

STATE OF MICHIGAN  
IN THE SUPREME COURT

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Appeal from the Michigan Court of Appeals  
[Saad, C.J., and Talbot and Fort Hood, JJ.]

DANIEL ADAIR, a Taxpayer of the FITZGERALD  
PUBLIC SCHOOLS; and FITZGERALD PUBLIC  
SCHOOLS, a Michigan municipal corporation, et al,

Plaintiffs-Appellees,

Supreme Court No. 137453

v

Court of Appeals No. 230858

STATE OF MICHIGAN, DEPARTMENT OF  
EDUCATION; DEPARTMENT OF MANAGEMENT  
AND BUDGET; AND ROBERT J. KLEINE,  
TREASURER OF THE STATE OF MICHIGAN,

Defendants-Appellants.

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**DEFENDANTS-APPELLANTS' BRIEF ON APPEAL**

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## QUESTION PRESENTED FOR REVIEW

- I. The prohibition of unfunded mandates (POUM) clause in Michigan's *Headlee Amendment* requires the State to appropriate money to a local unit of government for any "necessary increased costs" that result from a new activity or service or an increase in the level of any activity or service beyond that required by existing law. This Court has further stated that to establish the "extent of the harm," plaintiffs must show that the State-mandated local activity was originated without sufficient State funding for the "necessary increased costs." The question presented is:**

**Whether the prohibition of unfunded mandates in Const 1963, art 9, § 29 requires the plaintiffs to prove specific costs, either through the reallocation of funds or out of pocket expenses, in order to establish their entitlement to a declaratory judgment?**

## INTRODUCTION

Proof of specific costs is essential in order to verify the legitimacy of a claim under the prohibition of unfunded mandates clause of the *Headlee Amendment*. Plaintiffs offered no proof of specific costs that they incurred because of the State's creation of the Center for Educational Performance and Information (CEPI). Despite this, the Court of Appeals ruled in favor of Plaintiffs.

This school funding/*Headlee* case has a long history both in this Court and the Court of Appeals. In 2006, this Court reversed a grant of summary disposition in favor of the State and remanded the matter for a second time to the Court of Appeals. The issue on remand was whether the State violated the "prohibition of unfunded mandate[s]" (POUM) in the *Headlee Amendment*, Const 1963, art 9, § 29, by providing that school districts report certain data electronically to CEPI as a condition of receiving discretionary funding. In its July 3, 2008 ruling, the Court of Appeals granted declaratory relief for Plaintiffs. This decision was wrong because plaintiffs did not submit proof of specific costs that resulted from the increased activity.

The Court of Appeals declared for the first time – and directly contrary to the *Headlee Amendment's* plain language – that a local government need not establish with specificity the amount of necessary costs it will incur as a result of an alleged new State mandate. The POUM clause requires the State to appropriate money to a local unit of government for any "necessary increased costs" that result from a new activity or service or an increase in the level of any activity or service beyond that required by existing law. Since Plaintiffs offered no proof of specific costs, there was no evidence comparing the specific cost of reporting data before the creation of CEPI with the specific cost of reporting data afterward. In fact, the special master that examined the issue of increased costs found that there was "little evidence" that the local school districts had incurred any additional costs as a result of the CEPI implementation. Thus,

there was no proof that any alleged increased costs were necessary, unnecessary, or *de minimis*. The statute defining "necessary costs" requires that the new mandate result in an increase in cost. Without this threshold showing, there is no basis on which to conclude that there was a new or increased cost imposed on the local government. In other words, there is no showing that the State violated the POUM clause.

In 2004, this Court expressly held in *Adair v Michigan* that the *Headlee Amendment* is not necessarily implicated every time the State increases or changes information it requires where the schools' obligation to provide that information already exists.

If Plaintiffs are not required to establish specific "necessary increased costs," there will be a significant increase in litigation against the State every time any reporting requirements change, the required format changes, or technology changes. The State will also be left with a declaratory judgment without guidance as to the appropriation that is sufficient to fund the activity and the prospect of further litigation concerning the appropriate amount of funding. Moreover, the standard created by the published decision of the Court of Appeals will apply to not only school funding questions, but to all issues related to the funding of local government under the *Headlee Amendment*.

The ratifiers of the *Headlee Amendment* did not intend that the State be required to make and disburse an appropriation where there is no proof of specific necessary increased costs associated with a new or increased level of activity or service. This Court should reverse the Court of Appeals and order judgment in favor of Defendants/Appellants.

## STATEMENT OF PROCEEDINGS AND FACTS

Plaintiffs brought this case as an original action in the Court of Appeals. As originally filed, Plaintiffs raised a *Headlee Amendment* challenge to several sections of the Revised School Code, the State School Aid Act, the Pupil Transportation Act, several special education administrative rules, and Executive Order 2000-9. Defendants moved for summary disposition pursuant to MCR 2.116(C)(8), and the Court of Appeals granted the motion and dismissed Plaintiffs' complaint in its entirety with prejudice.<sup>1</sup>

Plaintiffs applied for leave to appeal. In 2002, this Court granted that application, limiting the appeal to three issues:

(1) whether *res judicata* bars the claims of those plaintiffs who also were plaintiffs in *Durant v State of Michigan*, 456 Mich 175 (1997) [*Durant I*];

(2) whether the claims of those plaintiffs who were not parties to *Durant I* are barred because the current plaintiff school districts released or waived their current claims by adopting resolutions that conformed to MCL 388.1611f(8); and

(3) whether the Court of Appeals erred by granting summary disposition for the defendants on the recordkeeping claim that the Court determined was not barred by either *res judicata* or release.<sup>2</sup>

This Court then affirmed the Court of Appeals' decision in part, reversed in part, and remanded.<sup>3</sup> The Court found that all but three of Plaintiffs' claims were barred by *res judicata* or release because the claims were based on statutes or rules in effect during the pendency of *Durant I*,<sup>4</sup> and were raised or could have been raised in that litigation.<sup>5</sup>

With regard to the remaining three claims, this Court held that two were properly dismissed because they were beyond the scope of a *Headlee* challenge; one statute was

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<sup>1</sup> *Adair v Michigan*, 250 Mich App 691; 651 NW2d 393 (2002).

<sup>2</sup> *Adair v Michigan*, 467 Mich 920; 654 NW2d 318 (2002).

<sup>3</sup> *Adair v Michigan*, 470 Mich 105, 129; 680 NW2d 386 (2004) (*Adair I*).

