

# **Rate-Making – An Historical Review of the Law Since Prop. 13**

County Counsels' Ass'n of  
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# Before 13: Legislative Discretion

- Rates presumed reasonable, fair and lawful
- Challenger bore burden of proof
- Rates overturned only if “unreasonable” or “unreasonably discriminatory”
- “Reasonableness ... is the beginning and end of the judicial inquiry.”
- Rates could be based on cost of service or any other reasonable basis

*Hansen v. City of San Buenaventura* (1986) 41  
Cal.3d 1172, 1180-81

October 6, 2012

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# Before 13: Legislative Discretion

- General fund transfers, life-line rates and other cross-subsidies were permissible
  - *Hansen*
  - *Oneto v. Fresno* (1982) 136 CA3d 460, 464
- Case overturning rates were rare
  - *Elliott v. Pacific Grove* (1975) 54 CA3d 53 (challenge to 4:1 ratio of in-city to out-of-city sewer rates survived demurrer)

# Prop. 13's Revolution

- Limited Property Taxes (13A, section 1)
- Allowed special taxes on 2/3 voter approval (13A, section 4)

# Prop 13 Legislation

- GC 50076:
  - Authorizes local governments to impose special taxes with  $\frac{2}{3}$ -voter approval
  - Defined “special tax” to exclude “any fee which does not exceed the reasonable cost of providing the service or regulatory activity for which the fee is charged and which is not levied for general revenue purposes.”

# Prop. 13 Litigation

- Prop. 13 does not interfere with assessments
  - *County of Fresno v. Malmstrom* (1979) 94 CA3d 974
- Prop. 13 exception for pre-1978 debt covered property tax to cover take-or-pay obligation under state water contract
  - *Kern Co. Water Agency v. Bd. of Sups.* (1979) 96 CA3d 874.



# More Prop. 13 Litigation

- Prop. 13 did not require voter approval to extend special taxes to annexed territory
  - *Metropolitan v. Dorff* (1979) 98 CA3d 109
- Now being litigated as to Prop. 218
  - *Citizens Ass'n of Sunset Beach v. OC LAFCO*, 4<sup>th</sup> DCA Case No. G045878 (decision due 10/22/12)

# Still More Prop. 13 Litigation

- Special tax means tax imposed for a specific purpose
  - *San Francisco v. Farrell* (1982) 32 Cal.3d 47
- Prop. 218 preserves this rule: 13C, §1(d)

# Proposition 218

- Primary goal was to restrain assessments
- Also extended initiative power to repealing taxes, assessments & fees (13C, §3)
- Created new category of “property related fees”

# Prop. 218's Assessment Rules

- Demanding new definitions of “special benefit” and “proportionality” (13D, §§ 2(i), 4(a))
- No exemption of public property (13D, §4(a))
- Requires engineer's report (*id.*)
- Weighted ballot “election” among property owners (13D, §4(c) – (e))

# Property Related Fees Under 218

- “Fee” or “charge” means any levy other than an ad valorem tax, a special tax, or an assessment, imposed by an agency upon a parcel or upon a person as an incident of property ownership, including a user fee or charge for a property related service.

(13D, §2 (e)).

# Property Related Fees

- “Property ownership” ... include[s] tenancies of real property where tenants are directly liable to pay the assessment, fee, or charge in question. (13D, §2(g))
- “Property-related service” means a public service having a direct relationship to property ownership. (13D, §2(h))

# Property Related Fees

- Reliance by an agency on any parcel map, including, but not limited to, an assessor's parcel map, may be considered a significant factor in determining whether a fee or charge is imposed as an incident of property ownership for purposes of this article.

(13D, §6(b)(5)).

# 218 Procedures for Fees

- 45 days' mailed notice to all property owners (13D, §6(a))
- Majority protest hearing (*id.*)
- Election for fees for services other than water, sewer & trash (13D, §6(c))
  - 50% of property owners **or**
  - $\frac{2}{3}$  of registered voters



# Substantive Rules for Fees

- Revenues cannot exceed cost (13D, §6(b)(1))
- Revenues not used for other purposes (13D, §6(b)(2))
- Fee cannot exceed proportional cost of service attributable to the parcel (13D, §6(b)(3))
- Standby fees approved as assessments (13D, §6(b)(4))

# Substantive Rules for Fees

- No fee for general service “where the service is available to the public at large in substantially the same manner as it is to property owners” (13D, §6(b)(2))
- *Cf.* Prop. 26: “a charge imposed for a ... service ... provided directly to the payor that is not provided to those not charged ...which does not exceed the reasonable costs ...”

