

# **Proposition 26**

# **Implementation Guide**

**April 2011**



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# Table of Contents

- I. Introduction and General Interpretation Issues .....1**
  - A. The Developing Law of Local Revenue Measures ..... 1
  - B. *Sinclair Paint Company v. State Board of Equalization* .....2
  - C. Proposition 26: A new definition of “tax” .....4
  - D. A Framework for Applying Proposition 26.....5
  - E. What Interpretive Issues Arise from the Opening Provision of Section 1(e)? .....6
  - F. Is Proposition 26 retroactive? .....7
  - G. Does Proposition 26 apply to pre-Proposition 26 fees or charges when they are increased or extended? .....8
  - H. Are there fees to which Proposition 26 does not apply? .....9
  - I. What does “levy, charge or exaction of any kind” mean?.....10
  - J. How do Proposition 26’s provisions regarding state revenue measures affect interpretation of its provisions regarding local government revenues? .....11
  - K. Does Proposition 26 Create More Reimbursable Mandates? .....12
- II. Exception No. 1: Section 1(e)(1) Exception for Fees for Benefits and Privileges Conferred .....15**
  - A. What Impact Does Proposition 26 Have on Free and Discounted Fees for Government-Provided Benefits and privileges? .....15
  - B. How does Proposition 26 affect Tipping Fees imposed at local agency-owned landfills?.....17
  - C. How does Proposition 26 Affect Non-Property-Based Business Improvement Districts? .....18

<b>III. Exception No. 2: Section 1(e)(2) Exception for Fees for Services and Products Provided</b> .....	<b>20</b>
A. Application of Proposition 26 to park and recreation fees. ....	20
1. In General.....	20
B. Fees for Services that are not “imposed.”.....	22
1. Are certain charges for services entirely outside Proposition 26’s definition of “tax” and, therefore, need not be justified by an exception?.....	22
2. Are retail electricity, gas, and other utility services charges “imposed” by a local agency?.....	23
3. Are wholesale water, sewer, electricity and other services provided by a local agency subject to Proposition 26?.....	23
C. Fees for Utility Services Generally.....	24
1. May general fund transfers from gas and electric utilities be maintained after the effective date of Proposition 26?.....	24
2. Are fares for municipal bus, trolley, or other transportation services subject to Proposition 26? .....	26
3. If a Utility Service Charge is Subject to Proposition 26, What Exceptions Apply? .....	26
D. What impact does Proposition 26 have on fees for booking City and Special District arrestees into County Jails?.....	28
<b>IV. Exception No. 3: Section 1(e)(3)’s Exception for Permitting and Inspection Fees</b> .....	<b>29</b>
A. Do the “reasonable regulatory costs” protected by Section 1(e)(3) include rule making?.....	30
B. What implications does Section 1(e)(3) have for regulatory fees to protect the environment, public health, and quality of life?.....	30

<b>V.</b>	<b>Exception No. 4: Section 1(e)(4)’s Exception for Use of Government Property .....</b>	<b>33</b>
A.	How does this exception affect franchise fees?.....	33
1.	Cable television franchises.....	34
2.	Oil and gas pipeline franchises .....	35
3.	Telephone and electricity franchises .....	36
4.	Solid waste franchises .....	36
5.	Removal of abandoned vehicles – towing franchises .....	37
B.	How does this exception affect fees on cable franchisees to fund public, educational and government access channels on cable systems (“PEG fees”)? .....	37
C.	How does this exception affect AB 939 fees to fund local government regulatory programs associated with solid waste? .....	38
D.	How does this exception effect fees imposed on those who cut trenches in public rights-of-way?.....	39
E.	How does this exception affect tolls imposed for use of toll roadways? .....	40
<b>VI.</b>	<b>Exception No. 5: Section 1(e)(5)’s Exception for Fines &amp; Penalties .....</b>	<b>41</b>
<b>VII.</b>	<b>Exception No. 6: Section 1(e)(6)’s Exception for Fees Imposed as a Condition of Property Development.....</b>	<b>42</b>
<b>VIII.</b>	<b>Exception No. 7: Section 1(e)(7)’s Exception for Assessments and Property Related Fees Subject to Proposition 218 .....</b>	<b>43</b>
A.	Are Assessments Exempted from Proposition 218 by Article XIID, Section 5 Also Exempt from Proposition 26? .....	43
<b>IX.</b>	<b>What is the Effect of Section 1(e)’s Trailing Paragraph Regarding Burden of Proof?.....</b>	<b>45</b>
<b>X.</b>	<b>Conclusion .....</b>	<b>48</b>
<b>XI.</b>	<b>Attachments.....</b>	<b>49</b>

# I. Introduction and General Interpretation Issues

## A. *The Developing Law of Local Revenue Measures*

Over the past 30 years, California voters have insisted that local voters be consulted on a variety of revenue-raising measures. Prior to Proposition 13 in 1978, voter approval was not required for taxes, charges or fees. Beginning with Proposition 13, the following progression has occurred:

- Proposition 13 (1978):  $\frac{2}{3}$  voter approval required for “special taxes” and property tax otherwise limited to 1% of assessed valuation;
- Proposition 62 (1984): majority voter approval required for “general taxes” in general law cities and counties; and
- Proposition 218 (1996): majority vote approval required for “general taxes” in general law and charter cities and counties; property-owner approval required for assessments and property-related fees and charges.

Proposition 13 made the definition of “tax” important for the first time. It led to the adoption of Gov. Code § 50076, which states:

“A special tax shall not include 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.”

The authority to impose regulatory fees was well established when Proposition 13 was adopted in 1978. It derives from the “police power,” the inherent reserved power of government to subject individual rights to reasonable regulations for the general welfare.<sup>1</sup> Fees, charges, and rates must be reasonable, fair and equitable in nature and proportionately representative of the costs incurred by the regulatory agency.<sup>2</sup> Early in the developing history of the distinction between fees and charges, fees imposed as a condition of development were considered “regulatory fees” imposed to defray all or part of the cost of public facilities related to a development project. For such fees to be valid, there must be a reasonable relationship between the fee’s use and type of project; and between the need for the public facility and the type of development project on which the fee is imposed.<sup>3</sup> The authority to impose service fees was similarly well established but, in addition to sometimes being grounded on the “police power,” was often justified as incidental to the power to provide the service or on the privilege of

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<sup>1</sup> Cal. Const. art. XI, § 7; *County of Plumas v. Wheeler* (1906) 149 Cal. 758; *Associated Home Builders of the Greater East Bay, Inc. v. City of Walnut Creek* (1971) 4 Cal.3d 633.

<sup>2</sup> *Associated Homebuilders of the Greater East Bay, Inc. v. City of Livermore* (1961) 56 Cal.2d 847.

<sup>3</sup> Gov. Code §§ 66000(b), 66001

receiving the service.<sup>4</sup> The principle that fees must reasonably relate to the cost of providing service also applies in these rate cases.<sup>5</sup>

Proposition 218 created a new category: property-related fees for services with a direct relationship to property ownership.<sup>6</sup>

## **B. *Sinclair Paint Company v. State Board of Equalization***

Shortly after the adoption of Proposition 218, the California Supreme Court faced a new issue in *Sinclair Paint Co. v. State Board of Equalization* (1997) 15 Cal. 4th 866: Was a charge imposed to mitigate the impact of the fee-payor's activity a tax when:

- The business was not property development; and
- The business did not receive a direct benefit, privilege or service from the government?

The fee at issue was assessed on manufacturers of materials that contributed to environmental lead contamination by the Childhood Lead Poisoning Prevention Act of 1992. The Act imposed a fee on paint manufacturers and others whose products exposed children to lead contamination. The Act's intent was to require manufacturers to bear a fair share of the cost of mitigating the resulting adverse health impacts of their products. The proceeds of the fee funded a program for evaluation, screening, and medically necessary follow-up services for children exposed to lead in the environment.

The appellant paint manufacturer claimed that this fee was a tax because it:

“...neither reimburse[d] the state for special benefits conferred on manufacturers of lead-based products nor compensate[d] the state for governmental privileges granted to those manufacturers.”<sup>7</sup>

The Court of Appeal found the fee to be a tax because its proceeds were not used “to regulate Sinclair.” The Supreme Court concluded otherwise, holding that because such fees are imposed under a public agency's police power rather than its taxing power, use of fee proceeds need not

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<sup>4</sup> *Carlton Santee Corp. v. Padre Dam Mun. Water Dist.* (1981) 120 Cal.App.3d 14, 24; *Durant v. Beverly Hills* (1940) 39 Cal.App.2d 133, 137.

<sup>5</sup> *English Manor Corp. v. Vallejo Sanitation & Flood Control Dist.* (1974) 42 Cal.App.3d 996, 1004; *Boynton v. City of Lakeport Mun. Sewer Dist.* (1972) 28 Cal.App.3d 91, 96.

<sup>6</sup> For more information about Proposition 218, The Proposition 218 Implementation Guide, published by the League of California Cities, is available by contacting the League at (916) 658-8200.

<sup>7</sup> *Sinclair Paint*, 15 Cal.4th at 875.

confer benefits or privileges on the fee payor provided, the fee bears a reasonable relationship to the burden imposed on society by those charged.<sup>8</sup>

Sinclair Paint also disputed the state’s authority to impose industry-wide “remediation fees” to compensate for the adverse societal effects generated by an industry’s products. The Supreme Court, however, acknowledged that:

“[T]he police power is broad enough to include mandatory remedial measures to mitigate the past, present, or future adverse impact of the fee payer’s operations, at least where, as here, the measure requires a causal connection or nexus between the product and its adverse effects.”<sup>9</sup>

Other recent cases have defined a regulatory fee as an imposition that funds a regulatory program or that distributes the collective cost of a regulation and is:

“...enacted for purposes broader than the privilege to use a service or to obtain a permit . . . [T]he regulatory program is for the protection of the health and safety of the public.”

*Calif. Ass’n of Prof’l Scientists v. Dept. of Fish & Game (2000)* 70 Cal. App. 4th 935, 952 (cost of comprehensive environmental review far surpassed the amount of the fees generated and therefore was a legal use of regulatory fees). In general, courts have upheld regulatory fees that:

- Are imposed in an amount necessary to carry out the purposes and provisions of the regulation;
- Do not exceed the reasonable cost of providing the services necessary to the activity on which the fees are based; and
- Are not levied for an unrelated revenue purpose.

These “mitigating-effects regulatory fees” are the primary targets of Proposition 26. Proposition 26’s “Findings and Declarations of Purpose” indicates the drafters’ intent to reclassify as taxes many of the regulatory fees imposed to mitigate the adverse health, environmental, and other societal effects of regulated activities. As taxes, these charges historically imposed as fees are now subject to the voter approval requirements of art. XIIC.

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<sup>8</sup> *Id.* at 875-76. Development impact fees are a common type of “regulatory fee” in that they are imposed to mitigate the impacts of a development project on a community. No service or product is provided to the developer because development in California is a “privilege” rather than a right. A fee imposed as a condition of development is exempt from the definition of “tax” in art. XIIC, § 1(e)(6).

<sup>9</sup> *Id.* at 877-878.

### **C. *Proposition 26: A new definition of “tax”***

Proposition 26 adds a definition of “tax” to the Constitution:

“(e) As used in this article, “tax” means any levy, charge, or exaction of any kind imposed by a local government, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.

(3) A charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law.

(6) A charge imposed as a condition of property development.

(7) Assessments and property-related fees imposed in accordance with the provisions of art. XIID.

“The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity.”

Art. XIIC, § 1, subd. (e).

Previously, the Constitution’s definitions of “general tax” and “special tax” (added by Proposition 218) did not directly define “tax,” but rather the Constitution and statutes

described what a tax was not. For example, Gov. Code § 50076 provides that a fee that does not exceed the reasonable cost of providing a service is not a “tax.”<sup>10</sup>

After November 3, 2010, the date on which Proposition 26 became effective, the measure prohibits a local government from enacting, increasing, or extending any levy, charge, or exaction of any kind without voter approval unless an exceptions can be identified. The discussion of the seven exceptions quoted above begins in Part II of this Guide.<sup>11</sup>

#### **D. A Framework for Applying Proposition 26**

In light of the analysis of this Guide, questions arising under Proposition 26 can be analyzed using the following four-step process:

1. Was the fee in question authorized prior to the effective date of Proposition 26 – November 3, 2010 for local government and January 1, 2010 for state government? If so, the fee can be implemented without voter approval until it is “increased” or “extended” by legislative action, or otherwise within the meaning of Gov. Code § 53750(h). See Part 1.F below as to the non-retroactivity of Proposition 26 as to local governments.

2. As to post-Proposition 26 fees, was the fee “imposed” so as to bring it within the reach of Proposition 26 because some government force or authority obliges the payor to pay the fee, and it is therefore not meaningfully voluntary? If not, Proposition 26 does not apply. See Part III.B, below, as to the meaning of “impose.”

3. If a post-Proposition 26 fee is “imposed,” does one of the seven stated exceptions apply? See Parts II through VIII of this Guide below discussing those exceptions in turn.

4. If a post-Proposition 26 fee is “imposed” and does not fall within one of the seven stated exceptions, then Proposition 26 defines it as a “tax” for which voter approval is required under either:

- Proposition 62 (Gov. Code § 53720 et seq.) as to counties and general law;
- Proposition 218 (Art. XIII C, § 2) as to all local agencies.

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<sup>10</sup> The Gann Initiative defines “proceeds of taxes” as proceeds from “regulatory licenses, user charges, and user fees to the extent that those proceeds exceed the costs reasonably borne by [the government] in providing the regulation, product or service.” Art. XIII B, § 8 (c).

<sup>11</sup> Most of this Guide is devoted to a discussion of what levies will be included in those exceptions and, therefore, not be considered taxes. Proposition 26 also amended the Constitution to require  $\frac{2}{3}$  approval of each chamber of the Legislature for any change in state statute that results in any taxpayer paying a higher tax. The meaning of Proposition 26 for state levies is largely beyond the scope of this Guide.

General taxes, which provide discretionary revenue to be spent as a local agency’s governing body directs, require majority approval. Art. XIIC, § 2(b). Special taxes, the proceeds of which may be spent only on specified purposes, require two-third voter approval. Art. XIIC, § 2(d).<sup>12</sup>

### **E. *What Interpretive Issues Arise from the Opening Provision of Section 1(e)?***

Article XIIC, § 1(e) begins with this phrase:

As used in this article, “tax” means any levy, charge, or exaction of any kind imposed by a local government, except the following: ...

This phrase raises two questions: First, what is meant by “impose?” This term appears intended to refer only to situations in which some degree of government coercion is involved—either because it requires a fee or charge to be paid as a matter of law (as by adopting an ordinance or other legislation) or because government has conferred upon itself a monopoly and those who wish to receive a service or product, which might be an essential, such as water or sewer service, must pay the sums demanded by the government to do so. This point is elaborated in Part III. A below.

Second, are there meaningful distinctions among the terms “levy, charge or exaction of any kind?” The first six of the seven exception that follow the introductory language use only the word “charge” (although the fifth exception refers to a “fine, penalty or other charge) and the seventh exception uses terms that do not appear in the introductory phrase: “assessments and property-related fees.” Article XIIC does not otherwise define these terms. But Article XIID provides a definition of “fee or charge” but does not provide a definition of “levy” or “exaction.” The Proposition 218 Omnibus Implementation Act is similarly silent as to the meaning of these terms. See Gov. Code § 53750 (providing definitions to govern Articles XIIC and XIID).

The authors of this Guide believe the phrase “levy, charge or exaction of any kind” is intended to expansively include all revenue sources “imposed by a local government” under art. XIIC, § 1(e) or, as to the state, under art. XIIA, § 3(b). In this regard, Proposition 26 is akin to Proposition 218, which uses the phrase “fee or charge” without intending a distinction between the two terms. As the California Supreme Court explained as to Proposition 218:

“Because article XIII D provides a single definition that includes both ‘fee’ and ‘charge,’ those terms appear to be synonymous in both article XIII D and article XIII C. This is an exception to the normal rule of construction that each word in a

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<sup>12</sup> Further discussion of these requirements appears in The California Municipal Law Handbook (Cal CEB 2010 Annual) at §§ 5.105 – 5.120 and League of California Cities, Proposition 218 Implementation Guide (2007) at pp. 9-20.

constitutional or statutory provision is assumed to have independent significance. (citation omitted.) We use the terms interchangeably in this opinion.”<sup>13</sup>

## **F. *Is Proposition 26 retroactive?***

An initiative measure will not be given retroactive effect unless the measure contains an express retroactivity provision or “it is very clear from extrinsic sources that the Legislature or the voters must have intended retroactive application.” (See *Strauss v. Horton* (2009) 46 Cal. 4th 364, 470 [citing *Evangelatos v. Superior Ct.* (1988) 44 Cal.3d 1188, 1209].) Proposition 26 expressly applies retroactively to state measures adopted during the 11-month period between January 1, 2010 and the measure’s effective date of November 3, 2010. (See art. XIII A, § 3, subd. (c).)

No similar provision exists as to local levies, providing a text from which to argue that Proposition 26 has no retroactive effect on local agency levies. Furthermore, the summary of the measure prepared by the Legislative Analyst states that fees and charges in existence are not affected unless they are later increased or extended. (Ballot Pamp., General Elec. (November 2, 2010) analysis of Proposition 26 by Legislative Analyst, p. 58.)

Thus, even if a fee enacted prior to November 3, 2010 does not fit within any of Proposition 26’s exceptions, it will nonetheless remain valid provided that the legislation authorizing it is not amended so as to extend or increase the fee. The effect of Proposition 26 on extensions and increases of pre-Proposition 26 fees is discussed in the next section.

The authors of this Guide caution that Proposition 26’s provisions placing the burden on the government to prove by a preponderance of the evidence that a levy, charge, or other exaction is not a tax (art. XIII A § 3(d); art. XIII C, § 1(e)) may be viewed as procedural amendments. As such, these requirements may apply to judicial challenges to existing fees. (See, *Murphy v. City of Alameda* (1992) 11 Cal. App. 4<sup>th</sup> 906, 913; *Anton v. San Antonio Community Hospital* (1982) 132 Cal. App. 3d 638, 650.) See Part IX of this Guide for further discussion of Proposition 26’s provisions regarding burden of proof.

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<sup>13</sup> *Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4th 205, 222.

**G. Does Proposition 26 apply to pre-Proposition 26 fees or charges when they are increased or extended?**

Proposition 26 does not require voter approval for adjustments of local levies for inflation if the formula or schedule for changes was approved before the measure’s effective date, although there may be some uncertainty on this point.<sup>14</sup> This conclusion is based upon the definition of “increased” in the Proposition 218 Omnibus Implementation Act. Gov. Code § 53750, subd. (h).

