

**S298916**

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**IN THE SUPREME COURT  
OF THE STATE OF CALIFORNIA**

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CALIFORNIA ASSOCIATION OF HEALTH PLANS,  
CALIFORNIA MEDICAL ASSOCIATION,  
DUSTIN CORCORAN, and CHARLES BACCHI,  
*Petitioners,*

*v.*

CALIFORNIA DEPARTMENT OF HEALTH CARE SERVICES,  
DIRECTOR MICHELLE BAASS, in her official capacity,  
CALIFORNIA DEPARTMENT OF FINANCE, DIRECTOR JOE  
STEPHENSHAW, in his official capacity, CONTROLLER MALIA  
M. COHEN, in her official capacity,  
*Respondents.*

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**PETITION FOR WRIT OF MANDATE**

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SHEPPARD, MULLIN, RICHTER &  
HAMPTON LLP

\*Moe Keshavarzi, SBN 223759  
*mkeshavarzi@sheppard.com*

David M. Poell, *pro hac vice* pending  
*dpoell@sheppard.com*

John M. Landry, SBN 194374  
*jlandry@sheppard.com*

Matthew G. Halgren, SBN 305918  
*mhalgren@sheppard.com*

Tori D. Kutzner, SBN 334057  
*tkutzner@sheppard.com*

350 South Grand Avenue, 40th Floor  
Los Angeles, California 90071  
213.620.1780

*Attorneys for Petitioners CALIFORNIA ASSOCIATION OF HEALTH  
PLANS, CALIFORNIA MEDICAL ASSOCIATION,  
DUSTIN CORCORAN, and CHARLES BACCHI*

Service on the Attorney General required by  
California Rules of Court, rule 8.29(c)(1)

NIELSEN MERKSAMER LLP

Kurt Oneto, SBN 248301  
*koneto@nmgovlaw.com*

1415 L Street, Suite 1200  
Sacramento, California 95814  
916.446.6752

## **CERTIFICATE OF INTERESTED ENTITIES OR PERSONS**

Petitioners California Association of Health Plans, California Medical Association, Dustin Corcoran, and Charles Bacchi certify that they know of no person or entity that must be listed in this certificate pursuant to California Rules of Court, rule 8.208.

DATED: October 1, 2026      SHEPPARD, MULLIN, RICHTER  
& HAMPTON LLP

By:           /s/ Moe Keshavarzi            
MOE KESHAVARZI  
Attorneys for Petitioners  
CALIFORNIA ASSOCIATION  
OF HEALTH PLANS,  
CALIFORNIA MEDICAL  
ASSOCIATION, DUSTIN  
CORCORAN, and CHARLES  
BACCHI

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## **PETITION**

Petitioners California Association of Health Plans, California Medical Association, Dustin Corcoran, in his capacity as one of the official proponents of Proposition 35, and Charles Bacchi, a California citizen and the President and CEO of the California Association of Health Plans (together, “Petitioners”), bring this verified petition for writ of mandate directing the California Department of Health Care Services; its Director, Michelle Baass; the California Department of Finance; its Director, Joe Stephenshaw; and California State Controller Malia M. Cohen (together, “Respondents”) to refrain from implementing Senate Bill 125 and to submit a proposed tax on managed care organizations to the Centers for Medicare and Medicaid Services that complies with Proposition 35 and federal law.

## **INTRODUCTION**

This case is about the Legislature’s unconstitutional gambit to amend a voter-approved ballot proposition governing California’s tax on managed care organizations (“MCOs”), which raises revenue for the Medi-Cal program. Less than two years ago, the voters passed Proposition 35, which prescribes how the MCO tax must operate. Now, the Legislature has amended Proposition 35 by enacting Senate Bill 125 (“SB 125”), which prescribes its own version of the MCO tax. Respondent Department of Health Care Services (“DHCS”) has announced that it intends to comply with SB 125 and imminently take steps that blatantly violate Proposition 35. This petition seeks to require DHCS to refrain from implementing SB 125, to comply

with Proposition 35, and to submit to the Centers for Medicare and Medicaid Services (“CMS”) for approval a proposed MCO tax that complies with Proposition 35 and federal law by the federal deadline of December 31, 2026.

This Court’s original jurisdiction is reserved for cases in which “ ‘the issues presented are of great public importance and must be resolved promptly.’ ” (*San Francisco Unified Sch. Dist. v. Johnson* (1971) 3 Cal.3d 937, 944.) This is such a case. If a tax that complies with both state and federal law is not proposed to CMS by December 31, California will face the potentially permanent loss of federal Medicaid contributions tied to the MCO tax. But the State will only have definitive direction on what state law requires once this Court has spoken. Only this Court, in the exercise of its original jurisdiction, can provide the prompt finality needed to prevent the State from jeopardizing critical federal funding before the inflexible December 31 deadline.

*The issues presented are of great public importance.* This case concerns the State’s attempt to collect billions of dollars through a tax that violates Proposition 35 and jeopardizes the federal financial contribution that helps to fund Medi-Cal, California’s healthcare safety net program that nearly one out of three Californians, including low-income families and vulnerable populations, rely upon. Medi-Cal is funded jointly by California and the federal government and is administered by DHCS. One of the principal ways California raises its share of that funding is through a tax on MCOs, which requires review and approval by CMS.

On November 5, 2024, California voters approved Proposition 35 by a two-to-one margin. Proposition 35 made the State's MCO tax permanent and capped the tax at specified maximum amounts. And to address concerns that the State had historically diverted MCO tax revenues while Medi-Cal providers remained inadequately reimbursed, thus limiting patients' access to care, Proposition 35 locked every dollar it raises into a dedicated trust fund to be used only for the Medi-Cal purposes specified by voters, including increased reimbursement to physicians and hospitals. Proposition 35 also prohibited the State from using tax proceeds to replace General Fund dollars it otherwise would spend on Medi-Cal. And it prohibited the Legislature from eliminating or modifying these protections except by a three-fourths supermajority acting in good faith to further the initiative's purposes of protecting Medi-Cal while also limiting financial burdens on California taxpayers and employers.

Earlier this year, CMS amended its MCO tax rules to implement provisions of a recent federal law known as H.R. 1. The new federal rules, combined with the caps established by Proposition 35, reduced the amount of matching funds the State can obtain from the federal government compared to prior years.

The State thus faced two lawful options: (1) amend Proposition 35 to increase its caps, which would permit the State to obtain additional federal matching funds; or (2) adjust the budget to account for the new limits on available federal funding. Because the Legislature could not reach the three-fourths

supermajority required for the former (and in any event was prohibited by Proposition 35 from amending the law to divert tax proceeds to backfill the General Fund, as it wished to do) and was unwilling to accept the fiscal consequences of the latter, it chose a third course: enact SB 125, which removes the caps Proposition 35 imposes to permit the State to levy a tax significantly above the limits the voters established.

SB 125 also discards Proposition 35's requirements governing how MCO tax proceeds must be spent, including its prohibition against using those proceeds to backfill the General Fund. It instead permits the State to use revenues the voters dedicated to specified Medi-Cal purposes, including increased payments to providers, for purposes unrelated to Medi-Cal. In this way, SB 125 purports to displace the spending rules the voters prescribed for the MCO tax.

Accordingly, this case directly implicates the lawmaking power granted to the electorate by the California Constitution. It asks whether the Legislature may circumvent the People's expressly stated will as to how the proceeds of this tax may be collected and spent. It seeks to vindicate the initiative power—a right enshrined in the California Constitution and repeatedly protected by this Court, which has recognized that article II, section 10, subdivision (c) protects voters' power by “ ‘precluding the Legislature from undoing what the people have done.’ ” ( *People v. Kelly* (2010) 47 Cal.4th 1008, 1025.)

That constitutional guarantee is being violated now in real time. SB 125 directly violates Proposition 35 by imposing a per-

member, per-month tax on commercial health plans—which provide health care coverage to millions of Californians—that exceeds by billions of dollars the taxation limits in Proposition 35. And it does so through ordinary legislation passed without the three-fourths supermajority vote Proposition 35 requires. If the Legislature can nullify a voter initiative in this manner and have that nullification take practical, irreversible effect before any court passes on its validity, the constitutional protection this Court has historically enforced will now exist in name only. This Court is uniquely positioned to prevent that result before it occurs.

*The issues must be resolved promptly, on a timeline that only this Court’s original jurisdiction can accommodate.* This Court’s intervention is urgently required to prevent irreversible loss to Medi-Cal, the millions of Californians who rely on it, and the providers who care for them. Recent federal regulations require California to submit to CMS, no later than December 31, 2026, an MCO tax proposal that complies with the new federal requirements, with an effective date of January 1, 2027. (42 C.F.R. § 433.68(e)(4)(i)(A), (ii)(A).) That deadline is not negotiable, and the consequences of noncompliance are severe. The new federal law *prohibits States from imposing new or increased MCO taxes.* (H.R. 1, Pub. L. No. 119-21, § 71115(a), 139 Stat. 72, 301-302 (2025).) Thus, if California does not have a compliant MCO tax in effect by January 1, 2027, it risks the potential permanent loss of federal matching funds. At best, California will be left dependent on the discretion of the federal

government and CMS to preserve federal funding. With millions of Californians depending on Medi-Cal for their healthcare, that is a precarious position for the State to place itself in.

With the stakes so high, the State cannot afford to pursue a course that puts future federal Medi-Cal funding at risk. Yet that is precisely the perilous path it has chosen. DHCS recently announced it intends to submit to CMS before year's end an MCO tax proposal with two components. The first will generally comply with Proposition 35, but not the new federal requirements. DHCS has acknowledged it expects CMS to reject this proposal. The second is the tax authorized by SB 125: one designed to satisfy federal law but that, as DHCS has acknowledged, does not comply with Proposition 35. That is the proposal DHCS hopes CMS will approve.

DHCS's two-tax strategy rests on a contrived premise: that Proposition 35 requires DHCS to submit a tax that will not qualify for federal matching funds, thereby making the withholding of federal funds inevitable and clearing the way for the supposedly necessary SB 125 alternative. But that premise is false. Proposition 35 not only authorizes, but expressly requires, DHCS to submit a tax that complies with both Proposition 35 and federal law. DHCS itself has acknowledged that California can submit a tax that complies with both Proposition 35 and federal law. The problem, from the State's perspective, is that such a tax would generate less revenue and would preserve Proposition 35's restrictions on how the State spends the proceeds. So DHCS has constructed a two-tax strategy with a built-to-fail Proposition 35

component to circumvent the will of the voters. In doing so, however, DHCS is putting at risk the future of federal funding for Medi-Cal and the healthcare of the millions of Californians who depend on it.

If DHCS proceeds with its intended plan and a court decides after January 1, 2027 that SB 125 is invalid, California may then find itself without a valid state-law tax satisfying the federal requirements for the period beginning January 1, 2027. And because H.R. 1 prohibits new MCO taxes, California cannot assume it can solve that problem by simply adopting another tax later and treating it as though it existed on January 1. The result would be a potentially permanent loss of federal matching funds. Thus, the federal deadline and DHCS's two-tax proposal make the issue presented by this petition exigent.

Even on an expedited basis, resolution through the ordinary course of litigation would consume months this case does not have. Nor would a direct petition, or a transfer, to the Court of Appeal adequately address the problem. Even if the Court of Appeal decides the case on an expedited basis, its decision would remain subject to review by this Court. The result would be a second round of expedited briefing before this Court, only later, with the December 31 deadline drawing closer and the State's options correspondingly narrower.

The December 31 deadline therefore makes this Court's original jurisdiction uniquely appropriate. A decision by this Court before year's end would give DHCS an opportunity to submit an MCO tax that complies with both Proposition 35 and

federal law, or to pursue whatever other lawful alternatives remain available, before the federal deadline closes that window.

