

# Update on the Law of Public Revenues

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## Utility Users Taxes

- *Ardon v. City of LA* (Cal. S. Ct. 2011)
  - Los Angeles lacked ordinance imposing local claiming requirement
  - Gov't Claims Act does not prohibit class claims for refunds of taxes and fees
  - Local governments should adopt local claiming ordinances that expressly bar class and representative claims

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## Utility Users Taxes (Cont.)

- *Sipple v. City of Alameda & 134 other UUT Agencies*
  - AT&T / New Cingular Wireless settled consumer class action in Illinois, agreeing to refund taxes on wireless packages that included internet due to preemption by Internet Tax Freedom Act of 2009
  - AT&T sued all California agencies w/ telephone taxes in Los Angeles Superior Court in July 2011

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## Utility Users Taxes (Cont.)

- *Sipple v. City of Alameda & 134 other UUT Agencies*
  - Case just getting underway
  - Forensic review of AT&T claims may facilitate settlement or litigation
  - A number of firms are representing various groups of cities in the case
  - Stay tuned

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## Utility Users Taxes (cont.)

- Federal Legislation Proposed to Bar New or Amended Cell Taxes above 1% for 5 years
  - HR 1002 (Lofgren, D-San Jose)
  - S 543 (Wyden, D-OR)
  - 25 CA co-sponsors on House bill as of August 2011 (Baca, Bass, Bono Mack, Calvert, Capps, Cardoza, Costa, Denham, Eshoo, Gallegly, Herger, Honda, Hunter, Issa, Lungren, Matsui, McKeon, McNerney, Gary Miller, Richardson, Rohrabacher, Roybal-Allard, Royce, Loretta Sanchez, Speier)

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## Property Tax Administration Fees

- R&T 97.75 allows Counties to recover “actual cost” to implement Triple Flip & VLF Swap
- Many counties are recovering more than the marginal cost to do so
- 47 Los Angeles County cities and 7 Fresno County cities sued to test this issue
- LA victory pending S. Ct. review; Fresno victory held by 5<sup>th</sup> DCA pending LA decision

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## Property Taxes

- *Ribiero v. County of El Dorado* (3<sup>rd</sup> DCA 2011)
  - Investor’s mistake in buying real estate at tax sale without knowing amount of bond arrearages did not entitle him to rescind sale

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## Property Taxes

- *Lowe v. Washoe County* (9<sup>th</sup> Cir., 2010)
  - No federal class action to challenge property tax assessments in South Lake Tahoe, Nevada
  - Individual refund actions are sufficient state law remedy to prevent federal civil rights action
  - Underlying dispute turned on violation of State Constitutional requirement (comparable to CA’s) that valuations be “equal and uniform.”

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## Post-Bell Legislation re Taxes

- AB 1350 (Lara, D-Bell Gardens)
  - County Auditor must determine lawfulness of property tax overrides before collecting
  - Authorized by Art. XIII, § 20 and applies to charter cities
  - Pending Assembly Floor adoption of Senate amendments in late August 2011

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## Special Parcel Taxes

- *Sacks v. City of Oakland* (2010) 190 Cal.App.4<sup>th</sup> 1070
  - Deferential review of City's implementation of special parcel and parking tax measure
  - Court interprets measure practically and flexibly to attain its purpose to fund police services
  - Court looked to City Att'y opinion & Council reso. adopted after dispute arose to interpret measure

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## Property Taxes

- *First American Commercial Real Estate Svcs., Inc. v. County of San Diego* (4<sup>th</sup> DCA, 2011)
  - Clerical error was not “circumstance beyond the taxpayer’s control” sufficient to exonerate property tax payment service from 10% payment on erroneously delayed \$6.3m wire

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## Property Taxes

- *Avalon Bay Communities, Inc. v. County of Los Angeles* (2<sup>nd</sup> DCA 2011)
  - Employee error that delayed wire payment of property taxes was not “act outside the taxpayer’s control” sufficient to protect taxpayer from \$215k penalty

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## Property Taxes

- *ZC Real Estate Tax Solutions Ltd. v. Ford* (5<sup>th</sup> DCA 2010)
  - Mortgage lender's tax service sent Stanislaus property tax payments to SF
  - This was not error beyond control of taxpayer to protect tax service from \$551k late penalty

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## Under-Collection of Bed Tax by Online Resellers

- Resellers are subject to bed tax as sellers of hotel nights
- Hotels pay tax on wholesale rent reseller pays hotel, reseller collects tax on retail rent from customer and pockets the difference
- Class action counsel pursuing this issue for LA, San Diego, Anaheim & W. Hollywood

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## Under Collection of TOT by Online Resellers (Cont.)

