by simply contributing to the purchase price of a piece of property may not give sufficient indicia of ownership to the State of Oregon to carry out the voter's intent. Article XI-Q relates to property that is owned **or** operated by the state. As we noted previously, by use of the word "or" it is apparent that Article XI-Q bonds may be used for purposes that are broader than the certificates of participation referenced in the voters' pamphlet.

Nevertheless it is also apparent from the context of the article and the voters' pamphlet materials that the purpose of Article XI-Q is to provide a flexible financing tool to carry projects that the Legislative Assembly determines are of benefit to the state or to carry out a state purpose, including if tax-exempt bonds were issued to protect the tax-exempt nature of those bonds.[2] For instance, the caption of the measure referred to the "state's real and personal property projects." The emphasis in the voters' pamphlet discussion was on lowering costs for the state to carry out its projects and lower the state's borrowing costs through the issuance of bonds.

To assure that property owned through a tenancy in common meets the state's objectives and restricts the use of the property in a way that is authorized by Article XI-Q, the state should not enter into a co-tenancy without an agreement between the state and the co-tenant as to how the property is to be used and maintained, including covenants from the state's co-tenant that the property would be used in accord with the state's purposes and the authorizing legislation for the bonds that were used to purchase the state's interest. The agreement should provide that if the co-tenant uses the property in a manner that forecloses the state from carrying out those purposes on its share of the property, or excludes the state from possession of the property, the co-tenant is obligated to compensate the state for the value of its interest. ***Remington v. Landolt***, 273 Or. 297, 541 P.2d 472, (1975) (use by one tenant to exclusion of other is conversion for which other tenant is compensated); citing ***Rosenau v. Syring***, 25 Or 386, 389, 35 P 844, 845 (1894); ***Nusshold v. Kruschke***, 175 Or 697, 159 P2d 819 (1945). The value of the state's interest should be measured at the very least by the amount the state contributed to the property, or the rental value of the property. The state's interest may include additional factors, however, such as protecting the tax-exempt status of the bonds issued to finance the property. If a co-tenant interferes with the state's use of the property, the payment required from the co-tenant could be used to defease or refund the bonds. If the co-tenant excluded the state from possession or used of the property in an manner inconsistent with the purpose for which the bonds were issued, the bonds would need to be defeased or refunded to avoid an unconstitutional use of the proceeds, and if the bonds were sold on a tax-exempt basis, to avoid rendering the bonds taxable.

Not all co-tenancies will meet the requirements of Article XI-Q. We advise, however, that if properly structured to give the state control over the use of the property, and with appropriate remedies, including payment of an amount sufficient to defease the state's bonds, a co-tenancy may meet the requirements of Article XI-Q. If the documents creating the co-tenancy give the state sufficient control over the property, the property may also fall within the scope of Article XI-Q because the state "operates" the property, as well as having an ownership interest.

[2] To be financed with certificates of participation, property must be owned "and" operated by the state. As a statutory program, the Legislative Assembly may expand, and has expanded, the authorized use of certificates of participation when it needed to finance a program that was not eligible for financing with constitutionally authorized bonds. For instance, ORS 283.085 was amended to permit financing of pension liabilities in the event Article XI-O was not adopted by the voters. Because the constitution cannot be amended by the Legislative Assembly, arguably to provide a flexible financing tool, the legislature used "or" instead of "and" in Article XI-Q.