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# UPDATE ON MUNICIPAL FINANCE:
# Propositions 13, 62 and 218 and Related Law

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by

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## *I. Introduction.*

The restrictions on local government finance in California have become much contested areas of the law. This paper covers developments in roughly the twenty-four months prior to the date of this paper. There is much to report. The paper is organized with respect to revenue type: taxes (of various sorts), assessments, and fees. A discussion of initiative and election issues concludes this paper.

## *II. Taxes.*

A. Proposition 62 and Utility Users Taxes. The decisions in *Santa Clara County Local Transportation Authority v. Guardino*, 11 Cal.4th 220 (1995), and *Howard Jarvis Taxpayers Association v. City of La Habra*, 25 Cal.4th 809 (2001), answered most questions regarding Proposition 62 adversely to the taxing power of local governments, holding that voter approval of general taxes is required of counties and general law cities. However, a few questions remain unresolved, such as: Is the *Guardino* decision, holding Proposition 62 enforceable and overruling the prior Court of Appeals decisions to the contrary, retroactively applicable to taxes increased during the time Proposition 62 was thought to be unenforceable, even in the face of strong equities, such as reliance on the revenue stream in employee contract negotiations? Was Proposition 218's tax provision intended to supersede Proposition 62 because it completely duplicates its provisions, moving them to the Constitution, but provides a later "window period," perhaps suggesting intent to override the earlier "window period" established by Proposition 62?

A utility users tax case involving the County of Santa Cruz and the City of Scotts Valley had promised to provide published authority on these questions. However, the voters intervened – affirming Scotts Valley's tax and repealing the County's. In *Griffith v. County of Santa Cruz*, Sixth District Court of Appeal Case No. H019505, the Santa Cruz County Superior Court ruled on remand that the Scotts Valley case was entirely moot, that the case against the County was moot as to prospective relief and the claim for retrospective relief was barred by the plaintiffs' failure to file timely claims.

A number of other Proposition 62 cases have been filed in the last two years, including *Howard Jarvis Taxpayers Association v. City of Norwalk*, Los Angeles County Superior Court Case No. VC 038845 and *Scherzer v. City of East Palo Alto*, San Mateo County Superior Court. Most have either settled or been resolved in the trial court without appeal. While it remains possible that appellate guidance on the defenses noted above will be forthcoming, no currently pending case is an obvious candidate to provide it.

A recent utility users tax case which did not turn on Proposition 62 is *City of Pasadena v. AT&T Communications of California, Inc.*, 103 Cal.App.4th 981 (2002). This case interpreted the term "remit" as used in Pasadena's utility users tax ordinance to require the utility to "send" tax payments by the date specified in the ordinance rather than to require that the City "receive" the money in that time. This provides instruction for drafters of tax ordinances and guidance for late payment disputes and will be of interest in non-tax fiscal cases, too.

B. Property Taxes. Orange County has become a hotbed of property tax litigation of late. First was *Bunker v. County of Orange*, 103 Cal.App.4th 542 (2002), in which the Court of Appeal upheld the application of Revenue & Taxation Code § 1604, which provides that if a County fails to provide a hearing on a Prop. 8 property tax assessment appeal within 12 months, the County is obliged to adopt the taxpayer's proposed valuation. This decision, made applicable to a large number of Prop. 8 appellants, had a significant impact on property tax proceeds payable to the County and other local governments in Orange County.

Of much greater consequence is *Orange County v. Bezaire*, 117 Cal.App.4th 121 (2004), which rejected a trial court ruling that had threatened to overturn the assessment practices of all 58 counties and to deprive local governments of $10 billion of property tax revenues. Proposition 13, as perhaps all California homeowners know, requires County Assessors to assess the value of property at its historic acquisition cost or purchase price. The valuation may not increase by more than 2% per year. Proposition 8 allows property owners whose properties have declined in fair market value since they were acquired (a common occurrence in Southern California in the early and mid-1990's) to apply for a reduced assessment. When fair market values increase again (as they have done quite strongly in Southern California since the late 1990's) assessors have recouped the reduced valuations by more than 2% as necessary to regain the ground lost to Proposition 8 reassessments. In this case, a Seal Beach lawyer-homeowner filed suit, contending that the 2% cap on annual reassessments applies to a Prop. 8-reduced assessment, too, giving Proposition 8 a downward-ratcheting effect and making a temporary reduction in fair market value a permanent benefit for a property owner. The trial court ruled against the County and the matter was appealed. Media reports note that the trial judge himself filed (and lost) a Proposition 8 appeal following his ruling.

The case attracted considerable attention; *amicus* briefs were filed on behalf of the County Assessors Association of California, the California State Association of Counties, the League of California Cities, the state Department of Finance, the Education Legal Alliance of California (an affiliate of the California School Boards Association), the State Senate, and by Patrick Woosley, the plaintiff in *Woosley v. State of California*, 3 Cal.4th 758 (1992), a decision which had invalidated the application of the vehicle license fee to vehicles brought into California from out of state. KOCE-TV, the public television station serving Orange County, covered the appellate arguments.

In a brief, unanimous opinion, the appellate court reversed, ordering the trial court to grant judgment to the County. The court ruled that the language and intent of Propositions 13 and 8 was to allow the assessment of property based on 2% appreciation from historic acquisition cost, even if recoupment of a Proposition 8 reassessment lead to greater than 2% increases in a given year:

> "We conclude that the intent of the drafters of Proposition 13, as it was amended in 1978 within six months of its passage by Proposition 8, a measure for which Paul Gann himself co-wrote the ballot argument, is that the inflation factor is calculated against the original purchase price. … Calculating the inflation cap based on a previous year's reassessed value is fundamentally inconsistent with the system that Proposition 13 put in place." 11 Cal.Rptr.3d at 480.