- Industry pursuing lots of litigation
  - Use of contingency fee counsel (S. Ct. upheld)
  - Duty to pay before litigating (DCA loss for cities)
  - Judicial Review of administrative tax determinations (Anaheim loss and San Diego win on appeal)
- Litigation around USA: San Antonio won \$20m federal jury verdict

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## Bed Tax Legislation

- SB 670 (Calderon, D-Whittier)
  - Would limited TOT to room rent paid to operator
  - Exempts internet sales, parking & other charges
  - Died last year, author tells League of CA Cities he will not pursue it this year (yet he introduced it ...)
  - Never got a hearing, still in Senate Rules in late August 2011

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## Income Tax

- *Franchise Tax Board v. Superior Court* (Cal. S. Ct. 2011)
  - California Constitution does not require jury trial in statutory action for tax refund

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## Business License Taxes

- *Silvers v. SBE* (2010) 188 Cal.App.4<sup>th</sup> 1215 (2d DCA)
  - Unlicensed surplus line insurers are not subject to tax imposed for doing business in California
  - Provides support by analogy for meaning of “doing business” within a City for purposes of local business license taxes

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## Business License Taxes

- *Chodos v. City of Los Angeles* (2<sup>nd</sup> DCA, 2011)
  - Lawyer taxpayer must pay first and litigate later
  - Declaratory relief action properly dismissed in dispute involving inclusion in gross receipts of out-of-pocket costs and fees paid to contract counsel

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## Sales & Use Taxes

- *City of Industry v. City of Fillmore* (2<sup>nd</sup> DCA 2011)
  - Challenge to reallocation of sales tax to Fillmore of business with locations in Livermore and Industry
  - DCA reversed trial court victory for Fillmore, finding no duty to comply with Fillmore's claiming ordinance, no failure to exhaust administrative remedies, and no lack of standing

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## Sales & Use Tax

- *City of Fillmore v. State Bd. of Equalization* (2<sup>nd</sup> DCA 2011)
  - Industry and Livermore need not complete administrative review at SBE before suing
  - Industry and Livermore entitled to writ to compel SBE to implement supplementation decision allocating sales tax to them

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## Cigarette Taxes

- *Parmar v. Bd. of Equalization* (2<sup>nd</sup> DCA, 2011)
  - Owners of closely held corporation could not seek refund of taxes paid by corporation even though BOE credited corporation's tax payments to owner's account
  - May be helpful in telephone tax disputes

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## Prop. 218 Doesn't Apply to Reorganizations

- Att'y Gen. Op. No. 09-305 (Dec. 20, 2010)
  - Bond leveling among 4 merged school districts did not trigger election under Prop. 13
  - Cites case dating from adoption of Prop. 13 in 1979
  - Same logic should apply to Prop. 218

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## Prop. 218 and Annexation (cont.)

- *Citizen's Ass'n of Sunset Beach v. Orange County LAFCO* (Orange County Superior Ct. Case No. 30-2010-00431832)
  - Ass'n challenged LAFCO approval of island annexation for lack of election to approve extension of Huntington Beach's taxes into annexation area
  - Citing Prop. 13 precedent, trial court found no election required
  - Appeal likely

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## Fines are not Taxes

- *Cal. Taxpayers Ass'n v. Franchise Tax Board* (2010) 190 Cal.App.4th 1139 (3<sup>rd</sup> DCA)
  - 20% penalty on late corporate taxes raising \$1.4b not a tax requiring 2/3 vote of Legislature
  - Distinguishing characteristics: label, revenues diminish over time, triggered by violation
  - No need for findings or good faith defense; post-payment remedy sufficient

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## Constitutional Challenge to Prop. 13