<sup>4</sup> *Durant v Michigan*, 456 Mich 175; 566 NW2d 272 (1997).

<sup>5</sup> *Adair I*, 470 Mich at 125-128.

permissive and the other did not impose any "new" or "increased" requirements on schools as a matter of law.<sup>6</sup>

The third and last post-*Durant I* claim involved CEPI, and related to the districts' claim that they would incur costs in reporting various information to the State. In addressing this claim, this Court first noted that school districts have been under a general obligation to report any and all information the State requires for a long time. But this Court held that the Court of Appeals erred in granting the State's MCR 2.116(C)(8) motion because Plaintiffs' allegation was arguably based on more than just reporting information:

[T]he executive order, which established the Center for Educational Performance and Information [in 2000], empowered the Center to incorporate or implement two statewide databases: the Michigan Education Information System and the Database for Educational Performance and Information. Plaintiffs alleged that this requires school districts to create and maintain student data on an ongoing basis following state-specified data-gathering procedures and to transmit those data over the Internet to the state. The allegation here is that the state is not merely requiring different data from the school districts, but also requiring the districts to actively participate in maintaining data that the state requires for its own purposes.<sup>7</sup>

Consequently, given that mere data reporting is something that districts have long been required to do, and thus would have been barred under the *res judicata* analysis, this Court remanded the CEPI claim to the Court of Appeals on the basis that the claim could be construed as being something different than just a challenge to the type or amount of data districts must report.

On remand, Plaintiffs filed a Third Amended Complaint. Plaintiffs claimed that local school districts must collect, maintain, continually update, and electronically transmit specifically-identified data in a format and according to instructions prescribed by CEPI for five of the six databases within the Michigan Education Information System (MEIS). (Third

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<sup>6</sup> *Adair I*, 470 Mich at 130-132.

<sup>7</sup> *Adair I*, 470 Mich at 129-130.

Amended Complaint, ¶ 16.)<sup>8</sup> The five counts in the complaint related to the five challenged databases, which are all maintained by CEPI for State purposes. Plaintiffs alleged that the State violated the *Headlee Amendment*, i.e., imposed an unfunded mandate on the Plaintiff school districts, by failing to pay Plaintiff school districts for the necessary increased costs associated with that activity. (Third Amended Complaint, ¶¶ 19-20.)

After the first remand, Defendants again moved for summary disposition, this time under MCR 2.116(C)(10). (Defendants' Motion for Summary Disposition, November 4, 2004). The Court of Appeals granted Defendants' motion, and again dismissed the Plaintiffs' complaint in its entirety.<sup>9</sup>

Plaintiffs applied for leave to appeal. (Plaintiffs' Application for Leave to Appeal, September 13, 2005). On March 8, 2006, this Court, in lieu of granting leave to appeal, vacated the opinion of the Court of Appeals and directed it to determine whether the State off-loaded its responsibilities with respect to CEPI onto local school districts without providing the necessary funding.<sup>10</sup>

On April 18, 2006, the Court of Appeals appointed the Honorable Pamela Harwood to serve as Special Master to conduct fact-finding. (Appendix p. 19a, Order, April 18, 2006). It directed her to answer one question: "whether the record-keeping obligations imposed on plaintiff school districts by MCL 388.1752 and Executive Order No. 2000-9 constitute either a new activity or service or an increase in the level of a state-mandated activity or service within the meaning of Mich Const of 1963, art 9, § 29's prohibition of unfunded mandates." The

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<sup>8</sup> The MEIS is a data warehouse that contains six separate databases: the School Code Master (SCM), the Single Record Student Database (SRSD), the Registry of Educational Personnel (REP), the School Infrastructure Database (SID), the Financial Information Database (FID), and the Student Test and Achievement Repository (STAR). CEPI is the state agency that maintains the data within the MEIS for State purposes.

<sup>9</sup> *Adair v Michigan*, 267 Mich App 583; 705 NW2d 541 (2005).

<sup>10</sup> *Adair v Michigan*, 474 Mich 1073; 712 NW2d 702 (2006) (*Adair II*).

Special Master had to consider two factors: (1)"the extent to which plaintiffs possess and use the computer and other facilities and equipment required for plaintiffs to perform data collection, maintenance, and reporting required under the CEPI dictates for purposes unrelated to those dictates;" and (2)"the extent to which, as a result of the adoption of Proposal A, Const 1963, art 9, § 11, the state already furnishes the funding with which plaintiffs purchase such computer and other facilities and equipment."<sup>11</sup>

On April 2, 2007, after the close of discovery, the State filed a motion for summary disposition pursuant to MCR 2.116(C)(10). (Defendants' Motion for Summary Disposition, April 2, 2007). The State contended that an essential element of a *Headlee* claim is proof that the State-mandated activity was originated without sufficient State funding after the *Headlee Amendment* was adopted, or if properly funded initially, that the mandated local role was increased by the State without State funding for the necessary increased costs. Consequently, Plaintiffs' failure to present proofs about the costs of complying with the alleged mandate showed that there is no genuine issue as to any material fact.

Defendants also argued that since the adoption of the Proposal A Amendment to Const 1963, art 9, § 11, the State furnished the funds used by school districts for general school operations. Since any costs Plaintiffs may have incurred for the alleged mandates came from the district's general operating funds, Plaintiffs cannot establish that the State has not furnished the funds for the activities at issue in this case.

Finally, Defendants argued that increases in the quantity of data that is collected and changes in the way that data is reported, the alleged mandated activities, merely continue school districts' long-standing obligation to report information to the State and, therefore, do not implicate the *Headlee Amendment*.

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<sup>11</sup> *Adair II*, 474 Mich at 1073-1074.

The Court of Appeals denied Defendants' motion for summary disposition without prejudice, recognizing that the Special Master could decide motions for summary disposition in the first instance. (Appendix p. 20a, Order, June 13, 2007.)