Another property tax case affecting some 25 California cities is *Howard Jarvis Taxpayers Association v. County of Orange (City of Huntington Beach)*, 110 Cal.App.4th 1375 (2003), involving a voter-approved property tax override to fund public safety pensions. Following the adoption of Proposition 13, the California Supreme Court held in *Carman v. Alvord*, 31 Cal.3d 318 (1982), that a tax in excess of 1% of assessed value could be imposed to fund such pension programs by virtue of the exception of Article XIII A, § 1(b) for "interest and redemption changes on any … [i]ndebtedness approved by the voters prior to July 1, 1978." HJTA sued Huntington Beach when that City imposed a property tax override to fund pension and related benefits for City employees established by the City after the 1978 date of the voter approval of the City's Charter provisions authorizing the local pension system. The City argued that the voters had authorized a pension system, including later-conferred benefits. HJTA argued that the voter approval should be limited to benefits in existence when the voters approved the Charter amendment in 1978. The Court of Appeal ruled for HJTA and the California Supreme Court denied review. It now lies for the City (and 24 others) to sort out the difficult problem of determining the amount of a property tax override allowable given the practical difficulty of separating the cost of pension benefits awarded prior to 1978 from the cost of subsequently granted benefits. Assemblyman Harman (R-Huntington Beach) has submitted a request for an Attorney General's opinion on this issue to assist Huntington Beach

C. Business Taxes: *Pacific Gas & Electric Co. v. City of Oakland*, 103 Cal.App.4th 364 (2002), involves a rather obscure limitation on business license taxes. Article XIII, § 19 of the California Constitution provides, in relevant part:

> "The Board [of Equalization] shall annually assess (1) pipelines, flumes, canals, ditches, and aqueducts lying within 2 or more counties and (2) property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the State, and companies transmitting or selling gas or electricity. This property shall be subject to taxation to the same extent and in the same manner as other property.
>
> *No other tax or license charge may be imposed on these companies which differs from that imposed on mercantile, manufacturing, and other business corporations*. This restriction does not release a utility company from payments agreed on or required by law for a special privilege or franchise granted by a government body. …" (Emphasis added.)

PG&E objected to Oakland's business license tax, arguing that this constitutional provision entitled it to be taxed in the same classification as retailers, which were subject to a lower tax rate than the rate Oakland imposed on PG&E. The Court of Appeal affirmed judgment for PG&E, upholding a judgment for almost $4 million:

> "By 'other businesses,' therefore, section 19 should be read as referring to other businesses in the same class as manufacturing or mercantile businesses; *i.e.,* businesses that, like public utilities, manufacture and sell a product. A tax imposed on a particular kind of public utility – such as a producer of electricity – therefore, is invalid if it differs from that imposed on businesses comparable to mercantile and manufacturing businesses."

In light of this case and related case law developing under the Dormant Commerce Clause of the federal Constitution, which prohibits local taxes which discriminate against inter-state or inter-city commerce,[1] it is no longer safe to ignore local business license taxes. Any city that obtains meaningful revenue under its business license tax would do well to review its ordinance for problems of this kind. Recent dormant Commerce Clause cases have cost San Francisco and Los Angeles hundreds of millions of dollars, finding that credits against gross receipts business license taxes for payments of payroll taxes amounted to a preference for in-city manufacturers at the expense of those who manufacture elsewhere.

Also of note is *Opinion No. 03-412 of the California Attorney General* (September 25, 2003), which concludes that a

> "city may, by ordinance, shift the burden of collecting an annual business license fee from individual swap meet vendors to the operator of the swap meet without the prior approval of the city voters if the fee is imposed as a regulatory measure."

If the legal incidence of the tax were shifted from vendors to the swap meet operator, this would be a new or increased tax within the meaning of Government Code § 53750(h), requiring voter approval under Proposition 218. If, however, the legal incidence of the tax remains on the vendors, but the duty to collect the tax on behalf of the City is made a regulatory obligation of the swap meet operator, this is not taxation, but regulation, and outside the voter-approval requirements of Propositions 62 and 218 under *Sinclair Paint Co. v. State Board of Equalization*, 15 Cal.4th 866 (1997).

D. Transient Occupancy Taxes. Given the voter approval requirements of Propositions 62 and 218, many cities and counties are turning to transient occupancy, or hotel bed, taxes to fund general fund programs. There has been increasing litigation in this area, too. A recent decision is *Patel v. City of San Bernardino*, 310 F.3d 1138 (9th Cir. 2002). In 1998, the Fourth District Court of Appeal invalidated San Bernardino's bed tax ordinance because it did not clearly provide a basis to distinguish taxable occupancies of hotels and motels from nontaxable, short-term occupancies of houses and apartments and was therefore in violation of the requirements of federal due process that tax and penal ordinances not be unduly vague. *City of San Bernardino Hotel/Motel Ass'n v. City of San Bernardino*, 59 Cal.App.4th 237 (1997). This federal action followed, seeking a remedy under 42 U.S.C. § 1983 for taxes paid under the invalid ordinance, in what appeared to be an end-run around the City's claiming ordinance. The 9th Circuit acknowledged that the federal Tax Injunction Act prohibited injunctive relief against tax measures, and a prior federal Supreme Court ruling that § 1983 does not allow an end-run around that Act. The Court accepted, as required on review of a dismissal for lack of subject matter jurisdiction, the plaintiffs' allegation that the City continued to enforce the tax after entry of a final judgment invalidating it. The Court ruled the case should go forward notwithstanding the Act and the prior Supreme Court ruling because the plaintiffs had no remedy at state law as the state courts had granted declaratory relief, but refused to grant injunctive relief. The case is very narrow and likely limited to its facts. It is demonstrative, however, of the extent the hotel industry is prepared to go to litigate these taxes.

