S185457

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

CITY OF ALHAMBRA, et al.,
Plaintiffs and Appellants,

vs.

COUNTY OF LOS ANGELES, et al.,
Defendants and Respondents.

From a Published Decision of the Second District Court of Appeal
Reversing a Judgment Entered by the Superior Court of the
State of California for the County of Los Angeles
Case No. BS 116375
Honorable James Chalfant, Presiding
[By C.C.P. § 638 Reference to the Hon. Dzintra Janavs (Ret.)]

APPLICATION OF THE LEAGUE OF CALIFORNIA CITIES TO FILE *AMICUS* BRIEF IN SUPPORT OF THE CITY OF ALHAMBRA, ET AL., PLAINTIFFS AND APPELLANTS BELOW; PROPOSED BRIEF OF *AMICUS CURIAE*

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TO THE HONORABLE CHIEF JUSTICE OF THE SUPREME COURT OF THE STATE OF CALIFORNIA:

The League of California Cities, pursuant to Rule 8.520, subdivision (f), of the California Rules of Court, respectfully requests permission to file the accompanying *amicus curiae* brief in support of the 47 cities, plaintiffs and appellants below.

The League of California Cities (the "League") is an association of 474 California cities united in promoting the general welfare of cities and their residents. The League is advised by its Legal Advocacy Committee, which is comprised of 24 city attorneys representing all 16 geographical divisions of the League from all parts of the state. The committee monitors appellate litigation affecting municipalities and identifies those cases, such as the matter at hand, that are of statewide significance.

The League and its member cities have a substantial interest in the outcome of this case. In this case the County of Los Angeles ("the County") advocates a method of calculating the Property Tax Administration Fee ("PTAF") that it charges to cities for assessing, collecting, and allocating their property taxes that significantly increases the amount of the fee. For the 47 cities in this lawsuit, this method of calculating the PTAF has led to an annual increase of approximately $5 million in PTAF. (Joint Appendix, vol. 1, p. 49.) It is our understanding that this method is being used by most, but not all, counties in California, and therefore the increased PTAF charges to cities across that state are substantial.

In support of its position, the County points to guidelines prepared by the California State Association of County Auditors ("County Auditors' Association"). The Legislature, however, has directed that these guidelines be subjected to the public review process of the Administrative Procedure Act before they may have any legal effect, and that has not occurred. Nevertheless, county auditors continue to rely on these guidelines, and therefore establishing that these guidelines should be subjected to the rigors of the Administrative Procedure Act is a matter of great interest to the cities of California.

Furthermore, the County asserts in its briefing that the League participated in the preparation of these guidelines. The fact is, notwithstanding the County's claims to the contrary, the League did not collaborate in the preparation of these guidelines, and has never endorsed them. The League thus finds it necessary to submit this *amicus* brief to set the record straight.

The League believes its perspective on this matter is worthy of the Court's consideration and will assist the Court in deciding this matter. The League's counsel has examined the briefs on file in this case and is familiar with the issues involved and the scope of their presentation and does not seek to duplicate that briefing.

We believe there is a need for additional briefing on this issue, and hereby request that leave be granted to allow the filing of the accompanying *amicus curiae* brief.

No party or counsel for a party in this appeal authored any part of the accompanying *amicus curiae* brief or made any monetary contribution to fund the preparation of the brief. No person or entity other than the League

and its attorneys in this matter made any monetary contribution to fund the preparation of the brief.

Dated: February 10, 2011

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AMICUS CURIAE BRIEF

I. INTRODUCTION

The issue in this case is whether Los Angeles County ("the County") may lawfully charge fees to cities for certain expenses incurred by the County in its administration of property taxes. The resolution of this issue requires this Court to interpret statutes in the Revenue and Taxation Code. Applying basic principles of statutory interpretation, the California Court of Appeal for the Second District concluded that these charges were unlawful. Because of the large amount of money at stake, and because the Second District's decision affects every county in this State, the County persuaded this Court to accept review of the decision, arguing that the issue is of significant statewide importance. The League of California Cities ("the League") agrees that the issue is of statewide importance, and thus submits this *amicus* brief. The League also submits this brief to respond to misleading assertions by the County that the League collaborated in the preparation of self-serving guidelines by the California State Association of County Auditors ("County Auditors' Association") which the County asserts supports its position. For the reasons set forth in the Plaintiff Cities' brief and in this *amicus* brief, the Second District correctly interpreted the relevant statutes to find that the fees in question are unlawful.