Proposition 26 is an amendment to art. XIIC (which was originally adopted by Proposition 218 in 1996).<sup>15</sup>

The Proposition 218 Omnibus Implementation Act’s definitions apply by its terms to art. XIIC (see Gov. Code § 53750) and, given there is no indication of a contrary intent, the Act may be of help in interpreting the provisions of Proposition 26. The choice to implement the goals of Proposition 26 by a narrow amendment of art. XIIC, evidences an intent that those other terms continue to apply under a rule of statutory construction identified by its Latin label “*in pari materia*.”<sup>16</sup>

Thus, terms used in Proposition 26 that are also defined in the Omnibus Act will be subject to the already existing meanings provided in the Omnibus Act. Specifically, the Omnibus Act states that a “tax, fee, or charge is not deemed to be ‘increased’ by an agency action that” only adjusts “the amount of a tax or fee or charge in accordance with a schedule of adjustments,<sup>17</sup> including a clearly defined formula for inflation adjustment that was adopted by the agency prior to

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<sup>14</sup> For the purposes of this section, “adjustment” includes any method of increasing (or decreasing) the amount of a levy that was approved prior to Proposition 26’s effective date. It therefore encompasses, but is not limited to, automatic changes to account for inflation, a prescribed schedule of increases, adjustments under a maximum approved amount, and formulas to account for changes in population.

<sup>15</sup> Since the 1996 adoption of Proposition 218, the courts have provided guidance on the application of Articles XIIC and XIID and this case law informs the interpretation of Proposition 26. See *Fields v. Eu*, (1976) 18 Cal.3d 322 (“It is a cardinal rule of construction that words or phrases are not to be viewed in isolation; instead, each is to be read in the context of the other provisions of the constitution bearing on the same subject. The goal, of course is to harmonize all related provisions if it is reasonably possible to do so without distorting their apparent meaning, and in so doing to give effect to the scheme as a whole.”)

<sup>16</sup> *In re Wright’s Estate*, (1929) 98 Cal.App. 633, 635, (“[I]t is a settled rule that all statutes which relate to the same general subject-matter – briefly called statutes in *pari materia* – must be read and construed together, as one act, each referring to and supplementing the other, though they were passed at different times.”); see also *Kahn v. Kahn* (1977) 68 Cal.App.3d 372.

<sup>17</sup> “Schedule of adjustments” is a broad phrase that readily encompasses a range of types of changes, including both a series of increases in specific amounts over time and an automatic adjustment for inflation that occurs at regular intervals, such as at the beginning of each fiscal or calendar year.

November 6, 1996.”<sup>18</sup> (Gov. Code § 53750(h)(2)(A).) Thus, increasing a levy according to a “schedule of adjustments” included in the levy prior to the effective date of Proposition 26 should not constitute an increase that requires voter approval. The strength of the argument is uncertain because of the phrase “including a clearly defined formula for inflation adjustment that was adopted by the agency prior to November 6, 1996.” The mention of this specific date could limit the validity of existing inflationary adjustments to those in effect prior to November 6, 1996, the effective date of Proposition 218. On the other hand, this phrase begins with “including” and this illustrates, but does not limit the phrase which precedes it, suggesting a broader interpretation is appropriate.

The authors of this Guide conclude that the better reading disfavors any retroactive application of either Proposition 218 or Proposition 26<sup>19</sup> because one could argue that the date was included solely to reflect the effective date of Proposition 218, and as a result of the amendments made by Proposition 26, the date should be read as the effective date of the newer measure.

Further, the last clause of the definition – “including a clearly defined formula for inflation adjustment that was adopted by the agency prior to November 6, 1996” – is an example of the types of “schedules of adjustments” that are permitted, not a limitation. That interpretation is consistent with the grammatical construction of the sentence, although it has not previously been the general understanding of that clause by public agency attorneys. Such an interpretation would not necessarily be consistent with the intent of Proposition 218 to require voter approval of tax and fee increases after its effective date, although the levies made taxes by Proposition 26 were not taxes subject to of Proposition 218.

Despite the arguments outlined in this section, the authors of this Guide recommend caution before continuing to implement adjustments for any levies that may not fall within one of Proposition 26’s seven exceptions. Further, compliance with Proposition 26 is likely required if an adjustment is based upon factors other than a previously-adopted schedule, for example, because the revenue requirement cannot be met by charges imposed at previously authorized amounts.

#### **H. *Are there fees to which Proposition 26 does not apply?***

By its terms, Proposition 26 applies only to fees that are “imposed” by a government. Fees imposed by private parties (like telephone charges and many solid waste collection fees) are not within the scope of Proposition 26. Moreover, many fees collected by local governments are not “imposed” by them, either because local government is collecting a fee imposed by the state or because the fee is voluntarily paid. Courts can be expected to rely, as they have in similar

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<sup>18</sup> November 6, 1996 was the effective date of Proposition 218.

<sup>19</sup> A legislative amendment may be necessary to change the date from November 6, 1996 to November 3, 2010 (the effective date of Proposition 26).

contexts, on the dictionary meaning of “impose,” which is to establish or apply by authority or force.<sup>20</sup>

Accordingly, if a franchise agreement is voluntarily negotiated between a local government and a benefited business, fees paid under that agreement may not be “imposed” for purposes of Proposition 26, but rather the payments are meaningfully voluntary.

A complete discussion of the meaning of “impose” is found in Part III.B. of this Guide.

### **I. What does “levy, charge or exaction of any kind” mean?**

There are no meaningful distinctions among the terms “levy, charge or exaction of any kind.” The first six of the seven exceptions that follow this introductory language use only the word “charge” (although the fifth refers to a “fine, penalty or other charge”) and the seventh exception uses terms that do not appear in the introductory phrase: “assessments and property-related fees.” Art. XIIC does not define these terms, while art. XIID, adopted along with art. XIIC by Proposition 218, defines “fee or charge” but does not define “levy” or “exaction.” The Proposition 218 Omnibus Implementation Act is similarly silent as the meaning of these terms. *See* Gov. Code § 53750 (definitions section of Omnibus Act).

Rather, the authors of this Guide believe that the phrase “levy, charge or exaction of any kind” is merely intended to expansively include all revenue sources “imposed by a local government” under art. XIIC, § 1(e) or, as to the state, under art. XIIA, § 3(b). In this regard, Proposition 26 is akin to Proposition 218, which uses the phrase “fee or charge” without intending any distinction between the two terms. As the California Supreme Court explained as to Proposition 218:

“Because article XIII D provides a single definition that includes both ‘fee’ and ‘charge,’ those terms appear to be synonymous in both article XIII D and article XIII C. This is an exception to the normal rule of construction that each word in a constitutional or statutory provision is assumed to have independent significance. (citation.) We use the terms interchangeably in this opinion.”

*Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4th 205, 222.

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<sup>20</sup> *Ponderosa Homes, Inc. v. City of San Ramon* (1994) 23 Cal.App.4th 1761, 1770 (citing Webster’s Third Internat. Dict. (1970) in construing “impose” as used in the Mitigation Fee Act.) The Proposition 218 Implementation Guide (2007 ed.) at p. 60 also discusses the meaning of “impose,” citing to Black’s Law Dictionary.

**J. How do Proposition 26's provisions regarding state revenue measures affect interpretation of its provisions regarding local government revenues?**

Three parts of Proposition 26 are relevant to this question:

- 1) Amendment to art. XIII A, § 3(a) to state that “Any change in state statute which results in any taxpayer paying a higher tax” requires  $\frac{2}{3}$  vote of the legislature. [Former law: “Any changes in state taxes enacted for the purpose of increasing revenues collected pursuant thereto” required  $\frac{2}{3}$  vote of the Legislature].
- 2) Addition of § 3(b) to art. XIII A to define state “tax.”
- 3) Addition of § 1(e) to art. XIII C to define local government “tax.”

The second and third amendments are almost identical with the following exceptions:

1. Article XIII A, § 3(b)(3) compared to Article XIII C, § 1(e)(3).

Article XIII A, § 3(b)(3) states an exception to the definition of state tax for:

“A charge imposed for the reasonable regulatory costs to the State **incident to** issuing license and permits, performing investigations, inspections and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.” (Emphasis added.)

Article XIII C, § 1(e)(3) uses this same language except that “incident to” is replaced with “for.”

These provisions are the exceptions for “reasonable regulatory costs.” For the state, the exception includes a charge imposed for the reasonable regulatory costs to the state incidental to issuing licenses and permits, etc. For local governments, the exception includes a charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, etc. For purposes of Proposition 218, a property-related fee is one that is imposed as “an incident of property ownership” or for a “property-related service” (Art. XIII D, § 2(e)). The California Supreme Court has interpreted “an incident of” to mean “by virtue of.”<sup>21</sup>

Using this construction, it appears that the exception for state charges in this category is slightly broader than the exception for local charges. The use of the word “for” implies a more direct connection between the charge and the activity: issuing licenses and permits etc. However, the text and legislative history of Proposition 26 does not indicate any intent to treat state and local regulatory fees differently. Throughout the ballot materials, state and regulatory fees are treated the same. Consequently, the difference in language, “incident to” and “for,” may be negligible.

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<sup>21</sup> *Apartment Ass'n of Los Angeles County, Inc. v. City of Los Angeles* (2001) 24 Cal.4th 830, 842.

2. Article XIII A, § 3(b)(4) compared to Article XIII C, § 1(e)(4)

Article XIII A, § 3(b)(4) excludes from the definition of state taxes:

A charge imposed for entrance to or use of state property, or the purchase, rental, or lease of state property, **except charges governed by Section 15 of Article XI** [i.e., the vehicle license fee]. (Emphasis added.)

Article XIII C, § 1(e)(4) uses this same language, except that the trailing phrase emphasized above is omitted. The omitted reference is to the vehicle license fee (VLF) – a tax paid at the time of vehicle registration. The VLF, although labeled a “fee,” is a tax and is not a charge imposed for entrance to or use of state property, nor for the purchase, rental or lease of state property. This clause appears to reinforce this understanding and forestalls an argument that the VLF is a charge for use of the state road system.

3. Article XIII C, §§ 1(e)(6) and (7)

Article XIII C, § 1(e)(6) and (7) state exceptions to Proposition 26’s the definition of “tax” applicable to local government:

(6) A charge imposed as a condition of property development.

(7) Assessments and property-related fees imposed in accordance with the provisions of Article XIII D [added to the Constitution by Proposition 218].

These exceptions apply only to local governments because there are no like charges imposed by the state.

### **K. *Does Proposition 26 Create More Reimbursable Mandates?***

One consequence of Proposition 26 is that by reclassifying certain fees as taxes, local agencies may be in a better position to seek reimbursement for the costs of programs and services that are unfunded state mandates. Art. XIII B, § 6 provides that except in certain specific circumstances:

“Whenever the Legislature or any state agency mandates a new program or higher level of service on any local government, the state shall provide a subvention of funds to reimburse that local government for the costs of the program or increased level of service.”

A “new program” within the meaning of art. XIII B, § 6 is a program that carries out the governmental function of providing services to the public, or a law that, to implement state policy, imposes unique requirements on local agencies and does not apply generally to all residents and entities in the state. *County of Los Angeles v. Comm’n on State Mandates*, (1995) 32 Cal.App.4th 805, 816.

“Costs” is defined as costs mandated by the state for any increased costs that the local agency is required to incur as a result of any statute, or any executive order implementing any statute, which mandates a new program or higher level of service of any existing program within the meaning of art. XIII B, § 6; Gov. Code § 17514; *County of Fresno*, 53 Cal.3d at 484. A reimbursable “higher level of service” concerning an existing “program” exists when a state law or executive order mandates not merely some change that increases the cost of providing services, but an increase in the actual level or quality of governmental services provided or a transfer of financial responsibility for a program from the state to a city or county. *San Diego Unified Sch. Dist. v. Comm’n on State Mandates*, (2004) 33 Cal.4th 859, 877.

Both art. XIII B, § 6 and state law establish exceptions to the requirement that the state reimburse local governments for the cost of state mandates. Among those is California Gov. Code § 17556(d), which provides that a state mandate does not impose reimbursable “costs” if a local agency “has the authority to levy service charges, fees, or assessments sufficient to pay for the mandated program or increased level of service.” The converse to this exception is that if a local agency does **not** have authority to levy a service charge, fee, or assessment sufficient to pay for the mandated program or increased level of service, then it does incur costs which the state must reimburse.

The Legislature has established an administrative process for determining that a mandate is subject to reimbursement pursuant to art. XIII B, § 6; Gov. Code §§ 17500 et seq. These procedures are the sole and exclusive procedure by which a local government may claim reimbursement for state-mandated costs. Gov. Code § 17552. The procedures require filing a test claim with the Commission on State Mandates (the “Commission”). Judicial review is only available after a final determination by the Commission. Gov. Code §§ 17553, 17559.

In a March 2010 test claim before the Commission, local agencies successfully argued that certain requirements mandated by the state for storm water pollution prevention were subject to reimbursement because the local agencies effectively did not have the authority to levy a service charge, fee, or assessment sufficient to pay for the mandated program or increased level of service. The test claim was filed by the County of San Diego and other cities located within the county (the “Claimants”) alleging that various activities to reduce storm water pollution to comply with a National Pollutant Discharge Elimination Permit (“NPDES Permit”) issued by the Regional Water Quality Control Board mandated a new program or required a higher level of service, and were therefore unfunded mandates. The Claimants successfully argued that they could not unilaterally impose a fee on water and sewer bills to recover the cost to comply with certain requirements of the NPDES Permit because of *Howard Jarvis Taxpayers Association v. City of Salinas* (2002) 98 Cal.App.4th 1351, 1358-1359.

In the *Salinas* case, the court invalidated a storm water management fee imposed by the city on all owners of undeveloped parcels in the city. The court held that the storm water fee was a property-related fee pursuant to art. XIII D, § 6. Pursuant to art. XIII D, § 6(c), except for fees or charges for sewer, water, and refuse collection, no property-related fee or charge may be imposed or increased until it is submitted to and approved by either:

- A majority vote of the property owners of the property subject to the fee or charge; or
- A  $\frac{2}{3}$  vote of the electorate residing in the affected area. Because the city's storm water fee was not a water or sewer fee, the court held that the city was required to submit the fee for voter approval.

The Commission recognized that the Claimants, under their police powers, have the authority to impose fees for certain NPDES Permit activities that constitute a state mandated new program or higher level of service. The Commission found however, that the Claimants do not have sufficient fee authority within the meaning of California Government Code § 17556 if the fee or assessment is contingent on the outcome of an election by voters or property owners. Thus, under the constraints of Proposition 218, the Commission found the local agencies have no authority to impose fees for certain NPDES activities without the consent of the voters or property owners. The Commission noted:

“[I]t is possible that the local agency's voters or property owners may never adopt the proposed fee or assessment, but the local agency would still be required to comply with the state mandate. Denying reimbursement under these circumstances would violate the purpose of Article XIII B, § 6, which is ‘to preclude the state from shifting financial responsibility for carrying out governmental functions to local agencies . . .’”

Statement of Decision, Discharge of Stormwater Runoff – Order No. R9-2007-0001, Case No. 07-TC-09 (March 26, 2010), p. 106. The Commission held the voting requirements do not impose a mere practical or economic hurdle, but a legal and constitutional one. *Id.* at 107. Consequently, the Commission held that certain of the NPDES activities are unfunded mandates of the state.

As noted above, the Commission did recognize that the Claimants, pursuant to their police powers have the authority to impose fees for certain of the NPDES Permit activities that constitute a state-mandated new program or higher level of service. In particular, the Commission noted the regulatory fee authority of the Claimants under their police powers. See *Id.* at 103-106. Proposition 26 may greatly curtail the authority of local agencies to impose regulatory fees for the purpose of mitigating the adverse impacts of storm water pollution. This application of § 1(e) may allow local agencies to argue that certain regulatory activities required under their NPDES permits, as well as other state-mandated services and programs, are mandates within the meaning of art. XIII B, § 6. Art. XIII B, § 6(b)(1) requires the Legislature either to fully fund reimbursable mandates or suspend the obligation of local governments from the duty to implement them.

## II. Exception No. 1: Section 1(e)(1) Exception for Fees for Benefits and Privileges Conferred

Section 1(e)(1) excludes from the new definition of “tax”:

“A charge imposed for a **specific benefit conferred or privilege granted** directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.” (Emphasis added.)

It is not clear how the terms “specific benefit conferred” and “privilege granted” differ, nor is it clear what revenue measures may fall under each. Further, it is not clear how these terms will be distinguished from the “government service” or “product” exceptions in art. XIII C, § 1(e)(2). But this point may be of only academic interest given that the conditions in these first two exceptions are largely the same, both are limited to the reasonable cost to government of granting the benefit or privilege, or of providing the service or product.

### A. *What Impact Does Proposition 26 Have on Free and Discounted Fees for Government-Provided Benefits and privileges?*

This exception has three parts:

- A charge imposed for a specific benefit conferred or privilege granted;
- A benefit conferred or privilege granted that is not provided to those not charged; and
- A charge that does not exceed the local agency’s reasonable costs.

If the second part is to be taken literally, this language could mean that no one can be charged for a benefit or privilege if any other person receives it for free.

The “Findings and Declarations of Purpose” of Proposition 26 do not support such an interpretation of this exception. They focus on local governments having “disguised new taxes as ‘fees’ in order to extract even more revenue from California taxpayers without having to abide by these constitutional voting requirements.” Under well-settled law that predates Proposition 26, regulatory fees that include excess charges to fund discounts to other fee payors are already deemed to be taxes by the courts.<sup>22</sup>

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<sup>22</sup> E.g., Gov. Code § 50076 “special tax [subject to  $\frac{2}{3}$  voter approval requirement of Prop. 13, Art. XIII A, § 4] shall not include 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

Therefore, the first exception excludes from the definition of “tax” a fee that covers the cost of providing a benefit or privilege to a fee payer as long as the fee does not also include a subsidy to cover free or discounted services to other persons. A court is likely to conclude that Proposition 26 was not intended to exclude a local agency from offering free or discounted services that the local agency pays for from its general fund rather than from higher fees charged to other fee payors.

Even were this language to mean that discounts – no matter how deep – are permissible, but free services are not, the courts would be called upon to distinguish between very deep discounts and free services, the kind of line-drawing usually reserved to the legislative process. Moreover, the purpose of Proposition 26 is not to require government to place a burden on some service recipients more, but rather the purpose is to burden all of them less. For these reasons, the authors of this Guide conclude that local agencies may allow both free and discounted services to some service recipients without converting the fees charged others into taxes, provided that the cost of these subsidies is not funded from higher fees charged to other persons.<sup>23</sup>

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revenue purposes.” Art. XIII B, § 8, subd. (c) defining “proceeds of taxes” subject to Gann limit to “include, but not be restricted to, all tax revenues and the proceeds to an entity of government, from ... regulatory licenses, user charges, and user fees to the extent that those proceeds exceed the costs reasonably borne by that entity in providing the regulation, product, or service ...”

<sup>23</sup> It is worth noting that “charging” does not mean “collecting.” Therefore, the fact that an agency may not be covering the entire cost of an enterprise from rates because of external factors, such as debt, mean that the agency cannot set rates at a level that takes into account this cost to the agency. Just as private-sector utility providers and others treat bad debt as a cost of doing business, a government service provider need not itself subsidize the service by failing to recover from fee payers the cost of providing the privilege or benefit that the provider cannot efficiently collect from others liable for the fee.