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[1] Among the more recent cases in this line is *General Motors Corp. v. City of Los Angeles*, 35 Cal.App.4th 1736 (1995).

Another pending case which will explore similar issues regarding bed taxes is *City of Vacaville v. Pitamber*, First District Court of Appeal Case No. A104634. As this paper is written, the case is being briefed and the League of California Cities is considering *amicus* support. The case raises the vagueness issue in *Patel* as well as the power of the City to issue an administrative subpoena for tax records to aid in enforcement of the tax.

E. Mello-Roos Special Taxes. Of note with respect to special taxes imposed on Community Facilities Districts under the Mello-Roos Act is Government Code § 53343.1, added by Chapter 960 of the Statutes of 2002 (A.B. 2851, Cogdill, R-Modesto). This measure requires any Mello-Roos district formed after January 1, 1992, on request by a resident or property owner of the district, to prepare within 120 days of the end of its fiscal year an "annual report." That report must include:

"(a) The amount of special taxes collected for the year.
(b) The amount of other moneys collected for the year and their source, including interest earned.
(c) The amount of moneys expended for the year.
(d) A summary of the amount of moneys expended for the following:

(1) Facilities, including property.
(2) Services.
(3) The costs of bonded indebtedness.
(4) The costs of collecting the special tax under § 53340.
(5) Other administrative and overhead costs.

(e) For moneys expended for facilities, including property, an identification of the categories of each type of facility funded with amounts expended in each category, including the total percentage of the cost of each type of facility that was funded with bond proceeds or special taxes.
(f) For moneys expended for services, an identification of the categories of each type of service funded with amounts expended in each category, including the total percentage of the cost of each type of service that was funded with bond proceeds or special taxes.
(g) For moneys expended for other administrative costs, an identification of each of these costs.
(h) A certification and explanation by the district of how the moneys described in subdivisions (d), (e), (f), and (g) comply with Section 53343."

The measure also requires that the annual report "contain references to the relevant sections of the resolution of formation of the district so that interested persons may confirm that bond proceeds and special taxes are being used for authorized purposes." The statute states that local governments need not be reimbursed for this mandate because they have the power to impose a fee to recover the cost of compliance.

The measure is apparently intended to create accountability in the management of Mello-Roos funds and may prove a popular device for gadflies, taxpayer advocates and, eventually, litigants. For Mello-Roos funds that support bonded indebtedness, however, the risk that the

revenue stream will be imperiled by such a suit is small, due to the short statutes of limitation and other protections afforded bonded debt.

Chapter 771 of the Statutes of 2002 (A.B. 337, Correa, D-Santa Ana) amended Civil Code § 1102.6b to impose duties on sellers of property subject to Mello-Roos taxes to disclose those taxes to their buyers.

F. Real Property Transfer Taxes. The Attorney General has opined that cities are immune from county real property transfer taxes as "political subdivisions" within the intent of an exemption to the tax for such entities granted by Revenue and Taxation Code § 11922. 85 *Ops. Calif. Att'y Gen'l* 235 (2002). The reasoning of the opinion extends to special districts, as well:

> "At the time the California Legislature adopted almost all of the language of [the since-repealed federal stamp tax on real property conveyances] in enacting § 11922 …, the term 'political subdivision' as used in both statutes was intended to be broad enough to include special districts …. This same analysis may be made with respect to cities." *Id.*, slip op. at 3-4.

G. Other Special Taxes. Roseville continues to be the unfortunate jurisdiction most often lending its name to adverse appellate decisions in municipal finance. The latest is *Howard Jarvis Taxpayers Ass'n v. City of Roseville*, 106 Cal.App.4th 1178 (2003). When an initiative to repeal the City's utility users tax qualified for the ballot, the City Council proposed a competing measure to amend the City's charter to preserve the tax, but providing: "All Utility Users Tax Revenue received shall be budgeted and appropriated solely for police, fire, parks and recreation or library services." Both measures passed by simple majority, with the charter amendment receiving more votes. The City contended its measure controlled by virtue of having received more votes. The HJTA sued, contending the City's measure was a special tax, required two-thirds voter approval and, because it did not attain that level of support, was a nullity and that the repeal measure controlled. HJTA prevailed in both trial and appellate courts.

The Court of Appeal declined to decide whether Proposition 62 applied to charter cities (an issue resolved in favor of charter cities in several other appellate cases, both before and after Proposition 218) and relied solely on Proposition 218. It had little difficulty concluding the tax measure proposed by the City restricted the use of tax proceeds to specific purposes and thus made the measure a special tax requiring two-thirds voter approval.

Most interesting is the case's discussion of Proposition 219, adopted in 1998 to add Article XI, § 7.5 to the California Constitution, providing that no local government may submit measures to the voters that "Contain alternative or cumulative provisions wherein one or more of those provisions would become law depending upon the casting of a specified percentage of votes for or against the measure." Thus, a measure must be a general or a special tax on its face and not merely on the basis of the number of votes it receives:

> "If the local government asks the voters to approve a special tax, it might gain an electoral advantage; but a two-thirds vote is required for approval. Such a measure must be placed before the voters on an all-or-nothing basis.

Accordingly, if a special tax fails to gain a two-thirds voter approval, it is not approved and the measure can be given no effect." 106 Cal.App.4th at 1189.

While the case breaks little new ground, it does provide a helpful reminder of the potential relevance of Proposition 219 to discussions of special and general taxes.