On June 19, 2007, following receipt of Plaintiffs' trial brief, the State filed a renewed motion for summary disposition. (Defendants' Renewed Motion For Summary Disposition Based on Fatal Admissions Made in Plaintiffs' Trial Brief, June 18, 2007.) Plaintiffs stated that they "did not intend to introduce evidence as to the amount by which the State is underfunding these State required activities and services." (Appendix p.23a, Plaintiffs' Trial Brief, p. 16.) Plaintiffs claimed that it was merely their "burden to establish they are incurring necessary increased costs for the activities and services that were either newly required of them since 1978 or that represent an increase in the level of activities and services required of them in 1978 and that no appropriation was made by the Michigan Legislature and disbursed to pay for those necessary increased costs." The State's renewed motion again argued that proof of necessary increased costs is an essential element of a claim under the POUM clause of the *Headlee Amendment*. (Defendants' Renewed Motion For Summary Disposition Based on Fatal Admissions Made in Plaintiffs' Trial Brief, June 18, 2007.) This motion was denied without prejudice. (Appendix p. 25a, Order, June 26, 2007.)

On July 17, 2007, in response to motions filed by the parties, the Special Master ruled that the relevant time period for Plaintiffs' claim was December 23, 1978, the effective date of the *Headlee Amendment*. It was further ruled that the relevant point in time for determining whether Plaintiffs' claim is barred by *res judicata* was July 31, 1997, the date of the Supreme Court's decision in *Durant I*.

On July 19, 2007, following the close of Plaintiffs' proofs, the State brought a motion for a directed verdict on the grounds that Plaintiffs' claims failed, as a matter of law, because

Plaintiffs had not offered any specific proofs verifying necessary increased costs and, therefore, had failed to meet their burden of proof. The Special Master took that motion under advisement. (Appendix p. 77a; Tr., pp. 1350-1351.)

On January 27, 2008, the Special Master issued an opinion, noting that there was little dispute over the facts. The dispute was over the legal conclusions, or inferences, to be drawn from the facts. The Special Master's findings of fact are contained on pages 10–23 of the opinion. (Appendix pp. 160a; 169a-182a; Special Master's Opinion).

The Special Master concluded that (1) the record keeping requirements imposed by MCL 388.1752 and EO 2000-9 violate the POUM clause of the *Headlee Amendment* because they constitute an increase in the level of an activity beyond that required prior to 1997, the conclusion of *Durant I*; (2) despite not showing actual costs of the alleged mandates, Plaintiffs met their burden of proof with respect to the "necessary increased costs" requirement of Const 1963, art 9, § 29; and (3) the increased record keeping requirements have resulted in additional necessary costs to school districts that have not been funded by the State.

On July 3, 2008, the Court of Appeals granted a declaratory judgment in favor of Plaintiffs and denied the State's motion for summary disposition. (Appendix p. 204a, Judgment on Second Remand, July 3, 2008.) The Court of Appeals adopted the Special Master's findings of fact and conclusions of law, except as specifically noted. On August 27, 2008, the Court of Appeals issued an Order denying the State's motion for reconsideration. (Appendix p. 213a, Order, August 27, 2008.)

On April 3, 2009, this Court granted leave to appeal the July 3, 2008 judgment of the Court of Appeals. (Appendix p. 214a, Order, April 3, 2009.) For purposes of the State's application for leave to appeal in Supreme Court Docket No. 137453, leave was granted, limited to the issue of "whether the prohibition of unfunded mandates in Const 1963, art 9, § 29 requires

the plaintiffs to prove specific costs, either through the reallocation of funds or out of pocket expenses, in order to establish their entitlement to a declaratory judgment."<sup>12</sup>

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<sup>12</sup> This Court also granted plaintiff's application for leave to appeal in Supreme Court Docket No. 137424 limited to the issue of whether plaintiffs are entitled to recover the "costs incurred in maintaining" this suit pursuant to Const 1963, art 9, § 32. Defendants will address this issue in their responsive brief in Docket No 137424. Accordingly, this brief only discusses the first issue.

## ARGUMENT

**I. The prohibition of unfunded mandates (POUM) clause in Michigan's *Headlee Amendment* requires the State to appropriate money to a local unit of government for any "necessary increased costs" that result from a new activity or service or an increase in the level of any activity or service beyond that required by existing law. This Court has determined that to establish the "extent of the harm," Plaintiffs must show that the State-mandated local activity was originated without sufficient State funding for the "necessary increased costs." The POUM clause requires the plaintiffs to prove specific costs, either through the reallocation of funds or out of pocket expenses, in order to establish their entitlement to a declaratory judgment.**

**A. Standard of Review**

This Court reviews *de novo* a trial court's decision to grant or deny a motion for summary disposition.<sup>13</sup> Likewise, questions of constitutional and statutory construction are reviewed *de novo* by this Court.<sup>14</sup>

When interpreting constitutional provisions, this Court's primary objective "is to realize the intent of the people by whom and for whom the constitution was ratified."<sup>15</sup> In analyzing constitutional language, the first inquiry is to determine if the words have a plain meaning or are obvious on their face.<sup>16</sup> "There is a presumption that words in the Constitution have been used according to their plain, natural import, and a court is not at liberty to disregard the plain meaning of the words in order to search for some other conjectured intent."<sup>17</sup> "[I]t is not to be supposed that [the people] have looked for any dark or abstruse meaning in the words employed, but rather that they have accepted them in the sense most obvious to the common understanding,

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<sup>13</sup> *City of Taylor v Detroit Edison Co*, 475 Mich 109, 115; 715 NW2d 28 (2006).

<sup>14</sup> *City of Taylor*, 475 Mich at 115.

<sup>15</sup> *Studier v Michigan Pub School Employees Retirement Bd*, 472 Mich 642, 652; 698 NW2d 350 (2005), quoting *Wayne Co v Hathcock*, 471 Mich 445, 468; 684 NW2d 765 (2004).

<sup>16</sup> *Silver Creek Drain Dist v Extrusions Division Inc*, 468 Mich 367, 374-375; 663 NW2d 436 (2003).