- Former UC Chancellor filed original action in Cal. Supreme Court arguing requirement for 2/3 vote of Legislature for taxes is a Constitutional revision & cannot be accomplished by initiatives. Court denied the writ; refiled in LA trial court, motion for judgment granted to HJTA in 2010, appealed in 2011
- *Young v. Schmidt*, 2<sup>nd</sup> DCA No. B230729

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## Taxpayer Challenge Cannot Enjoin Collection of Tax

- *Chiatello v. CCSF* (2010) 189 Cal.App.4<sup>th</sup> 169 (1<sup>st</sup> DCA)
  - Non-taxpayer could not challenge payroll tax on profit distributions to employee/owners of business organizations
  - CCP 526a not an and-run around anti-tax-injunction and pay-first-litigate-later rules

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## Groundwater Extraction Charges

- *Pajaro Valley Water Mgmt Agency v. Amrhein*
  - Subject to Prop. 218
- Are they “water” fees exempt from election requirement?
  - Pending in 6<sup>th</sup> DCA (3<sup>rd</sup> DCA case dismissed as moot)
- Subsidy of agriculture plainly violates 218’s proportionality requirement

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## Groundwater Extraction Charges

- *Cerritos, Downey & Signal Hill v. Water Replenishment District of So. Cal.* LA Superior Court Case No. BS128136
  - Trial court invalidated WRD's charges for non-compliance w/ 218; appeal likely
- *Ventura v. United Water Conservation Dist.*, Ventura Superior Court Case. No. 56-2011-00401714
  - Filed August 2011, challenges 218 compliance and statutory requirement of 3:1 fee ratio of M&I to agricultural customers
- *Pendry v. Pajaro Valley Water Agency*, Sta. Cruz Superior Court Case No. CV 168936
  - Challenge to fee adopted after *Amrhein* w/ Prop. 218 compliance
  - Is 6(c) election required? May ballots be weighted?

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## Groundwater Management Charges

- *Great Oaks Water Company v. Santa Clara Valley Water District*, 6<sup>th</sup> DCA Case No. H035885
  - Revisits *Amrhein v. Pajaro* and application of 218
  - Did SCVWD comply w/ 218?
  - Is charge exempt from election as "water" charge?

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## Flood Control & Water Quality Fees

- *Greene v. Marin County Flood Control District* (Cal. S. Ct. 2010)
  - Ballot secrecy does not apply to 218 elections on property-related fees for things other than water, sewer and trash
  - 218 Omnibus Act is good authority
  - Deference to local procedural rules on property-related fees

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## Water Fees

- *City of Palmdale v. Palmdale Water District* (2<sup>nd</sup> DCA 2011)
  - City challenged conservation water rates, claiming Prop. 218 disallows them
  - DCA found 218 and Constitutional provision against wasting water could be harmonized but struck down PWD rates as insufficiently justified
  - Caution required when constructing conservation rates
  - Petition for review or request for depublication likely

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## Water Fees

- SB 1035, Ch. 485 Stats. of 2010 (Hancock, D-Berkeley)
  - Prior law authorized municipal utility districts to collect delinquencies on tax roll, but excluded those for water, sewer and power service
  - This repeals exemption for water and sewer service (but maintains power exemption) until 1/1/16

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## State Water Fees

- SB 34 (Simitian, D-Palo Alto)
  - Would impose state fee on water retailers based on volume of non-ag sales and acreage for ag sales to fund state and local water programs
  - Requires 2/3 approval under Prop. 26
  - Pending in Senate Appropriations since May 2011

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## Sewer Fees

- *California Restaurant Mgmt. Systems v. City of San Diego* (4<sup>th</sup> DCA 2011)
  - Putative class action on behalf of restaurants for allegedly excessive sewer fees
  - City won summary judgment for failure to file timely claim
  - Appellate court upheld City victory, refusing to find claiming period tolled by a resident's earlier claim

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## Development Impact Fees

- AB 1084, Ch. 507 of 2009 (Adams, R-Hesperia)
  - GC 66019: 14-days notice of new or increased development impact fees to those who request it
  - GC 66023: if requestor pays for audit of AB 1600 fee, agency must conduct audit and implement its recommendations

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## Development Impact Fees

*Homebuilders Ass'n v. Lemoore* (5<sup>th</sup> DCA, 2010)