Only this Court can supply the final, authoritative answer the State, health plans, providers and Medi-Cal beneficiaries need before the federal deadline passes.

This case thus presents precisely the combination of great public importance and the need for prompt and final resolution that warrants this Court's exercise of its original jurisdiction.

Petitioners represent the entire spectrum of the health care delivery system that Proposition 35 was designed to protect. The California Medical Association speaks for the physicians and other providers who were promised permanent, dedicated funding to improve Medi-Cal reimbursement rates and access to care—funding that SB 125 would strip away and never replace. The California Association of Health Plans speaks for the health plans that will be forced to absorb and pass through an unlawful, uncapped tax increase. And an official proponent of Proposition 35 speaks for the People who enacted the statute by exercising their constitutional initiative power.

Together they petition this Court to exercise its original jurisdiction and provide the definitive answer California needs to the important issues raised by this petition before the federal deadline passes, which only this Court can provide.

## ALLEGATIONS

Petitioners allege as follows:

### **A. Authenticity of Exhibits**

1. All exhibits accompanying this petition are true copies of original documents, as authenticated in the Verifications. The exhibits are numerically tabbed and consecutively paginated. Citations to the record in this petition are to the consecutive pagination of the Petitioners' Appendix filed concurrently herewith: "PA [page]." The exhibits in the Petitioners' Appendix are incorporated by reference as though fully set forth herein.

### **B. The Parties**

2. Petitioner California Association of Health Plans ("CAHP") is a tax-exempt nonprofit organization under Internal Revenue Code section 501(c)(6). Specifically, CAHP is a statewide trade association classified under Internal Revenue Code section 501(c)(6) as a "business league" that promotes the common business interests of its members (i.e., California health plans). CAHP is organized under the laws of the State of California. CAHP has "associational standing" to assert its claims in this lawsuit. (*Amalgamated Transit Union, Local 1756, AFL-CIO v. Superior Court* (2009) 46 Cal.4th 993, 1004-1005.) CAHP also has standing to seek a writ of mandate pursuant to Code of Civil Procedure sections 1085 and 1086 because it has a "beneficial interest" in the outcome of this controversy—CAHP's members will pay the tax. (Code Civ. Proc., § 1086.) Finally, CAHP has "public interest" standing to seek a writ of mandate as this case concerns a matter of great public concern—i.e., the

People’s ability to vindicate an initiative statute that has come under assault by the State. (*Save the Plastic Bag Coalition v. City of Manhattan Beach* (2011) 52 Cal.4th 155, 166-169.)

3. Petitioner California Medical Association (“CMA”) is a tax-exempt nonprofit organization under Internal Revenue Code section 501(c)(6). CMA is classified under Internal Revenue Code section 501(c)(6) as a “business league” that represents and advances the interests of California physicians and the medical profession. CMA is organized under the laws of the State of California. CMA has “associational standing” to assert its claims in this lawsuit. (*Amalgamated Transit Union, supra*, 46 Cal.4th at pp. 1004-1005.) CMA also has standing to seek a writ of mandate pursuant to Code of Civil Procedure sections 1085 and 1086 because it has a “beneficial interest” in the outcome of this controversy. (Code Civ. Proc., § 1086.) Finally, CMA has “public interest” standing to seek a writ of mandate as this case concerns a matter of great public concern—i.e., the People’s ability to vindicate an initiative statute that has come under assault by the State. (*Save the Plastic Bag, supra*, 52 Cal.4th at pp. 166-169.)

4. Petitioner Dustin Corcoran is a California citizen and one of the official proponents of Proposition 35. “California courts have routinely permitted the official proponents of an initiative to intervene or appear as real parties in interest to defend a challenged voter-approved initiative measure in order ‘to guard the people’s right to exercise initiative power’ . . . .” (*Perry v. Brown* (2011) 52 Cal.4th 1116, 1125.) This rule “enable[s] such

proponents to assert *the people's*, and hence *the state's*, interest in defending the validity of the initiative measure.” (*Ibid.*)

5. Petitioner Charles Bacchi is a California citizen. Mr. Bacchi is also the President and CEO of CAHP.

6. Respondent California Department of Health Care Services is a state government department within the California Health and Human Services Agency. DHCS is headquartered in Sacramento, California.

7. Respondent Ms. Michelle Baass is the Director of DHCS. Ms. Baass is being sued in her official capacity only.

8. Respondent California Department of Finance (“DOF”) serves as the Governor’s chief fiscal and budget agency. DOF is headquartered in Sacramento, California.

9. Respondent Mr. Joe Stephenshaw is the Director of DOF. Mr. Stephenshaw is being sued in his official capacity only.

10. Respondent Ms. Malia M. Cohen is the current California State Controller. Ms. Cohen is being sued in her official capacity only. As Controller, Ms. Cohen “superintend[s] the fiscal concerns of the state” (Gov. Code, § 12410), “draw[s] warrants on the Treasurer for the payment of money directed by law to be paid out of the State Treasury” (*id.*, § 12440), and executes the transfers of money among the funds and accounts of the State (see Cal. Const., art. XVI, § 7), which will include deposits into and disbursements from the Protect Access to Health Care Fund established by Proposition 35 and, under SB 125, the newly created Medi-Cal Stability Fund. The State Controller’s Office is located in Sacramento, California.

**C. Jurisdiction and Venue**

11. Because Petitioners seek mandamus relief, this Court has original jurisdiction over this action pursuant to article VI, section 10 of the California Constitution and California Code of Civil Procedure section 1085, subdivision (a).

12. A traditional writ of mandate is “appropriate for challenging the constitutionality or validity of statutes or official acts.” (*Wenke v. Hitchcock* (1972) 6 Cal.3d 746, 751.)

**D. Material Facts**

**1. Medi-Cal and the MCO Tax**

13. Congress created Medicaid as a joint federal-state program to provide health care coverage for individuals and families with limited income and resources. Medi-Cal is California’s Medicaid program. Today Medi-Cal is one of the largest public health insurance programs in the United States, covering about one-third of Californians. (Legislative Analyst’s Office (“LAO”), *The 2026-27 Budget: Medi-Cal Analysis*, at p. 5 (Mar. 2026), [https://lao.ca.gov/reports/2026/5146/2026-27\\_Medi-Cal\\_Analysis\\_030226.pdf](https://lao.ca.gov/reports/2026/5146/2026-27_Medi-Cal_Analysis_030226.pdf).)

14. Medi-Cal is administered by DHCS. (See *Dameron Hospital Assn. v. Progressive Casualty Ins. Co.* (2025) 111 Cal.App.5th 530, 546.) DHCS contracts with MCOs, also known as health insurance plans, to coordinate health care services for Medi-Cal enrollees. (See *Allied Anesthesia Medical Group, Inc. v. Inland Empire Health Plan* (2022) 80 Cal.App.5th 794, 803-804.) The State pays MCOs a fixed monthly payment per enrollee, and the MCOs arrange health care for their enrollees. (LAO, *The*

*2025-26 Budget: MCO Tax and Proposition 35* (Feb. 26, 2025), <https://lao.ca.gov/Publications/Report/4992>.)

15. The federal government and the State share fiscal responsibility for Medi-Cal. (LAO, *2026-27 Budget: Medi-Cal Analysis, supra*, at p. 5.) For every dollar California spends on Medi-Cal, the federal government reimburses a set percentage known as the federal matching rate. (See 42 U.S.C. §§ 1396b(a)(1), 1396d(b).) To qualify for these matching funds, federal law requires California to cover a portion of the non-federal share of Medi-Cal costs. (See 42 U.S.C. § 1396a(a)(2); 42 C.F.R. § 433.53.) One way federal law allows states to raise this share is through a “health care related tax.” (See, e.g., Medicaid Program: Preserving Medicaid Funding for Vulnerable Populations—Closing a Health Care-Related Tax Loophole, 91 Fed. Reg. 4794, 4795 (Feb. 2, 2026) (“2026 Final Rule”); 42 C.F.R. § 433.55 [defining “health care-related tax”].) In California, the MCO tax is one such tax. (LAO, *2026-27 Budget: Medi-Cal Analysis, supra*, at pp. 17-18.) It is charged directly to MCOs, and the revenue raised, combined with the matching federal funds it generates, is used to pay for Medi-Cal. (*Ibid.*) The MCO tax is charged per enrolled member, per month. (Welf. & Inst. Code, § 14199.85, subds. (i)(2), (j)(2).) California then uses the tax levied on MCOs to draw down matching funds from the federal government. (LAO, *2025-26 Budget: MCO Tax and Proposition 35, supra*; 42 U.S.C. § 1396b(w)(1)(A)(ii)-(iii).)

16. To qualify for federal matching funds, federal law and regulations require a state’s MCO tax to be both broad-based and

uniform. (42 U.S.C. § 1396b(w)(3)(B), (C); 42 C.F.R. § 433.68(c), (d).) This means the State must levy a tax on both Medi-Cal and non-Medi-Cal insurance (i.e., private/commercial insurance), and federal law requires the tax rate to be equal across both classes of insurance. (2026 Final Rule, 91 Fed. Reg. at 4795.) If the tax does not meet these requirements, a state may request a waiver from CMS. (42 U.S.C. § 1396b(w)(3)(E).) To qualify for the waiver, the state must demonstrate that the tax is “generally redistributive,” meaning it equitably spreads the tax burden across health plans and classes, and that the tax is not directly tied to Medicaid payments for the services being taxed. (*Id.* § 1396b(w)(3)(E)(ii)-(iii); 2026 Final Rule, 91 Fed. Reg. at 4796; 42 C.F.R. § 433.68(e)(1)-(3).)

17. Historically, California used the “generally redistributive” exception to structure its MCO tax in a way that generated substantial federal matching funds. (2026 Final Rule, 91 Fed. Reg. at 4797-4798.) Rather than taxing all MCO business equally, the State imposed much higher taxes on Medi-Cal business while imposing substantially lower taxes on commercial insurance business. (*Ibid.*) The State used the tax revenue to fund Medi-Cal payments that qualified for federal matching funds. (*Ibid.*)

18. This structure made it possible to generate substantial federal funding while limiting the tax burden borne by MCOs. By concentrating the tax on Medi-Cal business, California could return much of the tax to MCOs through increased Medi-Cal payments funded with both state and federal

dollars. At the same time, MCOs with little Medi-Cal business (and therefore less opportunity to receive those increased payments) were taxed at lower rates. The disparity was substantial. For 2025, California levied a tax of \$274.00 per Medi-Cal member per month, compared to \$2.00 per non-Medi-Cal member. (Welf. & Inst. Code, § 14199.85, subds. (g)(2), (h)(2).)

19. The arrangement also produced substantial benefits for the State's General Fund. By using MCO tax revenue to obtain federal matching funds, California could use those federal funds to support existing Medi-Cal services that otherwise would have required General Fund support. (2026 Final Rule, 91 Fed. Reg. at 4796.) The MCO tax thus allowed California to reduce the General Fund dollars needed for Medi-Cal, freeing those dollars for other state purposes. (LAO, *2025-26 Budget: MCO Tax and Proposition 35*, *supra*.)

20. Notwithstanding the disparity between the Medi-Cal and non-Medi-Cal tax, each year CMS has approved California's proposed MCO tax. Starting in 2023, however, CMS put California on notice that future waivers based on this design may be denied.

21. In a companion letter to Director Baass delivered with CMS's MCO-tax approval letter in 2023, CMS wrote that "California's tax on [MCOs], due to its tendency to derive revenues from Medicaid, does not appear consistent with the definition of 'generally redistributive' as defined" in federal rules. (Companion Letter from Rory Howe, CMS, Director, Fin. Mgmt.