<sup>17</sup> *Council 23 AFSCME v Wayne Co Civil Service Comm*, 32 Mich App 243, 247-248; 188 NW2d 206 (1971).

and ratified the instrument in the belief that that was the sense designed to be conveyed."<sup>18</sup>

"[Constitutional] provisions must be interpreted within the context of the times."<sup>19</sup> The same general principles to be applied in construing statutes may be utilized, and govern, in the construction of the constitution.<sup>20</sup>

When interpreting a statute, the Court examines the language of the statute itself. "If the statute is unambiguous it must be enforced as written."<sup>21</sup> "It is axiomatic that statutory language expresses legislative intent."<sup>22</sup> When interpreting a statute, this Court attempts to give effect to the Legislature's intent by looking at the statutory text, giving meaning to every word, phrase, and clause in the statute and considering both their plain meaning and their context.<sup>23</sup> "A fundamental principle of statutory construction is that a clear and unambiguous statute leaves no room for judicial construction or interpretation."<sup>24</sup> Where the statute unambiguously conveys the Legislature's intent, the proper role of a court is simply to apply the terms of the statute to the circumstances in a particular case.<sup>25</sup>

## B. Analysis

The POUM clause and the *Headlee* implementing legislation prohibit the State from shifting fiscal responsibilities for services from State government to local government. In order to achieve this end, the POUM clause requires the State to appropriate sufficient funds to local units of government for necessary increased costs when the State mandates an increased level of

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<sup>18</sup> *Traverse City School Dist v Attorney General*, 384 Mich 390, 405; 185 NW2d 9 (1971) (citations omitted).

<sup>19</sup> *People v Neumayer*, 405 Mich 341, 365; 275 NW2d 230 (1979).

<sup>20</sup> *Board of Education v Elliott*, 319 Mich 436, 29 NW2d 902 (1947).

<sup>21</sup> *Title Office, Inc. v Van Buren Co Treasurer*, 469 Mich 516, 519; 676 NW2d 207 (2004).

<sup>22</sup> *Michigan Dep't of Transportation v Tomkins*, 481 Mich 184, 191; 749 NW2d 716 (2008) (Citations omitted).

<sup>23</sup> *Shinholster v Annapolis Hosp*, 471 Mich 540, 548; 685 NW2d 275 (2004)

<sup>24</sup> *Tomkins*, 481 Mich 184, 191 (Citations omitted).

<sup>25</sup> *Tomkins*, 481 Mich 184, 191 (Citations omitted).

activities or services. But a State appropriation is not required unless the changes in the mandated activities or services result in a specific net increase in cost to local units of government. Applying the plain language of Michigan law, the determination of net increased costs requires a comparison of the specific current costs of providing mandated activities and services and the specific costs of performing the increased level of the activities or services. The Court of Appeals improperly determined that a plaintiff in a declaratory action can establish a *Headlee* violation under the POUM clause by only establishing a complete failure on the part of the State to fund an increased level of activity without proof of any specific costs. The factual record does not support the conclusion that the revision to the reporting requirements results in net necessary increases in costs to the local school districts. This Court should reverse the Court of Appeals and enter judgment in favor of the State Defendants-Appellants.

1. **The *Headlee Amendment* and the implementing legislation only require a State appropriation to local units of government for necessary increased costs when the State mandates an increased level of activities or services.**

Sections 25 through 34 of article 9 of the Constitution of 1963, commonly known as the *Headlee Amendment*, became effective on December 23, 1978. The *Headlee Amendment* "imposes on state and local government a fairly complex system of revenue and tax limits."<sup>26</sup>

Art 9, § 25 provides in pertinent part that:

The state is prohibited from requiring any new or expanded activities by local governments without full state financing, from reducing the proportion of state spending in the form of aid to local governments, or from shifting the tax burden to local government.<sup>27</sup>

These requirements are implemented in § 29, which provides in part:

The state is hereby prohibited from reducing the state financed proportion of the necessary costs of any existing activity or service required of units of Local Government by state law. A new activity or service or an increase in the level of

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<sup>26</sup> *Durant I*, 456 Mich at 182.

<sup>27</sup> Const 1963, art 9, § 25.

any activity or service beyond that required by existing law shall not be required by the legislature or any state agency of units of Local Government, unless a state appropriation is made and disbursed to pay the unit of Local Government for any necessary increased costs. . .<sup>28</sup>

The first sentence, which addresses activities and services existing in December 23, 1978, the effective date of the *Headlee Amendment*, is called the "maintenance of support" or "MOS" clause. The second sentence of § 29 addresses new activities or services or increases in the level of activities or services beyond those existing in December 1978 and is called the "prohibition of unfunded mandate" or "POUM" clause.<sup>29</sup> The POUM clause is at issue in the present case.

In an attempt to ascertain the intent of the voters when they enacted § 29, this Court has said:

Having placed a limit on state spending, it was necessary to keep the state from creating loopholes either by shifting more programs to units of local government without the funds to carry them out, or by reducing the state's proportion of spending for "required" programs in effect at the time the Headlee Amendment was ratified.<sup>30</sup>

Under § 29, the State may not burden local units of government by improper revenue shifting.<sup>31</sup> In *Judicial Attorneys Ass'n v Michigan*, this Court has articulated the parameters of § 29:

The first sentence of this provision prohibits reduction of the state proportion of necessary costs with respect to the continuation of state-mandated activities or services. The second sentence requires the state to fund any additional **necessary costs** of newly mandated activities or services and increases in the level of such activities or services from the 1978 base year. This language does not guarantee that local units' spending levels will not increase from the 1978 level. Rather, the Headlee Amendment only guarantees that the state will not reduce its proportion of the necessary costs of existing activities or services, **and that the state will pay entirely for necessary costs when it mandates new activities or services or to the extent the state increases the level of an existing activity or service.** Increased levels of local spending attributable to other causes, e.g., inflation or the

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<sup>28</sup> Const 1963, art 9, § 29.

<sup>29</sup> *Adair I*, 470 Mich at 111.

<sup>30</sup> *Livingston Co v Dep't of Management & Budget*, 430 Mich 635, 644; 425 NW2d 65 (1988).

<sup>31</sup> *Oakland Co v Michigan*, 456 Mich 144, 150; 566 NW2d 616 (1997).

greater utilization of a program by the public, are not addressed by this provision of the Headlee Amendment.<sup>32</sup>

Consequently, this Court recognized that not every change in school activities established by statute or rule constitutes a new or increased level of an activity or service requiring State funding under the *Headlee* Amendment.<sup>33</sup> This Court has often stated that at its core, art 9, § 29 reflects a voter effort to prevent the Legislature from shifting fiscal responsibilities from State government to local government.<sup>34</sup> But unless the local government establishes its specific increased necessary costs from the new activity or service, there can be no shifting of fiscal responsibilities under *Headlee*.