## **B. How does Proposition 26 affect Tipping Fees imposed at local agency-owned landfills?**

A tipping fee (sometimes referred to as a gate fee) is a charge levied upon a given quantity of waste received at a waste processing facility. In 1988, the Legislature passed the Waste Management Act. Its goals were to reduce, recycle, and reuse solid waste to the extent possible. Local agencies that were responsible for waste disposal within their boundaries were obliged to enact comprehensive waste management plans that would eventually divert half of their trash from landfills<sup>24</sup> to preserve landfill capacity in California.<sup>25</sup> The Act allows local agencies to determine aspects of solid waste handling that are of local concern including charges and fees.<sup>26</sup> Among others, some local agencies charge “tipping fees” to fund the waste diversion program.

As an example, the County of Alameda adopted a Recycling Plan that included several programs:

- A countywide source reduction program to minimize the generation of refuse, residential and commercial recycling programs; and
- Recycled product market development and purchase preference programs.<sup>27</sup>

A \$6 per ton “tipping fee” on materials deposited in county landfills provided funding for the plan. The City of Dublin challenged the fee as a special tax. In upholding the fee against the argument that it was actually a special tax, the court analyzed whether the charges “bear a fair or reasonable relationship to the payor’s burdens on or benefits from the activity at issue.”<sup>28</sup> The court noted that the overall goal of the plan was:

“ . . . reduction of the refuse landfilled in the County. Whether or not that goal is accomplished will have effects on the maintenance, operation, and longevity of the existing landfills, as well as on the need to develop new sites. The surcharge is directly related to the burdens imposed by the payors on the landfills; it is imposed on waste haulers based on tonnage, and will be passed on to those who generate the waste in the form of increased garbage collection rates. Thus the surcharge is intended to distribute the financial burden of source reduction in proportion to the contribution of each waste generator to the problem, and at the

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<sup>24</sup> *City of Alhambra v. P.J.B. Disposal Co.* (1998) 61 Cal.App.4th 136, 138; *Valley Vista Services, Inc. v. City of Monterey Park* (2004) 118 Cal.App.4th 881.

<sup>25</sup> Public Resources Code § 40000(e). Other reasons cited for the reduction, recycling, or reuse requirement were conservation of water, energy, and other natural resources.

<sup>26</sup> Public Resources Code § 40059.

<sup>27</sup> *City of Dublin v. County of Alameda* (1993) 14 Cal.App.4th 264.

<sup>28</sup> The court’s inquiry is the same as the standard of review in Proposition 26.

same time it provides incentives for the control and reduction of waste generation.”<sup>29</sup>

The authors of this Guide conclude Proposition 26 does not apply to the type of tipping fee described in the *City of Dublin* case for three reasons:

(1) Art. XIIC, § 1(e)(1) excepts from the definition of “tax,” “a charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.” Maximizing and preserving landfill capacity is a specific benefit conferred upon the payor of the tipping fee that is not provided to those not charged in the same manner and with the same benefit as to those in the waste hauling business subject to the fee receive. The Integrated Waste Management Act notes that other reasons for reduction, recycling and reuse are conservation of water, energy and other natural resources. A local agency defending a tipping fee against a Proposition 26 challenge must demonstrate that the amount is no more than is necessary to cover the reasonable costs of the government activity of maximizing and preserving landfill space.

(2) Art. XIIC, § 1(e)(4) excepts from the definition of “tax” a charge imposed for entrance to or use of local government property. To the extent that the landfill is owned and operated by the local government, the “tipping fee” is a charge imposed to enter and use the property.

(3) To the extent that a “tipping fee” is passed on to the customer who places refuse at the curb, the “tipping fee” is part of the refuse collection rate. Refuse collection rates that are property-related fees subject to Proposition 218 fall under the exception in art. XIIC, § 1(e)(7).

### **C. How does Proposition 26 Affect Non-Property-Based Business Improvement Districts?**

State law authorizes two kinds of business improvement district (BID) assessments— assessments against real property and assessments against businesses. Real property assessments must comply with Proposition 218, and, therefore, are fall under the exception in art. XIIC, § 1(e)(7).

BID assessments against businesses, by contrast, are not levies or charges “upon real property ...for a special benefit conferred upon the real property.” (Art. XIIC, § 2(b)). Consequently, they are not subject to the requirements of Proposition 218. (*Howard Jarvis Taxpayers Ass’n v. City of San Diego* (1999) 72 Cal.App.4th 230).

Assessments against businesses are most often levied under the Parking & Business Improvement Area Law of 1989 (Streets & Highways Code § 36500 *et seq.*) (“the 1989 Act”) or under a similar local ordinance adopted by a charter city. These assessments may fund a variety

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<sup>29</sup> *Id.* at p. 285 (citing *San Diego Gas & Electric Co. v. San Diego County Air Pollution Control District*).

of services to a business district. Some examples include security programs, street and sidewalk cleaning, installation and maintenance of landscaping, banners and street furniture, street fairs, concerts, and events, and advertising and marketing services. Under the 1989 Act, assessments must be levied on the basis of the estimated benefit to the businesses and property within the district. (Streets & Highways Code § 36536). The Property and Business Improvement District Act of 1994 (Streets and Highways Code §36600 *et seq.*) also permits business-based assessments, but is more commonly used for property-based assessments.

Under § 1(e)(1), an assessment is exempt if it is:

“a charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit ...”

Non-property assessments against business are based, in concept, on the benefit of activities to those businesses that are funded by the assessment. Therefore, at least some assessments against businesses could fall within this exception. But the exception applies only if the “specific benefit” is conferred “directly” to the business being assessed **and** the benefit is “not provided to those not charged.”

It is not clear how these requirements will be applied to an assessment on a business. An argument can be made that security patrols in the vicinity of assessed businesses are provided directly to the businesses and are only provided to those businesses being assessed. This logic has been accepted by at least one appellate court in the property assessment context (*Dahms v. Downtown Pomona Property Ass’n* (2009) 174 Cal.App.4th 708,722). That case did not apply the Proposition 26’s “specific benefit” standard, but rather applied Proposition 218’s requirement that a “special benefit” must:

“...affect the assessed property in a way that is particular and distinct from [its] effect on other parcels and that real property in general and the public at large do not share.” *Id.* (internal quotation omitted).

A contrary argument can also be made that where a service or program, such as street furniture or concerts, is provided to an area, rather than directly to a business, that service or program is also “provided” to the public. Therefore, the service or program is being “provided” to those not charged the assessment.

Another area of uncertainty concerns hotel and tourism BID assessments. These BIDs levy assessments against hotels (usually based on gross revenue or on occupied room nights to fund marketing efforts and similar services. Arguably, the benefits of marketing a community may extend beyond those hotels being assessed, and therefore, those businesses not being assessed may realize a benefit from the services being funded by the assessment proceeds. On the other hand, if the marketing services are limited to the assessed hotels, a stronger argument can be made that the services are provided to the hotels, even if other businesses may receive an incidental benefit.

An argument might also be made that business assessments actually are charges for services despite being cast in BID law, and in many local ordinances, as assessments for benefits. Under this argument, the applicable exception would be that of § 1(e)(2), which excepts charges:

“imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.”

This argument could deflect a claim that while BID services are provided “directly” to business, they “benefit” the public. But it would also invite a new question – whether the services “are provided those not charged.” Local governments may find this question easier to persuasively answer.

### **III. Exception No. 2: Section 1(e)(2) Exception for Fees for Services and Products Provided**

Section 1(e)(2) excludes from the new definition of “tax”:

“A charge imposed for a **specific government service or product provided** directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.” (Emphasis added.)

This exception covers utility fees not subject to Proposition 218,<sup>30</sup> some park and recreation fees that are not admission or equipment rental fees, transit fees, emergency response fees,<sup>31</sup> and a wide range of other government fees.

#### **A. *Application of Proposition 26 to park and recreation fees.***

##### **1. In General**

For purposes of Proposition 26, park and recreation fees can be divided into two general categories – those best analyzed under §1(e)(2)’s exception for service fees, and those best analyzed under § 1(e)(4) exception for fees for the use of government property. The first category includes fees imposed for a service – like lessons, transportation, child care, etc. The fee for services exception requires that such fees be limited to “the reasonable costs to the local government of providing the service.”

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<sup>30</sup> Gas and electric charges are exempted from Proposition 218 by Article XIID, § 3(b).

<sup>31</sup> By emergency response fees, we mean those authorized by Gov. Code §§ 53150-53158. We do not mean the 911 response fees called into question by *Bay Area Cellular Tel. Co. v. City of Union City*, (2008) 162 Cal.App.4th 686 (fee imposed on phone bills for 911 services was tax requiring voter approval).

The second category includes fees for the use of government property. Fees imposed for admission to parks, rental of government property (like bikes, boats and recreation equipment), and for the rental of fields, meeting rooms and the like, are best analyzed under § 1(e)(4). The language of that exception does not include the “reasonable costs” limitation. But a general law city is subject to the constraint on the amount of a fee charged either under either category imposed by Gov. Code § 50402, which provides, in part, as follows:

“A city, county or city and county owning property or leasing property which is devoted to park, amusement, or recreational purposes may make a charge for use or services provided therein in the amount as may be provided by resolution by the governing body. No charge shall be imposed which exceeds the cost of the service provided. To the extent feasible, charges for similar uses or services imposed by a governing body pursuant to this section shall be uniform throughout its area of jurisdiction.”

Are charges for services offered in connection with recreational, cultural, educational, or other similar programs subject to Proposition 26?

Many local governments own and operate a wide variety of park, recreation, and cultural facilities. These may include facilities such as tennis courts, golf courses, fitness centers, swimming pools, museums, interpretive centers, and other similar civic facilities. The agency frequently provides classes, lessons, and other recreational, cultural, and educational programs at those facilities, often in competition with private enterprise. Additionally, agencies may sponsor running, cycling, or similar athletic events for which a participation fee is charged. Although admission charges are covered by the exception in art. XIII C, § 1(e)(4) for charges “imposed for entrance to or use of local government property,” there is a question whether charges for lessons, classes, or programs fall within the exception as a “use” of property, or whether the charges are “imposed” at all and, if not, excluded from the reach of Proposition 26’s definition of “tax” for that reason.

There is a reasonable argument that a charge for a lesson, class, program, and other participation is not “imposed” within the meaning of Proposition 26 if the participants have meaningful private market options and participation is meaningfully voluntary. A local government may wish to document the market options available to consumers, demonstrating that participation in the government’s program is meaningfully voluntary, to support its determination that charges for recreational, cultural and educational programs are not subject to Proposition 26.

To the extent that the charges are “imposed,” the exceptions for conferring a benefit or privilege (§ 1(e)(1)) or providing a service or product (§ 1 (e)(2)) would appear to apply as long as the cost of service test is met.

## ***B. Fees for Services that are not “imposed.”***

Part I.H of this Guide discusses the meaning of the term “impose” as used in Proposition 26. Determining whether a charge is “imposed” in a particular instance will likely turn not only on the particular nature of the service, but also on such factors as:

- Whether the charge is in connection with a service the provision of which is a statutory purpose of the local agency;
- Whether the charge is in connection with a service for which the local agency is the exclusive provider within its service territory or otherwise exercises monopoly pricing power;
- Whether the charge is in connection with a service, product, or opportunity the local government provides in competition with others, particularly private enterprises; or
- Whether the charge is established by arm’s length voluntary contract negotiations.

### **1. Are certain charges for services entirely outside Proposition 26’s definition of “tax” and, therefore, need not be justified by an exception?**

A credible argument can be made that certain charges for services provided by a public entity are entirely outside the scope of Proposition 26 because the charges are not “imposed,” even though the amount of the charge may be set by official agency action. For example, an agency that provides wholesale water or electric service pursuant to a service contract may desire to charge the same market rate that is available to the customer from other sources. *See, e.g., City of Oakland v. Burns*, (1956) 46 Cal.2d 401, 407 (“When a governmental entity is authorized to exercise a power purely proprietary, the law leans to the theory that it has full power to perform it in the same efficient manner as a private person.”)

Where a private market co-exists with the provision of the same services by local government, it is arguable that charges for the services provided by local government are not “imposed”. Although these charges may be established by the governing body of the local agency, the services are not provided pursuant to a statutory obligation. In these circumstances, if they are provided in competition with the same or similar services provided by others, and if the recipients of the service have a choice to receive the service or not, then rate-payers are protected from excessive rates by market forces, or their own power to meet their needs in other ways.

If a local agency is an exclusive provider of a utility service, provides the service pursuant to a statutory purpose for which it is organized, or is providing a service commonly associated with

government services, then a court will likely conclude that its service charges are “imposed” for purposes of Proposition 26.

## **2. Are retail electricity, gas, and other utility services charges “imposed” by a local agency?**

If a local agency is the exclusive retail provider of a utility service within its jurisdiction either in fact or by virtue of a legally enforceable monopoly, a court is likely to conclude that its charges for that service are “imposed.” Otherwise, a government’s pricing power would arise from its governmental power to create a monopoly for itself, and therefore, the purpose of Proposition 26 – to protect fee payors from “hidden taxes”--would be defeated.

Even when such rates are “imposed,” the exception provided by §1(e)(2) for charges for a specific government service or product that is sold at no more than the local agency’s reasonable costs of service would apply. Further the exception in § 1(e)(4) for a charge for the purchase, rental or lease of government property would apply. That exception does not, by its terms, limit charges within its scope to recovery of reasonable acquisition or production costs.

## **3. Are wholesale water, sewer, electricity and other services provided by a local agency subject to Proposition 26?**

Because wholesale service is provided by a variety of different arrangements, it is necessary to evaluate all the circumstances to determine whether the charges for that service are “imposed” within the meaning of Proposition 26. For example, regional sewer service provided by a city, district, or a joint powers agency may be entirely contractual. In that case, the charges for the service may be more akin to a voluntary market arrangement even if the provider sets the charge. The payment obligations may be established as a function of an arm’s-length contract. Therefore, the charge is not “imposed” upon the entity receiving the service, but voluntarily assented to. Similarly, a city may generate electrical power and sell that power on the wholesale market or pursuant to contract to another entity that may have many other sources of power available. Therefore, the price set by the city may be controlled by the relevant market and not “imposed” for purposes of Proposition 26.

In some cases, such sales benefit utility ratepayers. For instance, a water purveyor might have electricity to sell because it operates a reservoir suitable for a hydroelectric generation. Any revenues generated from electricity sales can be used to offset costs of the water utility. Similar circumstances might arise in the sewer context, where revenues from sales of recycled water offset costs of the sewer utility. If Proposition 26 were interpreted to apply to wholesale charges in such contexts, it would have the perverse result of increasing fees and charges, which would be contrary to Proposition 26’s stated intent.

By contrast, if a wholesale service is provided by a local agency organized for that purpose, it is likely that its service charges will be subject to Proposition 26. This is especially the case where

there is reason to believe the agency was formed to fill a service void, has a “natural monopoly” in that the barriers to entry of a competitor are prohibitive (like the cost to establish a second electric utility overlying the territory of an existing provider) or can exercise monopoly power by law (as where competition with the agency is forbidden by legislation).

For example, statute authorizes a metropolitan water district to provide wholesale water to its member public agencies. (West’s Annot. Cal. Wat. C. Append. §§ 109-25, 109-26). The statute requires the district’s board of directors to fix uniform charges for the service. (West’s Annot. Cal. Wat. C. Append. §§ 109-133, 109-134.) The district has adopted policies discouraging duplicate service within its territory. (Metro. Wat. Dist. of So. Cal. Admin. C. § 4202; see Cal. Const. art. XI, § 9 (a).) *Cf.* Public Utilities Code § 1503-1505 (public utility which parallels facilities or private utility is liable for taking). Under these circumstances it is likely that charges for wholesale water service are imposed by the district and, therefore, subject to the Proposition 26 because the charge is for a service that is statutory purpose of the agency and the agency is the sole provider of the service both de facto and by virtue of anti-paralleling laws.

### **C. Fees for Utility Services Generally**

#### **1. May general fund transfers from gas and electric utilities be maintained after the effective date of Proposition 26?**

Proposition 218 prevents local government providers of water, sewer and refuse collection services from transferring the proceeds of rates for those services to the local government’s general fund without demonstrating that doing so is justified by costs borne by the general fund that are associated with the utility operation. *Howard Jarvis Taxpayers Ass’n v. City of Fresno* (2005) 1267 Cal.App.4th 914 (charter-authorized payment in lieu of taxes by water, sewer and trash utilities violated Prop. 218 unless cost justified); *Howard Jarvis Taxpayers Ass’n v. City of Roseville* (2002) 97 Cal.App.3d 637 (franchise fee charged to water, sewer and trash utilities violated Prop. 218 unless cost justified). That measure also exempted fees for gas and electric services. Article XIID, § 3(b). Proposition 26 has no similar exception.

Accordingly, gas and electric service fees imposed by public utilities constitute taxes under Proposition 26 unless they:

- Are imposed pursuant to legislation which predates its adoption; or
- Comply with one of its exceptions, such as the exception of § 1(e)(2) for “[a] charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.”

Arguably, transferring funds from a gas or electric utility to a local government’s general fund without a cost justification to do so is evidence the fees exceed the reasonable cost to provide service and therefore constitute taxes under Proposition 26’s definition of the term. Accordingly,

agencies that benefit from transfers from gas and electric utilities must rely on the fact that Proposition 26 is not retroactive as discussed above or demonstrate that those transfers are justified by costs borne by the general fund for the benefit of the utility. These issues are being litigated as this Guide is written in *Citizens for Fair REU Rates, et al. v. City of Redding, et al.*, Shasta Superior Court Case No. 11-0171377. The City demurred to the complaint, arguing:

- Its payment in lieu of taxes (PILOT) from its electric utility to its general fund predated Proposition 26 and was unaffected by it;
- Proposition 26 is an unconstitutional revision of the California Constitution under *Raven v. Deukmejian* (1990) 52 Cal.3d 336 (Prop. 115 was unconstitutional revision because it fundamentally altered the power of the state judiciary) because it fundamentally alters the power of local government to fund services and regulatory programs and thus cannot be enacted by initiative under art. XVIII, § 2 (amendment or revision by Legislature or Convention), § 3 (amendment by initiative); and
- The city’s electric rates are not “imposed” so as to bring them within the reach of Proposition 26 because off-the-grid and non-electricity sources of power are available in the city; such that the city’s electric customers are not compelled to purchase that service from the city.

The city’s demurrer remains pending as this Guide went to print. Local governments interested in this issue should follow the *Redding* case, which may be appealed to the Third District Court of Appeal regardless of how the trial court decides it.

In addition to the arguments raised in the *Redding* litigation, some local agencies may be in a position to argue that their general fund transfers are valid because they approved by the voters. Many city charters contain provisions authorizing transfers to general funds on various theories (in-lieu of property taxes, in-lieu of franchises, return on investment, profit). Since the charter provision was at some point approved by the voters, the city can argue that the levy complies with Proposition 26 because it received voter approval.