# Construction of 218

- Substantive rules for fees inform construction of the procedural requirements and vice versa:
  - *Richmond v. Shasta CSD* (2004) (connection charge not property related because can't know to whom to send notice)
  - *Morgan v. IID*, 4<sup>th</sup> DCA No. D061087 (ACWA brief argues 1 protest proceeding required for all customer classes to ensure compliance with 6(b))

# 218 Assessment Litigation

- *Silicon Valley Taxpayers Ass'n v. Sta. Clara Co. Open Space Authority* (2008) 44 Cal.4<sup>th</sup> 431
  - Independent judicial review of findings re special benefit and proportionality
  - Rejects *Not About Water's* reliance on pre-218 standard of review

# Current Spate of Assessment Cases

- *Dahms v. Downtown Pomona PBID (2009)* 174 CA4th 708
- *Tiburon v. Bonander (2009)* 180 CA4th 1057
- *Beutz v. Co. of Riverside (2010)* 184 CA4th 1516
- *Golden Hill Neighborhood Ass'n v. San Diego (2011)* 199 CA4th 416

# Pending Assessment Case

- *Concerned Citizens for Responsible Gov't v. W. Point FPD*, Cal. S. Ct. Case No. S195152
  - Are service assessments permitted?
  - How demanding is the special benefit test?
  - How demanding is the proportionality test?

Fully briefed since March 2012 and awaiting argument

# Early 218 Fee Litigation

- *Apt. Ass'n of LA County, Inc. v. City of LA* (2001) (housing code enforcement fee on apts. not subject to 218 b/c participation in housing market voluntary)
- *HJTA v. Roseville* (2002) (franchise fee paid from water utility to general fund violated 218)
- *HJTA v. Fresno* (2005) (same as to PILOT)
- *HJTA v. Salinas* (2002) (impervious coverage fee to fund NPDES compliance violated 218)

# 218 Litigation re Water Rates

- *Richmond v. Shasta CSD* (2004) 32 Cal.4<sup>th</sup> 409 (connection charge not subject to 218, but dicta states that water service fee is)
- *Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4<sup>th</sup> 205 (metered water charges subject to 218 and can be reduced by initiative)



# More 218 Litigation re Water Rates

- *Pajaro Valley WMA v. AmRhein* (2007) 150 CA4th 1365
  - Groundwater charges subject to 218 if domestic users pay
- Many ongoing cases
  - Is *Pajaro* good law?
  - Are groundwater charges exempt from 6(c) election as water charges?
  - If election required, can ballots be weighted?

# Recent 218 Fee Litigation

- *Greene v. Marin Co. Flood Cont. & Water Cons. Dist.* (2010) 49 Cal.4<sup>th</sup> 277
  - Art. II, §7 secrecy requirement doesn't apply to 6(c) elections
  - 218 Omnibus Act is good law
  - Some deference to local rules adopted under §6(c) and §4

# The Latest 218 Fee Litigation

- *Palmdale v. Palmdale Water Dist. (2011) 198 CA4th 926*
  - Art. X, §2 can be reconciled with Prop. 218
  - Some justification for conservation rate tiers required
  - Probably motivated by underlying equities and poor record for rates Board actually adopted

# Prop. 26

- All revenue sources are taxes unless an exception applies (13C, §1(e))
- 3 exceptions limited to cost: benefit or privilege, service or product, regulatory fee
- 2 not limited to cost: use of gov't property, fines & penalties
- 2 limited to cost by other law: development fees and 218 revenues

# 26 Litigation

- *Cal. Tax. v. FTB* (2010) 190 CA4th 1129
  - 20% penalty on late corporate taxes expected to raise \$1.7b not a tax under Prop. 13
  - Indicia of fine are
    - Label (not determinative)
    - Revenues fall over time
    - Triggered by violation of law
  - Will be helpful in construing 5<sup>th</sup> exception to 26

# 26 Litigation

- *Griffith v. City of Santa Cruz* (2012) 207 CA4th 982
  - Challenge to rent registration fees, claiming violation of 218 and 26
  - 218 claim easily dispatched by *Apartment Ass'n*
  - 26 claim
    - Retroactivity not briefed
    - Found to be within permitting exception
    - Costs adequately justified
    - *Sinclair Paint* precedents helpful

# Pending 26 Litigation

- *Ventura v. UWCD*, Sta. Barbara Superior No. VENCI-00401714
  - Challenge to 3:1 ratio of M&I to ag. groundwater rates
- *Citizens for Fair REU Rates v. Redding*, 3<sup>rd</sup> DCA Case No. C071906
  - Pre-26 PILOT on Redding Electric Utility

# Pending 26 Litigation

- *Schmeer v. Co. of LA*, 2<sup>nd</sup> DCA No. B240592
  - 10¢ fee for paper bags under plastic bag ban
- *Bauer v. Harris*, ED Cal. No. 11 CV 01440
  - Challenge to gun registration fees under 26 and 2<sup>nd</sup> Amendment



# What Happened?

- Over 34 years, rate-making law has been transformed from a rule of judicial deference to the legislative process to one of strict judicial oversight of exacting standards
- Still, voters expect basic services and governments have the power to recover their cost to provide them

# How to cope

- Rate-making requires partnership of rate-making consultant and legal counsel
- Good communication with the rate-paying public is now required

# More on How to Cope

- Goals of rate-making counsel
  - Make a good record
    - Document proper role of discretion
    - Allow for board to disagree w/ recommendation
    - Revise rate study if board does so
  - Avoid procedural error
    - Protest-handling reso. is vital
  - Respect substantive limits of 13D, §6(b)

# Questions?