- Fees can be based on service standards rather than CIP
- Quimby Act doesn't preempt park fees
- Fees can repay general fund loans
- Fees can be used for trash trucks & bins

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## Development Impact Fees

*Trinity Park, LP v. City of Sunnyvale* (6<sup>th</sup> DCA 2011)

- Developer challenge to inclusionary housing condition of approval time-barred
- 90-day period for challenges to development permits applied rather than 180-day limit of Mitigation Fee Act

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## Emergency Response Fees

### SB 49 (Strickland, R-Simi Valley)

- Would prohibit all local governments, including charter cities, from imposing a fee to recover the expense of emergency responses by police, fire, and ambulance crews without statutory authorization (like the DUI fee)
- Prop. 26 issue re exemption for residents
- Controversy re Sacramento's fee
- Died in Comm. on Public Safety in May 2011

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## Prop. 26

- Overturns *Sinclair Paint*
- All fees are taxes unless exception applies

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## Prop. 26 Exceptions Limited to Cost of Service or Regulation

- Specific Benefit / Privilege (permits, franchises)
- Specific Service / Product (utility charges, park & rec. fees)
- Reasonable Regulatory Fees for licenses & permits (permits, inspections)

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## Prop. 26 Exceptions not limited to Cost Recovery

- Fee for entry, use or purchase of gov't property (park & rec entrance fees, equipment rental, some franchises)
- Fines & penalties

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## Other Prop. 26 Exceptions

- Fees imposed as a condition of property development (limited to cost by other law)
- Assessments & property-related fees subject to Prop. 218 (limited to cost by 218)

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## Major Impacts of Prop. 26

- Non-property-based BIDs
- Park & Rec. service fees (*cf.* GC 50402)
- Discounts & free passes for fees excepted as benefit/privilege or service/product
- Scope of recoverable regulatory costs
- App'n to voluntary payments (development agreements, *e.g.*)
- In-lieu fees

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## More Impacts of Prop. 26

Some good news for cities

- Fish & Game Fees
- Booking Fees
- Property Tax Administration Fees

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## Prop. 26 To-Do's

- Get legal advice before adopting or increasing fee
- Review Existing Fees
- Considering segregating discretionary from non-discretionary fee proceeds
- Consider fees by agreement rather than by ordinance or rule
- Stay tuned!

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## Prop. 26

- Full paper at [www.cllaw.us](http://www.cllaw.us)
- **Prop. 26 Implementation Guide** available from League: [www.cacities.org](http://www.cacities.org)

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## Pre-Prop. 26 Fee Case Sheds Light on Proportionality Requirement

*Equilon Enterprises v. SBE* (2010) 189 Cal.App.4<sup>th</sup> 865

- Upheld regulations dividing lead fee between gasoline and paint industries b/c it reasonable to base fee on industry's contribution to environmental lead contamination rather than childhood health impacts
- Deferential review of agency determination of proportionality of fee to contribution to problem

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## Constitutional limit on fees

### *Cal. Farm Bureau v. SWRCB* (Cal. S. Ct. 2011)

- Water rights holders challenge fee to fund SWRCB
- S. Ct. reversed win for challengers and remanded for fact-finding, held fee must be proportionate to cost in aggregate, not fee payor by fee payor
- Less impact than expected, but helpful
- Prop. 13 case; Prop. 26 demands more

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## Assessments

### *Silicon Valley Taxpayer's Ass'n v. Sta. Clara Co. Open Space Authority* (Cal. S. Ct. 2008)

- Independent judicial review of assessment decisions
- Tighter definition of special benefit
- Open space and other services that benefit public broadly harder to justify
- Proportionality requirement unclear

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## BID Assessments

*Dahms v. Downtown Pomona PBID* (2<sup>nd</sup> DCA 2009), allows:

- exemption of residential pty from assessment for security, streetscape maintenance & marketing
- discounted assessments for non-profits
- use of front-street frontage for apportionment, along with lot & bldg size
- Very generous to agency; later cases less so

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## Utility Undergrounding Assessments

*Tiburon v. Bonander* (1<sup>st</sup> DCA 2010)

- No general benefit for utility undergrounding
- Court can look outside agency's own record
- Invalidated allocation of assessment and establishment of zones of benefit

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## Park Assessments

*Beutz v. Riverside Co.* (4<sup>th</sup> DCA 2010)