In order to prevail on such an argument, a local government would have to distinguish *Howard Jarvis Taxpayers Ass’n v. City of Fresno* (2005) 127 Cal.App.4th 914 or persuade an appellate court to overrule it. Fresno’s charter specifically authorized its council to set fees in lieu of taxation by ordinance; thus, this provision had been approved by the voters. In rejecting the City’s argument that its in-lieu fee should be upheld as a voter-approved tax, the court focused on two things: First, the court noted that Fresno’s charter specifically prohibited the City from imposing a tax on the consumption of utility service. (*Id.* at p. 926.) Second, the court noted that the payments did not have the characteristics of a tax on utility customers because the payment obligation was imposed on the utilities rather than the individual ratepayers. (*Id.*)

*Fresno’s* analysis may be distinguishable from the circumstances in some cities. First, unlike Fresno’s charter limit on utility user taxes may not appear in other charters. Second, *Fresno* was decided under Proposition 218, which specifically limits the force of legislation predating it by stating, in art. XIII, § 6(d) that “Beginning July 1, 1997, all fees or charges shall comply with this section.” By contrast, Proposition 26 is not retroactive and permits continued

implementation of prior legislation as discussed in part I.E of this Guide above. Third, it is also notable that Proposition 26 defines many levies as taxes that do not otherwise have the characteristics of a tax. Still further, why is a tax collected at wholesale less a tax than one collected at retail? This justification for the *Fresno* decision seems less than persuasive.

## **2. Are fares for municipal bus, trolley, or other transportation services subject to Proposition 26?**

There may be a reasonable argument that bus, trolley, or similar transportation fares are not “imposed” and thus outside the scope of Proposition 26 given there are competing sources of transportation service in the private market, in many jurisdictions, transportation services that meaningfully competes with public transit do not exist. However, these charges are subject to the service exception under § 1(e)(2), which is subject to the reasonable cost-of-service test. Although it might be possible to argue that transit charges are exempt under § 1(e)(4) for charges imposed for entrance to or use of local government property, which is not subject to a cost of service test, it may not be plausible to argue that a transit fee is for entrance to property and it may be difficult to claim that a person is meaningfully “using” property when they have no control over it. These issues may require further clarification by the courts.

## **3. If a Utility Service Charge is Subject to Proposition 26, What Exceptions Apply?**

Utility service charges generally fall within the exception of § 1(e)(2) provided that the charges do not exceed the reasonable cost of providing the service or product. Further, in certain limited circumstances the exception for charges for the purchase, rental, or lease of government property may apply. Lastly, there is the exception for property-related fees imposed in accordance with art. XIID may apply.

Section 1(e)(2) establishes an exception for “A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.” This cost-of-service limitation is likely to be similar in substance to those imposed by the provisions of art. XIID, § 6(b), and reflect common law cost of service principles.

The placement of Proposition 26 in Articles XIII A and XIII C without displacing the other provisions of those articles suggests its terms are to be interpreted in light of those other provisions and the authorities construing them. This is consistent with the rule that legislation is construed consistently with related legislation on the same subject supports this conclusion.<sup>32</sup>.

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<sup>32</sup> *In re Wright's Estate*, (1929) 98 Cal. App. 633, 635, (“[I]t is a settled rule that all statutes which relate to the same general subject-matter – briefly called statutes in *pari materia* – must be read and construed together, as one act, each referring to and supplementing the other, though they were passed at different times.”); see also *Kahn v. Kahn* (1977) 68 Cal.App.3d 372.

Section 1(e)(4) provides an exception for “A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property.” This exception is not subject to a cost-of-service limitation. While agencies could justify utility charges using cost-of-service principles, the agency may choose to demonstrate that the charges are not imposed and, therefore, Proposition 26 does not apply at all. Further, although electricity and water are technically property (*Terrace Water Co. v. San Antonio Light & Power Co.* (1905) 1 Cal.App. 511, 513), it is unlikely this exception will apply except in very limited contexts such as the sale of surplus water where the selling agency does not also provide for transmission of that water. In most instances, a local agency provides a utility service that includes all aspects of the production, transportation, and distribution of the commodity to the customer. Because of the rule of statutory construction that narrowly construes exceptions to a general rule, courts are not likely to give an expansive construction of § (e)(4)’s exception that would reach the provision of utility services. (*City of National City v. Fritz* (1949) 33 Cal.2d 635, 636.)

There must be some distinction, reasonably related to the purposes of Proposition 26 to protect fee payors from “hidden taxes” between a service charge limited to cost by § 1(e)(2) and an unlimited fee for the use of government property under § 1(e)(4). Two criteria characterize this distinction: the extent to which market forces can be expected to prevent excessive fees and the degree of control the government has over the use of property, with more government control indicating provision of a service is provided and less indicating a use of property. This is the common-sense distinction between a cab ride – a service in which a passenger is a passive recipient of a service and a car rental, as to which the renter has complete freedom to make use of the car during the term of the rental agreement. These ideas of pricing power and a common understanding of the distinction between receiving a service and renting property should assist courts in distinguishing between services fees limited to cost by § 1(e)(2) and charges for the purchase, rental, or lease of property limited only by market forces under § 1(e)(4).

Section 1(e)(7) provides an exception for “property-related fees imposed in accordance with the provisions of Art. XIII D.” However, the utility service charges discussed in this section are generally not subject to the substantive and procedural requirements of Proposition 218. Thus, this exception merely bolsters the conclusion that other charges imposed by a local government are taxes unless they can be found to fit within another exception.

***D. What impact does Proposition 26 have on fees for booking City and Special District arrestees into County Jails?***

A county may impose a fee upon a city, special district, school district, community college district, college, or university for reimbursement of county expenses incurred with respect to the booking or other processing of persons arrested by an employee of the entity paying the fee. Gov. Code § 29550. The fee imposed by a county may not exceed the actual administrative costs incurred in booking or otherwise processing arrested persons.<sup>33</sup>

Booking fees may be exempt from Proposition 26 under § 1(e)(2) because they are imposed for a “specific government service” (booking or other processing of persons who have been arrested) and they may not exceed the actual administrative costs incurred in booking or otherwise processing arrested persons. However, booking fees might not fall into the exception since they are charges for a service that is in fact provided to those not charged. For example, the State Highway Patrol is not charged to book or otherwise process persons arrested by the State Highway Patrol.

Before concluding that a booking fee is a “tax” under Proposition 26, consideration should be given to the following:

- What incidence is there, if any, of CHP bookings into county jails?
- Are there agencies other than the CHP that are not charged a booking fee but book arrested persons into the county jail? For example, does a warden of the State Fish and Game Department with the power to arrest book persons into the county jail?
- Does government immunity prevent imposing a fee on the state (CHP or Fish and Game Department) thereby negating the exception for providing a service for those not charged?

Even if a persuasive argument can be made that booking fees are not excluded from Proposition 26’s definition of tax, Proposition 26 is not retroactive and counties may therefore maintain booking fees in place under local legislation that existed prior to November 3, 2010.

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<sup>33</sup> As of this Guide’s publication, the County Counsels’ Association took the position that “booking fees” are not covered by Proposition 26 because the measure does not apply to fees imposed upon another local government agency. The authors of this Guide note that broad language of the introductory phrase of Art. XIII C, § 1, subd. (e): “As used in this article, ‘tax’ means **any** levy, charge, or exaction **of any kind** imposed by a local government ...” (Emphasis added.)

## IV. Exception No. 3: Section 1(e)(3)'s Exception for Permitting and Inspection Fees

Article XIII C § 1(e)(3) excludes from the new definition of “tax”:

A charge imposed for the reasonable regulatory costs to a local government for<sup>34</sup> issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders,<sup>35</sup> and the administrative enforcement and adjudication thereof.<sup>36</sup>

This exception will cover a wide range of local government regulatory fees such as building permit fees, fire inspection fees, assessments to recover the cost of weed abatement services provided to property the owners of which failed to comply with a weed abatement requirement, alarm permit fees, sales tax audit fees and the like. The list of permitted “reasonable regulatory costs” is a closed list (it does not say “including” or “such as”) and includes (i) issuing permits and licenses; (ii) performing investigations and audits; and (iii) administrative enforcement and adjudication. Like the first two exceptions, fees protected by this exception are limited to the local government’s reasonable costs.

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<sup>34</sup> The version of this exception applicable to the State uses the phrase “incident to” rather than “for.” *Compare* art. XIII A, § 3(b)(3) *with* Art. XIII C, § 1(e)(3). As with the differences between the State and local versions of the first two exceptions discussed at pages 10 and 11 above, the courts may have need to find meaning in this difference. On one hand, it could be that “for” requires a closer relationship between an expense and the regulatory activities that follow (issuing and enforcing permits) than does “incident to.” On the other hand, courts might be persuaded that this is a mere drafting error and that no substantive difference was intended, notwithstanding the slightly different language.

<sup>35</sup> The inclusion of “agricultural marketing orders” in the local government provision of Proposition 26 appears to be in error, as those programs are operated by the state. Marketing Orders and Marketing Agreements are authorized by the California Marketing Act of 1937 (Division 21 of the California Food and Agricultural Code). Thus, its presence in the local government section, which the law assumes was intentional, will create interpretive puzzles in applying this exception.

<sup>36</sup> It is not entirely clear what “thereof” modifies, but the legislative history of Proposition 26 suggests it should be read expansively to allow enforcement and adjudication of all of the other regulatory activities listed here – licensing, inspections, etc., an interpretation which is supported by ballot materials as discussed in the subsection A below.

***A. Do the “reasonable regulatory costs” protected by Section 1(e)(3) include rule making?***

Under Proposition 26, a fee can be used to pay for rule making for a regulatory program.

Section 1(e)(3)’s exception covers the range of activities that an agency would perform in order to regulate a business or activity. The enactment of regulations or rules is a necessary aspect of these activities. “[A]dministrative enforcement and adjudication thereof” implies the existence of rules to be applied or adjudicated.

Moreover, the ballot arguments in favor of Proposition 26 make it clear that the proposition was not intended to bar the use of fees to create regulations. The argument states:

“PROPOSITION 26 PROTECTS ENVIRONMENTAL AND CONSUMER REGULATIONS AND FEES

Don’t be misled by opponents of Proposition 26. California has some of the strongest environmental and consumer protection laws in the country. Proposition 26 preserves those laws and PROTECTS LEGITIMATE FEES SUCH AS THOSE TO . . . FUND NECESSARY CONSUMER REGULATIONS.”

This supports a conclusion that Proposition 26 was not intended to prohibit the use of a fee to fund regulatory rulemaking.

This conclusion is also consistent with the “Findings and Declarations of Purpose” in the uncodified § 1 of Proposition 26, which explains that the purpose of Proposition 26 is to prohibit fees that “are not part of any licensing or permitting program.” (§ 1(e).) The proponents of Proposition 26 were trying to prohibit fees that are imposed on an industry and used to fund a program addressing conditions caused by that industry – such as levying a fee on paint manufacturers to pay for lead testing in children – but are not used to actually regulate that industry. This prohibition would not apply to the preparation of regulations that would be applied to that industry.

***B. What implications does Section 1(e)(3) have for regulatory fees to protect the environment, public health, and quality of life?***

Section 1(e)(3) provides that a fee is not a tax if it is imposed for the reasonable regulatory costs of the local agency. By definition, reasonable regulatory costs are solely limited to recovering the costs of “issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.”

Because the history of this measure involves the proponents' dissatisfaction with *Sinclair Paint Co. v. State Board of Equalization*,<sup>37</sup> and because the ballot arguments described above support "legitimate fees such as those to...fund necessary consumer regulations," the breadth of this exception will most likely be determined by the courts. In the meantime, it may be helpful to review the difference between the Court of Appeal and Supreme Court opinions in *Sinclair*. The Court of Appeal opinion stated:

"[T]here is nothing on the face of the [Childhood Lead Poisoning Prevention] Act to show the fees collected are used to regulate Sinclair...The Act does not require Sinclair to comply with any other conditions; it merely requires Sinclair to pay what the Department determines to be its share of the program cost."

The Supreme Court viewed it differently. Just because the fee was not part of the "regulatory program" did not mean that the state could not require the mitigation of Sinclair's impacts on childhood health. A local agency, therefore, should ask the following questions when determining whether its fee comes within this exception:

- Is the fee payor regulated?
- If so, what is the regulatory program?
- Does the program involve the issuance of a license or permit or authorize or require an investigation, inspection or audit? .

The following hypothetical regulatory fees are provided to demonstrate the types of regulatory fees that may be implicated by § 1(e)(3):

- A city imposes a business license fee on businesses that sell alcoholic beverages. The fee funds a program to address public nuisances associated with those sales that do not arise on or adjacent to the site of the beverage sales. Such a fee does not reflect a direct connection between the fee payer and the program that the fee funds.
- A city establishes regulations requiring businesses that operate surface parking lots to comply with best management practices to prevent storm water run-off. The city imposes an annual inspection fee on such businesses to ensure compliance with the regulations and to mitigate the adverse impacts of uncontained storm water runoff on groundwater. A portion of the fee is used to fund a storm water pollution education program in local schools.
- A city adopts a fee to be imposed on all persons who use grocery store carryout plastic and paper bags. The fee is imposed to mitigate the adverse impact that the fee payer's use of such materials has on the district's landfill.<sup>38</sup>

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<sup>37</sup> See discussion of case at in Part I.B. of this Guide above.

<sup>38</sup> If such a fee were restructured as a minimum price for bags to be charged and retained by the retailer, Proposition 26 may not apply because there is nothing in the legislative history of the

In each of these instances, pursuant to § 1(e)(3) at least some portion of the fee could be deemed to be a tax because it is imposed to recover costs other than the reasonable regulatory costs to the local agency for issuing licenses and permits, performing investigations, inspections, and audits, and the administrative enforcement of the regulations. Moreover, in each instance, because the local fee would be imposed for a specific purpose, it would be deemed to be a special tax requiring a  $\frac{2}{3}$ voter approval under art. XIII, § 2(d).

One example of a regulatory fee within the exception of § 1(e)(3), but which is designed to enforce a regulation established to mitigate the adverse impacts of a regulated activity on a community follows:

- All restaurants and other food establishments must obtain a license from the county to operate their businesses. The county prohibits restaurants and other food establishments from using Styrofoam® products in the distribution and sale of food products. The purpose of the regulation is to mitigate the adverse impacts that Styrofoam has on the county's landfill. The county imposes a fee on all restaurants and other food establishments for the reasonable costs of issuing the license, performing investigations, and inspections and enforcement of the regulation.

In this instance, the purpose of the regulation is to mitigate the adverse impact of the fee payor's operations on the community. The fee, however, is only used for those purposes authorized pursuant to § 1(e)(3) – to recover the reasonable costs to the local agency for issuing permits, performing investigations, inspections, and audits, and the administrative enforcement of the regulations. The regulatory fee in this hypothetical would not be deemed to be a tax within the meaning of § 1(e)(3) for these reasons.

To fully understand the scope of the new definition of “tax” added by Proposition 26, the courts may need to reconcile the “Findings and Declaration of Purpose” with the proponents’ ballot arguments in which they state:

- Proposition 26 protects environmental and consumer regulations and fees...
- Proposition 26...protects legitimate fees as those to clean up environmental or ocean damage...
- Proposition 26...won't eliminate or phase out any of California's environmental or consumer protection laws including Oil Spill Prevention and Response Act; Hazardous Substance Control Laws; California Clean Air Act; and California Water Quality Control Act.

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measure to suggest it was aimed at economic legislation that adjusts economic relationships between private parties, as opposed to revenue measures that fund government activity.

Ballot arguments are of course an extrinsic aid courts consider to determine the intent of voters in adopting an initiative. (*Calif. for Political Reform Foundation v. Fair Political Practices Comm'n* (1998) 61 Cal.App.4th 472.)

## **V. Exception No. 4: Section 1(e)(4)'s Exception for Use of Government Property**

Section 1(e)(4) excludes from the new definition of “tax:”

A charge imposed for entrance to or **use of local government property**, or the purchase, rental, or lease of local government property. (Emphasis added.)

Notably, this exception does not include the “reasonable costs” limitation found in the first three exceptions. Nor is this exception limited to real property. If a local government makes personal property available for purchase or rental, it can charge whatever the market will bear. Among the fees that will be protected by this exception are:

- Franchise fees for which rights to use rights-of-way or other government property are provided, like cable, gas, electric, and pipeline franchises;
- Park and recreation entrance fees and equipment rental fees (but not fees for park and recreation services, like classes, which are discussed above in Part III.A regarding § 1(e)(2)); and
- Leases of government property such as museum operated by a non-profit organization). It might be used to defend trench cut fees and protect such fees from the cost-recovery limit of the first three exceptions discussed above.

### ***A. How does this exception affect franchise fees?***

The court in *Howard Jarvis Taxpayers Ass'n v. City of Roseville* (2002) 97 Cal.App.4th 637 noted that “private utilities pay public authorities franchise fees to use government land such as streets, or for rights-of-way to provide utility services.” This characterization supports the exception found in Section 1(e)(4) for fees imposed for “entrance to or use of local government property.” The court specifically stated that Roseville was free to impose franchise fees on private utilities on the basis of contractual negotiation rather than costs.

Similarly, the court in *Santa Barbara County Taxpayer Ass'n v. Board of Supervisors* (1989) 209 Cal.App.3d 940<sup>39</sup> described a “franchise agreement” as granted by a governmental agency to

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<sup>39</sup> The case considered whether franchise fees are “proceeds of taxes” for purposes of the Gann Appropriation limit or Article XIII B.

enable an entity to provide vital public services with some degree of permanence and stability. A “franchise” is:

- A grant of a possessory interest in public real property, similar to an easement” and
- “A negotiated contract between a private enterprise and a governmental entity for the long term possession of land.”<sup>40</sup>

A “franchise fee” is:

- “paid as compensation for the grant of a right of way, not for a license or tax nor for a regulatory program of supervision or inspection;” or
- Paid for the governmental grant of a relatively long possessory right to use land, similar to an easement or a leasehold, to provide essential services to the general public.<sup>41</sup>

Accordingly, fees collected pursuant to a contractual agreement with a private entity that utilizes local government right-of-way or other real property are exempt from Proposition 26 either:

- Because they are imposed by the state; or
- They are imposed locally for “entrance to or use of local government property” (Art. XIIC, § 1(e)(4)).

Franchise fees in the first category – i.e., fees are not imposed by the state rather than a local agency – include cable television franchise fees, oil and gas pipeline franchise fees, and telephone and electricity franchise fees. Franchise fees in the second category – i.e., fees imposed by a local agency, but exempt from Proposition 26 under the exception for “entrance to or use of local government property” – include solid waste franchise fees, and towing franchise fees.

## 1. Cable television franchises

Since 2008, cable television franchises have been regulated under state law (Public Utility Code 5800 et seq.), known as the Digital Infrastructure and Video Competition Act of 2006 (“DIVCA”) Cable television is also regulated by federal law.<sup>42</sup> Several provisions of the state law are worthy of note:

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<sup>40</sup> 209 Cal.App.3d at 949.

<sup>41</sup> *Id.*

<sup>42</sup> The Communications Act of 1934 (47 U.S.C. §151 et seq., (1934)), as amended by the Cable Communications Policy Act of 1984 (P.L.98-549, 98<sup>th</sup> Cong., 2d Sess. (1984)); 47 U.S.C. §521 et seq., as further amended by the Cable Television Consumer and Protection Act of 1992 (P.L.102-385, 102<sup>nd</sup> Cong., 2d Sess. (1992)); and the Telecommunications Act of 1996 (104 P.L. 104, 104<sup>th</sup> Cong., 2<sup>d</sup> Sess. (1996)).