Previously in this case, this Court addressed the special pleading requirements necessary for claims brought under Const 1963, art 9, § 29:

[P]laintiffs must allege the type and extent of the harm so that the court may determine if a § 29 violation occurred for purposes of making a declaratory judgment. In that way, the state will be aware of the financial adjustment necessary to allow for future compliance.<sup>35</sup>

This Court added that to establish the "extent of the harm," Plaintiffs must show that the State-mandated local activity was originated without sufficient State funding after the *Headlee Amendment* was adopted, or, if properly funded initially, that the mandated local role was increased by the State without State funding for the necessary increased costs.<sup>36</sup>

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<sup>32</sup> *Judicial Attorneys Ass'n v Michigan*, 460 Mich 590, 595; 597 NW2d 113 (1999), quoting *Mayor of Detroit v Michigan*, 228 Mich App 386, 396-398; 579 NW2d 378 (1998) (emphasis added).

<sup>33</sup> *Adair I*, 470 Mich at 112. See also MCL 21.234(5).

<sup>34</sup> *Adair I*, 470 Mich at 112. See also *Judicial Attorneys*, 460 Mich at 595; *Schmidt v Dep't of Ed*, 441 Mich 236, 250; 490 NW2d 584 (1992); *Durant v State Bd of Ed*, 424 Mich 364, 379; 381 NW2d 662 (1985).

<sup>35</sup> *Adair I*, 470 Mich at 119-120, quoting from *Oakland Co*, 456 Mich at 166. While *Oakland County* dealt with MOS claims, the Supreme Court has held that the requirements of the POUM clause are similar. See *Adair I*, 470 Mich at 120, n 13.

<sup>36</sup> *Adair I*, 470 Mich at 111.

To implement § 29 of the *Headlee* Amendment, the Legislature enacted 1979 PA 101, now codified in MCL 21. 231 *et seq* as §§ 1 through 14 of the State Disbursements to Local Government Units Act (*Headlee* implementing act). In its remand order, this Court specifically directed the Court of Appeals to consider the provisions of this statute:

In performing its factfinding functions on remand, the Court of Appeals may employ the referral procedure prescribed by MCL 600.308a(5), and **shall** apply the provisions of MCL 21.231 *et seq.*, and the definitions contained therein.<sup>37</sup>

The *Headlee* implementing statute defines the term "necessary cost" as:

[T]he net cost of an activity or service provided by a local unit of government. The net cost shall be the actual cost to the state if the state were to provide the activity or service mandated as a state requirement, unless otherwise determined by the legislature when making a state requirement. Necessary cost does not include the cost of a state requirement if the state requirement satisfies one or more of the following conditions:

- (a) The state requirement cost does not exceed a *de minimis* cost.
- (b) The state requirement will result in an offsetting savings to an extent that, if the duties of a local unit which existed before the effective date of the state requirement are considered, the requirement will not exceed a *de minimis* cost.
- (c) The state requirement imposes additional duties on a local unit of government which can be performed by that local unit of government at a cost not to exceed a *de minimis* cost.
- (d) The state requirement imposes a cost on a local unit of government that is not recoverable from a federal or state categorical aid program, or other external financial aid.<sup>38</sup>

The *Headlee* implementing statute defines "de minimis cost" as "a net cost to a local unit of government resulting from a state requirement which does not exceed \$300.00 per claim."<sup>39</sup>

Consistent with the implementing act, this Court has stated that "necessary costs" are those essential to maintain a mandated program.<sup>40</sup> Actual cost in the marketplace is also a

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<sup>37</sup> *Adair II*, 474 Mich at 1073-1074.(emphasis added).

<sup>38</sup> MCL 21.233(6).

<sup>39</sup> MCL 21.232(4)

<sup>40</sup> *Durant v State Bd of Ed*, 424 Mich 364, 391; 381 NW2d 662 (1985).

reliable measure of what must be paid in order for a service or activity to be provided.<sup>41</sup> The Court of Appeals previously interpreted this language to mean that "absent countervailing evidence—[]whether based on realized costs or theoretical costs—actual costs would be satisfactory as a prima facie indicator of 'necessary costs.'"<sup>42</sup>

In *Oakland County*, this Court stated that Const 1963, art 9, § 29 directs the State to reimburse only the necessary costs of a state requirement and explained the meaning of "necessary costs" as used in § 29:

The Headlee implementing act defines a "necessary cost" as "the net cost of an activity or service provided...." MCL 21.233(6); MSA 5.3194(603)(6). The net cost is the actual cost the state would incur if it provided the activity. Also, a cost incurred by a local unit because of a state mandate is not a necessary cost if less than "a *de minimus* cost." A *de minimus* cost is "a net cost to a local unit of government resulting from a state requirement which does not exceed \$300.00 per claim." MCL 21.232(4); MSA 5.3194(602)(4).<sup>43</sup>

Since the cases in *Oakland County* were decided by summary disposition, this Court noted that the parties did not have an opportunity to develop a record showing necessary costs of the state requirement; including proofs showing the "claims" for which the local units of government sought reimbursement. "These proofs are needed for a determination of what constitutes a 'claim' for purposes of MCL 21.234(4); MSA 5.3194(602)(4)."<sup>44</sup> This Court stated that on remand, "the trial court must decide what costs are necessary county foster care costs, including whether any fall within the *de minimus* exclusion."<sup>45</sup>

In 2004, this Court expressly held in *Adair I* that the *Headlee Amendment* is not necessarily implicated every time the State increases or changes information it requires where

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<sup>41</sup> *Durant*, 424 Mich at 391.

<sup>42</sup> *Durant v Dep't of Ed (On Third Remand)*, 203 Mich App 507, 514; 513 NW2d 195 (1994).

<sup>43</sup> *Oakland Co*, 456 Mich at 163 - 164.

<sup>44</sup> *Oakland Co*, 456 Mich at 165.

<sup>45</sup> *Oakland Co*, 456 Mich at 165.

the schools' obligation to provide that information already exists.<sup>46</sup> In this case, however, the Court of Appeals specifically rejected the State's argument that the Plaintiffs must prove – as an element of their claim under the POUM clause – that the alleged new activity or increase in the level of an activity resulted in the districts actually incurring additional specific costs or out of pocket expenses. (Appendix, pp. 204a-206a, Court of Appeals Opinion on Second Remand, pp. 1-3.) Plaintiffs made a calculated decision not to introduce evidence of the amount they claim the State has not funded any new or increased activities (Appendix p. 23a, Plaintiffs' Trial Brief, p 16).