Another special tax issue facing the state is the looming expiration by their terms of special half-cent sales taxes for transportation programs, like San Bernardino's Measure I (slated for extension on the November 2004 ballot), Orange County's Measure M and Los Angeles County's Measures A and C. The bulk of these were approved by simple majority votes before the decision in *Rider v. County of San Diego*, 1 Cal.4th 1 (1991), which rejected an earlier Proposition 13 precedent and held such special-purpose taxes to require ⅔-voter approval. Gaining renewed approval of this substantial element of transportation funding under the ⅔-voter approval requirement will be a daunting challenge, especially in the more conservative areas of the State. Accordingly, two proposals were made in the current Legislature to amend Proposition 13 to allow such taxes to be approved by 55% of the electorate, as is now required for school bonds under Proposition 34. The measures are ACA 7 (Dutra, D-Fremont) and SCA 2 (Torlakson, D-Contra Costa). The Assembly measure is now dead, but Senator Torlakson's measure may reach the Senate floor, having been referred there on a 3-2, party-line committee vote. In its current form, the Torlakson bill would allow such taxes to be renewed on a simple majority vote. Unless the Republican legislators soften their stance against measures they view as taxes, this measure may not move to the ballot except by initiative.

A similar measure is Senator Alarcon's (D-Los Angeles) SCA 11, which would allow 55% voter approval of general obligation bonds or special sales taxes to fund "infrastructure projects," defined to include affordable housing; transportation; acquisition of land for agriculture, recreation, or open space use; and "general infrastructure." As this paper is written, the measure is slated to be heard in the Senate Constitutional Amendments Committee on April 28, 2004.

H. General Taxes. The City of San Diego is now litigating the consequences of two charter amendments on its March 2002 ballot. Measure E, an initiative charter amendment sponsored by the leaders of the City's Libertarian Party, amended the charter to require ⅔-voter approval of general taxes. It passed with 54% of the vote. On an 8-1 vote, the City Council placed Measure F on the ballot to require proposals such as Measure E to obtain ⅔-voter approval to be valid. It passed with a bit more than 50% of the vote. The City refused to certify the adoption of Measure E, asserting that it was subject to the ⅔-voter approval requirement of Measure F. The San Diego Superior Court ruled for the Howard Jarvis Taxpayers Association in the ensuing litigation, concluding: (i) the threshold for approving amendments to local charters is 50% pursuant to state law, and cannot be altered by local action; (ii) Measures E and F were in conflict, thus triggering the rule that the measure which obtained the greater number of "yes" votes prevails – in this case Measure E; and (iii) Measure F would have taken effect in any event only 50 days after the certification of the election result and was not retroactively applicable to the March 2002 ballot on which it appeared. The measure is now pending before Court of Appeal as *Howard Jarvis Taxpayers Association v. City of San Diego*, Fourth District Court of Appeal Case No. D042801. As this paper is written, the case is fully briefed and awaiting oral argument.

An interesting, and controversial, proposal to allow local governments to impose an income tax by majority vote of the electorate to fund police and fire programs is A.B. 1690 (Leno, D-San Francisco). The proposal is now pending in the Senate Appropriations Committee.

## *III. Assessments.*

A. Assessments on Public Agencies. Several developments are worthy of note in this area of the law. First is Government Code § 53752, adopted by Chapter 981 of the Statutes of 2002 (S.B. 1961, Polanco, D-Los Angeles). This measure requires the Department of General Services to "develop compliance standards … to inform owners of state property of their duties and responsibilities pursuant to … [Proposition 218]." It remains to be seen how the Department will comprehend those duties, but the Department will likely consider such questions as whether state agencies should pay local assessments or vote in local assessment protest proceedings. As this paper is written, it does not appear that the DGS has yet complied with this directive.

Second is Chapter 194 of the Statutes of 2003 (S.B. 392, Senate Committee on Local Government) which made technical corrections to the Municipal Improvement Acts of 1911 and 1913 to comply with the majority property-owner protest proceedings required by Proposition 218. However, new Streets & Highways Code § 5302.5 establishes interesting enforcement mechanisms for assessing agencies and new Streets & Highways Code § 5303 makes the assessing local government's general fund liable for unpaid assessments levied against state or federal property.

B. Open Space Assessments. Two lawsuits were filed in Los Angeles and Santa Clara County Superior Courts questioning whether the acquisition of open space provides special benefit to property sufficient to allow an assessment under Proposition 218. The Los Angeles case, *Badtax v. Mountains Recreation and Conservation Authority*, Los Angeles County Superior Court Case No. LC 062 303, resulted in a victory for the local government and the appeal has been dismissed. Judge Richard A. Adler concluded that the MRCA had power under its Joint Powers Agreement to impose an assessment notwithstanding that one of its "parent" agencies is a limited-purpose, park district. He also concluded that open space acquisition provides the special benefit Proposition 218 requires.

Citable, appellate authority may result from *Silicon Valley Taxpayers Association v. Santa Clara County Open Space Authority*, Sixth District Court of Appeal Case No. H026759, which is being briefed as this paper is written. Santa Clara County Superior Court Judge William Elfving concluded that open space acquisition does provide the requisite "special benefit" to allow an assessment under Proposition 218. In addition, he upheld the Authority's refusal to honor protest ballots presented on photocopies of the official ballot form, rather than on the official ballots distributed by the Authority. Those disputed ballots held the balance of success for the assessment. *Amicus* participation is likely in this case, including local government, business, and environmental interests; the League of California Cities and the California State Association of Counties will file a joint *amicus* brief.

C. 100% Special Benefit Assessment. Another special benefit case is *City of Saratoga v. Hinz*, 115 Cal.App.4th 1202 (2004), in which the City established an assessment district to improve a private cul-de-sac and to include it in the City's street system. Although the assessed property owners approved the assessment in a majority protest proceeding under

Proposition 218, a property owner who was not assessed, but whose land would be partly taken to accomplish the improvement, resisted the eminent domain action. He argued, in a nutshell, that if there is no "general benefit" that requires a portion of the program to be charged other than to the assessed properties, there can be no "public necessity" to justify the taking. Both the trial and appellate courts rejected his argument that these two terms have the same meaning.