Grp., to Michelle Baass, Director & Interim State Medicaid Director, DHCS (Dec. 15, 2023), <https://www.dhcs.ca.gov/wp-content/uploads/2025/10/Certification-of-CMS-Approval-of-Waiver-for-Managed-Care-Organization-Tax.pdf>.) The companion letter also informed California that it intended to develop new requirements and warned DHCS that “any future changes to the federal requirements concerning health care-related taxes may require the state of California to come into compliance by modifying its tax structure.” (*Ibid.*)

22. In 2024, CMS again approved California’s proposed MCO tax, but again sent a companion letter advising it was “concerned that this tax program fails to be generally redistributive in nature.” CMS urged California to plan for changes in federal rules that would prevent the State from using the same tax structure to draw down federal funds: “Please be advised that any future changes to the taxing structure, including a non-uniform change to the approved tax rates, may require the state of California to submit a new broad-based and/or uniformity waiver request.” (Companion Letter from Rory Howe, CMS, Director, Fin. Mgmt. Grp., to Tyler Sadwith, State Medicaid Director, DHCS (Dec. 20, 2024), <https://www.dhcs.ca.gov/wp-content/uploads/2025/10/1903w3B-and-C-MCO-Tax-2023-2026-Amendment.pdf> (“2024 Ltr.”).)

23. California has had a form of an MCO tax in place since 2009. (Stats. 2009, ch. 13 (AB 1422) [codified at Rev. & Tax. Code, § 12201 et seq.].) But the Legislature never made it permanent. Instead, it renewed the tax for fixed periods of time,

with the tax expiring at the end of each authorized period unless the Legislature acted to extend it. (See, e.g., Welf. & Inst. Code, § 14199.87(b)(1).) The current structure of the MCO tax was authorized in State law by Assembly Bill No. 119 (Chapter 13, Statutes of 2023), effective April 1, 2023, through December 31, 2026, and further amended by Senate Bill No. 136 (Chapter 6, Statutes of 2024) and Assembly Bill No. 160 (Chapter 39, Statutes of 2024), effective January 1, 2024, through December 31, 2026.

24. In the last decade, the amounts California has obtained from the federal government have risen sharply and consistently year over year. For 2016-2019, the MCO tax generated approximately \$1.5 billion net to the State. (LAO, *The MCO Tax Item 4260-101-0001* (May 2019), [https://lao.ca.gov/handouts/Conf\\_Comm/2019/MCO-Tax-053019.pdf](https://lao.ca.gov/handouts/Conf_Comm/2019/MCO-Tax-053019.pdf).) The current MCO tax, which expires on December 31, 2026, generates between \$7 billion and \$8 billion in net revenue annually. (LAO, *2026-27 Budget: Medi-Cal Analysis*, *supra*, at p. 18.)

25. Despite this steadily growing revenue stream, the State has continued to underfund provider reimbursement and spent most of the MCO tax proceeds for other purposes and to backfill the General Fund. (*Ibid.*; see also Welf. & Inst. Code, § 14199.101(d) [“Most Medi-Cal reimbursement rates have not been adjusted in more than a decade, and some providers have not seen a payment increase in over 25 years.”].)

**2. Proposition 35—The Protect Access to Health Care Act of 2024**

26. On November 5, 2024, California voters approved Proposition 35 by an overwhelming two-to-one margin. (Cal. Secretary of State, Statement of Vote: General Election Nov. 5, 2024, at 64 [67.9% of electorate voting “yes” for Proposition 35], <https://elections.cdn.sos.ca.gov/sov/2024-general/sov/complete-sov.pdf>.) Proposition 35 took effect on January 1, 2025. (Welf. & Inst. Code, § 14199.135, subd. (d).) The voters made clear that they intended to “address[ ] many of the current flaws in Medi-Cal funding” and to ensure the State spends MCO tax revenue on Medi-Cal and to “make[] it impossible to divert these dollars to unrelated uses.” (Welf. & Inst. Code, §§ 14199.101, subd. (k), 14199.102, subd. (d).)

27. Proposition 35 comprehensively addresses all issues related to the MCO tax, including the amount of the tax, compliance with federal requirements, including anticipated changes in federal law, the process for obtaining federal approval of the tax, including the consequences of non-approval, how tax proceeds are to be used, and the rules governing any amendments to the Proposition. (Welf. & Inst. Code, § 14199.100, et seq.) Proposition 35 further requires DHCS “to implement and administer the tax as set forth in this article.” (*Id.*, § 14199.123, subd. (c).)

28. *Permanent MCO Tax Effective January 1, 2027:* California’s current MCO tax expires on December 31, 2026. (Welf. & Inst. Code, § 14199.87, subd. (b)(1).) After December 31, 2026, the MCO tax, as provided by Proposition 35, “shall hereby

continue to be imposed” and will “permanently continue in existence.” (*Id.*, § 14199.123, subd. (a).)

29. *Maximum Tax Amounts:* Proposition 35 sets strict limits on the MCO tax. Specifically, it caps the tax the State can levy on non-Medi-Cal (i.e., private/commercial health insurance) at \$2.50 per member per month, with a limit of \$36 million in total annual revenue from the tax on private insurance. DHCS can increase these limits by no more than 10 percent if doing so is necessary to obtain federal approval. (Welf. & Inst. Code, § 14199.126, subd. (a)(1)-(2).)

30. These limits are categorically fixed unless the statute is properly amended pursuant to Proposition 35. (Welf. & Inst. Code, § 14199.124, subd. (a)(1).)

31. *Mandatory Compliance With Federal Laws:* Proposition 35 requires DHCS to periodically seek approval of the MCO tax from CMS and mandates that DHCS “shall implement and administer the tax as set forth in this article.” (Welf. & Inst. Code, § 14199.123, subd. (c).) In doing so, DHCS “shall adhere” to, among others, the following:

- The tax “shall not” exceed the limits set forth in Proposition 35;
- Consistent with the limits imposed by Proposition 35, DHCS “shall attempt to maximize” federal funding;
- The tax “shall comply with federal Medicaid requirements”;
- If “any . . . provision of federal law” governing the MCO tax is amended or replaced, including “the requirements set forth in Section 433.68 of Title 42 of the Code of Federal Regulations,” DHCS “shall

ensure” the MCO tax complies with revised federal law, but must do so without exceeding the tax limits imposed by Proposition 35;

- To ensure compliance with federal law, DHCS may, after consultation with stakeholders, modify or make minor adjustments to the tax so long as such changes are consistent with the tax limits imposed by Proposition 35; and
- In implementing the tax, DHCS is required to use the “models and methodologies” it used to implement the existing MCO tax (Assembly Bill No. 119), but only “*to the extent permitted by federal law.*”

(Welf. & Inst. Code, §§ 14199.124, subds. (a)(1)-(4), (b)(1)-(2), (d)(1), 14199.123, subd. (d), italics added.)

32. *Consequences of Federal Non-Approval:*

Proposition 35 also addresses what must happen if, for any tax period, CMS does not approve California’s proposed MCO tax. It provides that, in that event, only Article 6 within Proposition 35 “shall be inoperative” during any period for which DHCS does not obtain the necessary federal approval, or “for any affected tax period or periods” during which CMS determines that the tax required by Proposition 35 “cannot be implemented.” (Welf. & Inst. Code, § 14199.127, subds. (a)-(b).) In that event, the statute directs DHCS to undertake “appropriate wind-down and closeout activities,” including refunds. (*Id.*, § 14199.127, subd. (c).)

33. *Expenditure of MCO Tax Proceeds:* Proposition 35 prescribes the allocation of every dollar of MCO tax revenue and unequivocally prevents MCO tax proceeds “from ever being used to fund” any State programs other than investments to improve access to critical health care services, and makes it impossible to

divert those dollars to unrelated ones. (Welf. & Inst. Code, § 14199.102, subd. (c).) Among other things, it:

- Creates the Protect Access to Health Care Fund (the “Fund”) in the State Treasury, to be maintained “irrevocably separate” from the General Fund or any other state fund or account (*Id.*, §§ 14199.103, subd. (a), 14199.105, subd. (c)(1));
- Strictly prohibits use of moneys in the Fund for the State’s General Fund. (*Id.*, §§ 14199.105, subd. (c)(2)(A), 14199.107, subd. (a)(1).);
- Requires that moneys in the Fund be used for specified purposes related to Medi-Cal, including increasing payments to providers. (*Id.*, §§ 14199.103, 14199.107.)

34. *Amendments to the Proposition:* Proposition 35 can be amended only by three-fourths supermajority vote of the Legislature and, even then, any amendment must be “consistent with, and further[] the purpose of” Proposition 35. (Welf. & Inst. Code, § 14199.134, subd. (a).) Proposition 35 underscores this point with respect to its tax limits: “[C]hanges to the limits set forth in subdivision (a) shall only be made pursuant to Section 14199.134.” (*Id.*, § 14199.126, subd. (d).) Moreover, a bill to amend Proposition 35 “shall not be passed or ultimately become a statute unless the bill has been printed and distributed to members, and published on the Internet, in its final form, for at least 10 business days before its passage in either house of the Legislature.” (*Id.*, § 14199.134, subd. (b).)

35. *Liberal Construction and Severance:* Proposition 35 is to be “liberally construed to effectuate the purposes set forth in [Proposition 35].” (Welf. & Inst. Code, § 14199.135, subd. (b).)

Proposition 35 also contains a broad severability clause. (*Id.*, § 14199.135, subd. (a).)

### **3. H.R. 1 and 2026 Federal MCO Tax Rules**

36. On July 4, 2025, Congress passed H.R. 1, which imposes new rules on how states can draw down matching federal Medicaid funds.

37. In February 2026 CMS issued a final rule based on H.R. 1. (2026 Final Rule, 91 Fed. Reg. at 4836-4838 [codified at 42 C.F.R. § 433.68(e)(3), (4)].) CMS noted that federal Medicaid statutes and CMS regulations “were intended to prevent States from shifting a disproportionate amount of the tax burden to entities with a high percentage of Medicaid business, thus shifting the State responsibility for financing of the program to the federal government.” (*Id.*, 91 Fed. Reg. at 4794.) CMS found, however, that some states were using the non-uniform taxing strategy to transfer the financial burden of paying for Medicaid to the federal government, which “creates a substantial risk to the fiscal integrity and effective operation of the Medicaid program.” (*Id.*, 91 Fed. Reg. at 4800.) CMS also observed that the new rules were necessary because states were using federal matching funds under the Medicaid program for non-Medicaid purposes: “Certain states are using the revenue to fill shortfalls that exist in their State budgets as opposed to reinvesting this money in the Medicaid program.” (*Ibid.*)

38. CMS adopted the new rules to address these concerns. Under the 2026 Final Rule, a state can no longer charge a higher tax rate on a health plan’s Medicaid members than it charges on

that same plan’s non-Medicaid (private insurance) members. (42 C.F.R. § 433.68(e)(3).) The MCO tax rate now must be the same for both groups. For example, if California imposes a per-enrollee tax of \$2.50 on Medi-Cal, then the tax on private health insurance must be the same. The 2026 Final Rule also does not permit the types of exceptions that California had utilized historically. (2026 Final Rule, 91 Fed. Reg. at 4799-4800.)

39. CMS gave states a “transition period” to come into compliance with the new rules. Under the transition period applicable to California, the State has until December 31, 2026, to submit to CMS a federally compliant MCO tax with an effective date of January 1, 2027. (42 C.F.R. § 433.68(e)(4)(i)(A), (ii)(A).)

