Clerk of the Superior Court
*** Filed ***
MAR 11, 2022 10:16 a.m.

SUPERIOR COURT OF ARIZONA
MARICOPA COUNTY

CV2020-015495 03/11/2022

HONORABLE JOHN R. HANNAH JR

CLERK OF THE COURT
A. Walker
Deputy

KAREN FANN, ET AL.

v.

STATE OF ARIZONA, ET AL.

BRETT W JOHNSON

BRIAN M BERGIN
DANIEL J ADELMAN
ROOPALI HARDIN DESAI
JOHN SUD
STEPHEN W TULLY

COURT ADMIN-CIVIL-ARB DESK
DOCKET-CIVIL-CCC
JUDGE HANNAH

RULING

Proposition 208, the Invest in Education Act, enacted by initiative in 2020, is again before the Superior Court, this time on remand by order of the Arizona Supreme Court in *Fann v. State of Arizona*, 251 Ariz. 425, 493 P.3d 246 (2021).

The parties have addressed the remand order in cross-motions for judgment on the pleadings: Plaintiffs' Motion for Judgment, filed by majority legislative leadership ("legislator plaintiffs") and political organizations and citizens who join the legislators in opposition to Proposition 208 (collectively "Plaintiffs"); and Intervenor-Defendants' Motion for Entry of Judgment of Dismissal, filed by education funding advocates Invest in Arizona (sponsored by AEA and Stand for Children) and David Lujan (collectively "IIA"). Defendants State of Arizona and Arizona Department of Revenue (collectively "ADOR") join the plaintiffs' request for a

declaration that Proposition 208 is unenforceable and an injunction that would bar its operation. All parties agreed that the remand issue would be decided on a written factual record without a hearing.

This Court understands the remand order as a direction to declare Proposition 208 unconstitutional in its entirety, and to enjoin its operation permanently, if the Court finds as a fact that the annual education spending limits imposed by the Arizona Constitution will prevent Arizona's public schools from spending a "material" amount of Proposition 208 tax revenue in 2023. On that basis, the Court is obligated to strike down Proposition 208. This order explains that decision. It also raises an issue that the Court respectfully suggests the higher courts may wish to consider if this case comes before them again on appeal.

PROCEDURAL HISTORY AND QUESTION PRESENTED

This case was last before the Superior Court on Plaintiffs' motion for a preliminary injunction against Proposition 208. The motion was denied by written order. Minute Entry Ruling filed 2/5/2021. That order did not decide whether or how the constitutional spending limits would apply to Proposition 208, or what would happen to Proposition 208 as a whole if the spending limits applied, because the factual and legal record had not yet been fully developed. *Id.* at 9-15.

On appeal from the order denying the preliminary injunction, the plaintiffs convinced the Arizona Supreme Court to reach the spending limit issues. The Supreme Court decided that the funds Proposition 208 will generate for the benefit of Arizona's public schools are "local revenues" subject to the education spending limits in the Arizona Constitution, article 9, section 21 (the "Education Expenditure Clause"). *Fann v. State of Arizona*, 251 Ariz. 425 ¶¶ 18-31. The Court held that the Proposition 208's "Local Revenues Provision," A.R.S. section 15-1285(1), is unconstitutional on its face because it characterizes the Proposition 208 payments to school districts as "grants" to which the spending limits do not apply, and that the "Allocation Provision" specifying how the schools must spend the money, A.R.S. section 15-1281(D), is unconstitutional as applied "to the extent allocated revenues exceed the expenditure limit set by the Education Expenditure Clause." *Id.*, ¶ 18.[1] The Court then decided that Proposition 208 is not "severable"

[1] The decision does not make clear why exactly the Allocation Provision is unconstitutional even on an "as-applied" basis. As the dissent points out, nothing in Proposition 208 requires schools to spend the funds they will receive from Proposition 208, let alone spend them in violation of the constitutional expenditure limits. *Fann v. State,* 251 Ariz. 425 ¶ 70-71 (Timmer, V.C.J., dissenting in part). The *Fann* majority never explains why accumulating the excess revenue without spending it, either at the state level or at the school district level, would be illegal as such.

Attempting to plug this hole on remand, the plaintiffs cite an old Attorney General opinion for the proposition that education funding counts toward the spending limits upon receipt of the

– that is, that the valid parts of the law cannot stand on their own without the invalid parts -- if the expenditure limits will thwart Proposition 208's policy goal of providing increased support for school districts. *Id.*, ¶¶ 36-51.