- *Definition of “franchise:”* “an initial authorization, or renewal of an authorization ... whether the authorization is designated as a franchise, permit, license, resolution, contract, certificate, agreement or otherwise, **that authorizes the construction and operation of any network in the right-of-way** capable of providing video service to subscribers.” (emphasis added) (PUC § 5830(f)).
- *Characterization of franchise fee:* The state law adopts a “state franchise fee” payable as “rent or a toll for the use of the public rights-of-way by holders of the state franchise...” (PUC § 5840(q)(1)).
- *Requirement to pay franchise fee:* The state law requires the holder of a state franchise to pay to the local entity a “state franchise fee” (PUC §§ 5860(a); 5840(q)).

Under Proposition 26, franchise fees paid to local entities for cable television franchises pursuant to DIVCA<sup>43</sup> are not local “taxes” for the purposes of Proposition 26 because the fees are imposed by the state not by local government.

## 2. Oil and gas pipeline franchises

There are two types of oil and gas pipelines that might be subject to franchise agreements: public utility and nonpublic utility pipelines.

- *Public utility pipelines:* Public Utility Code § 6231.5(a)(3) establishes the amount of the fee that an applicant to build and operate a pipeline system transmitting oil or products thereof pays to the local government entity. The statute utilizes “franchise” interchangeably with “permit, license, or other privilege.” An annual inflationary adjustment is included (§ 6231.5(b)).
- *Nonpublic utility pipeline:* The franchise fee is the amount “agreed to” with the applicant (§ 6231.5(e)).

Under Proposition 26 the authors of this Guide conclude that franchise fees collected for public utility pipelines are imposed by the state, not the local government entity, and therefore are not local “taxes” within the meaning of Proposition 26 even though the local government has discretion in the grant or denial of a franchise – once the franchise is granted, the fee is determined by state, not local, law. Franchise fees collected for nonpublic utility pipelines are not “imposed” by local governments because they are, by definition, “agreed to” by the local government and the applicant. This reasoning, of course, will not apply to franchise fees authorized by charter city legislation independently of state law. Such fees will require justification under the “use of property” exception of art. XIIC, § 1(e)(4) or another exception from Proposition 26’s definition of “tax.”

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<sup>43</sup> Franchise fees imposed under a local franchising ordinance are analytically distinct from those imposed under DIVCA and should be analyzed as are other local franchise fees as discussed in the balance of this section.

### 3. Telephone and electricity franchises

Two statutory schemes control this area:

- *Broughton Act* (PUC § 6001): State statute limits franchise fee to 2% of the value of the goods transmitted via the franchised facility and interchangeably refers to “franchise” or “**privilege**” to erect or lay telegraph or telephone wires, construct or operate railroads, or lay gas pipes for the purpose of carrying gas for light, heat, or power, etc. (Emphasis added.) Section 6006 describes the franchise fee as arising from the “use, operation or possession of the franchise.”
- *1937 Act* (PUC § 6231): State statute limits franchise fee to 2% of the value of the goods transmitted via the franchised facility.

The franchise fees for these purposes are not “imposed” by local governments but rather by state statute and therefore do not appear to be affected by Proposition 26.<sup>44</sup>

### 4. Solid waste franchises

Solid waste services are provided by some local governments through a contract or “franchise” with a solid waste hauler:

- *City contract*: “A city may contract for the collection or disposal of garbage, waste, refuse...under the **terms and conditions** that are prescribed by the legislative body” (emphasis added) (Public Resources § 49300).
- *County franchise*: County authority to franchise or “permit” solid waste services (Public Resources 49200). A bidder for such a franchise or permit may set forth any terms and conditions that the bidder may desire to offer (§ 49204).
- *Franchise, contract, license, or permit*: A local agency may provide for exclusive solid waste handling services by franchise, contract, license, permit or otherwise (Public Resources Code § 49501).

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<sup>44</sup> Note that this statutory scheme, wherein the State imposes a tax that is directly payable to a local government entity would require  $\frac{2}{3}$  vote of the Legislature (in the future) under Proposition 26 because it would “result in any taxpayer paying a higher tax.” Art. XIII A, § 3(a). This, of course, assumes the measure is a tax and not a fee justified by one or another of Proposition 26’s exceptions such as those for fees imposed on uses of government property. Art. XIII A, § 3(b)(4); art. XIII C, § 1(e)(4). Note that the latter exception is for fees for use of local government property imposed by local government. State imposition of a fee for use of local government property might not be within this exception unless viewed as a statute authorizing a local action to impose the fee.

The statutory context does not provide direction on the application of Proposition 26 to solid waste “franchises” except to the extent that (1) a city franchise is referred to as a “contract;” and (2) a county franchise is an acknowledged arms-length negotiation. Neither appears to “impose” a fee. Further discussion of these distinctions appears in this section, below.

## **5. Removal of abandoned vehicles – towing franchises**

Removal of abandoned vehicles is often accomplished through a franchise or contract entered into under the authority Vehicle Code § 22671. The statutory context does not provide direction on the application of Proposition 26 to towing franchises/contracts. If the towing contractor agrees to a franchise fee under such a contract or franchise as a result of an arms-length negotiation, then an argument can be made that either the fee is not a “tax” because it is a charge for entrance to government property; or it is not “imposed.”

### ***B. How does this exception affect fees on cable franchisees to fund public, educational and government access channels on cable systems (“PEG fees”)?***

In 2006, the Legislature enacted the Digital Infrastructure and Video Competition Act of 2006 (“DIVCA”), which usurped local authority to issue and renew video services franchises. In addition to the state franchise fee, DIVCA provides that a local agency “may, by ordinance, establish a fee to support PEG [public, educational, and governmental access] channel facilities consistent with federal law that would become effective” after the expiration of any fee arising from a cable franchise that existed prior to the enactment of DIVCA. (See Pub. Util. Code, § 5870(n).) The amount of this fee is limited to 1% of the franchisee’s gross revenues. (*Id.*) The PEG fee ordinance expires, and must be reauthorized, once a state franchise expires. (*Id.*)

Although there is some uncertainty, the authors of this Guide believe that PEG fees are covered by the use-of-property exception. Federal law specifically provides that capital costs that a franchise agreement requires to be incurred by a cable operator are not franchise fees. However, since that definition is only for the purposes of the 5% cap on franchise fees, and since the basis for local regulation of cable franchisees has always been the provider’s use of rights of way, nothing in federal law prevents local agencies from arguing that PEG fees are imposed for the use of local government property. While DIVCA does not refer directly to the fact that the ability to impose this fee arises from the fact that the franchisee is using the rights of way, viewed from a historical and practical perspective, the use of the right of way is the basis for imposing such a fee. For these reasons, a strong case can be made that PEG fees are covered by the use-of-property exception. And, thus, such PEG fee ordinances can be adopted, renewed, and increased without voter approval, notwithstanding Proposition 26.

***C. How does this exception affect AB 939 fees to fund local government regulatory programs associated with solid waste?***

Public Resources Code § 41901 authorizes cities and counties to impose fees to recover the costs of preparing, adopting and maintaining county-wide integrated waste management plans. Public Resources Code § 41902 provides that a local agency may:

“[D]irectly collect the fees authorized by [§ 41901] or may, by agreement, arrange for the fees to be collected by a solid waste hauler providing solid waste collection for the city or county.”

Pursuant to this and other authority, many local jurisdictions generate revenue from solid waste customers to fund regulatory programs aimed at dealing with or reducing the impact of solid waste generation. The mechanisms used to generate such revenue take many forms and are often dependent on the language of applicable franchise agreements.

No matter the mechanism, such fees that were in existence as of November 3, 2010 will not be subject to the requirements of Proposition 26 because it is not retroactive, as discussed in Part I.F above. Thus, only AB 939 fees that are newly adopted or increased within the meaning of Gov. Code § 53750(h) after November 3, 2010 are subject to Proposition 26’s requirements.

In some cases, a local agency requires a franchisee (a hauler) to pay the AB 939 fee, rather than requiring the franchisee to collect the fee from its customers and remit its proceeds to the local agency. In those cases, the authors of this Guide conclude the AB 939 fee should be evaluated as are other franchise fees. (See discussion in Part V.A above.)

In other cases, the AB 939 fees are imposed by the local agency directly on solid waste customers (see discussion of Public Utilities Code §§ 41901 and 41902 above) and collected either by the local agency or the hauler. Such fees will have to come within one of Proposition 26’s seven stated exceptions. AB 939 fees are regulatory in nature, but if imposed directly on consumers, are not associated with the issuance of any permit and thus are “not part of any licensing or permitting program.” Art. XIIC, § 1, subd. (e)(3). Such fees would also not seem to meet the requirement of the benefit or privilege exception and the service or product exception that the benefit, privilege, exception, or product be conferred, granted, or provided directly to the fee payor because government is not providing the service. Art. XIIC, § 1, subs. (e)(1), (e)(2).

***D. How does this exception effect fees imposed on those who cut trenches in public rights-of-way?***

In recent years, cities and counties began to require those excavating in public streets to pay trench cut fees. Research disclosed that trenching in public streets shortens the life of street paving. Most trench-cut fees are styled as “regulatory fees.” They are based on the concept that the activity of the excavator imposes costs on the street’s owner that should be borne by the excavator and not by the street owner.

Trench cut fees are typically imposed when utilities and others propose trenching or excavation in the right-of-way. The amount of the fee is typically based on studies that indicate that trenching decreases the useful life of streets. Thus, the amount of the trench cut fee decreases as the end of the useful life of the street approaches.

Several lawsuits have successfully challenged the application of trench cut fee ordinances to utilities with existing franchises. The courts have accepted the basic premise of these lawsuits that the ordinances impair existing contracts – utility franchises – in violation of the Contracts Clause of the United States Constitution. These cases effectively eviscerated most trench cut fee ordinances, since they mean that public utilities, which are the primary “trenchers,” are not subject to the fee.

In response to these cases, some cities and counties have continued to impose trench cut fees upon those not protected by a franchise agreement. Other cities, such as San Francisco, have repealed their trench cut fee programs and created more stringent standards for restoration of the public right-of-way following excavations.

For those local agencies that desire to increase a trench cut fee, or desire to adopt one, Proposition 26 must be analyzed. Three of the exceptions would seem to exempt trench cut fees from the voter approval requirement. First, trench cut fees could fit within the narrow version of regulatory fees that is permitted by Proposition 26, since the fees are associated with the issuance of a permit and a regulatory program. (Art. XIII C §§ 1(e)(3).)

Second, the property exception of § 1(e)(4) should apply since the fees are imposed when public property is used. Third, since most trenching is associated with development and is charged in conjunction with the issuance of a permit that authorizes development, the development exception of § 1(e)(6), discussed in Part VII. below could apply as well. None of these three exceptions contains the “not provided to those not charged” language that is found in the privilege and benefit exception of § 1(e)(1) and the service or product exception of § 1(e)(2); therefore, the fact that many utilities will not be charged the fee does not make the exceptions inapplicable.

***E. How does this exception affect tolls imposed for use of toll roadways?***

Three exceptions to Proposition 26's definition of tax may be applicable to road tolls:

- § 1(e)(1) – Fees or charges for a specific benefit conferred or privilege granted;
- § 1(e)(2) – Fees or charges for a service or product provided; or
- § 1(e)(4) – Fees or charges for entrance to or use of local government property, or the purchase, rental, or lease of local government property.

Arguably, tolls imposed by a city are fees imposed for a specific benefit conferred (*i.e.*, the benefit of enhanced driving time and traveling in less congested lanes), privilege granted (*i.e.*, the privilege of traveling on the toll road or in high occupancy toll (HOT) lanes), or government service or product provided (*i.e.*, transit services in toll roads and HOT lanes). Assuming the tolls fall within the first two exceptions, they will be deemed to be a tax if:

- The same benefit is conferred, privilege is granted, or service or product is also provided to others who are not charged for such benefit, privilege, or service or product; and
- The fee or charge exceeds the reasonable costs of providing the benefit, privilege, or service or product.

As to the first test, drivers cannot travel on toll roads or in HOT lanes without paying a toll. While these non-paying travelers may be incidentally benefited by those who pay the toll and thereby reduce congestion on the road or highway, they are not conferred the same benefit, granted the same privilege, or provided the same service or product as those who pay the toll. Consequently, the tolls meet the first prong of this fee analysis.

As to the second test, the tolls may not exceed the reasonable cost to a city of conferring the benefit, granting the privilege, or providing the service or product if they are to be justified under the first two exceptions noted above. To the extent that toll revenues are used to expand other travel options or to make capacity or operational improvements designed to reduce congestion or improve the flow of traffic on other roadways or highways, the tolls may be subject to challenge if justified under the first two exceptions. Using revenues from the tolls for these purposes arguably would result in the tolls:

- Exceeding the reasonable cost of conferring the benefit, granting the privilege, or providing the service or product; and
- Being used to fund transit services and facilities that benefit those who do not use the toll road or HOT lanes and do not pay the tolls. In such an instance, the tolls would be deemed to be taxes within the meaning of art. XIIC, § 1(e)(1) or § 1(e)(2).

Also, the Public Utilities Code provides in some instances that a local agency operating a toll road may establish varying rates for tolls imposed to use toll roads and HOT lanes. The rates

may vary according to the levels of congestion anticipated or experienced (“congestion pricing”) or the occupancy of the vehicle. In order to impose such varying rates, however, a city operating a toll road or HOT Lane must be able to demonstrate that there is a higher cost associated with conferring the benefit, granting the privilege, or providing the service or product due to higher levels of congestion or lower vehicle occupancy.<sup>45</sup>

Also, art. XIIC, § 1(e)(4) provides that a fee imposed for entrance to or use of local government property is not a tax. Unlike the fees identified in § 1(e)(1) and § 1(e)(2), there are no other limitations on the amount that a local government may impose for these purposes.

Whether a local government enters into a lease or franchise with Caltrans for the operation of a toll road or HOT lanes, in both instances the local agency will have a property interest in that portion of the road or highway subject to the lease or franchise. Any toll imposed by the city for entrance to or use of the toll road or HOT lanes therefore would fall within the exception provided in art. XIIC, § 1(e)(4) – a charge imposed for entrance to or use of local government property.

Accordingly, unless a government operating a toll road wishes to justify its tolls based on its costs, it will need to rely on the exception of § 1(e)(4).

## **VI. Exception No. 5: Section 1(e)(5)’s Exception for Fines & Penalties**

Section 1(e)(5) excludes from the definition of “tax:”

“A **fine, penalty**, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law.” (Emphasis added.)

The power to enact laws is granted to the Legislature pursuant to art. IV, § 1. The Legislature may make no law except by statute. Art. IV, § 8(b). Cities are vested with the power to make and enforce within their limits local, police, sanitary and other ordinances and regulations not in conflict with the general laws of the state. Art. XI, § 7. “An ordinance in its primary and usual sense means a local law. It prescribes a rule of conduct prospective in operation, applicable generally to persons and things subject to the jurisdiction of the city. ‘Resolution’ denotes something less formal. It is the mere expression of the opinion of the legislative body concerning some administrative matter for the disposition of which it provides ...” *Central Mfg. Dist., Inc. v. Bd. of Supervisors*, (1960) 176 Cal.App.2d 850, 860. A duly enacted local ordinance has the same binding force within its corporate limits as a statute passed by the

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<sup>45</sup> The courts have recognized that in some instances it is appropriate to impose a higher rate for a service in order to manage available resources. See *Brydon v. East Bay Mun. Util. Dist.*, (1994) 24 Cal.App.4th 178, 193 (inclining block water rate structure reasonably allocates costs based on the premise that the more unreasonable the use, “the greater the regulatory job of the district,” and is not a special tax).

Legislature has throughout the state. See *Empire Fire & Marine Ins. Co. v. Bell*, (1997) 55 Cal.App.4th 1410, 1419, 1422; *Evola v. Wendt Construction Co.*, (1959) 170 Cal.App.2d 21, 24. Consequently, for purposes of § 1(e)(5), a violation of law plainly includes a violation of a city ordinance.

The authors of this Guide read “violation of law” broadly to include city ordinances, regulations and policies (like library policies for the timely return of books) and not just state statutes or city ordinances. “Law” generally has a broad and encompassing meaning and the framers of this measure could easily have used narrower terms like “legislation,” “ordinance,” and “regulation.” Such more specific terms are used elsewhere in art. XIIC.<sup>46</sup> Thus, this exception will include parking fines, administrative penalties imposed in the code enforcement context, late payment fees, interest charges, and any “other monetary charge imposed by” the city “as a result of a violation of law,” defining the last term broadly. A question arises regarding nuisance abatement assessments *i.e.*, use of the property tax roll to recover a local government’s cost to abate a nuisance on private property. These are not in the nature of fines for a violation of law, but rather cost recovery for a service. Accordingly, they are probably better justified under §1(e)(2), discussed in Part III above, and limited to the reasonable cost to the local government of providing and administering the abatement services.

Helpful guidance as to what constitutes a “penalty” appears in a recent decision of the Third District Court of Appeal concluding that a penalty for understating corporate income taxes is not a “tax” within the meaning of Proposition 13. *California Taxpayer’s Association v. Franchise Tax Board* (2010) 190 Cal.App.4th 1139, 1148 (distinguishing penalty from tax, the court noted that “there is one important distinction between a penalty and a tax: while a tax raises revenue if it is obeyed, a penalty raises revenue only if some legal obligation is disobeyed.”).

## VII. Exception No. 6: Section 1(e)(6)’s Exception for Fees Imposed as a Condition of Property Development

Section 1(e)(6) excludes from the new definition of “tax”:

A charge imposed as a **condition of property development**. (Emphasis added.)

This language is, in substance, the same as the comparable exception from Proposition 218’s provisions governing assessments and property-related fees. Art. XIID, § 1(b), enacted by Proposition 218, excludes “the imposition of fees or charges as a condition of property development” from the sweep of arts. XIIC and XIII D. This broad language encompasses more than development impact fees under the Mitigation Fee Act, Gov. Code §§ 66000 et seq. (“A.B. 1600”) and extends to any fee or charge imposed “as a condition of property development,” including permit and inspection fees, and fees to recover the cost of advance

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<sup>46</sup> For example, art. XIIC, § 1(c) defines “special district” as “an agency of the state, formed pursuant to general law or a special act” and art. XIIC, § 3 refers to “the Legislature nor any local government charter.”

planning services such as a building permit surcharge to recover the cost of general and specific plans applicable to the project for which the building permit issues.

Of course, an ample body of constitutional law above and beyond the Mitigation Fee Act limits the power of government to exact money and property from those who wish to develop private property. *E.g.*, *Nollan v. California Coastal Commission* (1987) 483 U.S. 825 (there must be a “logical nexus” between the impacts of development and the use of land or money exacted from the developer to mitigate those impacts); *Dolan v. City of Tigard* (1994) 512 U.S. 374 (an exaction must be at least roughly proportionate in amount to impacts of the development of the land from which the exaction is made). For a fuller discussion of that topic, consult CEB, *The California Municipal Law Handbook* (2010), §10.391 et seq. In general, most fees currently imposed by local planning and building departments will be exempt from Proposition 26 under this sixth exception or under one or more of the first three exceptions discussed in Parts II to IV above.