40. If California fails to enact necessary and lawful modifications to its MCO tax by December 31, 2026, and if it does not have a compliant MCO tax in effect on January 1, 2027, it cannot assume that it can later come into compliance and CMS will deem the State retroactively compliant. That is because federal law forbids it from imposing a new or increased MCO tax in 2027. (H.R. 1, Pub. L. No. 119-21, § 71115(a), 139 Stat. 72, 301-302 (2025); 42 C.F.R. § 433.68(e)(4)(i)(A), (ii)(B); Medicaid Program; Amending the Indirect Hold Harmless Threshold of Health Care-Related Taxes, 91 Fed. Reg. 46,562-01, 46,589 (July 23, 2026); Press Release, CMS, *Section 71115 and 71117 of Working Families Tax Cuts Legislation on Provider Taxes* (Nov. 14, 2025).)

**4. California Adopts SB 125 to Circumvent Proposition 35's Caps and Restrictions on Use of Tax Proceeds**

41. As a result of H.R. 1, the MCO tax now must be the same amount for both Medi-Cal and non-Medi-Cal enrollees. (42 C.F.R. § 433.68(e)(3).) At the same time, Proposition 35 caps the MCO tax at \$2.50 per private insurance enrollee per month (with a limit of \$36 million in total annual revenue from the private insurance portion of the tax). (Welf. & Inst. Code, § 14199.126, subd. (a).) Together, H.R. 1 and Proposition 35 now limit California to a Medi-Cal per-enrollee tax that is far below the rates the State had historically set. (LAO, *Medi-Cal Analysis*, *supra*, at p. 19.) The net effect is that California can no longer draw down federal matching funds in the amount it has historically collected. (*Id.*, at p. 20.)

42. None of this was, or should have been, a surprise to the State. For years, CMS warned California that this would happen and advised the State to “carefully consider how to mitigate or avoid any possible budgetary and program challenges that could result” from changes in CMS rules governing MCO taxes. (2024 Ltr. from Rory Howe to Tyler Sadwith, *supra*.)

43. In January 2026, after H.R. 1 had passed, the State acknowledged that a federally compliant MCO tax within Proposition 35's caps would not yield the same revenue and if the State wanted to increase revenue, it would have to amend Proposition 35. (Cal. Health & Human Services Agency, Governor's Budget Summary 2026-27, at p. 78,

<https://ebudget.ca.gov/2026-27/pdf/BudgetSummary/HealthandHumanServices.pdf>.)

44. Increasing Proposition 35’s caps on tax amounts, however, would have required a three-fourths vote of the Legislature. But even then, the State would have to spend the revenue as required by Proposition 35 and could not use it for General Fund purposes. (Welf. & Inst. Code, § 14199.105, subd. (b) [“Moneys deposited into the [Protect Access to Health Care] Fund . . . shall only be used for the specific purposes set forth in [Proposition 35].”].) That is because Proposition 35 requires any amendment to be consistent with the voters’ intent and objectives. (*Id.*, § 14199.134, subd. (a).)

45. In June 2026, six months after acknowledging that to levy an MCO tax in excess of Proposition 35’s limits it would have to amend the Proposition, the Legislature passed, and the Governor signed, SB 125, a statute that fundamentally amends Proposition 35 and drastically alters California’s MCO tax. SB 125 was not passed with a three-fourths supermajority vote. (See Sen. Bill No. 125 (2025-2026 Reg. Sess.) Voting Records <https://legiscan.com/CA/votes/SB125/2025>.<sup>1</sup>)

46. When enacting SB 125 the Legislature declared that Proposition 35 requires the State to submit an MCO tax that violates federal law, and that SB 125 is therefore needed to bring

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<sup>1</sup> SB 125 passed by a vote of 54-19 (with six abstentions) in the 79-member Assembly on June 15, 2026; SB 125 then passed by a vote of 27-9 (with four abstentions) in the 40-member Senate on June 18, 2026.

California’s MCO tax into compliance with federal law. (Welf. & Inst. Code, § 14199.90, subds. (d)-(f).)

47. This is incorrect. Proposition 35 does not require the State to submit a noncompliant tax. In fact, it expressly requires DHCS to comply with federal law, including the specific regulation CMS recently revised. (Welf. & Inst. Code, § 14199.124(a)(3) [“The tax shall comply with federal Medicaid requirements applicable to permissible health care-related taxes, including, but not limited to, [42 C.F.R.] Section 433.68.”].) Proposition 35 anticipates changes in federal rules and requires DHCS to modify the MCO tax to comply with the new rules. (*Id.*, § 14199.124, subd. (b)(1).)

48. DHCS knows it can submit an MCO tax to CMS that satisfies both Proposition 35 and H.R. 1. The only problem is that doing so would not yield the State the amount of revenue it wants. (LAO, *The 2026-27 Budget: Medi-Cal at the May Revision*, at p. 6 (May 2026), <https://abgt.assembly.ca.gov/system/files/2026-05/initial-lao-analysis-of-medi-cal-at-may-revision.pdf> [“Absent amending Proposition 35, the state can only scale back the Medi-Cal tax to comply with both laws.”].)

49. In its analysis of the MCO tax and the State’s 2026-2027 budget, the LAO described the State’s strategy of using SB 125 to circumvent the limits of Proposition 35 as “novel” and recommended that, during Senate hearings, the Legislature ask DHCS to explain “what is the administration’s legal reasoning for how this proposal complies with Proposition 35?” (LAO, *The*

*2026-27 Budget: Medi-Cal at the May Revision* at p. 1 (May 2026), <https://abgt.assembly.ca.gov/system/files/2026-05/initial-lao-analysis-of-medi-cal-at-may-revision.pdf>.) The LAO also advised the State that it could increase Proposition 35’s commercial insurance tax by amending Proposition 35 (by three-fourths vote) but then any resulting proceeds would have to be spent on “more funding for provider rate increases,” as Proposition 35 requires. (*Id.*, at p. 7.) The LAO also recognized that the State’s SB 125 strategy enables it to use MCO tax proceeds for General Fund purposes. (LAO, *Medi-Cal at the May Revision*, *supra*, at p. 6.)

50. SB 125 became law in June 2026. As described in more detail below, it amends Proposition 35 in several material respects. Among other things:

- It violates the maximum rates established by Proposition 35 by levying a flat \$8.85 per-member-per-month rate, more than triple Proposition 35’s \$2.50 maximum non-Medi-Cal tax amount. Moreover, the proposed tax will cause the aggregate tax to vastly exceed the \$36 million total aggregate tax amount in a single calendar year. (Welf. & Inst. Code, § 14199.126, subd. (a).)
- Proposition 35 establishes the Fund as a “special fund, permanently separate and apart from the General Fund or any other state fund or account.” (Welf. & Inst. Code, § 14199.103, subd. (a)(2)(A).) But SB 125 amends those provisions because it *does* permit transferring MCO tax proceeds to “any other state fund or account”—specifically, the new Medi-Cal Stability Fund. (*Id.*, § 14199.92.)
- Proposition 35 establishes highly detailed and mandatory spending allocations for MCO tax revenues, with the first \$4.3 billion transferred to the Improving Access to Health Care Subfund to fund 14

separate accounts created within the Improving Access to Health Care Subfund. (*Id.*, § 14199.108, subd. (d).) This funding is also permanent. (See *id.*, § 14199.108, subd. (e).) SB 125 does not comply with this mandatory, itemized spending structure.

- SB 125 also discards Proposition 35's restrictions on how MCO tax proceeds may be spent, allowing the State to use those proceeds to pay ordinary Medi-Cal expenses that otherwise would be paid from the General Fund, thereby freeing General Fund dollars that otherwise would be dedicated to Medi-Cal for the State to spend on other purposes, precisely the result Proposition 35 sought to prevent. (*Id.*, § 14199.92, subd. (d)(4).)

51. On August 12, 2026, DHCS advised MCOs that it intends to submit to CMS before December 31, 2026, two tax proposals: The first complies with selective provisions of Proposition 35 but not federal law. Specifically, it levies a much higher tax (\$192.50) on Medi-Cal insurance than on private insurance (\$1.79), in violation of federal law. DHCS itself concedes CMS will reject this proposal. (PA 50-52.) The second proposal is based on SB 125 and complies with federal law but not Proposition 35. Specifically, this proposal levies a tax of \$8.85 per-member-per-month on both Medi-Cal and non-Medi-Cal (commercial) enrollees. This proposal is the one DHCS expects (and hopes) CMS will approve. (*Ibid.*)

**E. This Court Should Exercise Its Original Jurisdiction**

52. This Court has jurisdiction in proceedings for extraordinary relief in the nature of mandamus. (Cal. Const., art. VI, § 10.) This Court will exercise its original jurisdiction in cases in which “ ‘the issues presented are of great public

importance and must be resolved promptly.’” (*San Francisco Unified, supra*, 3 Cal.3d at p. 944.) As discussed in Section II of the accompanying memorandum, the issues presented are of great public importance because they implicate a core constitutional right and the proper allocation of a significant amount of tax revenue to a critical government service. The issues also must be resolved promptly because, among other reasons, if DHCS continues on its current path, California will not have a valid MCO tax in place as of January 1, 2027, and it could forever lose the ability to obtain federal matching funds for any MCO tax.

**F. The Requirements for Writ Relief Are Satisfied**

53. The writ “must be issued in all cases where there is not a plain, speedy, and adequate remedy, in the ordinary course of law” and “must be issued upon the verified petition of the party beneficially interested.” (Code Civ. Proc., § 1086.) For the reasons stated in Section III of the accompanying memorandum, these requirements are satisfied.

**PRAYER**

Wherefore, Petitioners pray that this Court:

1. Issue an order to show cause or an alternative writ of mandate directing Respondents to show cause why they should not be directed to refrain from implementing SB 125, restrained from presenting the SB 125 MCO tax to CMS for approval, directed to present an MCO tax that complies with Proposition 35 and federal law to CMS for approval on or before December 31,

2026, and directed to use all revenue derived from any MCO tax only as allowed by Proposition 35;

2. Upon return of the order to show cause or alternative writ, grant the petition and issue a peremptory writ (i) directing Respondents to refrain from implementing SB 125, (ii) restraining them from presenting the SB 125 MCO tax to CMS for approval, (iii) directing them to present an MCO tax that complies with Proposition 35 and federal law to CMS for approval on or before December 31, 2026, and (iv) directing them to use all revenue derived from any MCO tax only as allowed by Proposition 35 (see Welf. & Inst. Code, §§ 14199.108, 14199.108.5, 14199.109-14199.120.9);

3. Award Petitioners their costs and attorneys' fees in this proceeding, pursuant to Code of Civil Procedure section 1021.5; and

4. Grant such other relief as may be just and proper.

DATED: October 1, 2026      SHEPPARD, MULLIN, RICHTER  
& HAMPTON LLP

By:           /s/ Moe Keshavarzi            
MOE KESHAVARZI  
Attorneys for Petitioners  
CALIFORNIA ASSOCIATION  
OF HEALTH PLANS,  
CALIFORNIA MEDICAL  
ASSOCIATION, DUSTIN  
CORCORAN, and CHARLES  
BACCHI

## VERIFICATION

I, Dustin Corcoran, declare as follows:

I am a petitioner. I have read the foregoing Petition for Writ of Mandate and know its contents.

The matters stated in the foregoing document are true of my own knowledge. The document appearing as Tab 1 of the Petitioners' Appendix is a true and correct copy of a cover letter sent to the Attorney General by Kurt Oneto, who served as counsel to me and the other individual proponents of Proposition 35, as well as the documents transmitted with that letter, including a letter I signed on October 16, 2023 in my capacity as a proponent of Proposition 35.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and that this Verification was executed on October 1, 2026, at Sacramento, California.