County auditors are charged with the responsibility of distributing the proceeds of property taxes to various local entities, including cities, within their jurisdiction. One such entity which receives such funds is the "Educational Reserve Augmentation Fund" ("ERAF"). ERAF was created by the Legislature in the early 1990s to provide funding for schools by diverting property taxes from cities, counties, and non-school special districts.

In 2003 and 2004, the Legislature made changes to the tax laws that

reduced other tax revenues that had previously accrued to both cities and counties. Specifically, the Legislature (1) reduced the share of sales taxes going to cities and counties by a quarter of a cent and used the proceeds to secure state bonds and (2) reduced the Vehicle License Fee ("VLF") that was paid to cities and counties.

In order to compensate cities and counties for this loss in income – in essence, to make the cities and counties "whole" – the Legislature adopted sections 97.68 and 97.70 of the Revenue and Taxation Code. Section 97.68,[1] referred to as the "Triple Flip," reimbursed cities and counties with funds from ERAF to make up for the lost sales tax. Section 97.70, known as the "VLF Swap," likewise reimbursed cities and counties for the lost VLF revenue, again using ERAF as the source.

In addition to Sections 97.68 and 97.70, the Legislature enacted Section 97.75, which authorized counties, after two fiscal years, to charge cities for the cost of their services to implement Sections 97.68 and 97.70. After two fiscal years, however, the County greatly increased the Property Tax Administration Fee ("PTAF") that it charges to cities – a $5 million increase, although the County's cost to implement the Triple Flip and the VLF Swap was only $35,000.

Section 95.3 of the Revenue and Taxation Code authorizes a county to charge PTAF to cities for the costs it incurs assessing, collecting, and allocating property taxes to cities. PTAF, however, is not charged on property taxes collected for ERAF or the schools. The County justified its increase in PTAF in 2006-07 and subsequent fiscal years by treating the funds transferred to the cities under the Triple Flip and the VLF Swap from ERAF as property taxes collected for the cities, and therefore subject to

[1] This reference, and all further references to an unidentified code section, is to the Revenue and Taxation Code.

PTAF, even though those funds replaced VLF and sales tax payments to which PTAF did not apply. It is this additional charge which the cities are challenging in this litigation.

There is no dispute that before the enactment of the Triple Flip and the VLF Swap, the County did not, and could not, collect PTAF on these property taxes. Moreover, Section 97.75, not Section 95.3, specifies what costs the County can recover for implementing Sections 97.68 and 97.70, and these costs only consist of the costs to makes the calculations and allocations required by the Triple Flip and the VLF Swap. They do not include the costs to assess, collect, and allocate the underlying property taxes that are redirected from ERAF to the cities.

Significantly, there is nothing in Sections 97.68, 97.70, or 97.75 to suggest any intent by the Legislature to transfer from counties to cities a significant portion of the cost to administer the property tax system. The Triple Flip and the VLF Swap treat cities and counties in most respects the same. They transfer revenues from cities and counties to the State, and from ERAF to cities and counties. There is no indication that the Legislature also sought to transfer any part of the costs for collecting property taxes from counties to cities.

In support of its position, the County has pointed to two sentences in an appendix to guidelines prepared by the County Auditors' Association. However, these guidelines are not entitled to any weight, as they have not been properly adopted or subjected to public review as the Legislature has required. In order to achieve greater uniformity in the process of property tax allocation across the state, the Legislature has directed that these guidelines be subjected to the public review process of the Administrative Procedure Act if they are to be given any legal weight. But this public review has not occurred, and until it does, the so-called guidelines have no legal status.

Furthermore, to give these guidelines credence, the County claims that the League participated in their preparation. This claim is untrue. Rather, the League was only provided an opportunity to comment on a draft version of these guidelines, which draft did not even contain the appendices with the two sentences on which the County relies.

II. ARGUMENT

A. The County's application of the PTAF upsets the equitable balance set up by the Legislature in the Triple Flip and the VLF Swap.

In both the Triple Flip and the VLF Swap, the Legislature took a stream of revenue that had been going to cities and counties – sales tax in the case of the Triple Flip and VLF in the case of the VLF Swap – and replaced it with property tax funds that previously flowed to ERAF. The Triple Flip was codified in Section 97.68, and the VLF Swap was codified in Section 97.70.