The case holds that, first, the 30-day statute of limitations of the Municipal Improvement Act of 1913 applies here and the fact that the challenge to the assessment district arose as a defense rather than as a plaintiff's claim did not vitiate that fact.

Second, the case holds that "general benefit" as used in assessment law and Proposition 218 does not mean the same thing as "public necessity," as used in the eminent domain statutes. The Court cites *Ventura Group Ventures, Inc. v. Ventura Port District* (2001) 24 Cal.4th 1089, 1106 for the proposition that "article XIIID [*i.e.,* the assessment provisions of Prop. 218] is consistent with decisional law prior to the adoption of Proposition 218." This is a very helpful statement, as much of that earlier law deferred to local government judgments about the extent and nature of special benefit. The Court also states:

> "The fact that the municipality is required to distinguish between the special and general benefits to be derived from the project during the assessment process does not detract from the inherently public nature of the project. The fact that a particular improvement project does not confer any general benefit on the community at large does not make the project any less public."

Third, the Court upheld Saratoga's determination that improving a street and opening it to the public, on the facts of this case at least, generated no "general benefit" and no duty to identify non-assessment proceeds to justify the assessment. The notion of a 100%-special-benefit, public street project seemed somewhat aggressive until this case. Still, the peculiar facts of the case must be taken into account and this notion should not be taken too far.

D. <u>Statutes of Limitation</u>. *Barratt American, Inc. v. City of San Diego*, 2004 WL 759247 (4th District Court of Appeal, April 9, 2004), involves a challenge to an assessment imposed pursuant to San Diego's charter authority on building permits issued to the plaintiff homebuilder to fund infrastructure. The City demurred on the basis of the 30-day statute of limitations of Code of Civil Procedure § 329.5, which applies to actions challenging assessments imposed by charter cities. The trial court sustained the City's demurrer without leave to amend and the plaintiff appealed, arguing that Proposition 218 invalidated the short statute of limitations provided by § 329.5. The trial court concluded that: (i) the assessment was exempt as a development fee, because it was imposed on building permits; (ii) that Proposition 218 provides no statutes of limitations and thus is not inconsistent with generally applicable statutes of limitations, and (iii) that the theory of continuous accrual relied upon in *Howard Jarvis Taxpayers Association v. City of La Habra,* 25 Cal.4th 809 (2001), was inapplicable because the act of imposing the assessment was a single event.

The Court of Appeal affirmed on the ground that the action was subject to the 30-day statute of § 329.5. The Court therefore did not reach the development fee issue. The Court held that § 329.5 is good law notwithstanding the language of Article 13D, § 5 ("all existing, new, or increased assessments shall comply with this article") because nothing in Proposition 218 or the

Proposition 218 Omnibus Implementation Act purports to alter statutes of limitation, even though Proposition 218 does expressly alter the burden of proof on certain issues. The "continuing violation" rule of *HJTA v. La Habra* is not applicable, the Court rule, because § 329.5 expressly states that its 30-day rule runs from the date an assessment is "levied," not the date it is paid, due or collected. This is an especially helpful ruling. Together with *Utility Cost Management v. Indian Wells Valley Water District*, 26 Cal.4th 1185, the case may mean that the *HJTA v. La Habra* case is largely limited to its facts.

The Court did not reach the argument that Prop. 218 preempts the power of charter cities to adopt assessment ordinances because Barratt did not adequately brief the issue, thus the Court viewed it as waived. The Court also did not reach the questions or whether the challenged assessment violated the assessment provisions of Article 13D, § 4 or the property-related fee provisions of Article 13D, § 6 because those claims were time-barred.

A contrary result was obtained in a case involving an assessment imposed by the Los Angeles MTA, in which the Second District Court of Appeal ruled that the relevant statute of limitations for a non-charter city assessment collected via the property tax roll is the 4-year rule of Revenue & Taxation Code § 5097. *Hanjin International Corp v. Los Angeles County Metropolitan Transportation Authority*, 110 Cal.App.4th 1109 (2003).

E. Assessments to Control Agricultural Vectors. Chapter 395 of the Statutes of 2002 (S.B. 1588, Senate Local Government Committee) was the Omnibus Local Government Act of 2002. Among its provisions was an amendment to Government Code § 53750(l) to define the "vector control," for which pre-Proposition 218 assessments may be maintained without a property-owner protest proceeding, to include both human and plant vectors. The original language of this provision of 1997's Proposition 218 Omnibus Implementation Act had limited the definition to human vectors, much to the chagrin of the agricultural community.

F. Business Improvement District (BID) Assessments. There are several business improvement district statutes, some of which impose traditional assessments on property and are subject to Proposition 218 and others which impose "assessments" on businesses rather than land and are therefore not subject to Proposition 218, under *Howard Jarvis Taxpayers Ass'n v. City of San Diego*, 72 Cal.App.4th 230 (1999). Recent legislation to amend the Business Improvement District Law of 1994, Chapter 763 of the Statutes of 2003 (A.B. 944, Steinberg, D-Sacramento), however, may itself require clean-up.

As to BIDs formed under the 1994 Act that are solely property-based and that do not involve the issuance of debt, the new law is unproblematic. The main change for these BIDs is that they do not need to be renewed by a vote of the affected property owners as often as was previously the case and formation petitions can now require the forming city or county to contract with a specified non-profit association to run the BID, if the city or county proceeds with the BID at all. While this appears to be a loss of local control, it does describe how most BIDs now operate and a city or county retains discretion to refuse to create a BID in the first place. The bond-financing provisions of this statute, however, based on those of the 1972 Landscaping and Light Act, and its provisions for assessments against businesses (rather than property owners), based on the BID Law of 1989, are not well drafted. It appears that it may be difficult to obtain an unqualified bond opinion for debt issued under this statute. Cities and

counties would be well advised not to levy a business-based assessment under the 1989 Law until clean-up legislation is adopted.