Signed by:  
  
F4D9694F74AA453...  
Dustin Corcoran

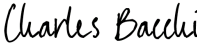
## VERIFICATION

I, Charles Bacchi, declare as follows:

I am a petitioner. I have read the foregoing Petition for Writ of Mandate and know its contents.

The matters stated in the foregoing document are true of my own knowledge. The email appearing as Tab 2 of the Petitioners' Appendix is a true and correct copy of an email I received from DHCS on August 12, 2026.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and that this Verification was executed on October 1, 2026, at Sacramento, California.

Signed by:  
  
C34CA58A2244474...  
\_\_\_\_\_  
Charles Bacchi

## VERIFICATION

I, Moe Keshavarzi, declare as follows:

I am one of the attorneys for Petitioners California Association of Health Plans, California Medical Association, Dustin Corcoran, and Charles Bacchi. I have read the above document and know its contents. The facts alleged in the petition are within my knowledge or are based upon my review of the materials cited herein. Because of my familiarity with the issues discussed in this Petition, I, in addition to two of the Petitioners, verify this Petition.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and that this Verification was executed on October 1, 2026, at Los Angeles, California.

/s/ Moe Keshavarzi

Moe Keshavarzi

## MEMORANDUM

### I. ARGUMENT

#### **A. SB 125 Unconstitutionally Amends Proposition 35**

SB 125 is unconstitutional and invalid because it amends Proposition 35 without voter approval and without compliance with Proposition 35's amendment requirements.

##### **1. The California Constitution Prohibits Legislative Amendments of Voter-Enacted Initiatives Without the Voters' Consent**

Under the California Constitution, the electorate's power to enact legislation is generally coextensive with that of the state Legislature. (*Professional Engineers in California Government v. Kempton* (2007) 40 Cal.4th 1016, 1042; see also Cal. Const., art. IV, § 1.) The power of the electorate to propose statutes and adopt or reject them has been described by this Court as “ ‘one of the most precious rights of our democratic process.’ ” (*Associated Home Builders etc., Inc. v. City of Livermore* (1976) 18 Cal.3d 582, 591.)

The California Constitution also significantly limits the Legislature's ability to amend or repeal an initiative statute without voter approval. Article II, section 10, subdivision (c) of the California Constitution provides:

The Legislature may amend or repeal an initiative statute by another statute that becomes effective only when approved by the electors unless the initiative statute permits amendment or repeal without the electors' approval.

(Cal. Const., art. II, § 10, subd. (c).)

This section prohibits the California Legislature from “amend[ing] an initiative statute without subsequent voter approval unless the initiative permits such amendment, ‘and then only upon whatever conditions the voters attached to the Legislature’s amendatory powers.’” (*People v. Superior Court (Pearson)* (2010) 48 Cal.4th 564, 568.) As a result, “ ‘the Legislature is powerless to act *on its own* to amend an initiative statute.’” (*People v. Bankston* (2026) 19 Cal.5th 786, 883.)

“[T]he purpose of California’s constitutional limitation on the Legislature’s power to amend initiative statutes is to ‘protect the people’s initiative powers by precluding the Legislature from undoing what the people have done, without the electorate’s consent.’” (*Kelly, supra*, 47 Cal.4th at p. 1025.) “In this vein, decisions frequently have asserted that courts have a duty to “ ‘jealously guard’ ” the people’s initiative power, and hence to “ ‘apply a liberal construction to this power wherever it is challenged in order that the right’ ” to resort to the initiative process “ ‘be not improperly annulled’ ” by a legislative body.” (*Ibid.* [collecting cases].)

California’s protection of the people’s initiative power remains absolute, and “the flexibility to make desirable or even *necessary* adjustments to initiative statutes long has been, and remains, foreclosed by article II, section 10, subdivision (c).” (*Kelly, supra*, 47 Cal.4th at p. 1044.) This Court has repeatedly upheld the People’s initiative power and rejected the Legislature’s attempts to modify initiative statutes without voter

approval or other voter-approved procedural safeguards. (See *id.*, at pp. 1036, 1041-1042, 1045.)

The constitutional protection afforded to initiatives is not limited to express amendments. The key question is whether legislation “prohibits what the initiative authorizes, or authorizes what the initiative prohibits.” (*Pearson, supra*, 48 Cal.4th at p. 571.) Legislation constitutes an amendment under article II, section 10, subdivision (c) if it “changes an existing initiative by taking away from it.” (*Kelly, supra*, 47 Cal.4th at p. 1027.) Article II, section 10, subdivision (c) prohibits the Legislature from “ ‘ ‘ ‘undoing what the people have done, without the electorate’s consent’ ” ’ ” regardless of the label the Legislature places on the enactment. (*County of San Diego v. Commission on State Mandates* (2018) 6 Cal.5th 196, 211.) In other words, “ ‘[w]hether an act is amendatory of existing law is determined not by title alone.’ ” (*Franchise Tax Board v. Cory* (1978) 80 Cal.App.3d 772, 777.)

“To determine whether [a legislative act] impermissibly takes away from [an initiative], [the court] must decide what the voters contemplated.’ ” (*Bankston, supra*, 19 Cal.5th at p. 883, first and second alterations in original.) Courts must examine how the legislation operates in practice, including whether it “ ‘indirectly amend[s]” an initiative statute or “ ‘otherwise circumvent[s] the intent of the electorate.’ ” (*People v. Solis* (2020) 46 Cal.App.5th 762, 778-779; see also *Proposition 103 Enforcement Project v. Quackenbush*, 64 Cal.App.4th 1473, 1487 [“[T]he Legislature cannot indirectly accomplish . . . what it

cannot accomplish directly by enacting a statute which amends the initiative's statutory provisions. To hold otherwise would elevate form over substance."].)

"Any doubts should be resolved in favor of the initiative and referendum power." (*Id.*, at p. 1486.) Therefore, "amendments which *may* conflict with the subject matter of initiative measures must be accomplished by popular vote, as opposed to legislatively enacted ordinances, where the original initiative does not provide otherwise." (*Ibid.*)

## **2. SB 125 Amends Proposition 35**

Under article II, section 10, subdivision (c), SB 125 constitutes an "amendment" that required the Legislature to comply with Proposition 35's amendment requirements.

Proposition 35 did not just specify the spending of tax proceeds *if* the Legislature chose to impose an MCO tax. It affirmatively imposed the post-2026 tax itself:

(a) It is the intent of the people of the State of California to *permanently continue in existence a [MCO] provider tax* upon the expiration of the tax imposed by [Welfare and Institutions Code] Section 14199.84.

(b) Therefore, upon the expiration of the [MCO] tax imposed pursuant to Article 7.1 . . . a [MCO] provider tax *shall* hereby continue to be imposed on and after January 1, 2027, *as provided in this article*.

(c) [DHCS] *shall* implement and administer the tax *as set forth in this article*.

(Welf. & Inst. Code, § 14199.123, subds. (a)-(c), italics added.)

In short, California voters decided the MCO tax prescribed by Proposition 35 shall replace the existing MCO tax upon its

expiration on December 31, 2026, and they left no room for imposing a different MCO tax, subject to different rules and requirements. (See *Howard Jarvis Taxpayers Assn. v. Bowen* (2011) 192 Cal.App.4th 110, 116, 122-124 [legislature impermissibly amended initiative by “negat[ing]” initiative’s requirement that the official summary of bill, ballot label, and title *shall* be prepared by Attorney General].)

Yet, that is precisely what SB 125 does. While Proposition 35 mandates the imposition of an MCO tax “subject to” Proposition 35, SB 125 purports to impose an MCO tax that is not subject to Proposition 35 and is governed by different requirements—both in terms of how the tax is structured and how the revenue therefrom is spent.

The Legislature did not characterize SB 125 as merely another unrelated provider tax. It titled SB 125 “Continuation of Managed Care Organization Provider Tax,” acknowledged that Proposition 35 requires DHCS to submit a “continued, permanent MCO provider tax,” and then expressly stated its intent to impose an MCO tax “*that is not subject to [Proposition 35]*.” (Welf. & Inst. Code, § 14199.90, subds. (d), (i), italics added.)

The fact that the Legislature placed SB 125 in a separate Chapter within the Welfare and Institutions Code does not change its substantive effect. The Legislature cannot circumvent a voter-approved initiative by labeling SB 125 a different tax “not subject to” Proposition 35. (Welf. & Inst. Code, § 14199.90, subd. (i); see also *People v. Cooper* (2002) 27 Cal.4th 38, 45

[“ [T]he Legislature should not be permitted to do indirectly that which it cannot do directly.’ ”].)

The California Constitution does not permit the Legislature to evade Proposition 35 simply by putting the MCO tax in a new statutory box and writing “Proposition 35 does not apply” on the outside. (See *People v. Armogeda* (2015) 233 Cal.App.4th 428, 432, 435 [finding legislative statute improperly amended voter initiative and holding the Legislature may not change initiative’s coverage simply by applying a “new label”].) If that were enough, the electorate’s restrictions on taxation would exist only at the Legislature’s sufferance: whenever the restriction became inconvenient, the Legislature could reenact the tax without the restriction, give it a new name, and declare itself free of the voters’ commands. “[T]he voters’ prohibition on any amendments . . . would be ‘of little worth if it can be evaded by so simple a device.’ ” (*Proposition 103 Enforcement Project, supra*, 64 Cal.App.4th at p. 1487 [“ ‘To give effect to the constitution, it is as much the duty of the courts to see that it is not evaded as that it is not directly violated.’ ”].)

SB 125 directs itself to the very same specific subject matter as Proposition 35. Hence, SB 125 is subject to the limits on amendments imposed by article II, section 10, subdivision (c). But SB 125 amends Proposition 35 with respect to multiple requirements and restrictions the voters established, including the following:

***SB 125 authorizes an MCO tax that exceeds the caps established by Proposition 35.*** Proposition 35 imposes

concrete limitations on the MCO tax, including the \$2.50 per-member, per-month and \$36 million aggregate limitation on private (i.e., non-Medi-Cal) plans, while allowing DHCS a unilateral, but limited, 10 percent adjustment if necessary to accommodate federal requirements. (Welf. & Inst. Code, § 14199.126, subds. (a)-(c).) Any further changes “shall” be made pursuant to Proposition 35’s amendment provision. (*Id.*, § 14199.126, subd. (d).)

SB 125 increases the per-member-per-month levy from \$2.50 to \$8.85, more than triple the cap the voters imposed in Proposition 35. (Welf. & Inst. Code, § 14199.95, subd. (a)(1).) It also gives DHCS substantially different adjustment authority and removes the \$36 million aggregate cap. (*Id.*, § 14199.95, subd. (b).) And the “findings and declarations” section of SB 125 declares the resulting tax exempt from Proposition 35 altogether. (*Id.*, § 14199.90, subd. (i).) This attempt to evade Proposition 35’s amendment requirement cannot stand. (See *Silva v. Humboldt County* (2021) 62 Cal.App.5th 928, 930 [legislation “impermissibly broadened” scope of tax created by voter initiative and thus was invalid because it was not approved by the electorate].)

***SB 125 permits diversion of tax proceeds to purposes and funds other than those established by Proposition 35.***

Proposition 35 creates a special fund, called the Protect Access to Health Care Fund, for safekeeping of MCO tax proceeds, establishes conditions on how the tax revenue is spent for the Medi-Cal program, and imposes detailed allocation and

nonsupplantation requirements. (See Welf. & Inst. Code, §§ 14199.103, 14199.105, 14199.107.) It provides that, starting on January 1, 2025, all MCO tax proceeds—including from the existing MCO tax (Assembly Bill No. 119, codified at Welf. & Inst. Code, § 14199.80 et seq.)—“shall be deposited into the fund.” (*Id.*, § 14199.108, subd. (a)(1).) Proposition 35 makes clear the voters’ “*unqualified* intent” that all tax revenue deposited into the Fund “shall only be used for the specific purposes set forth in [Proposition 35].” (*Id.*, §§ 14199.104, subd. (a), 14199.105, subd. (b), italics added.) The voters made clear that DHCS has a “nondiscretionary ministerial duty” to use MCO tax proceeds as set forth in Proposition 35, including to increase payments to providers. (*Id.*, § 14199.106, subd. (b)(1)(A).)