The remand order says that the Superior Court "must declare Prop. 208 unconstitutional and enjoin its operation" if the measure "will result in the accumulation of money that cannot be spent without violating the expenditure limit." *Id.*, ¶ 54. "Moreover, to further clarify this inquiry for the trial court, if any material amount of the Prop. 208 revenue is sequestered in a designated state fund because it cannot be spent due to the expenditure limit, then Prop. 208, in its entirety, is unconstitutional." *Id.* "Material" is defined as "of such a nature that knowledge of the item would affect a person's decision-making; significant; essential." *Id.* (cleaned up).

WHY THE REMAND ORDER REQUIRES ABROGATION OF PROPOSITION 208

The parties disagree on the legal and factual issues that the remand order presents. The first task, then, is deciding which party is asking the right question.

IIA argues that the remand order calls for a permanent injunction against Proposition 208 only if the record establishes with "certainty" that school district spending will exceed the constitutional expenditure limits, not only in the upcoming fiscal year 2023 (the first in which Proposition 208 revenues may be distributed and spent) but also in future years. IIA points out that both the spending limits and the "local revenues" funding streams that count toward the limits vary from year to year, because of economic, demographic, and political factors that are sometimes hard to predict. IIA also identifies legal and political issues that could raise the spending limits or alter the relevant funding streams substantially. Because several issues of that nature have arisen since the enactment of Proposition 208, IIA also makes a causation argument: that the remand order requires a declaration of Proposition 208's invalidity only if the expenditure limits will be exceeded "because of" Proposition 208 revenues as opposed to some other educational funding source.

The plaintiffs say none of that matters. According to the plaintiffs, the remand order requires an injunction against the operation of Proposition 208 if the measure will "more likely

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funds by the prospective spender. *See* Plaintiffs' Response to Intervenor/Defendants' Motion for Entry of Judgment of Dismissal at 13, *citing* Ariz. Att'y General Op. 81-009 (1981). What the opinion actually says, though, is that the funds count them toward the spending limit in the year in which the recipient entity intends to spend them. Nothing in the AG opinion stands for the counter-intuitive notion that a school district must count monies received in a given year toward the spending limit for that year even if they will not be spent in that year.

than not" generate a material amount of revenue that expenditure limits will prevent the schools from spending for educational purposes in fiscal year 2023. IIA and ADOR "do not contest that, based on current projections, it is more likely than not that school district spending will exceed the [Aggregate Expenditure Limit] in 2023 regardless of whether the amounts attributable to the former capital levy are excluded, [2] and without consideration of any revenues from Proposition 208." Joint Factual Stipulation ¶ 9. The plaintiffs say that factual concession ends the inquiry.

This Court understands the remand order the same way Plaintiffs do. As noted above, the Supreme Court treated the plaintiffs as having made an "as-applied" challenge to the provision of Proposition 208 that tells the school districts how they must spend the Proposition 208 money. *Fann v. State*, 251 Ariz. 425 ¶¶ 13, 18, 42-44. In the preliminary injunction ruling, this Court observed:

> The dollar amounts that the school districts will receive and the amounts they will be permitted to spend, at any given point in time, are classic "adjudicative facts" that require presentation of evidence tested in the adversary process. So far the parties have offered only back-of-the envelope calculations that are wholly inadequate even for a preliminary adjudication.

Minute Entry Ruling filed 2/5/2021 at 14. The parties presumably gave the Supreme Court the same "back of-the-envelope" calculations. Thus the remand order can be understood as a directive to the Superior Court to make the factual findings that had not previously been made. The standard of proof for finding "adjudicative facts" in a civil action is "preponderance of the evidence," which requires the fact-finder to decide whether a fact sought to be proved is more probable than not. *Kent K. v. Bobby M.*, 210 Ariz. 279 ¶ 25, 110 P.2d 1113 (2005).