*IV. Fees.*

A. Storm Water Fees. Many cities and counties around California are struggling to finance the huge unfunded mandates imposed by the Regional Water Quality Control Boards pursuant to the Clean Water Act's National Pollutant Discharge Elimination System (NPDES). This task was made more difficult by *Howard Jarvis Taxpayers Association v. City of Salinas,* 98 Cal.App.4th 1351 (2002), invaliding Salinas' property-tax-roll fee for storm water abatement programs as a property-related fee requiring voter approval under the fee provisions of Proposition 218. ACA 10 (Harman, R-Huntington Beach) would add "storm water and urban runoff management" to "water, sewer or refuse collection" in the list of services for which Proposition 218 does not require an election but allows approval after only a majority protest proceeding (in which silence equals consent). Assemblyman Harman placed his measure in the inactive file, so this measure will likely expire with the current Legislature. Given the import of the issue, however, it can be expected to be renewed in the future.[2]

To address this problem, Assemblyman Nation (D-San Rafael) has introduced A.B. 204, which would impose a $6/year regulatory fee on automobiles registered to addresses in participating counties to fund NPDES compliance and other water quality programs. Counties eligible to participate upon a majority vote of their Boards of Supervisors are the nine Bay Area counties of Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Santa Clara, Solano and Sonoma. The bill has passed the Assembly and the Senate Natural Resources and Wildlife Committee on April 13, 2004 on a 5-3, party-line vote. It is now pending in the Senate Transportation Committee.

B. Ambulance Subscription Fees. *City of Upland v. Bozar*, San Bernardino Superior Court Case No. RCV 069 669, is a *pro per* challenge to Upland's paramedic subscription fee which allows residents to receive emergency medical services at reduced rates if they pay an annual subscription fee to the City's Fire Department. Such fee programs are becoming increasingly popular around the state. The suit alleges that the fee is an illegal special tax. The trial court granted summary judgment for the City on a § 1983 claim, but found a triable issue of fact as to whether the fee exceeded the cost to provide ambulance service. Trial of that issue is set for May 24, 2004.

C. General Fund Transfers. *City of Fresno v. Howard Jarvis Taxpayers Ass'n*, Fifth District Court of Appeal Case No. F044561, is a challenge to a provision of the Fresno City Charter authorizing the City to transfer to the City's general fund monies from utility enterprise accounts in lieu of property taxes on utility assets. The petition alleged the transfer:

> "is preempted by state constitutional provisions and statutes which exempt public property from property taxation and violates state constitutional provisions and

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[2] The Alameda Countywide Clean Water Program, a cooperative effort of the County and its cities to jointly comply with NPDES mandates, retained the consulting firm of Hilton, Farnkopf & Hobson, LLC to prepare a December 3, 2003 report on alternative means to fund stormwater programs. The report provides a useful summary of current options and practice in this area. This report is entitled *Alameda Countywide Clean Water Program Stormwater Program Funding Options* and is available from the Authority, located in Hayward, California.

statutes which prohibit fees from exceeding the cost of providing service and prohibit the expenditure of fee revenue for purposes other than providing service."

My colleague Sandra J. Levin and I are defending the City and argue, among other things, that the voters' 1957 approval of this provision of the charter makes the transfer a voter-approved tax on utility services (and not on public property) collected at the wholesale level rather than a fee, that Proposition 218 requires nothing of property-related fees until they are "extended, imposed, or increased" as this charge has not been since Proposition 218 was adopted, and that the underlying utility fees are not property-related fees subject to Proposition 218. The Fresno Superior Court granted summary judgment to the HJTA, citing *Howard Jarvis Taxpayers Ass'n v. City of Roseville*, 97 Cal.App.4th 637 (2002), which turned on the last question and did not involve voter approval or the retroactivity question. The case is being briefed as this paper is written; the briefs will be posted to our firm's website at http://www.cllaw.us/cases.htm.

Roseville continues its efforts to cope with the consequence of its 2002 appellate loss. The Howard Jarvis Taxpayers Association reported to its supporters by email that the trial court:

> "found Roseville guilty of contempt of court for continuing to collect a fee on water, sewer, and garbage bills despite prior judicial rulings ordering its repeal [finding] … Roseville changed the name of its in-lieu franchise fee, but that the city still hasn't used it for its new purpose – to repair roads damages by its utility trucks." August 8, 2003 *Taxpayer Update* of the Howard Jarvis Taxpayers Association.

In late 2003 the City was working with a financial consultant to produce a study of the road maintenance costs attributable to the City's utilities.

D. Utility Charges. The most significant development in this area of the law is the California Supreme Court's decision in *Richmond v. Shasta Community Services District*, 32 Cal.4th 409 (2004). The case unanimously holds:

> (1) water capacity or connection charges and other charges triggered by the voluntary decision of private persons to seek government services are not "assessments" subject to property-owner approval; and
>
> (2) water capacity or connection charges are not "property related fees" subject to Proposition 218 even if used to recover capital costs for fire and emergency medical services.

At issue was the District's water connection charge, which has three elements: a water capacity component; a fire suppression component to fund capital purchases for the District's fire and emergency medical services programs; and, a water connection component, to recover the cost of installing a new meter and connecting a customer's property to the District's water system. The plaintiffs challenged an increase in the connection fee arguing, among many other claims, that the water capacity component was an assessment subject to the property-owner approval requirements of Article XIII D, § 4 of Proposition 218 and that the fire capacity component was a property-related fee and violated Article XIII D, § 6(b)'s requirement that such fees not be used for general governmental services such as fire suppression.