SB 125 removes these restrictions. It requires MCO tax deposits to be deposited into a different fund, called the Medi-Cal Stability Fund, with a materially different hierarchy of uses than those required by Proposition 35. (Welf. & Inst. Code, § 14199.92, subd. (b) [“All revenues, less refunds, derived from the taxes provided for in this article shall be deposited in the State Treasury to the credit of the Medi-Cal Stability Fund.”].) SB 125 thus intercepts the very revenue-generating mechanism the voters permanently provided for and places the resulting revenues into a different statutory funding architecture. This is an amendment of Proposition 35. (See *County of San Diego, supra*, 6 Cal.5th at p. 213 [statute that redirected tax revenues allocated by voter initiative to special “trust fund,” and thus

“sought to alter the voters’ careful handiwork,” constituted amendment].)

***SB 125 permits MCO tax proceeds to backfill the General Fund.*** Proposition 35 makes clear that MCO tax revenue “shall not be considered to be part of the General Fund” and, notwithstanding any other law, the Fund shall be kept “permanently and irrevocably separate and apart from the General Fund.” (Welf. & Inst. Code, § 14199.105, subd. (c)(1), (2)(A); see also *id.*, § 14199.103(a)(2)(A).) It also prohibits the State from using tax proceeds to replace General Fund dollars it otherwise would spend on Medi-Cal. (*Id.*, §§ 14199.103, 14199.107.)

SB 125, by contrast, allows the Controller to use MCO tax proceeds for cash-flow loans to the General Fund (see Welf. & Inst. Code, § 14199.92, subd. (e)) and authorizes the State to use those proceeds to pay ordinary Medi-Cal expenses that otherwise would be paid from the General Fund (*id.*, § 14199.92, subd. (d)(4)) thereby freeing General Fund dollars that otherwise would be dedicated to Medi-Cal for the State to spend on other purposes—precisely the result Proposition 35 prohibits.

***SB 125 overrides Proposition 35 requirements in the event of federal non-approval.*** Proposition 35 anticipates that for any given year, CMS may not approve California’s MCO tax and prescribed consequences if that were to happen. Welfare and Institutions Code section 14199.127, subdivision (a) provides that if DHCS does not obtain the necessary federal approvals for any given year, the tax article becomes “inoperative” for that period.

(Welf. & Inst. Code, § 14199.127, subd. (a).) DHCS must then conduct “wind-down and closeout activities,” including appropriate refunds of any tax collected. (*Id.*, § 14199.127, subd. (c).)

SB 125 modifies the consequences of federal non-approval. Rather than the required “wind-down and closeout activities,” SB 125 directs DHCS to proceed with a tax that simply disregards the limitations of Proposition 35.

### **3. SB 125 Does Not Comply With Proposition 35’s Amendment Requirements**

Article II, section 10, subdivision (c) of the California Constitution provides that an initiative statute may be amended by the Legislature, if at all, “ ‘only upon whatever conditions the voters attached to the Legislature’s amendatory powers.’ ” (*Pearson, supra*, 48 Cal.4th at p. 568.)

Proposition 35 allows amendment by the Legislature only if three-fourths of each house concurs and the amendment is “consistent with, and furthers the purpose of” Proposition 35. (Welf. & Inst. Code, § 14199.134, subd. (a).) SB 125 satisfies neither requirement.

Procedurally, SB 125 passed the Senate **27-9**, not the 30 votes that would constitute three-fourths of a 40-member Senate. (See <https://legiscan.com/CA/votes/SB125/2025>.) Further, SB 125 passed the Assembly **54-19**, not the 60 votes that would constitute three-fourths of an 79-member body. (*Ibid.*)

Substantively, SB 125 is an impermissible amendment because it is neither “consistent with” nor “furthers the purpose of” Proposition 35. (See Welf. & Inst. Code, § 14199.134,

subd. (a).) “In discerning the purposes of an initiative so as to determine whether a legislative amendment furthers its purpose and thus is valid,” courts “are guided by, but not limited to, the general statement of purpose found in the initiative.”

(*Proposition 103 Enforcement Project, supra*, 64 Cal.App.4th at pp. 1490-1491.)

The voters’ purpose in adopting Proposition 35 included prohibiting the State from using MCO tax revenue to backfill the General Fund and ensuring that taxpayers and employers do not bear the financial burden for the implementation of Proposition 35. (Welf. & Inst. Code, § 14199.102, subds. (c)-(d).)

SB 125 is inconsistent with and frustrates these purposes, rather than furthering them.

First, it redirects MCO tax proceeds to a different fund (the Medi-Cal Stability Fund) and permits the State to use tax revenue on unauthorized and unrelated programs and to supplant existing sources of money for Medi-Cal, for purposes other than those specified by Proposition 35. (Welf. & Inst. Code, § 14199.92.) As the LAO has acknowledged, SB 125 “is shifting existing Proposition 35 funds” to help the General Fund and “allocates no MCO tax funding for provider rate increases—a fundamental objective of Proposition 35.” (LAO, *Medi-Cal at the May Revision, supra*, at p. 7.)

Second, by removing Proposition 35’s caps and imposing a non-Medi-Cal private insurance tax that is billions of dollars in excess of the limits the voters set, SB 125 will increase health insurance premiums for Californians, in violation of

Proposition 35's mandate that taxpayers and employers "not bear the financial burden for the implementation of" Proposition 35's MCO tax. (Welf. & Inst. Code, § 14199.102, subd. (d).) The LAO has recognized that increasing taxes beyond Proposition 35's limits will cause higher healthcare costs for consumers. (LAO, *2026-27 Budget: Medi-Cal Analysis, supra*, at p. 20.)

**B. No Argument Purporting to Justify SB 125 Is Relevant to This Court's Validity Analysis**

This Court need not decide any further issue in order to find SB 125 unconstitutional. Respondents contend, however, that SB 125 was necessary because the MCO tax required by Proposition 35 would violate new federal law and, therefore, CMS will not approve an MCO tax that complies with Proposition 35. (See Welf. & Inst. Code, § 14199.90, subd. (f) ["These new federal requirements may result in a denial of federal approval for the MCO provider tax authorized in Article 6 (commencing with [Welfare and Institutions Code] Section 14199.123) of [Proposition 35]."].) This is incorrect.

But even assuming a scenario in which it is impossible for DHCS to devise any MCO tax that complies with both Proposition 35 and federal law, that would not save SB 125. The limitation article II, section 10, subdivision (c) imposes on the Legislature's power to amend an initiative statute is "absolute" and allows for no expansion of that power in *any* circumstance no matter how exigent or dire.

*Kelly, supra*, 47 Cal.4th 1008 is instructive. There, the Legislature passed a statute imposing objective quantity limits on medical marijuana that patients could lawfully possess in

place of an initiative statute’s purportedly difficult-to-apply “‘reasonable amount’ ” test. (*Id.*, at p. 1030.) The Legislature acted because it had determined that the initiative statute’s test created uncertainties hindering law enforcement while simultaneously depriving patients of the initiative’s protections from prosecution. (*Id.*, at p. 1013.) *Kelly* deemed the substitute test an impermissible amendment without needing to make any inquiry into the accuracy of the Legislature’s findings. (*Id.*, at pp. 1044-1046.) *Kelly* found article II, section 10, subdivision (c)’s “closely circumscribed limits” to be uniquely absolute and held that “the flexibility to make desirable or even *necessary* adjustments to initiative statutes long has been, and remains, foreclosed . . . .” (*Id.*, at p. 1045.)

This same unyielding limitation recognized in *Kelly* applies here. If the Legislature amends a voter-approved initiative without the voters’ consent, as it did here, the amendment is invalid. There are no exceptions to this constitutional rule. That should be the end of the analysis.

**C. Proposition 35 Imposes on DHCS a Ministerial, Non-Discretionary Duty to Submit to CMS a Tax That Complies With Both Proposition 35 and Federal Law**

DHCS has announced that before the end of 2026, it will submit to CMS two MCO tax proposals. The first complies with selective provisions of Proposition 35 but not federal law. DHCS itself concedes CMS will reject this proposal. (PA 50-52.) The second proposal is based on SB 125 and may comply with federal law but not Proposition 35, and it is the one DHCS expects CMS to approve. (*Ibid.*)

Proposition 35 prohibits DHCS from submitting either one of these proposals. It requires the opposite: DHCS “shall” submit to CMS a tax that complies with both Proposition 35 and federal law. (See Welf. & Inst. Code, § 14199.123, subd. (a).)

Proposition 35 requires DHCS to implement the tax as “*permitted by federal law.*” (Welf. & Inst. Code, § 14199.102, subds. (c)-(d), italics added.) And it provides that in implementing the tax, DHCS “shall adhere” to certain rules:

- The tax “shall not exceed the limits” the voters established. (*Id.*, § 14199.124, subd. (a)(1).)
- “The tax shall comply with federal Medicaid requirements applicable to permissible health care-related taxes, including, but not limited to, [42 C.F.R.] Section 433.68.” (*Id.*, § 14199.124, subd. (a)(3).)
- If federal rules governing the MCO tax are amended or modified, including Section 433.68, “[DHCS] shall ensure the tax imposed pursuant to this article complies with those amended or successor requirements.” (*Id.*, § 14199.124, subd. (b)(1).)
- If necessary to comply with federal law, and consistent with Proposition 35’s limits on tax amounts, DHCS may “modify or make minor adjustments to any methodology, tax amount, taxing tier, or other provision specified in this article to the extent it is reasonably necessary to meet the requirements of federal statute or regulations, to obtain or maintain federal approval, or to ensure federal financial participation is available or is not otherwise jeopardized.” (*Id.*, § 14199.124, subd. (d)(1).)

Proposition 35 also requires DHCS to submit a tax to CMS that meets these requirements:

- “[DHCS] shall be required to seek federal renewal and reauthorization as necessary to continue the imposition of the tax imposed by this article.” (Welf. & Inst. Code, § 14199.124, subd. (c)(1).)
- “[DHCS] shall request approval from the federal [CMS] as is necessary to implement this article.” (*Id.*, § 14199.124, subd. (c)(2).)

Proposition 35 thus requires DHCS to implement an MCO tax that complies with both Proposition 35 and federal law. It also prohibits the two-tax proposal DHCS intends to submit.

DHCS cannot ignore these mandates on the premise that a tax that complies with Proposition 35 cannot comply with federal law. Proposition 35 authorizes and *requires* DHCS to comply with federal law. The LAO has acknowledged that DHCS can levy a tax that complies with both Proposition 35 and federal law. (LAO, *Medi-Cal at the May Revision*, *supra*, at p. 6 [“Absent amending Proposition 35, the state can only scale back the Medi-Cal tax to comply with both laws.”].)

To comply with both Proposition 35 and federal law DHCS would simply have to: (i) reduce the Medi-Cal tax to be under Proposition 35’s cap on the private insurance tax (i.e., \$2.50 with an aggregate of \$36 million); and (ii) set the same tax rate for both the Medi-Cal and private insurance tax.

Moreover, even if the result of a Proposition 35 tax was non-approval by CMS, that still would not permit DHCS to disregard the voters’ mandate. Proposition 35 contemplates the possibility that DHCS may not succeed in securing CMS approval and expressly spells out what is to happen: only the taxing provisions contained in article 6 of Proposition 35 are affected.