As for the time period to be addressed, the Supreme Court focuses on the immediate future. The *Fann* opinion refers more than once to the 2023 projections of the Joint Legislative Budget Committee, concerning the amount of money that the school districts will be constitutionally permitted to spend and the revenue Proposition 208 will generate in the coming fiscal year. *Id.*, ¶¶ 39, 53. It disapproves of the idea that the measure could be "unconstitutional in some years" but "constitutional in others," allowing it to "lurch along." *Id.*, ¶ 43. It returns several times to the idea that the proponents of Proposition 208 promised a "permanent" increase in education spending to remedy "years of underfunding by the Legislature." *Id.*, ¶¶ 41, 47, 49. The dissent, for its part, criticizes the majority for "directing the trial court to employ an as-applied inquiry that

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[2] IIA contends that education funding sources that have replaced the former "capital levy" should not count toward the aggregate expenditure limit. If they are right, the total school district spending subject to the spending limits would be reduced by about $200 million. Joint Fact Stipulation ¶ 7.

examines *currently existing financial projections*" to determine whether the statute is unconstitutional in its entirety. *Id.*, ¶ 75 (emphasis added). These passages, together with the absence of any other guidance as to how many years of as-applied unconstitutionality might be enough to bring down the entire measure, indicate that the question is whether "any material amount of the Prop. 208 revenue [will be] sequestered in a designated state fund because it cannot be spent due to the expenditure limit" in 2023.

The Supreme Court's comments on what constitutes a "material amount" of money point in the same direction. Apparently anticipating the result of the inquiry it directs the Superior Court to undertake, the Supreme Court says,

> under the remaining statutory provisions of Prop. 208, *hundreds of millions of tax dollars* will be sequestered in a designated state fund, unable to be spent, to the extent they exceed the expenditure limit. This result makes the remaining portion of Prop. 208 unworkable and thus not severable from its unconstitutional provisions.

Id., ¶ 40 (emphasis added). IIA's expert estimates that the Proposition 208 income tax surcharge would generate approximately $289 million in 2023. Motion for Judgment, Exhibit 9 (Liddicoat expert report). Assuming the Supreme Court affirms that twelve percent of the Proposition 208 monies qualify as "grants" not subject to the Education Expenditure Clause even under the *Fann* definition, *id.*, ¶ 53 n.8, the amount that would count toward the 2023 spending limit decreases to about $254 million. According to the Joint Legislative Budget Committee, 20.2 percent of that money would go to charter schools. Motion for Judgment, Exhibit 4 (JBLC Report) at 9.[3] The amount ultimately allocated to the school districts in 2023, then, would be around $203 million. That is a lot less than the $827 million figure cited by the Supreme Court in *Fann*, 251 Ariz. 425 ¶¶ 39, 53, but it is still "hundreds of millions of dollars."

If school district spending more likely than not will exceed the predicted spending limit in 2023 without counting Proposition 208, as IIA concedes is the case, more than $200 million in Proposition 208 money will more likely than not "remain sequestered in a designated state fund" absent some remedial action. Under those circumstances, the remand order requires the Superior Court to strike down Proposition 208 in its entirety.

IIA argues that fiscal years 2022 and 2023 are outliers when it comes to the constitutional spending limits. They aver that there was plenty of "room" under the spending "cap" for most of the ten years prior to 2022. Intervenor-Defendants' Motion for Judgment of Dismissal at 8. They

[3] Charter schools are not subject to the Education Expenditure Clause, because they did not exist when the Arizona Constitution was amended to add that provision.

point out that both the expenditure limit calculation and the amount of spending on public education vary from year to year, based on economic, demographic and political factors that are sometimes hard to predict. IIA also identifies legal and political issues that could change how the expenditure limit is calculated or applied, or that could affect future education funding substantially. Several developments of that nature have impacted the spending limit equation this year, most notably that the Classroom Site Fund or "Proposition 301" monies for the first time will count as "local revenues" subject to the spending limits. *Id.* at 7. IIA argues that these events, not Proposition 208, are the "cause" of the predicted excess spending in 2023.

Though IIA is right about the effect of present events over which Proposition 208's proponents have no control, and about the likelihood that future events will make it possible for school districts to spend Proposition 208 funds as intended, the Supreme Court's analysis makes those considerations irrelevant for present purposes. Since the Supreme Court addressed the spending limit issues in the abstract, without a fully developed lower court record, IIA might be able to argue to the Supreme Court that the facts IIA now proffers require a different result. The Superior Court, however, cannot entertain that argument.

THE COURT AS A POLITICAL ACTOR

Under article IV, part 1, section 1(1) of the Arizona Constitution, the people "reserve the power to propose laws and amendments to the constitution and to enact or reject such laws and amendments at the polls, independently of the legislature." The people's power to create legislation through initiative is therefore part of the legislative process. *Winkle v. City of Tucson*, 190 Ariz. 413, 415, 949 P.2d 502, 504 (1997).