## **VIII. Exception No. 7: Section 1(e)(7)’s Exception for Assessments and Property Related Fees Subject to Proposition 218**

The last enumerated exception, § 1(e)(7) excludes from the new definition of “tax:”

Assessments and property-related fees imposed in accordance with the provisions of art. XIID.

This will include assessments on the property tax roll. The exception would also cover such property-related fees as retail fees for water, sewer, and trash services and other property tax roll fees. This would include property-related fees imposed by some local governments for flood control and water quality programs such as was considered in *Greene v. Marin County Flood Control and Conservation District* (2010) 49 Cal.4th 277.

### ***A. Are Assessments Exempted from Proposition 218 by Article XIID, Section 5 Also Exempt from Proposition 26?***

A number of cities formed assessment districts pursuant to the Landscaping and Lighting District Act of 1972 (Streets and Highways Code §§ 22500, et seq.) prior to 1996 when the voters approved Proposition 218, which added Arts. XIIC and XIID to California Constitution. Art. XIID sets forth substantive and procedural requirements applicable to assessments, including the requirements to separate special benefit from general benefit, to assess publicly owned property, and to conduct mailed ballot proceedings. Art. XIID provides that beginning July 1, 1997; all existing, new, or increased assessments must comply with such substantive and procedural requirements with certain exceptions. As provided in § 5 of art. XIID, one exception is for an assessment existing on the effective date of art. XIID imposed exclusively to finance the capital costs or maintenance and operation expenses for sidewalks and streets (i.e., street landscaping and lighting assessments). The exception provides that subsequent increases in such

assessments will be subject to the procedures and approval process set forth in art. XIID. In reliance on this exception, cities that have not increased their landscaping and lighting assessments since 1996 have continued to annually levy the assessments without complying with art. XIID. See *Howard Jarvis Taxpayers Ass'n v. City of Riverside* (1999) 73 Cal.App.4th 679.

1972 Act assessments must be levied annually pursuant to a resolution of the local agency adopted after a noticed public hearing (Streets and Highways Code § 22620, *et seq.*). The definition of “tax” in Proposition 26 includes levies “imposed” by a local government after November 3, 2010, except levies that fall within an enumerated exception. For grandfathered-1972 Act assessments that are levied again for fiscal year 2011-12 and subsequent years, the annual levy may mean that such assessments are “imposed” for purposes of Proposition 26. In such case, the assessments would be a “tax” requiring a  $\frac{2}{3}$  vote of the general electorate unless the assessments fit within an exception to Proposition 26.

Art. XIIC § 1(e)(7) provides an exception for “assessments ...imposed in accordance with the provisions of Art. XIID.” The question is whether grandfathered assessments that are exempt from, and therefore have not complied with, the procedural and substantive requirements of § 4 of art. XIID, are levied in accordance with the provisions of art. XIID. Proposition 26 does not specify that the § 1(e)(7) exception is only available for assessments imposed in accordance with the procedural and substantive requirements set forth in § 4 of art. XIID. Therefore, such assessments imposed in accordance with the exception set forth in § 5 of art. XIID appear to be imposed in accordance with the provisions of art. XIID.

This interpretation is consistent with the intent of the voters in enacting Proposition 26. In *City of Riverside* the court determined that Proposition 218 was enacted to close a loophole in Proposition 13, whereby local governments abused special assessments by imposing assessments for general governmental services. The court concluded that the exception in § 5 of art. XIID was intended to carve out traditionally appropriate, non-abusive, special assessments and that special assessments for street lighting are by no means an abuse or a loophole. The Findings and Declarations of Purpose section of Proposition 26 indicates that the purpose of Proposition 26 is to address the “recent phenomenon whereby ... local governments have disguised new taxes as ‘fees’ in order to extract even more revenue from California taxpayers without having to abide by [Proposition 13’s and Proposition 218’s] constitutional voting requirements.” Since grandfathered-1972 Act assessments are not new, and since, under Proposition 218, they cannot be increased without a mailed ballot proceeding, the purpose of Proposition 26 does seem to be advanced by eliminating the exception in § 5 of art. XIID for grandfathered,-1972 Act assessments. Therefore, grandfathered-1972 Act assessments likely fall within the exception to Proposition 26 set forth in § 1(e)(7).

## IX. What is the Effect of Section 1(e)'s Trailing Paragraph Regarding Burden of Proof?

The final, unnumbered paragraph of Article XIIC, § 1(e) states:

“The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is not more than necessary to cover the reasonable costs of governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from the governmental activity.”

At the outset, the authors of this Guide note that the language of this paragraph is confusing, and its interaction with the seven exceptions presents an interpretative challenge. Further, we note that the phrase “levy, charge, or other exaction” does not distinguish among those terms. This is so for the reasons stated in Part I.E. regarding the use of this same phrase in the introductory language of art. XIIC, § 1(e).

First, in litigation, a local government will bear the burden to justify its fees. While this is a change in the law, it may not be much of a change in how courts actually review such cases-- government has some duty to justify its revenue measures. *E.g. Beaumont Investors, LLC v. Beaumont-Cherry Valley Water District* (1985) 165 Cal.App.3d 227 (water district bore burden to produce a record on which to justify connection charge); *Home Builders Assn. of Tulare/Kings Counties, Inc. v. City of Lemoore* (2010) 185 Cal.App.4th 554, 560-563 (discussing burden of production and persuasion in challenge to development impact fee). Second, the lowest standard of evidence is required – a mere preponderance of evidence, as opposed to such higher standards as proof by “clear and convincing evidence” or “beyond a reasonable doubt.”

It is less clear is how the multi-part test included in this paragraph interacts with the exceptions which that precede it. This final, unnumbered paragraph states that the local government bears the burden of proving:

- (1) that a levy is not a tax;
- (2) that the amount is not more than necessary to cover the reasonable costs of the governmental activity; and
- (3) that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from the governmental activity. The language raises the following questions:

- Proposition 26 states that “any levy, charge, or exaction of any kind” is a “tax” unless it is covered by one of seven exceptions. Three of the seven exceptions require that the levy, charge, or exaction be based upon “reasonable costs to the local government.” Four of the seven exceptions do not include any “reasonable cost” limitation. The burden of proof paragraph states that a local government must prove that the amount of a fee is not more than

necessary to cover the “reasonable costs of the governmental activity.” What, if anything, does this language add to the language of the exceptions? More specifically, does the language add a “reasonable costs” limitation to the exceptions that don’t include that limitation?

- The burden of proof language requires the local government to prove that the manner in which those costs are allocated bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from the governmental activity. None of the exceptions contains this limitation. Does this mean that this standard must be applied to each of the exceptions? Can a local government choose whether to prove that the cost allocation is either fair or reasonable? Can a local government choose whether to prove that the cost allocation bears a fair or reasonable relationship either to the payor’s burdens on, or the payor’s benefits from the governmental activity?

These questions cannot be resolved definitely without the benefit of published appellate court decisions. The authors of this Guide have identified the following alternative interpretations:

1. The burden of proof paragraph is a restatement of the law found in *Beaumont Investors v. Beaumont Cherry Valley Water District*.<sup>47</sup> In that case, the District imposed a facilities fee payable upon application for connection to its water system. The fee was challenged as a special tax. The Court of Appeal held that the fee was a special tax, finding that the District had not met its burden of proving that the facilities fee does or does not “exceed the reasonable cost” of constructing the water system improvements contemplated by the District. The Court explained that such a showing would require, at the minimum, evidence of:
  - (1) The estimated construction costs of the proposed water system improvements; and
  - (2) The District’s basis for determining the amount of the fee allocated to plaintiff, *i.e.*, the manner in which defendant apportioned the contemplated construction costs among the new users, such that the charge allocated to plaintiff bore a fair or reasonable relation to plaintiff’s burden on, and benefits from, the system.<sup>48</sup>

The language from *Beaumont Investors* is almost identical to the language in the trailing paragraph of art. XIIC, § 1(e) regarding the burden of proof. Therefore, it can be argued that the drafters of intended to codify the holding of this case and to restate a requirement of law rather than to create a new one.

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<sup>47</sup> (1985) 165 Cal.App.3d 227.

<sup>48</sup> *Id.* at p. 235, citing *County of Fresno v. Malmstrom* (1979) 94 Cal.App.3d 974, 983-985. A recent decision characterizes *Beaumont Investors* as standing for the proposition that a government agency defending a challenge to a fee bears the burden to produce a record (as opposed to the burden of persuasion) on which to base judicial review of that fee. *Homebuilders Association of Tulare / King Counties, Inc. v. City of Lemoore* (2010) 185 Cal.App.4th 554, 562-63.

2. Alternatively, the tests in the next paragraph can be understood to establish sequential tests for a fee. Under this construction, a local agency must first prove that a charge is not a tax. It can do that by showing that the charge fits within one of the exceptions that does not contain a reasonable cost limitation. If the local agency cannot justify a levy within one of those exceptions, then it must fit it within an exception that contains a cost limitation. In that case, it must meet the second test of the next paragraph that the amount is not more than necessary to cover the reasonable costs of the governmental activity. Under both cases, the local government must demonstrate that the cost allocation bears a fair or reasonable relationship to the fee payor's burdens on or benefits received.
  
3. The multi-part test also can be understood to apply only to the exceptions that themselves include similar qualifications. As a matter of statutory construction, using words in one part of a law but leaving them out of another part is generally treated as having significance under the doctrine of *expressio unius est exclusio alterius*.<sup>49</sup> In this case, inclusion in some exceptions of a requirement that fees not exceed costs, coupled with the exclusion of that requirement from some other exceptions, suggests the requirement does not apply to those exceptions from which it was omitted. Additionally, the rules of statutory construction require every word in a statute or constitutional provision to be given meaning. If the trailing paragraph of art. XIIC, § 1, subd. (e) imports a cost limitation on the seven exceptions, what meaning is left to the cost limitation language in the first three exceptions? Does it not become surplusage, violating this rule of construction?

Regardless, the last phrase introduces a concept from *Sinclair Paint* and the cases citing it – allocation of costs in proportion to a fee payor's benefits or burdens from government activity – that is not easily applied to many fees since Proposition 26 converts to taxes many fees to which that standard previously applied.<sup>50</sup>

Therefore, to avoid characterizing a revenue measure as a tax requiring voter approval, local government must justify it as falling within one of the exceptions to Proposition 26's definition of tax. Each of these exceptions has its own requirements:

- some limit a fee to cost (§ 1(e)((1) - (3));
- one requires that the fee be justified by a benefit (§ 1(e)(1));
- others impose no cost or benefit limit at all (§ 1(e)(4) and (5));
- one is limited to cost by other principles of law (*e.g.*, Mitigation Fee Act) (§ 1(e)(6)); and

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<sup>49</sup> *E.g.*, *Arden Carmichael, Inc. v. County of Sacramento* (2001) 93 Cal.App.4th 507, review denied (February 13, 2002)

<sup>50</sup> *Sinclair Paint* cites this phrase, relying on *Beaumont Investors v. Beaumont-Cherry Valley Water District, supra*. Note that the standard may remain relevant when applied to non-property-based assessments such as those authorized by the Parking and Business Improvement Area Law of 1989, Streets & Highways Code 36500-36551, and *Evans v. City of San Jose* (1992) 3 Cal.App.4th 728.

- one limits assessments and property-related fees under Proposition 218 (§ 1(e)(7)).
4. Finally, it is possible to read the paragraph as imposing only a general “reasonableness” standard on those exceptions that do not otherwise include the “reasonable costs” limitation. For example, Section 1(e)(4) is the exception for a “charge imposed for entrance to or use of local government property.” The exception does not require that the charge not exceed the “reasonable costs to the local government of providing entrance to or use of local government property.” But the burden of proof paragraph requires the local government to demonstrate that the costs of allowing public use of local government property are “reasonable,” not arbitrary, and that the manner in which those costs are allocated bear either a fair or reasonable relationship to the payor’s burdens on, or benefits received from entrance to local government property. If so, this standard harkens back to pre-Proposition 13 law under which judicial review of legislative action to set rates was limited to a relatively deferential review to ensure rates were “reasonable.” E.g., *Elliott v. City of Pacific Grove* (1975)54 Cal.App.3d 53, 59.

On balance, the authors of this Guide conclude that the inclusion of the cost-of-service limit in the first three exceptions, and its exclusion from the final four exceptions, must be given some meaning under the *expressio unius* rule, and the rule against interpretations that render a part of a statute or constitutional provision surplusage. Further we conclude a duty to demonstrate the reasonableness of fees exists without respect to the requirements of Proposition 26 under the older, common law of rate-setting. Whether and how Proposition 26 changes that obligation remains to be determined by the courts.

## X. Conclusion

Proposition 26 includes many, broad exceptions and will therefore not require fundamental change in most of the fee-based revenues that flow to California’s local governments. But by providing a clear definition of the term “tax” – and a closed list of exceptions from that definition – it promises to significantly alter the legal analysis applied to various local government revenue sources. Many local fees will now plainly be subject to cost limitations, and there is plainly a need to prove that fees are covered by the exceptions of art. XIIC, § 1(e)(1) through (4). Thus, the process of adopting and justifying local government fees is now more demanding.

This Guide, of course, is written in the months immediately following the voters’ adoption of Proposition 26 and draws on the text of the measure, the ballot materials presented to the voters, and the body of law of which it was consciously made a part. Subsequent court interpretations will assist in future analysis. Accordingly, this area of the law, like all others, can be expected to develop over time and use of this Guide must be informed by subsequent legal developments.

## **XI. Attachments**

- A. Text of Proposition 26
- B. Proposition 26 Ballot materials
- C. Text of Articles XIIC and XIID with Proposition 26 Codified Therein

# Attachment A

(b) The Governor and the Governor-elect may require a state agency, officer or employee to furnish whatever information is deemed necessary to prepare the budget.

(c) (1) The budget shall be accompanied by a budget bill itemizing recommended expenditures.

(2) The budget bill shall be introduced immediately in each house by the persons chairing the committees that consider the budget.

(3) The Legislature shall pass the budget bill by midnight on June 15 of each year.

(4) Until the budget bill has been enacted, the Legislature shall not send to the Governor for consideration any bill appropriating funds for expenditure during the fiscal year for which the budget bill is to be enacted, except emergency bills recommended by the Governor or appropriations for the salaries and expenses of the Legislature.

(d) No bill except the budget bill may contain more than one item of appropriation, and that for one certain, expressed purpose. Appropriations from the General Fund of the State, except appropriations for the public schools; *and appropriations in the budget bill and in other bills providing for appropriations related to the budget bill*, are void unless passed in each house by rollcall vote entered in the journal, two-thirds of the membership concurring.

(e) (1) *Notwithstanding any other provision of law or of this Constitution, the budget bill and other bills providing for appropriations related to the budget bill may be passed in each house by rollcall vote entered in the journal, a majority of the membership concurring, to take effect immediately upon being signed by the Governor or upon a date specified in the legislation. Nothing in this subdivision shall affect the vote requirement for appropriations for the public schools contained in subdivision (d) of this section and in subdivision (b) of Section 8 of this article.*

(2) *For purposes of this section, "other bills providing for appropriations related to the budget bill" shall consist only of bills identified as related to the budget in the budget bill passed by the Legislature.*

(e) (f) The Legislature may control the submission, approval, and enforcement of budgets and the filing of claims for all state agencies.

(f) (g) For the 2004–05 fiscal year, or any subsequent fiscal year, the Legislature may not send to the Governor for consideration, nor may the Governor sign into law, a budget bill that would appropriate from the General Fund, for that fiscal year, a total amount that, when combined with all appropriations from the General Fund for that fiscal year made as of the date of the budget bill's passage, and the amount of any General Fund moneys transferred to the Budget Stabilization Account for that fiscal year pursuant to Section 20 of Article XVI, exceeds General Fund revenues for that fiscal year estimated as of the date of the budget bill's passage. That estimate of General Fund revenues shall be set forth in the budget bill passed by the Legislature.

(h) *Notwithstanding any other provision of law or of this Constitution, including subdivision (c) of this section, Section 4 of this article, and Sections 4 and 8 of Article III, in any year in which the budget bill is not passed by the Legislature by midnight on June 15, there shall be no appropriation from the current budget or future budget to pay any salary or reimbursement for travel or living expenses for Members of the Legislature during any regular or special session for the period from midnight on June 15 until the day that the budget bill is presented to the Governor. No salary or reimbursement for travel or living expenses forfeited pursuant to this subdivision shall be paid retroactively.*

SEC. 5. Severability.

If any of the provisions of this measure or the applicability of any provision of this measure to any person or circumstances shall be found to be unconstitutional or otherwise invalid, such finding shall not affect the remaining provisions or applications of this measure to other persons or circumstances, and to that extent the provisions of this measure are deemed to be severable.

## PROPOSITION 26

This initiative measure is submitted to the people in accordance with the provisions of Section 8 of Article II of the California Constitution.

This initiative measure amends sections of the California Constitution; therefore, existing provisions proposed to be deleted are printed in ~~strikeout type~~ and new provisions proposed to be added are printed in *italic type* to indicate that they are new.

### PROPOSED LAW

SECTION 1. Findings and Declarations of Purpose.

The people of the State of California find and declare that:

(a) Since the people overwhelmingly approved Proposition 13 in 1978, the Constitution of the State of California has required that increases in state taxes be adopted by not less than two-thirds of the members elected to each house of the Legislature.

(b) Since the enactment of Proposition 218 in 1996, the Constitution of the State of California has required that increases in local taxes be approved by the voters.

(c) Despite these limitations, California taxes have continued to escalate. Rates for state personal income taxes, state and local sales and use taxes, and a myriad of state and local business taxes are at all-time highs. Californians are taxed at one of the highest levels of any state in the nation.

(d) Recently, the Legislature added another \$12 billion in new taxes to be paid by drivers, shoppers, and anyone who earns an income.

(e) This escalation in taxation does not account for the recent phenomenon whereby the Legislature and local governments have disguised new taxes as "fees" in order to extract even more revenue from California taxpayers without having to abide by these constitutional voting requirements. Fees couched as "regulatory" but which exceed the reasonable costs of actual regulation or are simply imposed to raise revenue for a new program and are not part of any licensing or permitting program are actually taxes and should be subject to the limitations applicable to the imposition of taxes.

(f) In order to ensure the effectiveness of these constitutional limitations, this measure also defines a "tax" for state and local purposes so that neither the Legislature nor local governments can circumvent these restrictions on increasing taxes by simply defining new or expanded taxes as "fees."

SECTION 2. Section 3 of Article XIII A of the California Constitution is amended to read:

SEC. 3. (a) ~~From and after the effective date of this article, any changes in state taxes enacted for the purpose of increasing revenues collected pursuant thereto Any change in state statute which results in any taxpayer paying a higher tax whether by increased rates or changes in methods of computation must be imposed by an Act act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature, except that no new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property may be imposed.~~

(b) As used in this section, “tax” means any levy, charge, or exaction of any kind imposed by the State, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of conferring the benefit or granting the privilege to the payor.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of providing the service or product to the payor.