(Welf. & Inst. Code, § 14199.127, subd. (a).) The rest of Proposition 35, including rules governing how any revenue is spent, remains in full force and effect. (*Ibid.*; see also *id.*, § 14199.135, subd. (a).)

Proposition 35 imposes on DHCS a non-discretionary duty to submit to CMS a tax that complies with both federal law and Proposition 35.

**II. THIS COURT SHOULD EXERCISE ITS ORIGINAL JURISDICTION BECAUSE THE PETITION RAISES ISSUES OF GREAT PUBLIC IMPORTANCE WHICH MUST BE DECIDED PROMPTLY**

**A. This Court Has Considered in the First Instance Petitions Challenging the Constitutionality of Important Statutes**

This Court exercises its original jurisdiction in cases in which “ ‘the issues presented are of great public importance and must be resolved promptly.’ ” (*San Francisco Unified, supra*, 3 Cal.3d at p. 944.) Though this Court exercises this power infrequently, it does so in cases like this to resolve consequential, statewide constitutional questions involving statutes and ballot propositions.

In *California Redevelopment Association v. Matosantos* (2011) 53 Cal.4th 231, 241, this Court exercised its original jurisdiction to decide a constitutional challenge to statutes that provided for winding down redevelopment agencies unless the cities and counties that created them agreed to make payments into funds benefiting schools and special districts. The petitioners argued that the statutes violated “Proposition 22, which amended the state Constitution to place limits on the

state's ability to require payments from redevelopment agencies for the state's benefit." (*Ibid.*) This Court exercised its original jurisdiction because the statutes threatened to dissolve the redevelopment agencies and the petition called "into question the proper allocation of billions of dollars in property tax revenue." (*Id.*, at p. 253.) Similarly, this petition challenges a statute for unconstitutionally violating Proposition 35 and calls into question the collection and allocation of billions of dollars in tax revenue. (LAO, *The 2026-27 Budget: Overview of the Spending Plan*, at 12 (Aug. 2026), [https://lao.ca.gov/reports/2026/5197/2026-27\\_Budget\\_Overview\\_of\\_Spending\\_Plan\\_082626.pdf](https://lao.ca.gov/reports/2026/5197/2026-27_Budget_Overview_of_Spending_Plan_082626.pdf).)

This Court has also exercised original jurisdiction to decide important issues in light of federal mandates and deadlines. In *San Francisco Unified, supra*, 3 Cal.3d at p. 942, this Court considered a petition challenging a statute related to busing. The Court explained:

The issues here presented respecting the interpretation and constitutionality of section 1009.5 are of great public concern and importance; their prompt resolution is essential to orderly planning and pupil assignment not only in San Francisco but throughout the state. The United States Supreme Court has directed that segregation in public schools must terminate "at once." [Citation.] Since section 1009.5, under one interpretation, may delay desegregation, prompt judicial action is essential to comply with this direction.

(*Id.*, at p. 945.) The instant case also involves a tight federal deadline, with the looming requirement for the State to submit a compliant MCO tax by December 31, 2026.

There are a number of other cases in which this Court has used its jurisdiction to provide an authoritative, uniform interpretation of legislation of great public importance, particularly where ballot initiatives are involved. (*Strauss v. Horton* (2009) 46 Cal.4th 364, 399 [exercising original jurisdiction to decide constitutionality of Proposition 8 regarding right to same-sex marriage]; *Briggs v. Brown* (2017) 3 Cal.5th 808, 822 [exercising original jurisdiction to decide constitutionality of certain provisions in Proposition 66, the Death Penalty Reform and Savings Act of 2016]; *Hotel Employees and Restaurant Employees International Union v. Davis* (1999) 21 Cal.4th 585, 590 [exercising original jurisdiction to decide whether Indian gaming initiative violated voter-approved constitutional provision]; *Legislature v. Eu* (1991) 54 Cal.3d 492, 499-500 [exercising original jurisdiction to decide constitutionality of Proposition 140, The Political Reform Act of 1990]; *Raven v. Deukmejian* (1990) 52 Cal.3d 336, 340 [explaining that case was transferred from Court of Appeal so that this Court could exercise its original jurisdiction to decide challenge to Proposition 115, the Crime Victims Justice Reform Act]; *Brosnahan v. Brown* (1982) 32 Cal.3d 236, 240-241 [exercising original jurisdiction to decide constitutionality of The Victims' Bill of Rights]; *Amador Valley Joint Union High Sch. Dist. v. State Bd. of Equalization* (1978) 22 Cal.3d 208, 218-219 [exercising original jurisdiction to decide challenge to Proposition 13 regarding real property taxation and limitations on assessment and taxing powers of state and local

governments].) This case similarly presents issues of great public importance that must be resolved promptly.

**B. If California Does Not Have a Compliant Tax in Effect by January 1, 2027, the State Risks Permanently Losing Federal Medicaid Matching Funds**

Congress and CMS have imposed a rapidly approaching federal deadline that could make judicial review of SB 125 after January 1, 2027 too late. H.R. 1 imposed new restrictions on MCO taxes and directed that existing noncompliant MCO taxes be brought into compliance, subject only to a “transition period” established by CMS. (Pub. L. No. 119-21, §§ 71115, 71117(c).)

CMS subsequently exercised that authority and established the transition period applicable to California. Because California’s current MCO tax received its most recent federal waiver approval within two years of April 3, 2026, its transition period expires on December 31, 2026. (42 C.F.R. § 433.68(e)(4)(i).) Thus, California has until December 31, 2026, to submit to CMS a federally compliant MCO tax with an effective date of January 1, 2027. (42 C.F.R. § 433.68(e)(4)(i)-(ii).)

The consequences of noncompliance are severe and expose the State to the risk of permanent financial harm. That is because, in addition to implementing new rules, H.R. 1 *prohibits States from imposing new or increased MCO taxes after July 4, 2025*. (See H.R. 1, § 71115(a)(2) [codified at 42 U.S.C. § 1396b(w)(4)(D)(i)(II)(bb)]; 91 Fed. Reg. at 46,589.)

Thus, the question raised by this Petition—whether SB 125 is valid—is urgent. DHCS intends to submit two MCO tax

proposals to CMS by December 31, 2026. The first generally complies with Proposition 35 but not the new federal rules. DHCS has acknowledged that it expects CMS to reject it. The second is based on SB 125. If DHCS proceeds on that basis and a court decides after January 1, 2027 that SB 125 is invalid, California may then find itself without a valid state-law tax satisfying the federal requirements for the period beginning January 1, 2027. And because H.R. 1 prohibits new MCO taxes after July 2025 (subject to the transition period), California may not be able to solve that problem by simply adopting another tax later and treating it as though it had existed on January 1 (immediately following the end of the transition period).

At best, California will be left at the mercy of the federal government and will have to hope CMS will accept an alternative MCO tax proposal and deem California compliant retroactively to January 1, 2027 so the State remains eligible for federal matching funds. But the federal government's actions to date do not give reason for optimism that CMS will exercise its discretion to help California. In fact, they suggest the opposite. Indeed, when it changed the rules governing MCO taxes, the federal government made clear it was targeting California. In October 2025, when the White House announced the MCO tax changes, it described the new law under the heading "Closing the California Loophole." (White House, Memorandum Re: Democrat Plan to Fund Healthcare for Illegal Immigrants, at p. 2 (Oct. 1, 2025), <https://www.whitehouse.gov/wp-content/uploads/2025/10/WFTCA-Illegal-Immigrant-Healthcare->

Memo-FINAL.pdf.) And earlier this year, in announcing its new regulations, CMS specifically identified California’s tax structure as an example of the “loophole” it sought to close. (Fact Sheet, CMS, Preserving Medicaid Funding for Vulnerable Populations – Closing a Health Care-Related Tax Loophole Final Rule (Jan. 29, 2026) <https://www.cms.gov/newsroom/fact-sheets/preserving-medicaid-funding-vulnerable-populations-closing-health-care-related-tax-loophole-final>.) CMS also had California in mind when it set the transition period and the December 31, 2026, deadline. CMS explained that it deliberately imposed shorter transition periods on MCO taxes because “the most egregious examples of shifting the burden of financing Medicaid to the Federal government exist in MCO taxes.” (2026 Final Rule, 91 Fed. Reg. at 4820.)

California therefore cannot safely assume that, if SB 125 is invalidated after the transition period expires, the same federal government that adopted new requirements for the express purpose of eliminating California’s MCO tax structure will excuse California’s noncompliance.

The federal transition period, which expires on December 31, 2026, gives California a protection that will not exist indefinitely. Beginning January 1, 2027, California must have a tax that satisfies the new federal requirements. If California relies on SB 125 to cross that deadline and SB 125 is thereafter declared invalid, California could find itself without a valid tax for the post-transition period after the federal protection for its former tax has already expired. (H.R. 1, Pub. L. No. 119-21, §

71115(a), 139 Stat. 72, 301-302 (2025); 42 C.F.R.  
§ 433.68(e)(4)(i)(A), (ii)(B).)

The result is a genuine risk of irreversible loss. A judicial decision after January 1 cannot turn back the federal clock, extend the transition period, or guarantee CMS will treat a subsequently enacted or approved tax as though it had been validly in effect on January 1. The validity of SB 125 therefore presents a question that must be resolved before California's federal transition period expires, when meaningful relief remains available—not afterward, when some or all of the resulting federal funding loss may already be incapable of cure.

**C. A Prompt Decision is Also Needed Because of California's New Governor's January 10, 2027 Deadline to Submit a Budget to the Legislature**

The need for a prompt resolution of the validity of SB 125 and the State's proposed MCO tax based on that law is reinforced by an independent and imminent constitutional deadline: preparation of California's next state budget. Article IV, section 12, subdivision (a) of the California Constitution requires the Governor, "[w]ithin the first 10 days of each calendar year," to submit to the Legislature a budget for the ensuing fiscal year. If recommended expenditures in the budget exceed estimated revenues, the Governor must identify the sources from which the additional revenues should be provided. (Cal. Const., art. IV, § 12, subd. (a).) The Governor must submit the budget by January 10, 2027. (*Ibid.*)

That deadline assumes particular importance here because the State's existing budget and State budgets for 2027, 2028, and

2029 expressly depend upon revenue from the SB 125 MCO tax. (LAO, *2026-27 Budget: Overview of the Spending Plan*, *supra*, at p. 7.) The fiscal significance grows substantially thereafter: the Administration projects approximately \$2.3 billion annually from the SB 125 tax in subsequent years, with the revenue used to offset General Fund Medi-Cal costs. (*Id.*, at p. 12.) These are not incidental assumptions at the margins of the State’s fiscal plan. The LAO identifies the SB 125 MCO tax as one of the enacted budget’s three ongoing “revenue-related solutions.” And the Administration’s May Revision relied upon the larger renewed MCO tax based on SB 125 as part of approximately \$14 billion in proposed budget solutions. (*Id.*, at pp. 5, 11.)

The validity of SB 125 is thus a question of statewide importance in need of prompt resolution. The controversy does not merely concern the legality of a particular tax in the abstract. It concerns whether California will lose the ability to rely upon a major and ongoing financing mechanism for Medi-Cal, whether the State may obtain the federal Medicaid funding associated with that mechanism, and what revenues the next Governor may responsibly incorporate into the constitutionally mandated budget presented to the Legislature in January. Those are questions affecting the financing of one of California’s largest public programs and the fiscal planning of the State itself. They should be answered while the State can still act on the answer and modify its tax before December 31, 2026, not after the federal transition period has expired and the next Governor has already

been required to construct California's budget around an unresolved premise.