Prudential concerns dictate the exercise of judicial restraint when the courts are asked to involve themselves in the legislative process. *Bennett v. Napolitano*, 206 Ariz. 520 ¶ 15, 81 P.3d 311 (2003) (Jones, C.J.). The courts "ought not prematurely enter the political arena to referee" political disputes between political actors who have not yet "exercised available political means" to settle the dispute. *Id.*, ¶ 34. Caution is especially appropriate when the request for judicial intervention comes from individual legislators. *Id.*, ¶ 33.

When the people of Arizona enacted Proposition 208, they exercised their co-equal Constitutional authority to implement their desired public education funding and taxation policies. That touched off a policy dispute with (among others) a majority in the Arizona Legislature. The dispute has played out in a series of political events -- the Legislature's enactment of tax law changes that will substantially reduce the amount of revenue generated by Proposition 208, an initiative measure that will ask the voters to repeal some of those changes, proposed tax legislation that would attempt to moot the initiative. There are legal guardrails on this political maneuvering, notably the Voter Protection Act, article IV, part 1, section 1(6) of the Constitution, which prohibits

the legislature from simply repealing laws enacted by initiative. Within those guardrails, the political actors have worked their way toward a political resolution of their policy disagreement.

The main political players are also the parties to this lawsuit. The courts are responsible for answering their legal question – whether Proposition 208's Local Revenues Provision runs afoul of the Education Expenditure Clause – according to applicable legal rules. At the same time, however, judges must remain wary of political actors who want them to take sides in ongoing political disputes.

This case has cast the Superior Court as an unintentional player in the political drama that followed from Proposition 208. A journalist described the litigation on remand as "a game of chicken between lawmakers and Judge John Hannah." "Ending classes early, axing graduations: Arizona schools face big cuts as Legislature idles," Arizona Republic, February 7, 2022, found at https://www.azcentral.com/ story/news/local/arizona-education/2022/02/06/ (last visited March 7, 2022). That was never this Court's intention. It is safe to say that no judge of the Superior Court of Arizona would ever choose to be in that kind of pickle.

With the benefit of hindsight and the utmost respect for everyone concerned, this Court submits that the timing of the *Fann* decision, and the framing of the severance issue that follows from the invalidity of the Local Revenues Provision, caused this case to stray over the line between law and politics. The legal issue of severance is analyzed in political and policy terms. The political obstacle that the Education Expenditure Clause creates for implementation of Proposition 208 without the Local Revenues Provision is treated as grounds for affording the plaintiffs legal relief. As the dissent observes, that framing doomed Proposition 208. *Fann*, 251 Ariz. 425 ¶ 66 (Timmer, V.C.J., dissenting in part).

Arizona law establishes a two-part test for determining whether the unconstitutional portion of a law is "severable" from the rest. The first part of the test, applicable to both acts of the legislature and initiative measures, is whether the valid portion of the measure, considered separately, can operate independently and is enforceable and workable. *Randolph v. Groscost*, 195 Ariz. 423 ¶ 15, 989 P.2d 751 (1999). The second part, which asks whether those who enacted the law would have approved it as modified, is more lenient for voter initiatives than for ordinary legislation. The courts will uphold the valid portion of an initiative measure "unless doing so would produce a result so irrational or absurd as to compel the conclusion that an informed electorate would not have adopted one portion without the other." *Id.*

Past cases have uniformly treated "workability" as a practical legal question of whether "the valid parts are independently effective and enforceable as law." *E.g. McCune v. City of Phoenix*, 83 Ariz. 98, 106, 317 P.2d 537 (1957). Proposition 208 plainly meets this criterion, because the tax collection and financial administration parts of the law work perfectly well on their

own from a technical standpoint. The Education Expenditure Clause does not pose a problem until it comes time for the school districts to spend the money. *See infra* at 2, n.1

Fann reframes "workability" as a policy question of the law's "ability to accomplish its stated purpose without remedial [legislative] action." 251 Ariz. 425, ¶ 37 (emphasis added). "The stated purpose of Prop. 208 was to tax high-income individuals to raise revenue that would be directly provided to school districts based on 'years of underfunding by the Legislature'. . . ." *Id.,* ¶ 41. Since the Local Revenues Provision is invalid, Proposition 208 can accomplish that purpose only through the enactment of additional legislation to reconcile the measure with the Education Expenditure Clause. But the possibility of "remedial action" to make an initiative "workable" is not to be considered. *Id.,* ¶ 37. What's more, the legislators responsible for "years of underfunding" are unlikely to enact such legislation – so unlikely, in fact, that no rational voter could have thought otherwise. *Id.*, ¶ 49 ("we find it unlikely to the point of absurdity that an electorate who voted for an initiative to spend money directly on schools because the legislature had declined to do so, would have voted for an initiative that required annual legislative action for the money to be spent.") *Fann* says that makes Proposition 208 unconstitutional.