(3) A charge imposed for the reasonable regulatory costs to the State incident to issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of state property, or the purchase, rental, or lease of state property, except charges governed by Section 15 of Article XI.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or the State, as a result of a violation of law.

(c) Any tax adopted after January 1, 2010, but prior to the effective date of this act, that was not adopted in compliance with the requirements of this section is void 12 months after the effective date of this act unless the tax is reenacted by the Legislature and signed into law by the Governor in compliance with the requirements of this section.

(d) The State bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the governmental activity.

SECTION 3. Section 1 of Article XIII C of the California Constitution is amended to read:

SECTION 1. Definitions. As used in this article:

(a) “General tax” means any tax imposed for general governmental purposes.

(b) “Local government” means any county, city, city and county, including a charter city or county, any special district, or any other local or regional governmental entity.

(c) “Special district” means an agency of the State, formed pursuant to general law or a special act, for the local performance of governmental or proprietary functions with limited geographic boundaries including, but not limited to, school districts and redevelopment agencies.

(d) “Special tax” means any tax imposed for specific purposes, including a tax imposed for specific purposes, which is placed into a general fund.

(e) As used in this article, “tax” means any levy, charge, or exaction of any kind imposed by a local government, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.

(3) A charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law.

(6) A charge imposed as a condition of property development.

(7) Assessments and property-related fees imposed in accordance with the provisions of Article XIII D.

The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the governmental activity.

SECTION 4. Conflicting Measures.

In the event that this measure and another measure or measures relating to the legislative or local votes required to enact taxes or fees shall appear on the same statewide election ballot, the provisions of the other measure or measures shall be deemed to be in conflict with this measure. In the event that this measure shall receive a greater number of affirmative votes, the provisions of this measure shall prevail in their entirety, and the provisions of the other measure or measures relating to the legislative or local votes required to enact taxes or fees shall be null and void.

SECTION 5. Severability.

If any provision of this act, or any part thereof, is for any reason held to be invalid or unconstitutional, the remaining provisions shall not be affected, but shall remain in full force and effect, and to this end the provisions of this act are severable.

## PROPOSITION 27

This initiative measure is submitted to the people in accordance with the provisions of Section 8 of Article II of the California Constitution.

This initiative measure amends the California Constitution and repeals sections of the Government Code; therefore, existing provisions proposed to be deleted are printed in ~~strikeout type~~ and new provisions proposed to be added are printed in *italic type* to indicate that they are new.

### PROPOSED LAW

SECTION 1. Title.

This Act shall be known and may be cited as the “Financial Accountability in Redistricting Act” or “FAIR Act.”

SECTION 2. Findings and Purpose.

The people of the State of California hereby make the following findings and declare their purpose in enacting the FAIR Act is as follows:

(a) Our political leadership has failed us. California is facing an unprecedented economic crisis and we, the people (not the politicians), need to prioritize how we spend our limited funds. We are going broke. Spending unlimited millions of dollars to create multiple new bureaucracies just to decide a political game of Musical Chairs is a waste—pure and simple. Under current law, a group of unelected commissioners, making up to \$1 million a year

# Attachment B

PROPOSITION  
**26**

**REQUIRES THAT CERTAIN STATE AND LOCAL FEES BE APPROVED BY TWO-THIRDS VOTE. FEES INCLUDE THOSE THAT ADDRESS ADVERSE IMPACTS ON SOCIETY OR THE ENVIRONMENT CAUSED BY THE FEE-PAYER’S BUSINESS. INITIATIVE CONSTITUTIONAL AMENDMENT.**

OFFICIAL TITLE AND SUMMARY

PREPARED BY THE ATTORNEY GENERAL

**REQUIRES THAT CERTAIN STATE AND LOCAL FEES BE APPROVED BY TWO-THIRDS VOTE. FEES INCLUDE THOSE THAT ADDRESS ADVERSE IMPACTS ON SOCIETY OR THE ENVIRONMENT CAUSED BY THE FEE-PAYER’S BUSINESS. INITIATIVE CONSTITUTIONAL AMENDMENT.**

- Requires that certain state fees be approved by two-thirds vote of Legislature and certain local fees be approved by two-thirds of voters.
- Increases legislative vote requirement to two-thirds for certain tax measures, including those that do not result in a net increase in revenue, currently subject to majority vote.

**Summary of Legislative Analyst’s Estimate of Net State and Local Government Fiscal Impact:**

- Decreased state and local government revenues and spending due to the higher approval requirements for new revenues. The amount of the decrease would depend on future decisions by governing bodies and voters, but over time could total up to billions of dollars annually.
- **Additional state fiscal effects from repealing recent fee and tax laws: (1) increased transportation program spending and increased General Fund costs of \$1 billion annually, and (2) unknown potential decrease in state revenues.**

ANALYSIS BY THE LEGISLATIVE ANALYST

**BACKGROUND**

State and local governments impose a variety of taxes, fees, and charges on individuals and businesses. Taxes—such as income, sales, and property taxes—are typically used to pay for general public services such as education, prisons, health, and social services. Fees and charges, by comparison, typically pay for a particular service or program benefitting individuals or businesses. There are three broad categories of fees and charges:

- User fees—such as state park entrance fees and garbage fees, where the user pays for the cost of a specific service or program.
- Regulatory fees—such as fees on restaurants to pay for health inspections and fees on the purchase of beverage containers to support recycling programs. Regulatory fees pay for programs that place requirements on the activities of businesses or people to achieve particular public goals or help offset the public or environmental impact of certain activities.
- Property charges—such as charges imposed on property developers to improve roads leading to new subdivisions and assessments that pay for improvements and services that benefit the property owner.

Figure 1 Approval Requirements: State and Local Taxes, Fees, and Charges		
	State	Local
<b>Tax</b>	Two-thirds of each house of the Legislature for measures increasing state revenues.	<ul style="list-style-type: none"> <li>• Two-thirds of local voters if the local government specifies how the funds will be used.</li> <li>• Majority of local voters if the local government does not specify how the funds will be used.</li> </ul>
<b>Fee</b>	Majority of each house of the Legislature.	Generally, a majority of the governing body.
<b>Property Charges</b>	Majority of each house of the Legislature.	Generally, a majority of the governing body. Some also require approval by a majority of property owners or two-thirds of local voters.

**ANALYSIS BY THE LEGISLATIVE ANALYST**

**CONTINUED**

State law has different approval requirements regarding taxes, fees, and property charges. As Figure 1 shows, state or local governments usually can create or increase a fee or charge with a majority vote of the governing body (the Legislature, city council, county board of supervisors, etc.). In contrast, increasing tax revenues usually requires approval by two-thirds of each house of the state Legislature (for state proposals) or a vote of the people (for local proposals).

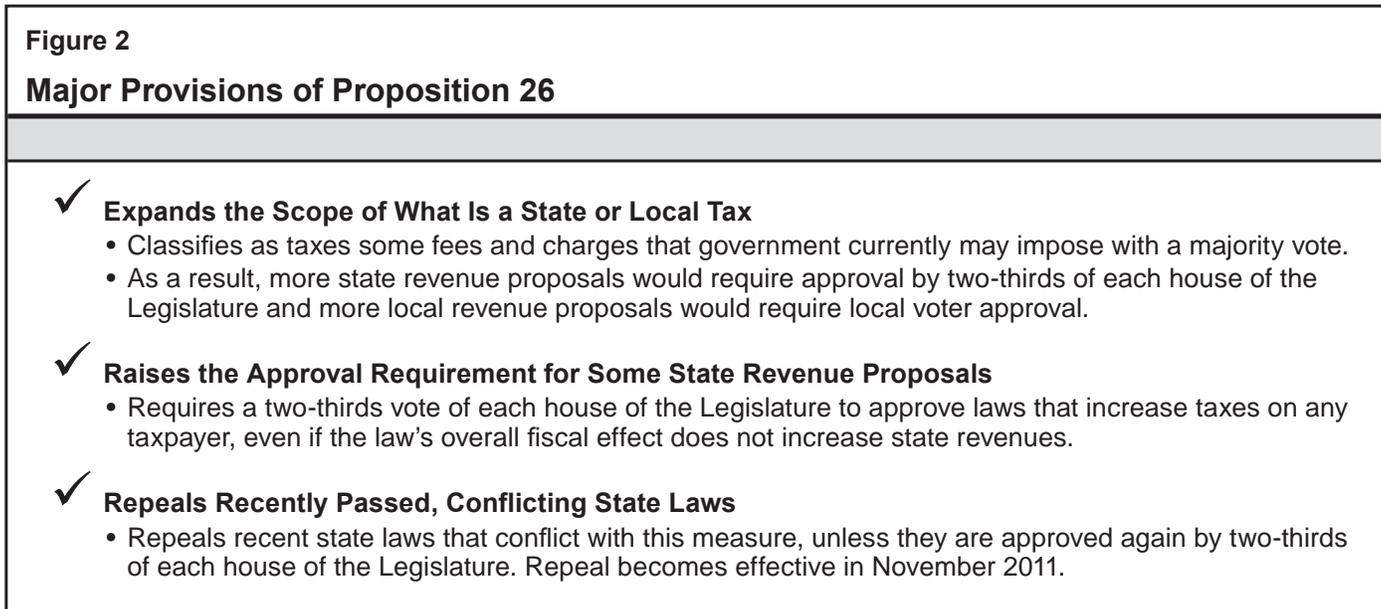
**Disagreements Regarding Regulatory Fees.** Over the years, there has been disagreement regarding the difference between regulatory fees and taxes, particularly when the money is raised to pay for a program of broad public benefit. In 1991, for example, the state began imposing a regulatory fee on businesses that made products containing lead. The state uses this money to screen children at risk for lead poisoning, follow up on their treatment, and identify sources of lead contamination responsible for the poisoning. In court, the Sinclair Paint Company argued that this regulatory fee was a tax

because: (1) the program provides a broad public benefit, not a benefit to the regulated business, and (2) the companies that pay the fee have no duties regarding the lead poisoning program other than payment of the fee.

In 1997, the California Supreme Court ruled that this charge on businesses was a regulatory fee, not a tax. The court said government may impose regulatory fees on companies that make contaminating products in order to help correct adverse health effects related to those products. Consequently, regulatory fees of this type can be created or increased by (1) a majority vote of each house of the Legislature or (2) a majority vote of a local governing body.

**PROPOSAL**

This measure expands the definition of a tax and a tax increase so that more proposals would require approval by two-thirds of the Legislature or by local voters. Figure 2 summarizes its main provisions.



**Definition of a State or Local Tax**

*Expands Definition.* This measure broadens the definition of a state or local tax to include many payments currently considered to be fees or charges. As a result, the measure would have the effect of increasing the number of revenue proposals subject to the higher approval requirements summarized in Figure 1. Generally, the types of fees and charges that would become taxes under the measure are ones that government imposes to address health, environmental, or other societal or economic concerns. Figure 3 provides examples of some regulatory fees that could be considered taxes, in part or in whole, under the measure. This is because these fees pay for many services that benefit the public broadly, rather than providing services directly to the fee payer. The state currently uses these types of regulatory fees to pay for most of its environmental programs.

Certain other fees and charges also could be considered to be taxes under the measure. For example, some business assessments could be considered to be taxes because government uses the assessment revenues to improve shopping districts

(such as providing parking, street lighting, increased security, and marketing), rather than providing a direct and distinct service to the business owner.

*Some Fees and Charges Are Not Affected.* The change in the definition of taxes would not affect most user fees, property development charges, and property assessments. This is because these fees and charges generally comply with Proposition 26's requirements already, or are exempt from its provisions. In addition, most other fees or charges in existence at the time of the November 2, 2010 election would not be affected unless:

- The state or local government later increases or extends the fees or charges. (In this case, the state or local government would have to comply with the approval requirements of Proposition 26.)
- The fees or charges were created or increased by a state law—passed between January 1, 2010 and November 2, 2010—that conflicts with Proposition 26 (discussed further below).

**Approval Requirement for State Tax Measures**

*Current Requirement.* The State Constitution currently specifies that laws enacted “for the purpose

<p><b>Figure 3</b> <b>Regulatory Fees That Benefit the Public Broadly</b></p>
<p><b>Oil Recycling Fee</b> The state imposes a regulatory fee on oil manufacturers and uses the funds for:</p> <ul style="list-style-type: none"> <li>• Public information and education programs.</li> <li>• Payments to local used oil collection programs.</li> <li>• Payment of recycling incentives.</li> <li>• Research and demonstration projects.</li> <li>• Inspections and enforcement of used-oil recycling facilities.</li> </ul>
<p><b>Hazardous Materials Fee</b> The state imposes a regulatory fee on businesses that treat, dispose of, or recycle hazardous waste and uses the funds for:</p> <ul style="list-style-type: none"> <li>• Clean up of toxic waste sites.</li> <li>• Promotion of pollution prevention.</li> <li>• Evaluation of waste source reduction plans.</li> <li>• Certification of new environmental technologies.</li> </ul>
<p><b>Fees on Alcohol Retailers</b> Some cities impose a fee on alcohol retailers and use the funds for:</p> <ul style="list-style-type: none"> <li>• Code and law enforcement.</li> <li>• Merchant education to reduce public nuisance problems associated with alcohol (such as violations of alcohol laws, violence, loitering, drug dealing, public drinking, and graffiti).</li> </ul>

of increasing revenues” must be approved by two-thirds of each house of the Legislature. Under current practice, a law that increases the amount of taxes charged to some taxpayers but offers an equal (or larger) reduction in taxes for other taxpayers has been viewed as not increasing revenues. As such, it can be approved by a majority vote of the Legislature.

**New Approval Requirement.** The measure specifies that state laws that result in *any* taxpayer paying a higher tax must be approved by two-thirds of each house of the Legislature.

### State Laws in Conflict With Proposition 26

**Repeal Requirement.** Any state law adopted between January 1, 2010 and November 2, 2010 that conflicts with Proposition 26 would be repealed one year after the proposition is approved. This repeal would not take place, however, if two-thirds of each house of the Legislature passed the law again.

**Recent Fuel Tax Law Changes.** In the spring of 2010, the state increased fuel taxes paid by gasoline suppliers, but decreased other fuel taxes paid by gasoline retailers. Overall, these changes do not raise more state tax revenues, but they give the state greater spending flexibility over their use.

Using this flexibility, the state shifted about \$1 billion of annual transportation bond costs from the state’s General Fund to its fuel tax funds. (The General Fund is the state’s main funding source for schools, universities, prisons, health, and social services programs.) This action decreases the amount of money available for transportation programs, but helps the state balance its General Fund budget. Because the Legislature approved this tax change with a majority vote in each house, this law would be repealed in November 2011—unless the Legislature approved the tax again with a two-thirds vote in each house.

**Other Laws.** At the time this analysis was prepared (early in the summer of 2010), the Legislature and Governor were considering many new laws and funding changes to address the state’s major budget difficulties. In addition, parts of this measure would be subject to future interpretation by the courts. As a result, we cannot determine the full range of state laws that could be affected or repealed by the measure.

### FISCAL EFFECTS

**Approval Requirement Changes.** By expanding the scope of what is considered a tax, the measure would make it more difficult for state and local governments to pass new laws that raise revenues. This change would affect many environmental, health, and other regulatory fees (similar to the ones in Figure 3), as well as some business assessments and other levies. New laws to create—or extend—these types of fees and charges would be subject to the higher approval requirements for taxes.

The fiscal effect of this change would depend on future actions by the Legislature, local governing boards, and local voters. If the increased voting requirements resulted in some proposals not being approved, government revenues would be lower than otherwise would have occurred. This, in turn, likely would result in comparable decreases in state spending.

Given the range of fees and charges that would be subject to the higher approval threshold for taxes, the fiscal effect of this change could be major. Over time, we estimate that it could reduce government revenues and spending statewide by up to billions of dollars annually compared with what otherwise would have occurred.

**Repeal of Conflicting Laws.** Repealing conflicting state laws could have a variety of fiscal effects. For example, repealing the recent fuel tax laws would increase state General Fund costs by about \$1 billion annually for about two decades and increase funds available for transportation programs by the same amount.

Because this measure could repeal laws passed *after* this analysis was prepared and some of the measure’s provisions would be subject to future interpretation by the courts, we cannot estimate the full fiscal effect of this repeal provision. Given the nature of the proposals the state was considering in 2010, however, it is likely that repealing any adopted proposals would decrease state revenues (or in some cases increase state General Fund costs). Under this proposition, these fiscal effects could be avoided if the Legislature approves the laws again with a two-thirds vote of each house.

**PROP 26** REQUIRES THAT CERTAIN STATE AND LOCAL FEES BE APPROVED BY TWO-THIRDS VOTE. FEES INCLUDE THOSE THAT ADDRESS ADVERSE IMPACTS ON SOCIETY OR THE ENVIRONMENT CAUSED BY THE FEE-PAYER'S BUSINESS. INITIATIVE CONSTITUTIONAL AMENDMENT.

★ ARGUMENT IN FAVOR OF PROPOSITION 26 ★

**YES ON PROPOSITION 26: STOP POLITICIANS FROM ENACTING HIDDEN TAXES**

State and local politicians are using a loophole to impose Hidden Taxes on many products and services by calling them “fees” instead of taxes. Here’s how it works:

At the State Level:

- California’s Constitution requires a two-thirds vote of the Legislature for new or increased taxes, but the politicians use a gimmick to get around this by calling their taxes “fees” so they can pass them with only a *bare majority vote*.

At the Local Level:

- Most tax increases at the local level require voter approval. Local politicians have been calling taxes “fees” so they can bypass voters and raise taxes without voter permission—taking away your right to stop these Hidden Taxes at the ballot.

**PROPOSITION 26 CLOSES THIS LOOPHOLE**

Proposition 26 requires politicians to meet the same vote requirements to pass these Hidden Taxes as they must to raise other taxes, protecting California taxpayers and consumers by requiring these Hidden Taxes to be passed by a two-thirds vote of the Legislature and, at the local level, by public vote.

**PROPOSITION 26 PROTECTS ENVIRONMENTAL AND CONSUMER REGULATIONS AND FEES**

*Don't be misled by opponents of Proposition 26.* California has some of the strongest environmental and consumer protection laws in the country. Proposition 26 preserves those laws and PROTECTS LEGITIMATE FEES SUCH AS THOSE TO CLEAN UP ENVIRONMENTAL OR OCEAN DAMAGE, FUND NECESSARY CONSUMER REGULATIONS, OR PUNISH WRONGDOING, and for licenses for professional certification or driving.

**DON'T LET THE POLITICIANS CIRCUMVENT OUR CONSTITUTION TO TAKE EVEN MORE MONEY FROM US**

Politicians have proposed more than \$10 billion in Hidden Taxes. Here are a few examples of things they could apply Hidden

Taxes to unless we stop them:

- Food
- Cell Phones
- Emergency Services
- Gas
- Electricity
- Insurance
- Toys
- Water
- Beverages
- Entertainment

**PROPOSITION 26: HOLD POLITICIANS ACCOUNTABLE**

“State politicians already raised taxes by \$18 billion. Now, instead of controlling spending to address the budget deficit, they’re using this gimmick to increase taxes even more! It’s time for voters to STOP the politicians by passing Proposition 26.” — Teresa Casazza, California Taxpayers’ Association

Local politicians play tricks on voters by disguising taxes as “fees” so they don’t have to ask voters for approval. They need to control spending, not use loopholes to raise taxes! It’s time to hold them accountable for runaway spending and to stop Hidden Taxes at the local level.