2. **A State appropriation is not required unless the changes in the mandated activities or services result in a specific net increase in cost to local units of government. The determination of net increased costs requires a comparison of the specific current costs of providing mandated activities and services and the specific costs of performing the increased level of the activities or services.**

To establish a violation under the plain language of the *Headlee Amendment* and its implementing statutes, a plaintiff must show either that the alleged new activity was not sufficiently funded initially, or that the alleged activity was later increased without sufficient funding for the necessary increased costs. In either case, Plaintiffs must establish the specific costs required to comply with the new or increased activity and compare it with the preexisting cost of performing the activities or services in order to determine whether the level of funding, if any, is sufficient.

If the activity does not result in necessary increased costs, Plaintiffs are not entitled to declaratory relief. Since Plaintiffs made a calculated decision not to offer any proofs of specific costs, their claim should fail. The *Headlee* implementing statute requires the Legislature to fund the **necessary increased costs** associated with new or increased activities or services required by

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<sup>46</sup> *Adair I*, 470 Mich at 129.

the State.<sup>47</sup> If there are no necessary costs associated with an alleged activity or service, the *Headlee Amendment* is not violated and relief is not available.

The POUM clause requires the State to appropriate money to a local unit of government for any "necessary increased costs" that result from a new activity or service or an increase in the level of any activity or service beyond that required by existing law. Since Plaintiffs offered no proof of specific costs here, there was no evidence that would establish whether any alleged costs were necessary, unnecessary, or *de minimis*. The statute defining "necessary costs" requires that the new mandate result in **an increase in cost**. Without this threshold showing, there is no basis on which to conclude that there was a new or increased necessary cost imposed on the local government, and there is no showing of a violation of the POUM clause.

For example, this Court recognized that school districts have been under a general obligation to report any and all information the State requires for a long time.<sup>48</sup> Thus, school districts have historically incurred costs related to reporting this data to the State. In order to determine whether the school districts have incurred necessary increased costs, section 3(6) of the *Headlee* Implementing Act, MCL 21.233(6), which defines "necessary costs" requires that the specific cost of reporting data before the change of the State requirement be compared with the specific cost of reporting data after the change. This comparison must take into account any offsetting savings that are incurred due to advances in technology and other efficiencies.

3. **The Court of Appeals standard does not properly address necessary increased costs under the POUM because it fails compare the specific preexisting costs to local units of government and the specific costs after the change in mandated activities or services.**

For this issue of first impression, the Court of Appeals created a new standard for establishing a *Headlee* violation in a claim filed pursuant to the POUM clause:

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<sup>47</sup> MCL 21.235.

<sup>48</sup> *Adair I*, 470 Mich at 129.

To demonstrate the existence of such an off-loading of state funding responsibilities and to demonstrate actual or imminent injury, we conclude that the school districts must only establish (1) an increase in the level of activity or services mandated by the state, and (2) a complete failure on the part of the state to provide any funding to off-set the necessary costs to be incurred. (Appendix p. 206a, Court of Appeals Opinion on Second Remand, p.3.)

Contrary to the plain language of the *Headlee Amendment* and its implementing statutes, under the Court of Appeals' standard, a plaintiff in a declaratory action can establish a *Headlee* violation under the POUM clause by simply establishing a complete failure on the part of the State to fund an increased level of activity without proof of any specific costs and without regard to whether there is in fact a net increase in cost. Under this new standard, a claimant can prevail even though the alleged new activity does not result in any essential costs to maintain the program. A claimant would not be required to demonstrate the amount of funding necessary to provide the activity, but would merely have to demonstrate a lack of any funding by the State. Moreover, the claimant would not have to show that costs to perform the new activity exceed a *de minimis* cost. In other words, the Court of Appeals has eliminated the requirement to prove specific "necessary increased costs."

If Plaintiffs are relieved of the requirement to establish specific "necessary increased costs," the State is left with a declaratory judgment that not only fails to provide guidance as to what amount an appropriation should be in order to be sufficient to fund the activity but also promises continued litigation concerning the appropriate amount of funding. Moreover, there will be a significant increase in litigation against the State every time any reporting requirements change, the required format changes, or technology changes. The standard created by the published decision of the Court of Appeals will apply to not only school funding questions, but to all issues related to the funding of local government under the *Headlee Amendment*.

The Court of Appeals attempted to distinguish this Court's decisions in *Durant* and *Oakland Co* because they were brought under the MOS clause.<sup>49</sup> But this Court has consistently held that the two sentences of § 29 must be read together because they were aimed at alleviating two possible manifestations of the same voter concern.<sup>50</sup> "Both sentences clearly reflect an effort on the part of the voters to forestall any attempt by the Legislature to shift responsibility for services to the local government, once its revenues were limited by the Headlee Amendment, in order to save the money it would have had to use to provide the services itself."<sup>51</sup> Moreover, this Court has previously rejected claims that cases analyzing the MOS clause are inapplicable to an analysis of the POUM clause.<sup>52</sup>

Both the MOS and POUM clauses require a determination of the amount of necessary costs of State required activities. The MOS clause is aimed at existing services or activities already required of local government. The POUM clause addresses future services or activities. Thus, both clauses of § 29 require a claimant to quantify the necessary costs of state mandated activities. The fact that this case involves a declaratory judgment, not a claim for money damages, does not change the requirement under the POUM clause that the State need only fund State requirements that result in "necessary increased costs." If the plaintiffs are not required to demonstrate that a State requirement will result in actual out-of-pocket expenses, then there is no showing of any "necessary increased costs" to be incurred. And the local school districts are in the best position to demonstrate that the revised reporting requirements will result in a net increase in their operating costs, rather than the Court presuming it.

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<sup>49</sup> *Adair*, 279 Mich App at 507, 512; 760 NW2d 544 (2008) (Appendix, p 205a).

<sup>50</sup> *Judicial Attorneys Ass'n*, 460 Mich at 597; *Schmidt v Dep't of Ed*, 441 Mich 236, 250; 490 NW2d 584 (1992), quoting *Durant v State Bd of Ed*, 424 Mich 364, 379; 381 NW2d 662 (1985)**Error! Bookmark not defined.**

<sup>51</sup> *Durant*, 424 Mich 364, 379-380.

<sup>52</sup> *Adair I*, 470 Mich at 120, n 13; *Judicial Attorneys Ass'n*, 460 Mich at 598 n 2.