The trial court concluded that the water capacity charge was not an assessment but rather a "development fee" exempted from Proposition 218 by Article XIII D, § 1(b), and that the fire suppression component of the charge was merely a continuation of a pre-Proposition 218 fee and immune from attack on that ground. The Court of Appeal affirmed on the assessment issue, concluding that the water capacity charge was an exempt development fee. Curiously, the appellate court ruled that fire capacity component of the same water meter fee was not a development fee, but an illegal, property-related fee.

Article XIII D, § 2(b) defines "assessment" for purposes of Proposition 218 as "any levy or charge upon real property by an agency for a special benefit conferred upon the real property." While acknowledging that the District's connection charge was not imposed on real property, the Supreme Court also found that an "assessment" under Proposition 218 could not include any revenue measure for which the assessing government cannot identify the affected properties at the outset.

The Supreme Court rejected the trial and appellate courts' reliance on the "development fee" exception to Proposition 218:

> "We agree with plaintiffs that the District's capacity charge is not a development fee. It is similar to a development fee in being imposed only in response to a property owner's voluntary application to a public entity, but it is different in that the application may be only for a water service connection without necessarily involving any development of the property. (Citations.) Our agreement that the capacity charge is not a development fee does not assist plaintiffs, however, because it does not mean that the capacity charge is an assessment within the meaning of article XIII D. The capacity charge is neither an assessment nor a development fee under article XIII D."

This is not a blanket statement that water fees can never be development fees, however. Rather, it is necessary to look to the activity on which the fee is imposed. For example, a condition of a subdivision map that a developer install water mains and convey them to the water utility or pay the utility to do so would seem to be a classic development fee notwithstanding that it relates to water service. On the other hand, where a fee is imposed on new users of services which sometimes, but not always, relate to development – as will be true of water, sewer and other utility services – this language suggests the development fee exception to Proposition 218 will be unavailable.

The Court concluded that the fire suppression component of the District's water connection fee was not a property-related fee or charge subject to Proposition 218 because it was triggered not by property ownership, but by "voluntary decisions to request water service." This restates the "voluntariness" test of the Court's decision in *Apartment Ass'n of Los Angeles County, Inc. v. City of Los Angeles*, 24 Cal.4th 830 (2001) .

This conclusion should have been enough to resolve the matter. However, the Court continued in what appears to be *dicta* that "supplying water is a 'property-related service' within the meaning of Article XIII D's definition of a [property-related] fee or charge." The Court also stated:

> "In the ballot pamphlet for the election at which article XIII D was adopted, the Legislative Analyst stated that '[f]ees for water, sewer, and refuse collection service probably meet the measure's definition of property-related fee.' The Legislative Analyst apparently concluded that water service has a direct relationship to property ownership, and thus is a property-related service within the meaning of article XIII D because water is indispensable to most uses of real property; because water is provided through pipes that are physically connected to the property; and because a water provider may, by recording a certificate, obtain a lien on the property for the amount of any delinquent service charges. But the Legislative Analyst was apparently referring to fees imposed on existing water service customers, not fees imposed as a condition of initiating water service in the first instance." (Citations omitted.)

These would also seem to be true of sewer services, but not of refuse collection services.

Taxpayer advocates can be expected to argue that this case unequivocally means that water service charges are necessarily subject to Proposition 218. Such a reading is overbroad. First, this discussion is *dicta*. Second, the parties to the *Richmond* case argued the relevant provisions of the *Apartment Ass'n* case and cited *Howard Jarvis Taxpayers Ass'n v. City of Los Angeles*, 85 Cal.App.4th 79 (2000), which concluded that metered water consumption fees are not property-related because they are not triggered by property ownership, but by voluntary decisions to consume water. Nonetheless, the Supreme Court found no need to discuss these authorities, much less overrule them. Moreover, the *Roseville* decision cited in the Court's discussion of this issue carefully distinguished the *Los Angeles* case.

Perhaps most convincing is the Court's own language on this issue:

> "Thus, we agree that water service fees, being fees for property-related services, may be fees or charges within the meaning of article XIII D. But we do not agree that *all* water service charges are necessarily subject to the restrictions that article XIII D imposes on fees and charges. Rather, we conclude that a water service fee is a fee or charge under article XIII D if, but only if, it is imposed 'upon a person as an incident of property ownership.' (Art. XIII D, § 2, subd. (e).) A fee for ongoing water service through an existing connection is imposed 'as an incident of property ownership' because it requires nothing other than normal ownership and use of property. But a fee for making a new connection to the system is not imposed 'as an incident of property ownership' because it results from the owner's voluntary decision to apply for the connection." (Original emphasis.)

Thus, to trigger Proposition 218's property-related fee provision, a utility service fee must constitute both a fee for a property-related service (because it "is indispensable to most uses of real property," "provided through pipes that are physically connected to the property," and because the fees can be enforced via liens on title) but must also be "imposed 'as an incident of property ownership' because it requires nothing other than normal ownership and use of property." If something other than ownership and use of property is required – such as a decision to consume a service on that property by a person who need not take the service and who need not be a property owner – then the fee is not within the scope of Proposition 218.

Clearly the case is good news for local government with respect to capacity and connection charges. As to the question of service charges for ongoing utility services such as water and sewer services and, perhaps, refuse collection services, a few points are noteworthy. First, the safest legal course is to comply with the property-related fee provisions of Proposition 218 when establishing or increasing such fees. Doing so eliminates any need to argue this point. Those procedures require notice by mail to all fee payers – a notice that can be included with another mailing, such as a periodic bill under Government Code § 53750(i) – and a majority protest proceeding. If an absolute majority of affected fee payers protests, the new or increased fee cannot be approved. Majority protests are rare in all but the smallest jurisdictions and these procedures will rarely block a necessary increase, although they will impose expense and delay.