The casting of "workability" in terms of immediate policy outcome gives the legislature a decisive advantage over the electorate in the event of a disagreement over policy like Proposition 208. Even under ordinary circumstances, the legislature has the advantage of being able to act faster than the electorate. That give the legislature a built-in edge in the political back-and forth. *Fann* widens that edge to an insurmountable lead, by accepting the legislator plaintiffs' assertion that the public cannot wait for a follow-up initiative to reconcile the Proposition 208 spending with the Education Expenditure Clause, or for an election that might change the political makeup of the legislature.

The legislature, notably, faces no such barriers. The legislature can authorize a tax for education funding without accounting for the constitutional spending limits, and then fix the problem at its leisure when necessary. It did exactly that, when this case was pending on remand, by authorizing school districts to spend "Proposition 301" sales tax money notwithstanding the expenditure limits. H.C.R. 2039, 55th Leg., Second Regular Sess. Ariz. 2022. The bill in which the Legislature re-authorized the tax formerly imposed by Proposition 301, in 2018, created *exactly the same Education Expenditure Clause issue* as the provisions of Proposition 208 that remain after the removal of the Local Revenues Provision. Yet that tax will remain in place, even as Proposition 208 is struck down.

The Supreme Court acknowledges in its ruling that legal doctrine should not interfere with the initiative side of the legislative process. The decision rejects the plaintiffs' argument that the courts should strike initiative measures "if any part is flawed. . . ." 251 Ariz. 425 ¶ 34. It reaffirms that *Randolph* properly accommodates initiatives by modifying the second part of the severance

test, concerning the need for a showing that the law's proponents would have enacted it even without the unconstitutional provision. *Id.* It says that "[p]recluding severance of laws enacted by initiative while allowing severance to save laws enacted by the legislature would improperly limit the people's power to legislate. *Id.*, ¶ 35. Yet that is precisely the result that follows from the manner in which *Fann* proceeds to apply *Randolph*. IIA understandably describes that result as turning the law relating to severability "on its head."

Moreover, the logic of *Fann* entirely relieves the legislature of any *political* responsibility for accommodating the policy decisions the electorate makes by initiative. If legislators can find a legal flaw in a measure they disagree with as a matter of policy, their incentive is now not to fix it but instead to exploit it. They can then point to the political obstacles created by their own opposition as a reason for the courts to stop the political fight and declare the legislature the winner. They are safe in that harbor, since they have been assured that "remedial action" is not required.

The muddle of law and politics drove the case on remand. The plaintiffs focused on their contention that Proposition 208 is disrupting the Legislature's budget process and education policy decisions. Fann Plaintiffs' Joinder in ADOR'S Request for Expedited Ruling on Pending Cross-Motions for Judgment, filed 02/01/2022, at 2 ("A lack of finality in this matter imperils budgetary decisionmaking generally and education funding specifically.") Underlying this argument was the refusal of some legislators to consider exempting the "Proposition 301" monies from the current-year spending limits until this Court had struck down Proposition 208. Their refusal was encouraged by *Fann*'s holding that Proposition 208 is unconstitutional if it is not politically feasible. At the same time, the legislator plaintiffs justifiably believed that they had been assured of a legal solution to their political problem. No wonder they were upset that the Court was unable to act more quickly.

This case illustrates the wisdom of the principles of judicial restraint that the late Chief Justice Jones laid down in *Bennett v. Napolitano*. IIA will be free to argue to the Arizona Supreme Court on appeal that it is not too late for the courts to step away. For now, however,

IT IS ORDERED Plaintiffs' Motion for Judgment is granted.

IT IS FURTHER ORDERED permanently enjoining Proposition 208 in its entirety.

IT IS FURTHER ORDERED Intervenor-Defendants' Motion for Entry of Judgment of Dismissal is denied.

IT IS FURTHER ORDERED directing Plaintiffs to submit a proposed form of judgment, and any application for costs and/or attorneys' fees that they believe is appropriate, within the time provided by the Rules of Civil Procedure.