If this Court upholds the Court of Appeals' determination that plaintiffs seeking declaratory relief in a claim under the POUM clause are not required to demonstrate specific increased necessary costs, the State would be left in an untenable situation in *Headlee* funding cases for three reasons. First, in every circumstance where there is an increased level of activity, the State is required to make an appropriation to avoid a declaratory action. The State is left to accept that every change in State required activities of local units of government will necessarily result in necessary increased costs and must be funded or the State will be faced with paying costs of a *Headlee* suit. Second, if funding from the State is presumptively required, the State is left guessing what appropriation is sufficient to avoid a shifting of a funding obligation to the local government – the standard from the Court of Appeals does not require proof of the specific increase in cost. Third, such a guessing-game promotes repeated and protracted *Headlee* litigation because the local unit of government could challenge the sufficiency of the appropriation at a later date, and it must be presumed that at some point a *Headlee* plaintiff would be required to demonstrate a lack of funding for necessary costs. Simply put, the Court of Appeals' opinion does not promote good government, judicial economy, or an analytical framework for *Headlee* cases consistent with the constitution, statute, and case law. The consequences of this decision will ripple far beyond the school reporting functions at issue in this case.

4. **The Plaintiffs failed to prove that they will incur necessary increased costs as a result of changes in reporting requirements because they did not present evidence comparing the specific cost of reporting data to the State prior to and after the creation of CEPI.**

The Court of Appeals' determination is especially troubling since there was little evidence in this case that showed the districts incurred actual additional costs or expenditures in order to comply with CEPI's reporting requirements:

There was little evidence of local districts or ISDs incurring actual additional costs or expenditures as a result of the implementation of the CEPI databases. There has been some hiring of additional staff and payment of overtime to meet the deadlines; after all, funding needs trump other concerns. Similarly, some local districts and ISDs incurred actual costs for programming changes but most did not due to contractual arrangements with vendors or in-house IT staff [Appendix pp. 182a-183a, Special Master Opinion, pp 23-24] [Citations omitted].

The Court of Appeals' standard is fundamentally at odds with the common understanding of the people who ratified the *Headlee Amendment*. It allows a claimant to obtain declaratory relief under the POUM clause despite the fact that a new activity or increased level of activity results in no essential additional expenditure of local funds.

To meet their burden, Plaintiffs should be required to show that they actually incurred, and will continue to incur, specific necessary costs because of CEPI. That is, they must show that they incurred, and will continue to incur, new or increased essential **net** costs that were more than *de minimis* and that were not recoverable from a federal or state categorical program. Plaintiffs did not meet this burden.

Plaintiffs claimed that they incurred two types of costs: (1) software costs, and (2) personnel costs. But the evidence at trial demonstrated that districts were not required to purchase or upgrade software to comply with the State's data reporting requirements after the creation of CEPI. The evidence further demonstrated that, with one exception, districts did not hire any new staff or pay any existing staff overtime for their work on CEPI-related activities.

While some districts chose to spend their general operating funds to buy or upgrade software packages, those expenditures did not constitute "necessary" costs under the *Headlee Amendment*. CEPI has never required school districts to use particular vendors and has never required school districts to use particular software to report data to the CEPI databases.

(Appendix p. 73a, Formberg, Tr 1144; Appendix p. 107a, Howell, Tr 2022, 2045; Appendix p. 88a, Ropp, Tr 1804; Appendix p. 82a, Erickson, Tr 1593; Appendix pp. 31a, 33a, Rocho, Tr 247,

267; Appendix p.37a, Martin, Tr 560-561; Appendix p. 45a, Cardinali, Tr 690; Appendix pp. 54a, 56a, Holloway, Tr 771, 779; Appendix p. 61a, Scherer, Tr 837; Appendix p. 66a, Arens, Tr 902). No particular type of computer is required to submit data to the CEPI databases (Appendix p. 88a, Ropp, Tr 1804). Districts use multiple vendors to run software systems, and CEPI works with the districts and their vendors (Appendix p. 106a, Howell, Tr. 2021). Furthermore, the evidence at trial showed that a district could submit data to the CEPI databases without purchasing new or upgrading existing software (Appendix p. 44a, Cardinali, Tr 687; see generally Appendix p. 90a, Howell's testimony).

The parties stipulated that some of the districts contract with Computer Management Technologies, a software vendor, to assist them with their CEPI data submissions. And districts likely paid Computer Management Technologies for those services. But the districts were not required to contract with Computer Management Technologies, and they could have made their data submissions without contracting with Computer Management Technologies. In fact, many have.

The testimony demonstrated that there are several options available for districts to choose from in order to make their required submissions. Plaintiffs' witnesses testified that those districts that use the Macomb ISD software did not have to purchase any new software or upgrade any software to submit their data to CEPI (Appendix pp. 44a, 49a, Cardinali, Tr 687, 705; Appendix p. 38a, Martin, Tr 564-564). This is also true of the over sixty school districts that use the Wayne RESA software. Those districts spent no public funds on software because of CEPI (Appendix pp. 27a, 29a, Rocho, Tr 174, 216; Appendix p. 158a, Gerrity deposition in lieu of testimony, 50-51).

Furthermore, for each of the databases, districts have available to them free options that they can use to make their CEPI submissions.<sup>53</sup> For the REP, districts can submit using either a text editor, which comes free with all Microsoft Windows software, or by logging on to the State operated website and entering in their data. Over 60% of school districts submit their REP data to the State through the online application (Appendix p. 81a, Erickson, Tr. 1483). Likewise, districts can submit their SID data to the State by using the state operated website. Over 97% of districts make their SID submission using the online application (Appendix p. 84a, Erickson, Tr. 1615).

For SRSD, a district can again use a text editor, or a district can use the software the Macomb ISD has developed and made available to districts for free. The Macomb ISD software does everything a district needs to make a valid SRSD submission (Appendix pp. 37a-39a, Martin, Tr. 562-563, 567-568).

For the FID, a district can make its submission using simple, off the shelf software like Microsoft Excel – software that at least two of the representative districts testified they used long before CEPI (Appendix p. 70a, Reynolds, Tr 993; Appendix p.52a, Holloway, Tr 753) (*See* generally Howell testimony for a description of the various ways a district can submit data to each of the CEPI databases, Appendix p. 90a).