A close reading of these provisions shows essentially no distinction between cities and counties, and the legislative history reveals no intent to make either the Triple Flip or the VLF Swap operate differently on cities and counties. And yet, the County is using the Triple Flip and the VLF Swap to shift to cities millions of dollars of property tax administration costs that, prior to the Triple Flip and the VLF Swap, the Legislature had determined counties ought to bear. As a result, the County ends up in a markedly better position, in relation to the cities, than before these provisions were enacted. This result was not the intent of the Legislature. The Triple Flip and the VLF Swap were intended to treat counties and cities the same, and they were meant to be largely revenue neutral as to local governments (although not as to schools or the State). They were not intended to create a windfall for counties at the expense of cities.

1. It is evident from Sections 95.3 and 97.75 that the Legislature did not expect cities to be charged PTAF for the ERAF funds redirected to cities under the Triple Flip and the VLF Swap.

Section 95.3, the PTAF statute, is broad. It directs counties to include in the PTAF all property tax administrative costs incurred by the assessor, the tax collector, the county board of equalization, the assessment appeals board, and the auditor. The implementation of the Triple Flip and the VLF Swap require various calculations and allocations to be made by the auditor (see, e.g., § 97.68 subds. (d)(1)(B), (d)(2)(B); § 97.70 subds. (a)(1), (b)(1)), and the cost to the auditor to make these calculations and allocations are the sorts of costs that would be included in the PTAF if Section 95.3 applied to the Triple Flip and the VLF Swap. But because PTAF is not charged for property taxes "determined with respect to . . . ERAF" (§ 95.3(b)(1)), and because the funds transferred to cities under the Triple Flip and the VLF Swap would otherwise have flowed to ERAF, these costs should not be included in the PTAF calculation.

It is evident that this was the Legislature's understanding, or it would not have enacted Section 97.75. Section 97.75 allows the counties, starting in the 2006-07 fiscal year, to charge cities "for the services performed by the county under Sections 97.68 and 97.70" (the Triple Flip and the VLF Swap). As the Court of Appeal correctly found, the only services performed by the County under Sections 97.68 and 97.70 are the calculations and allocations the auditor needs to do in order to make the fund transfers mandated in those sections. If, as the County contends, the County could charge PTAF under Section 95.3 for the funds transferred to the cities under the Triple Flip and the VLF Swap, then Section 97.75 would be unnecessary.

The County argues that the second sentence of Section 97.75 simply allows the County to collect the charges prohibited in the first sentence, but does not prohibit the collection of the full PTAF under Section 95.3.[2] (Reply Brief on the Merits, p. 3.) But if Section 95.3 applied to the Triple Flip and VLF Swap funds, then the cost of the services referred to in the second sentence of Section 97.75 would already be recoverable under Section 95.3 and therefore the second sentence of Section 97.75 would be meaningless surplusage. Consequently, the Legislature must have considered Section 95.3 to be inapplicable to the Triple Flip and VLF Swap funds, and that is why it needed to enact Section 97.75.

Importantly, Section 97.75 does not authorize counties to charge the full PTAF on the funds transferred to cities under the Triple Flip and the VLF Swap. By its own terms, Section 97.75 limits the charge to the cost of performing the services required by Sections 97.68 and 97.70. If the Legislature had wanted to allow the counties to start including the Triple Flip and VLF Swap funds in the PTAF, it would simply have said that, with a clear reference to Section 95.3. It did not. Instead, it assumed that the Triple Flip and VLF Swap funds were not included in the PTAF, and in Section 97.75 it authorized the counties to recover only the costs associated with the Triple Flip and VLF Swap – the actual costs incurred by the counties to do the calculations required by these provisions. It did not authorize the inclusion of the Triple Flip and VLF Swap funds in the PTAF calculations.

It was particularly reasonable for the Legislature to do this, and it coincides with the League's understanding of the policies behind both the Triple Flip and VLF Swap. The Triple Flip and VLF Swap took revenues

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[2] The second sentence of Section 97.75 states: "For the 2006-07 fiscal year and each fiscal year thereafter, a county may impose a fee, charge, or other levy on a city for these services, but the fee, charge, or other levy shall not exceed the actual cost of providing these services."

that had been going to cities and counties and replaced them with revenues that previously flowed to ERAF. No intent was expressed in either the statutes or the legislative history to treat cities differently from counties as to these State fiscal maneuvers – they were both getting the same deal. It therefore does not make sense to shift to the cities the cost of collecting and allocating the property taxes that had been destined to ERAF and which were redirected to the cities under the Triple Flip and VLF Swap. The counties bore these costs before the Triple Flip and VLF Swap, and there is no indication that the Legislature intended to shift those costs on account of the Triple Flip and VLF Swap.