- Park M&O can be 100% assessment financed b/c capital provided with other \$
- Agency must always prove special benefit and proportional allocation even if challenger doesn't raise these points
- Questions use of cost to allocate benefit

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## Fire Suppression Assessments

*Concerned Citizens v. West Point Fire Protection District* (3<sup>rd</sup> DCA, August 2011)

- Engineer's report insufficient to show special benefit or proportionality
- Language threatens all service assessments
- Also questions use of cost to allocate benefit
- Pet'n for review and local government assns' request for depublication pending

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## Advice re Assessments

- Use a strong, current engineer's report
- Get legal review of reports at least until assessment law stabilizes
- Watch for current developments

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## Assessment Legislation

### SB 321 (Benoit) (effective 1/1/10)

- Assessment ballots mailed in envelopes marked "Official Ballot Enclosed"
- Assessment ballots must be counted in public if counted by agency staff or consultant who worked on assessment
- Information used to weight ballots is disclosable public record once tallying begins

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## Mandate Legislation

### ACA 17 (Logue, R-Yuba County)

- Legislative and regulatory mandates may not become operative until funded
- Narrows mandate exemption for fee-funded local programs to reflect requirements of Prop. 26
- Would authorize law suits to challenge mandates without first going through Comm'n process
- Never heard in committee

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## Mandates Litigation

### *California School Boards Ass'n v. Brown* (2<sup>nd</sup> DCA 2011)

- Governor may veto appropriation for a mandate
- Result is a \$0 appropriation and suspension of mandate

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## Mandates Litigation

*California Sch. Bds. Ass'n v. State* (4<sup>th</sup> DCA, 2011)

- Nominal funding of mandate violates Prop. 13
- No writ relief b/c annual suit for declaratory relief is adequate legal remedy
- Courts do not generally compel appropriations

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## Bankruptcy

AB 506 (Wiekowski, D-Fremont)

- Federal bankruptcy law allows states to set limits on which local governments may file Ch. 9
- Current CA law allows broad local discretion
- This bill would require mediation before filing, State Auditor audit and petition to panel of (Democratic) state elected officials
- Union reaction to Vallejo's bankruptcy
- In Senate Appropriations suspense in Aug. 2011

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## Fiscal Ballot Measures

- *Vargas v. Salinas* (Cal. S. Ct. 2009)
  - Balanced public education at public expense okay; express advocacy and other campaign-like efforts are not
- *Sta. Barbara County Coalition Against Automobile Subsidies v. SBCAG* (2<sup>nd</sup> DCA 2008)
  - Can use public funds to draft a ballot measure

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## Audit Legislation post-Bell

5 bills announced 2/8/11:

- SB 186 (Kehoe, D-San Diego) would authorize Controller audits at city expense “to ensure compliance with state law, grant agreements, local ordinances, and to determine fiscal viability.” (failed in Committee)
- SB 449 (Pavley, D-Agoura Hills) would authorize Controller to audit agency facing insolvency (failed in Committee)

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## More Audit Legislation

AB 229 (Lara, D-South Gate) would increase Controller's quality-control reviews of local government auditors

- Must hire from list of auditors approved by Controller
- Must change auditors after 5 yrs
- Must w/hold 10% of fee till Controller certifies audit; half of 2<sup>nd</sup> yr fee if 1<sup>st</sup> yr not certified; must cancel multi-year contract if auditor de-listed
- Controller access to audit work papers
- Controller to hire auditor at agency expense if audit not timely filed
- Pending hearing in Senate Gov't Operations in mid-August 2011

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## Still More Audit Bills

AB 253 (Smyth, R-Sta. Clarita)

- Controller to prescribe uniform accounting & reporting procedures for cities and some districts
- Comm. on City Accounting Procedures appointed by and serving at pleasure of Controller
  - 5 CFOs
  - 3 City Managers
  - 2 Councilmembers
- Stuck in Senate Gov't & Finance in August 2011
- Cf. AB 1287 (Buchanan, D-San Ramon)

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## One Last Audit Bill

### AB 276 (Alejo, D-Salinas)

- Double or triple penalties for late-file audits
- Extend filing duty to JPAs that issue conduit financings
- In Senate Rules in August 2011

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## Questions?

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