Second, risk of suit can be mitigated by some or all of the following:

(i) tying charges to consumption or some other voluntary action by a fee payer rather than mere property ownership, such as a request for service (it may be useful to amend service initiation request forms to make clear that the fee payer is requesting service as a utility customer and not as a property owner),

(ii) imposing charges on those who use a service and not on those who own property on which it is used,

(iii) ceasing to charge "fixed, "service," "meter," "minimum monthly" and similar charges for customers who consume no service during a billing period,

(iv) clarifying that liening property to collect unpaid charges is only a debt collection device (approved in *Apartment Ass'n*) and not a basic aspect of the fee,

(v) avoiding the use of the property tax roll for fee collection,

(vi) relying on the discontinuance of service rather than liens to enforce fees where possible (this is problematic for sewer service providers that are not also water providers),

(vii) clarifying that property may be used without taking the service, by indicating that lawful wells, septic and leach systems may be used, or that documented self-hauling of refuse is permissible, and

(viii) demonstrating that the properties with respect to which the charge will be paid cannot be identified when the charge is established because the source of requests for service, and the volume of service requested, is not knowable.

## *V. Initiative and Election Issues.*

A. Scope of 218 Initiative Power. Article XIII C, § 3 extends the power of initiative to the repeal to "any tax, assessment, fee or charge." While Article XIII C defines the terms "general tax" and "special tax" and states that all local taxes are one or the other, it does not define "assessment," "fee" or "charge." This left open two arguments: that these terms have the

definitions provided in Article XIII D, the second constitutional article adopted by Proposition 218, or these terms have a broader, common-sense meaning. If the latter were true, some means would be necessary to limit the otherwise unbridled scope of fiscal initiatives in order to allow government to function.

Potential arguments are those that focus on limitations in the power of initiative itself, such as its limit to legislative matters; *e.g., Dare v. Lakeport City Council*, 12 Cal.App.3d 864 (1970); the rule that the initiative may not be used to "impair essential government functions," *e.g., City of Atascadero v. Daly*, 135 Cal.App.3d 466 (1982) (impairment of fiscal management powers), *Simpson v. Hite*, 36 Cal.2d 125 (1950) (siting a courthouse), *Newsom v. Board of Supervisors*, 205 Cal. 262 (1928) (franchising authority); and that the initiative power may not allow the voters to exercise a power the Legislature has conferred on a local elected body alone, *e.g., Committee of Seven Thousand v. Superior Court (City of Irvine)*, 45 Cal.3d 491 (1988).

The former argument – that the definitions of Article XIII D should be used to give some practical limit to the sweep of the initiative power conferred by Article XIII C, however, is that taken by the first published appellate authority on this subject: *Bighorn-Desert View Water Agency v. Beringson (Kelley)*, 114 Cal.App.4th 1213 (2004), a recent decision of the Inland Empire panel of the 4th District Court of Appeal.

The real party in the case, a former member of the Agency Board, submitted an initiative to reduce the Agency's water rates by roughly half and to forbid further increases in those rates without a ⅔-vote of the Agency's electorate. The Agency filed a suit seeking a declaration that the measure was invalid. The trial court ruled for the Agency, concluding the measure exceeded the power of the initiative and the Court of Appeal affirmed, concluding: (i) that the initiative power created by Article XIII C is limited to taxes and to assessments, fees, and charges as those later three terms are defined in Article XIII D, (ii) that the Agency's water rates were not property-related fees under Article XIII D because they are not imposed on all property owners within the Agency's boundaries, but only on those who consume water provided by the Agency; (iii) that the measure attempted to exercise by initiative a power conferred by the Legislature on the Agency's board alone; and (iv) that the initiative would have impaired an essential governmental function. It was a powerful and complete victory for local government. A petition for review filed February 23, 2004 is pending as this paper is written.

B. Signature Requirement for Special Initiative Elections. Another issue of concern under the initiative provisions of Proposition 218 regards special elections. Article XIII C, § 3 provides that: "neither the Legislature nor any local government charter shall impose a signature requirement higher than that applicable to statewide statutory initiatives." This sets a very low threshold of 5% of the number of voters of the jurisdiction who cast ballots in the last gubernatorial election. If there is a 40% turnout, as was true of the Davis – Simon election of 2002, then *just 2%* of the registered voters of a local government can compel an election to repeal a fiscal measure. Proposition 218, however, is silent as to whether a special election may be called under this low standard. As to general law cities, Elections Code § 9214 requires 15% of all registered voters to obtain a special election on an initiative measure. Local government counsel had argued that enforcing this 15% requirement does not violate Proposition 218, because nothing in the measure speaks to special elections and, moreover, Article XIII C, § 2(b) states a preference that tax measures be placed on general election ballots when City Council

seats are contested. The Attorney General adopted this construction in *Opinion No. 01-1114* (August 12, 2002).

C. Election Dates. Also relevant with respect to these election issues is Chapter 401 of the Statutes of 2003 (A.B. 1521, Parra, D-Bakersfield) which identifies specific dates on which mailed-ballot elections may be held, restricting the previous authority of general law cities to schedule such elections throughout the year. The approved dates are the first Tuesday after the first Monday of May and the last Tuesday of August of every year and the first Tuesday after the first Monday in June of even-numbered years. This measure applies not only to true "elections," but by virtue of the language of Elections Code § 4000(c)(9), can be read to extend to assessment protest proceedings as well. Such a restriction on the timing of assessment ballot proceedings would be problematic and appears to have been unintended. Fortunately, most assessment statutes expressly override any contrary provisions of the Elections Code. A legislative proposal to correct this problem is expected to be included in the 2004 Omnibus Local Government bill.

## *VI. Conclusion.*

The revenue side of public finance has become increasingly complex and new legal developments are frequent. Regular updates are provided via our firm website, located at www.cllaw.us, and our firm newsletter, to which you can subscribe via our website. We hope you find those materials useful.

As always, we'll keep you posted!