Districts complain that some of these free options are not as convenient as their privately purchased software packages. But the substantial evidence in the record demonstrates that there are alternate, less costly ways to perform an activity. A school district's decision to spend *more* money for convenience cannot be considered necessary costs within the meaning of art 9, § 29 of

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<sup>53</sup> The MEIS is a data warehouse that contains six separate databases: the School Code Master (SCM), the Single Record Student Database (SRSD), the Registry of Educational Personnel (REP), the School Infrastructure Database (SID), the Financial Information Database (FID), and the Student Test and Achievement Repository (STAR). CEPI is the state agency that maintains the MEIS.

the *Headlee Amendment*.<sup>54</sup> But *Headlee* does not require the State's taxpayers to foot the bill for a district's decision to spend more money for enhanced software that may make it more convenient for that district to comply with CEPI. This is particularly true when other school districts have had no trouble fully complying with CEPI without incurring additional software expenses.

A school district's decision on how it chooses to implement a requirement should not be the legal test for deciding if *Headlee* is implicated. Simply put, *Headlee* does not require such a subsidy.

Plaintiffs have not proved that they expended necessary costs related to software. Whatever costs may have been expended were not necessary costs. The record is clear that some districts chose to make those expenditures; districts could have chosen to use any of the free or less costly options available to make their CEPI submissions. Those Plaintiffs that chose to contract with Computer Management Technologies to make data collection and reporting more convenient were not making expenditures that were essential or indispensable to their data collection and reporting duties. Therefore, to the extent districts chose to spend money on software or software upgrades, those expenditures were not necessary costs under the *Headlee Amendment*.

As to personnel, Plaintiffs again did not prove that they incurred necessary costs as a result of CEPI. Plaintiffs' assertion that their existing staff had to spend more time collecting and reporting data does not satisfy their burden of proving "necessary costs." Plaintiffs' argument ignores the definition of "necessary costs." The *Headlee Amendment* implementing legislation defines "necessary costs" as net costs that are more than *de minimis*. Plaintiffs purposefully provided no proofs that any of the representative districts in this case incurred net personnel

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<sup>54</sup> *Durant*, 186 Mich App 83, 112-113; 463 NW2d 461 (1990).

costs because of data collection and reporting. While people may have spent more time collecting and reporting data after the creation of CEPI than they did before, those people were not paid more for their time.<sup>55</sup> In other words, their duties may have increased with respect to data collection and reporting, but those increased duties did not result in net increased costs to the district. In this regard the *Headlee* implementing statute specifically provides that where the state imposes additional duties on a local unit of government, but those duties do not result in more than a *de minimis* net increased cost, those duties are not necessary costs: "Necessary cost does not include the cost of a state requirement if. . . the state requirement imposes additional duties on a local unit of government which can be performed by that local unit of government at a cost not to exceed a *de minimis* cost."<sup>56</sup>

Furthermore, Plaintiffs offered no witnesses from any of the focus districts who testified about whether overall the school districts spent more or less time on data collection and reporting following the creation of CEPI in 2000 than they did before. Rather, individual employees testified that they spent more time collecting and reporting data, but those employees could not speak to whether the district as a whole spent more time on data collection or reporting. In fact, cost records and time records for data collection were not historically kept (Appendix p. 40a, Martin, Tr 593). Regardless, Plaintiffs failed to prove that any of the representative districts incurred net increased costs because of CEPI.

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<sup>55</sup> The only person that testified about receiving overtime was Holly Scherer, and she testified that her entire overtime payment was less than \$100.00 (Appendix pp. 60a, 62a, Scherer, Tr 813, 843). This is *de minimis*.

<sup>56</sup> MCL 21.235.

The Court of Appeals, however, ruled that Plaintiffs were entitled to declaratory relief under its new standard that only requires a new mandated activity and a complete failure to provide any funding. Under this new standard, the Court of Appeals did not examine the essential cost of performing the activity or the *de minimis* standard.

This Court has held that proof of actual necessary costs is an essential element of a *prima facie Headlee* claim.<sup>57</sup> The Court of Appeals failed to require proof of actual necessary costs. Instead, the Court of Appeals erroneously held that it was sufficient to merely establish a complete failure to provide any funding. Plaintiffs have never established a baseline against which necessary costs can be computed, nor have they provided any more than vague assertions that they even incurred actual costs associated with CEPI. And in those few instances where they can actually point to an actual cost incurred, the costs were either *de minimis* or unnecessary. Thus, Plaintiffs did not prove that the State required the districts to incur increased necessary costs associated with CEPI. But, the Court of Appeals still granted declaratory relief under its new "complete failure to provide funding" standard. Accordingly, this Court should reverse the Court of Appeals.

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<sup>57</sup> *Oakland Co.*, 456 Mich at 163-165, 168.

## CONCLUSION

The POUM clause requires a State appropriation to local units of government for necessary increased costs when the State mandates an increased level of activities or services. A State appropriation is not required unless the changes in the mandated activities or services result in a specific net increase in cost to local units of government. The determination of net increased costs requires a comparison of the specific current costs of providing mandated activities and services and the specific costs of performing the increased level of the activities or services. The Court of Appeals improperly determined that a plaintiff in a declaratory action can establish a *Headlee* violation under the POUM clause by only establishing a complete failure on the part of the State to fund an increased level of activity without proof of any specific costs. This Court should reverse the Court of Appeals and enter judgment in favor of the State Defendants-Appellants.

School districts have historically had the responsibility to collect, maintain, and report information to the State in order to comply with requirements of State and federal law. While the requirements of CEPI may have changed the way school districts electronically transmit data to the State, this change is not one that constitutes a new or increased level of an activity requiring State funding under the *Headlee Amendment*, *i.e.*, an off-loading of State funding responsibility.

The effect of the Court of Appeals' decision is to allow prospective declaratory relief concerning *any* increase in the level of an activity or service over that required by existing law under the *Headlee Amendment*, without proper consideration of whether an actual and essential increase in costs exists. The Court of Appeals' decision would also allow relief without regard to whether the amount of necessary cost incurred to perform a mandated activity falls within the *de minimis* exclusion, mandated by MCL 21.232(4). The Court of Appeals' opinion does not

promote good government, judicial economy, or an analytical framework for *Headlee* cases consistent with the constitution and statutes. The decision is contrary to the common understanding of the people that ratified the *Headlee Amendment* and should be reversed.

**RELIEF SOUGHT**

For the reasons set forth above, Defendants/Appellants respectfully request that this Honorable Court to issue an order reversing the Court of Appeals judgment and ordering judgment in favor of Defendants/Appellants.

Respectfully submitted,

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