2. Section 97.75 fairly apportions the new costs caused by the Triple Flip and the VLF Swap.

Section 97.75 allows counties to charge cities for the cities' share of the costs incurred by the counties in implementing the Triple Flip and the VLF Swap. This requirement is reasonable because these costs did not exist before the enactment of the Triple Flip and the VLF Swap. It would therefore be unfair to require the counties to bear this new cost on their own (although, as the parties agree, the Legislature did impose those costs on counties in the 2004-05 and 2005-06 fiscal years). Instead, the cities should bear their share of these new costs commencing in the 2006-07 fiscal year pursuant to Section 97.75.

In contrast, the costs to assess, collect, and allocate the property taxes that the Triple Flip and VLF Swap redirect from ERAF to the cities and counties, were costs counties bore before the Triple Flip and VLF Swap. Because those property taxes were "determined with respect to . . . ERAF" (§ 95.3(b)(1)), the counties absorbed the costs, and as pointed out above, there is no indication that the Legislature intended to shift these costs to the cities when it enacted the Triple Flip and the VLF Swap.

The County contends that the purpose of Section 97.75 was to ensure that the parties that benefited from the Triple Flip and VLF Swap were the ones that paid for the costs associated with collecting the property taxes that were ultimately used to fund the Triple Flip and VLF Swap. (Reply Brief on the Merits, p. 7.) There are several problems with this argument.

First of all, it is incorrect to say that cities (and counties) necessarily benefit from the Triple Flip and the VLF Swap. With the Triple Flip in particular, the funds the cities (and counties) receive from ERAF are calculated each year to match the sales tax they lose to the State. Cities (and counties) do not obtain any benefit from this arrangement. Although the County goes to great lengths to show that cities and counties have received more revenues under the VLF Swap than they would have without it because the growth in VLF Swap revenues is tied to the growth in real property values, it was never preordained that this would occur. As recent experience has shown, real property values can also decrease.

Moreover, because cities and counties win or lose together under the VLF Swap, any change in VLF cash flows over what was anticipated when the VLF Swap was adopted provides no reason to shift any of the property tax administration costs from counties to cities. To the extent the cities benefit, the counties do to the same extent, and there is no reason to provide an additional benefit to counties at the expense of cities.

Second, if the Legislature wanted the cities to pay the costs of assessing, collecting, and allocating the property taxes that are ultimately diverted from ERAF to the cities under the Triple Flip and the VLF Swap, it only needed to state that the PTAF calculation for those funds under Section 95.3 would be attributed to the city that receives the funds. Section 97.75 would be unnecessary, and because PTAF is directly related to the amount of tax allocated to an entity, no other entity would be charged for these costs.

But as already explained, the Legislature did not do this. Instead, it enacted Section 97.75, which is much more limited than Section 95.3 in the costs that it covers.

And third, as explained above, the Legislature intended to treat cities and counties the same under the Triple Flip and the VLF Swap. There is no evidence that it intended to use these provisions to shift to cities a cost that had until then been born by the counties. Section 97.75 requires that the new costs created by the Triple Flip and the VLF Swap be shared by the cities and the counties, but it does not allow the counties to shift preexisting costs to the cities.

B. The County Auditors' Guidelines have no legal status.

To support its legal position, the County cites to guidelines – the "SB 1096 Guidelines" – prepared by the California State Association of County Auditors ("the County Auditors' Association"). Although the County concedes that the guidelines "do not have the force and effect of law" (Opening Brief, p. 19), the County continues to refer to them. (See, e.g., Opening Brief, p. 22, fn. 35, Reply Brief on the Merits, p. 18.) This is particularly inappropriate because the Legislature has directed that these guidelines be subjected to the rigors of the Administrative Procedure Act ("the APA") before they be given legal effect, which the County concedes has not occurred.

The APA prohibits a state agency from issuing guidelines or a regulations interpreting a statute unless it follows the notice-and-comment procedures of the APA. (Gov. Code § 11340.5) A guideline or regulation that is not promulgated following the procedures of the APA is an invalid "underground regulation." (*Morning Star Co. v. State Board of Equalization* (2006) 38 Cal.4th 324, 333.)

Generally, the APA only applies to state agencies, and therefore would not apply to guidelines prepared by a non-state entity, such as the California State Association of County Auditors. However, in 2001 the Legislature amended section 96.1 of the Revenue and Taxation Code to provide that guidelines prepared by the County Auditors' Association for the application of the property tax allocation laws should be adopted by either the State Controller or the State Department of Finance and promulgated through the APA process:

> "Guidelines for legislation implementation issued and determined necessary by the State Association of County Auditors, and when adopted as regulations by either the Controller or the Department of Finance pursuant to Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code [the Administrative Procedure Act], shall be considered an authoritative source deemed correct until some future clarification by legislation or court decision." (§ 96.1, subd.(c)(1).)