**D. This Court Is Best Positioned to Address the Urgency Presented in This Petition**

Though this Court will typically transfer a petition for writ of mandate that has not previously been filed with the Court of Appeal to that court, such an additional layer of review would serve little purpose here. The central issue is a pure question of law: whether SB 125 impermissibly amends Proposition 35 in violation of article II, section 10, subdivision (c). The relevant statutes, constitutional provisions, federal requirements, and DHCS's announced course of conduct are already fixed. There is no factual record that must first be developed by a lower court.

Therefore, this Court—not the Court of Appeal—is in the best position to resolve the issues raised in this petition with the necessary finality on the short timeline allowed by the federal MCO tax deadline and the State budget deadline. What Petitioners and the State need before the deadlines is not only a prompt decision, but a final one. If this petition were transferred to the Court of Appeal, that court might decide the petition on an expedited basis, but its decision would remain subject to review by this Court. The result could be a second round of expedited proceedings before this Court occurring later in the year, with the December 31 and January 10 deadlines closer and the State's remaining options narrower. DHCS, CMS, health plans, and state budget officials could be left making consequential decisions while the validity of the governing tax remains unresolved. The problem therefore is not simply that litigation takes time. It is

that the federal deadline leaves insufficient time for sequential review. Accordingly, this Court should decide the petition in the first instance.

### **III. WRIT RELIEF IS PROPER**

A writ of mandate under Code of Civil Procedure section 1085 “is a vehicle to compel a public entity to perform a legal duty, typically one that is ministerial.” (*Citizens for Amending Proposition L v. City of Pomona* (2018) 28 Cal.App.5th 1159, 1173; see also *Knoll v. Davidson* (1974) 12 Cal.3d 335, 343, fn. 6 [“[M]andate does now clearly lie to compel performance of future acts where it is clear that public officers do not intend to comply with their obligation when the time for performance arrives.”].) Furthermore, a traditional writ of mandate is “appropriate for challenging the constitutionality or validity of statutes or official acts.” (*Wenke, supra*, 6 Cal.3d at p. 751.) In short, “[t]he lawful exercise of the ministerial duty may be compelled; the unlawful exercise of the duty may be restrained.” (*Planned Parenthood Affiliates v. Van de Kamp* (1986) 181 Cal.App.3d 245, 262.)

Prohibitory mandate writs have issued “to restrain a public official from the unlawful performance of a duty . . . where the performance of a statutory ministerial duty would violate the Constitution.” (*Planned Parenthood, supra*, 181 Cal.App.3d at p. 263.) The writ “has also been used to restrain state officials from enforcing ministerial statutory provisions found to be unconstitutional.” (*Ibid.*) This Court “issue[s] writs of mandate directing state officers not to enforce statutes [it] found unconstitutional” in original mandamus proceedings. (*Patterson*

*v. Padilla* (2019) 8 Cal.5th 220, 250; see also *Hardie v. Eu* (1976) 18 Cal.3d 371, 380.) Accordingly, there is a long history of granting writ relief of the sort sought in this case.

This Court recently reiterated the following requirements to obtain writ relief:

“[A] petitioner must demonstrate (1) no ‘plain, speedy, and adequate’ alternative remedy exists [citation]; (2) ‘a clear, present, . . . ministerial duty on the part of the respondent’; and (3) a correlative ‘clear, present, and beneficial right in the petitioner to the performance of that duty.’”

(*Family Violence Appellate Project v. Superior Court* (2026) 20 Cal.5th 564, 585; *id.* at pp. 585-586.) All of these requirements are satisfied here.

The first requirement may be satisfied “where ‘the issues presented are of great public importance and must be resolved promptly.’” (*Family Violence, supra*, 20 Cal.5th at p. 585.) These conditions exist here for the reasons stated above: the tremendous amount of money at issue will have a significant impact on the state and everyone who interacts with the health care system, and a failure to correct course before the federal December 31, 2026 deadline will result in the permanent loss of the opportunity to lawfully collect tax revenue.

The second requirement may be satisfied where a petition seeks “to compel a public agency’s performance or correct an agency’s abuse of discretion whether the action being compelled or corrected can itself be characterized as ‘ministerial’ or ‘legislative.’” (*Santa Clara County Counsel Attys. Assn. v. Woodside* (1994) 7 Cal.4th 525, 540.) This Court has recognized

that a writ may be issued to challenge an ordinance (which is usually a legislative act) that violated a previously enacted agreement. (*Ibid.*) Here, SB 125 amends the previously enacted Proposition 35—a step the Legislature did not have discretion to take without a three-fourths supermajority. DHCS therefore has a duty to refrain from implementing SB 125. Additionally, under Proposition 35, DHCS has a duty to submit a proposed tax to CMS that complies with Proposition 35 and current federal law and to refrain from submitting a non-compliant tax. Furthermore, Respondents have a duty to use all revenue derived from any MCO tax only as allowed by Proposition 35.

As for the third requirement, a “beneficial interest exists where a party has ‘ “some special interest to be served or some particular right to be preserved or protected over and above the interest held in common with the public at large.” ’ ” (*Family Violence, supra*, 20 Cal.5th at p. 595.) Petitioner Dustin Corcoran was one of the official proponents of Proposition 35, which SB 125 unlawfully amended and which DHCS has publicly stated it intends to violate. (PA 6, 50-52.) He has a beneficial interest in ensuring that the State complies with the ballot proposition for which he served as a proponent. CAHP and its President and CEO have a beneficial interest in ensuring their members are taxed in compliance with the law. CMA has a beneficial interest in ensuring that its members receive the benefits Proposition 35 promised.

Accordingly, this Court should issue an order to show cause or alternative writ and, upon return, grant the petition and issue

a peremptory writ for the reasons stated herein. (See Code Civ. Proc., §§ 1087, 1088.)

## IV. CONCLUSION

Petitioners respectfully request that this Court grant this  
Petition and the requested relief.

DATED: October 1, 2026      SHEPPARD, MULLIN, RICHTER  
& HAMPTON LLP

By: /s/ Moe Keshavarzi  
MOE KESHAVARZI  
Attorneys for Petitioners  
CALIFORNIA ASSOCIATION  
OF HEALTH PLANS,  
CALIFORNIA MEDICAL  
ASSOCIATION, DUSTIN  
CORCORAN, and CHARLES  
BACCHI

## **CERTIFICATE OF COMPLIANCE**

Pursuant to California Rules of Court, rules 8.204(c)(1) and 8.486(a)(6), I certify that, according to Microsoft Word, the attached petition and memorandum of points and authorities are proportionally spaced, have a typeface of 13 points, and contain a combined total of 13,987 words.

DATED: October 1, 2026      SHEPPARD, MULLIN, RICHTER  
& HAMPTON LLP

By:       /s/ Moe Keshavarzi        
MOE KESHAVARZI  
Attorneys for Petitioners  
CALIFORNIA ASSOCIATION  
OF HEALTH PLANS,  
CALIFORNIA MEDICAL  
ASSOCIATION, DUSTIN  
CORCORAN, and CHARLES  
BACCHI

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**IN THE SUPREME COURT  
OF THE STATE OF CALIFORNIA**

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CALIFORNIA ASSOCIATION OF HEALTH PLANS,  
CALIFORNIA MEDICAL ASSOCIATION,  
DUSTIN CORCORAN, and CHARLES BACCHI,  
*Petitioners,*

*v.*

CALIFORNIA DEPARTMENT OF HEALTH CARE SERVICES,  
DIRECTOR MICHELLE BAASS, in her official capacity,  
CALIFORNIA DEPARTMENT OF FINANCE, DIRECTOR JOE  
STEPHENSHAW, in his official capacity, CONTROLLER MALIA  
M. COHEN, in her official capacity,  
*Respondents.*

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**PROOF OF SERVICE**

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SHEPPARD, MULLIN, RICHTER &  
HAMPTON LLP

\*Moe Keshavarzi, SBN 223759  
*mkeshavarzi@sheppard.com*

David M. Poell, *pro hac vice* pending  
*dpoell@sheppard.com*

John M. Landry, SBN 194374  
*jlandry@sheppard.com*

Matthew G. Halgren, SBN 305918  
*mhalgren@sheppard.com*

Tori D. Kutzner, SBN 334057  
*tkutzner@sheppard.com*

350 South Grand Avenue, 40th Floor  
Los Angeles, California 90071  
213.620.1780

*Attorneys for Petitioners CALIFORNIA ASSOCIATION OF HEALTH  
PLANS, CALIFORNIA MEDICAL ASSOCIATION,  
DUSTIN CORCORAN, and CHARLES BACCHI*

NIELSEN MERKSAMER LLP

Kurt Oneto, SBN 248301  
*koneto@nmgovlaw.com*

1415 L Street, Suite 1200  
Sacramento, California 95814  
916.446.6752

## PROOF OF SERVICE

### STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

At the time of service, I was over 18 years of age and not a party to this action. I am employed in the County of Los Angeles, State of California. My business address is 350 South Grand Avenue, 40th Floor, Los Angeles, CA 90071.

On October 1, 2026, I served true copies of the documents described as PETITION FOR WRIT OF MANDATE; PETITIONER'S APPENDIX; and PROOF OF SERVICE as follows:

|                                                                                                                                                                                                                           |                                                                                                                                                                 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Department of Health Care Services<br>Office of Legal Services<br><i>By Overnight Delivery</i><br>1501 Capitol Ave, MS 0010<br>Sacramento, CA 95814<br><i>By Mail</i><br>P.O. Box 997413, MS 0010<br>Sacramento, CA 95899 | <i>Respondents</i> CALIFORNIA<br>DEPARTMENT OF HEALTH<br>CARE SERVICES and<br>DIRECTOR MICHELLE<br>BAASS<br><i>By Overnight Delivery and<br/>Mail</i>           |
| Department of Finance<br>1021 O Street, Suite 3110<br>Sacramento, CA 95814                                                                                                                                                | <i>Respondents</i> CALIFORNIA<br>DEPARTMENT OF<br>FINANCE and DIRECTOR<br>JOE STEPHENSHAW<br><i>By Overnight Delivery</i>                                       |
| State Controller's Office<br>Legal Office<br>300 Capitol Mall, Suite 1850<br>Sacramento, CA 95814                                                                                                                         | <i>Respondent</i> CONTROLLER<br>MALIA M. COHEN<br><i>By Overnight Delivery</i>                                                                                  |
| Office of the Attorney General<br>1300 "I" Street<br>Sacramento, CA 95814                                                                                                                                                 | Attorney General Rob Bonta<br><i>Service of petition only as<br/>required by California Rules<br/>of Court, rule 8.29(c)(1)</i><br><i>By Overnight Delivery</i> |

**IF BY OVERNIGHT DELIVERY:** I enclosed the documents in envelopes or packages provided by an overnight delivery carrier and addressed to each person listed in the Service List at the addresses stated therein. I placed the envelope or package for collection and overnight delivery at an office or a regularly utilized drop box or pick-up point of the overnight delivery carrier. I am a resident or employed in the county where the collection occurred.

**IF BY MAIL:** I enclosed the documents in a sealed envelope or package addressed to the persons at the addresses listed above and placed the envelope for collection and mailing, following our ordinary business practices. I am readily familiar with the firm's practice for collecting and processing correspondence for mailing. On the same day that correspondence is placed for collection and mailing, it is deposited in the ordinary course of business with the United States Postal Service, in a sealed envelope with postage fully prepaid. I am a resident or employed in the county where the mailing occurred.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct and that I am employed in the office of a member of the bar of this Court at whose direction the service was made.

Executed on October 1, 2026, at Los Angeles, California.

/s/ Regina Gordon