Given the conflict of interest inherent in having counties allocate property taxes between themselves and the other local governments that receive them, the need for a transparent process of public review for the preparation of uniform guidelines is obvious.[3]

[3] Recent litigation concerning the allocation of property taxes as well as audits by the State Controller show the need for uniformly applicable regulations. See, e.g., *City of Dinuba v. County of Tulare* (2007) 41 Cal.4th 859; *Los Angeles Unified School District v. County of Los Angeles* (2010) 181 Cal.App.4th 414; *City of Scotts Valley v. County of Santa Cruz* (pending in the 1st Dist. Court of Appeal, A126357); *City of Clovis v. County of Fresno* (pending the 5th District Court of Appeal, F060148). See also the State Controller's 2010 property tax audit of Los Angeles County, www.sco.ca.gov/Files-AUD/12_2010ptxlosangeles.pdf, cited in the County's Reply Brief on the Merits, p. 19, fn.40.

This process, however, has never been undertaken. The guidelines upon which the County would have this Court rely are not in the California Code of Regulations, and they have not been vetted through the public process of the APA. They have not been promulgated as directed by Section 96.1, and therefore they are not entitled to any deference. They are only the collective opinion of county officials acting through their private association with no legislative authority of any sort.

C. The League of California Cities neither collaborated in the preparation of the County Auditors' guidelines nor endorsed them.

The County also continues to assert, although with less enthusiasm than it did in the Court of Appeal, that the League participated in the creation of the "SB 1096 Guidelines." In its Opening Brief, the County states that "the Uniform Guidelines . . . had been promulgated with the involvement of . . . the League of Cities." (Opening Brief, p. 22, fn. 35.) In its Reply Brief the County states the "the evidence in the record is that the Guidelines were developed with input from representatives of the League of California Cities." (Reply Brief on the Merits, p. 18.) This claim is simply not true, particularly with regard to the one reference in the guidelines that the County points to in support of its position – two sentences in small print at the bottom of a chart in the appendix. (Joint Appendix, vol. 1, p. 95.)

The guidelines were drafted by county auditors and county tax managers. (See Joint Appendix, vol. 1, p. 58.) Although the County submitted several declarations in opposition to the Cities' writ petition (see, e.g., Joint Appendix, vol. 2, pp. 436-62), none avers that the League "collaborated" or "participated" in the preparation of these guidelines. The only evidence in the record of the League's participation in the preparation

of the guidelines is a vague statement on page six of the guidelines thanking ten different entities, including the League, for their "time and immeasurable help." (Joint Appendix, vol. 1, p. 59.) This vague statement is not evidence that the League actually participated in the creation of the guidelines, much less knew of and acquiesced in the two sentences buried in an appendix on which the County would have this case turn.

Given the opportunity, the League would show that the League's only involvement in the guidelines was to receive drafts of the guidelines for comment, and that none of these drafts included the appendix that contains the two sentences that support the County's theory in this case.[4] The League never saw the appendix at issue until after the guidelines were published, and had no opportunity to comment on these sentences.[5]

III. CONCLUSION

The County of Los Angeles has used the Triple Flip and the VLF Swap as an excuse to shift millions of dollars of its administrative costs to cities. But the Legislature intended the Triple Flip and the VLF Swap to treat cities and counties alike, and there is no indication that it intended this cost to be shifted to cities. The Legislature enacted Section 97.75 to address the allocation of the new costs caused by the Triple Flip and the VLF Swap, and as the Court of Appeal found, Section 97.75 only allows the County to

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[4] These guidelines are a 163-page document (Joint Appendix, vol. 1, pp. 53-215), and in this entire document the only direct support that that County finds for its theory in this case are two sentences in small print at the bottom of a chart in one of many appendices. (Joint Appendix, vol. 1, p. 95.)

[5] Since it is not a party to this action, the League has not had the opportunity to introduce evidence of these facts. However, the League recites them here to explain its indignation at the County's claims that the League collaborated with the County Auditors Association in the creation of these guidelines.

recover the costs actually caused by the Triple Flip and the VLF Swap. The League therefore urges this Court to affirm the decision of the Court of Appeal.

Dated: February 10, 2011

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WORD COUNT CERTIFICATION

I certify that this brief contains a total of 3,604 words as indicated by the word count feature of the Microsoft Word computer program used to prepare it.

Dated: February 10, 2011

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Benjamin P. Fay

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