**YES ON PROPOSITION 26: PROTECT CALIFORNIA FAMILIES**

California families and small businesses can’t afford new and higher Hidden Taxes that will kill jobs and hurt families. When government increases Hidden Taxes, consumers and taxpayers pay increased costs on everyday items.

“The best way out of this recession is to grow the economy and create jobs, not increase taxes. Proposition 26 will send a message to politicians that it’s time to clean up wasteful spending in Sacramento.” — John Kabateck, National Federation of Independent Business/California

**VOTE YES ON PROPOSITION 26 TO STOP HIDDEN TAXES—[www.No25Yes26.com](http://www.No25Yes26.com)**

**TERESA CASAZZA**, President  
California Taxpayers’ Association

**ALLAN ZAREMBERG**, President  
California Chamber of Commerce

**JOEL FOX**, President  
Small Business Action Committee

★ REBUTTAL TO ARGUMENT IN FAVOR OF PROPOSITION 26 ★

Do you want corporations to write special protections into California’s Constitution?

Should California protect polluters at the expense of public safety?

That’s what Prop. 26 is: big oil, tobacco, and alcohol companies want taxpayers to pay for cleaning their mess. As a result, local police and fire departments will have fewer resources to keep us safe.

The claim that Prop. 26 won’t harm consumers and the environment is false. Corporations are spending millions misleading voters into thinking that the payments made by companies that pollute or harm public health are “hidden taxes.” The campaign’s own website cited “Oil severance fee to mitigate oil spill clean up, and build larger response and enforcement capabilities” as a hidden tax.

Here are some other fees they don’t want to pay—listed in their own documents:

- Fees on polluters to clean up hazardous waste
- Fees on oil companies for oil spill cleanup
- Fees on tobacco companies for the adverse health effects of tobacco products.

**PROPOSITION 26 IS BAD FOR THE ENVIRONMENT, PUBLIC SAFETY, & TAXPAYERS.**

The California Professional Firefighters, League of Women Voters of California, California Nurses Association, Sierra Club, Planning & Conservation League, Californians Against Waste, and California Tax Reform Association all oppose 26 because it would force ordinary citizens to pay for the damage done by polluters.

Californians can’t afford to clean up polluters’ messes when local governments are cutting essential services like police and fire departments.

**WE NEED TO PROTECT THE PUBLIC, NOT POLLUTERS!  
VOTE NO on 26.**

**RON COTTINGHAM**, President  
Peace Officers Research Association of California

**WARNER CHABOT**, Chief Executive Officer  
California League of Conservation Voters

**PATTY VELEZ**, President  
California Association of Professional Scientists

**PROP 26 REQUIRES THAT CERTAIN STATE AND LOCAL FEES BE APPROVED BY TWO-THIRDS VOTE. FEES INCLUDE THOSE THAT ADDRESS ADVERSE IMPACTS ON SOCIETY OR THE ENVIRONMENT CAUSED BY THE FEE-PAYER'S BUSINESS. INITIATIVE CONSTITUTIONAL AMENDMENT.**

★ **ARGUMENT AGAINST PROPOSITION 26** ★

Should polluters be protected from paying to clean up the damage they do?

Should taxpayers foot the bill instead?

The answer is NO, and that's why voters should reject Proposition 26, the Polluter Protection Act.

Who put Prop. 26 on the ballot? Oil, tobacco, and alcohol companies provided virtually all the funding for this measure, including Chevron, Exxon Mobil, and Phillip Morris.

Their goal: to shift the burden of paying for the damage these companies have done onto the taxpayers.

How does this work? Prop. 26 redefines payments for harm to the environment or public health as tax increases, requiring a 2/3 vote for passage.

Such payments, or pollution fees on public nuisances, would become much harder to enact—leaving taxpayers to foot the bill. California has enough problems without forcing taxpayers to pay for cleaning up after polluting corporations.

Companies that pollute, harm the public health, or create a public nuisance should be required to pay to cover the damage they cause.

But the big oil, tobacco, and alcohol corporations want you, the taxpayer, to pay for cleaning up their messes. That's why these corporations wrote Proposition 26 behind closed doors, with zero public input, and why they put up millions of dollars to get Proposition 26 on the ballot.

Proposition 26 is just another attempt by corporations to protect themselves at the expense of ordinary citizens. The problem isn't taxes "hidden" as fees; it's the oil and tobacco companies hiding their true motives:

- Polluters don't want to pay fees used to clean up hazardous waste.
- Oil companies don't want to pay fees used for cleaning up oil spills and fighting air pollution.
- Tobacco companies don't want to pay fees used for addressing the adverse health effects of tobacco products.

- Alcohol companies don't want to pay fees used for police protection in neighborhoods and programs to prevent underage drinking.

One of the so-called "hidden taxes" identified by the Proposition 26 campaign is a fee that oil companies pay in order to cover the cost of oil spill clean-up, like the one in the Gulf. The oil companies should be responsible for the mess they create, not the taxpayers.

Proposition 26 will harm local public safety and health, by requiring expensive litigation and endless elections in order for local government to provide basic services. Fees on those who do harm should cover such costs as policing public nuisances or repairing damaged roads.

The funds raised by these fees are used by state and local governments for essential programs like fighting air pollution, cleaning up environmental disasters and monitoring hazardous waste. They require corporations such as tobacco companies to pay for the harm they cause.

If Proposition 26 passes, these costs would have to be paid for by the taxpayers.

**DON'T PROTECT POLLUTERS.** Join California Professional Firefighters, California Federation of Teachers, California League of Conservation Voters, California Nurses Association, Consumer Federation of California, and California Alliance for Retired Americans, and vote NO on 26.

[www.stoppolluterprotection.com](http://www.stoppolluterprotection.com)

**JANIS R. HIROHAMA**, President  
League of Women Voters of California

**JANE WARNER**, President  
American Lung Association in California

**BILL MAGAVERN**, Director  
Sierra Club California

★ **REBUTTAL TO ARGUMENT AGAINST PROPOSITION 26** ★

Proposition 26 fixes a loophole that allows politicians to impose new taxes on businesses and consumers by falsely calling them "fees".

Proposition 26 stops politicians from increasing Hidden Taxes on food, water, cell phones and even emergency services—**BILLIONS OF DOLLARS IN HIGHER COSTS THAT CONSUMERS WILL PAY, NOT BIG CORPORATIONS.**

Politicians and special interests oppose Prop. 26 because they want to take more money from working California families by putting "fees" on everything they can think of. Their interest is simple—more taxpayer money for the politicians to waste, including on lavish public pensions.

Here are the facts:

Prop. 26 protects legitimate fees and **WON'T ELIMINATE OR PHASE OUT ANY OF CALIFORNIA'S ENVIRONMENTAL OR CONSUMER PROTECTION LAWS**, including:

- Oil Spill Prevention and Response Act
- Hazardous Substance Control Laws
- California Clean Air Act
- California Water Quality Control Act
- Laws regulating licensing and oversight of Contractors, Attorneys and Doctors

"Proposition 26 doesn't change or undermine a single law protecting our air, ocean, waterways or forests—it simply stops the runaway fees politicians pass to fund ineffective programs."—Ryan Broddrick, former Director, Department of Fish and Game

Here's what Prop. 26 really does:

- **Requires a TWO-THIRDS VOTE OF THE LEGISLATURE FOR PASSING STATEWIDE HIDDEN TAXES** disguised as fees, just like the Constitution requires for regular tax increases.
- **Requires a POPULAR VOTE TO PASS LOCAL HIDDEN TAXES** disguised as fees, just like the Constitution requires for most other local tax increases.

**YES on 26—Stop Hidden Taxes. Preserve our Environmental Protection Laws.**

[www.No25Yes26.com](http://www.No25Yes26.com)

**JOHN DUNLAP**, Former Chairman  
California Air Resources Board

**MANUEL CUNHA, JR.**, President  
Nisei Farmers League

**JULIAN CANETE**, Chairman  
California Hispanic Chamber of Commerce

# Attachment C

CALIFORNIA CONSTITUTION  
ARTICLE 13A [TAX LIMITATION]

SECTION 1. (a) The maximum amount of any ad valorem tax on real property shall not exceed One percent (1%) of the full cash value of such property. The one percent (1%) tax to be collected by the counties and apportioned according to law to the districts within the counties.

(b) The limitation provided for in subdivision (a) shall not apply to ad valorem taxes or special assessments to pay the interest and redemption charges on any of the following:

(1) Indebtedness approved by the voters prior to July 1, 1978.

(2) Bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978, by two-thirds of the votes cast by the voters voting on the proposition.

(3) Bonded indebtedness incurred by a school district, community college district, or county office of education for the construction, reconstruction, rehabilitation, or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities, approved by 55 percent of the voters of the district or county, as appropriate, voting on the proposition on or after the effective date of the measure adding this paragraph. This paragraph shall apply only if the proposition approved by the voters and resulting in the bonded indebtedness includes all of the following accountability requirements:

(A) A requirement that the proceeds from the sale of the bonds be used only for the purposes specified in Article XIII A, Section 1(b) (3), and not for any other purpose, including teacher and administrator salaries and other school operating expenses.

(B) A list of the specific school facilities projects to be funded and certification that the school district board, community college board, or county office of education has evaluated safety, class size reduction, and information technology needs in developing that list.

(C) A requirement that the school district board, community college board, or county office of education conduct an annual, independent performance audit to ensure that the funds have been expended only on the specific projects listed.

(D) A requirement that the school district board, community college board, or county office of education conduct an annual, independent financial audit of the proceeds from the sale of the bonds until all of those proceeds have been expended for the school facilities projects.

(c) Notwithstanding any other provisions of law or of this Constitution, school districts, community college districts, and

county offices of education may levy a 55 percent vote ad valorem tax pursuant to subdivision (b).

SEC. 2. (a) The "full cash value" means the county assessor's valuation of real property as shown on the 1975-76 tax bill under "full cash value" or, thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred after the 1975 assessment. All real property not already assessed up to the 1975-76 full cash value may be reassessed to reflect that valuation. For purposes of this section, "newly constructed" does not include real property that is reconstructed after a disaster, as declared by the Governor, where the fair market value of the real property, as reconstructed, is comparable to its fair market value prior to the disaster. For purposes of this section, the term "newly constructed" does not include that portion of an existing structure that consists of the construction or reconstruction of seismic retrofitting components, as defined by the Legislature.

However, the Legislature may provide that, under appropriate circumstances and pursuant to definitions and procedures established by the Legislature, any person over the age of 55 years who resides in property that is eligible for the homeowner's exemption under subdivision (k) of Section 3 of Article XIII and any implementing legislation may transfer the base year value of the property entitled to exemption, with the adjustments authorized by subdivision (b), to any replacement dwelling of equal or lesser value located within the same county and purchased or newly constructed by that person as his or her principal residence within two years of the sale of the original property. For purposes of this section, "any person over the age of 55 years" includes a married couple one member of which is over the age of 55 years. For purposes of this section, "replacement dwelling" means a building, structure, or other shelter constituting a place of abode, whether real property or personal property, and any land on which it may be situated. For purposes of this section, a two-dwelling unit shall be considered as two separate single-family dwellings. This paragraph shall apply to any replacement dwelling that was purchased or newly constructed on or after November 5, 1986.

In addition, the Legislature may authorize each county board of supervisors, after consultation with the local affected agencies within the county's boundaries, to adopt an ordinance making the provisions of this subdivision relating to transfer of base year value also applicable to situations in which the replacement dwellings are located in that county and the original properties are located in another county within this State. For purposes of this

paragraph, "local affected agency" means any city, special district, school district, or community college district that receives an annual property tax revenue allocation. This paragraph applies to any replacement dwelling that was purchased or newly constructed on or after the date the county adopted the provisions of this subdivision relating to transfer of base year value, but does not apply to any replacement dwelling that was purchased or newly constructed before November 9, 1988.

The Legislature may extend the provisions of this subdivision relating to the transfer of base year values from original properties to replacement dwellings of homeowners over the age of 55 years to severely disabled homeowners, but only with respect to those replacement dwellings purchased or newly constructed on or after the effective date of this paragraph.

(b) The full cash value base may reflect from year to year the inflationary rate not to exceed 2 percent for any given year or reduction as shown in the consumer price index or comparable data for the area under taxing jurisdiction, or may be reduced to reflect substantial damage, destruction, or other factors causing a decline in value.

(c) For purposes of subdivision (a), the Legislature may provide that the term "newly constructed" does not include any of the following:

(1) The construction or addition of any active solar energy system.

(2) The construction or installation of any fire sprinkler system, other fire extinguishing system, fire detection system, or fire-related egress improvement, as defined by the Legislature, that is constructed or installed after the effective date of this paragraph.

(3) The construction, installation, or modification on or after the effective date of this paragraph of any portion or structural component of a single- or multiple-family dwelling that is eligible for the homeowner's exemption if the construction, installation, or modification is for the purpose of making the dwelling more accessible to a severely disabled person.

(4) The construction, installation, removal, or modification on or after the effective date of this paragraph of any portion or structural component of an existing building or structure if the construction, installation, removal, or modification is for the purpose of making the building more accessible to, or more usable by, a disabled person.

(d) For purposes of this section, the term "change in ownership" does not include the acquisition of real property as a replacement for comparable property if the person acquiring the real property has been displaced from the property replaced by eminent domain

proceedings, by acquisition by a public entity, or governmental action that has resulted in a judgment of inverse condemnation. The real property acquired shall be deemed comparable to the property replaced if it is similar in size, utility, and function, or if it conforms to state regulations defined by the Legislature governing the relocation of persons displaced by governmental actions. This subdivision applies to any property acquired after March 1, 1975, but affects only those assessments of that property that occur after the provisions of this subdivision take effect.

(e) (1) Notwithstanding any other provision of this section, the Legislature shall provide that the base year value of property that is substantially damaged or destroyed by a disaster, as declared by the Governor, may be transferred to comparable property within the same county that is acquired or newly constructed as a replacement for the substantially damaged or destroyed property.

(2) Except as provided in paragraph (3), this subdivision applies to any comparable replacement property acquired or newly constructed on or after July 1, 1985, and to the determination of base year values for the 1985-86 fiscal year and fiscal years thereafter.

(3) In addition to the transfer of base year value of property within the same county that is permitted by paragraph (1), the Legislature may authorize each county board of supervisors to adopt, after consultation with affected local agencies within the county, an ordinance allowing the transfer of the base year value of property that is located within another county in the State and is substantially damaged or destroyed by a disaster, as declared by the Governor, to comparable replacement property of equal or lesser value that is located within the adopting county and is acquired or newly constructed within three years of the substantial damage or destruction of the original property as a replacement for that property. The scope and amount of the benefit provided to a property owner by the transfer of base year value of property pursuant to this paragraph shall not exceed the scope and amount of the benefit provided to a property owner by the transfer of base year value of property pursuant to subdivision (a). For purposes of this paragraph, "affected local agency" means any city, special district, school district, or community college district that receives an annual allocation of ad valorem property tax revenues. This paragraph applies to any comparable replacement property that is acquired or newly constructed as a replacement for property substantially damaged or destroyed by a disaster, as declared by the Governor, occurring on or after October 20, 1991, and to the determination of base year values for the 1991-92 fiscal year and fiscal years thereafter.

(f) For the purposes of subdivision (e):

(1) Property is substantially damaged or destroyed if it sustains physical damage amounting to more than 50 percent of its value

immediately before the disaster. Damage includes a diminution in the value of property as a result of restricted access caused by the disaster.

(2) Replacement property is comparable to the property substantially damaged or destroyed if it is similar in size, utility, and function to the property that it replaces, and if the fair market value of the acquired property is comparable to the fair market value of the replaced property prior to the disaster.

(g) For purposes of subdivision (a), the terms "purchased" and "change in ownership" do not include the purchase or transfer of real property between spouses since March 1, 1975, including, but not limited to, all of the following:

(1) Transfers to a trustee for the beneficial use of a spouse, or the surviving spouse of a deceased transferor, or by a trustee of such a trust to the spouse of the trustor.

(2) Transfers to a spouse that take effect upon the death of a spouse.

(3) Transfers to a spouse or former spouse in connection with a property settlement agreement or decree of dissolution of a marriage or legal separation.

(4) The creation, transfer, or termination, solely between spouses, of any coowner's interest.

(5) The distribution of a legal entity's property to a spouse or former spouse in exchange for the interest of the spouse in the legal entity in connection with a property settlement agreement or a decree of dissolution of a marriage or legal separation.

(h) (1) For purposes of subdivision (a), the terms "purchased" and "change in ownership" do not include the purchase or transfer of the principal residence of the transferor in the case of a purchase or transfer between parents and their children, as defined by the Legislature, and the purchase or transfer of the first one million dollars (\$1,000,000) of the full cash value of all other real property between parents and their children, as defined by the Legislature. This subdivision applies to both voluntary transfers and transfers resulting from a court order or judicial decree.

(2) (A) Subject to subparagraph (B), commencing with purchases or transfers that occur on or after the date upon which the measure adding this paragraph becomes effective, the exclusion established by paragraph (1) also applies to a purchase or transfer of real property between grandparents and their grandchild or grandchildren, as defined by the Legislature, that otherwise qualifies under paragraph (1), if all of the parents of that grandchild or those grandchildren, who qualify as the children of the grandparents, are deceased as of the date of the purchase or transfer.

(B) A purchase or transfer of a principal residence shall not be excluded pursuant to subparagraph (A) if the transferee grandchild or

grandchildren also received a principal residence, or interest therein, through another purchase or transfer that was excludable pursuant to paragraph (1). The full cash value of any real property, other than a principal residence, that was transferred to the grandchild or grandchildren pursuant to a purchase or transfer that was excludable pursuant to paragraph (1), and the full cash value of a principal residence that fails to qualify for exclusion as a result of the preceding sentence, shall be included in applying, for purposes of subparagraph (A), the one-million-dollar (\$1,000,000) full cash value limit specified in paragraph (1).

(i) (1) Notwithstanding any other provision of this section, the Legislature shall provide with respect to a qualified contaminated property, as defined in paragraph (2), that either, but not both, of the following apply:

(A) (i) Subject to the limitation of clause (ii), the base year value of the qualified contaminated property, as adjusted as authorized by subdivision (b), may be transferred to a replacement property that is acquired or newly constructed as a replacement for the qualified contaminated property, if the replacement real property has a fair market value that is equal to or less than the fair market value of the qualified contaminated property if that property were not contaminated and, except as otherwise provided by this clause, is located within the same county. The base year value of the qualified contaminated property may be transferred to a replacement real property located within another county if the board of supervisors of that other county has, after consultation with the affected local agencies within that county, adopted a resolution authorizing an intercounty transfer of base year value as so described.

(ii) This subparagraph applies only to replacement property that is acquired or newly constructed within five years after ownership in the qualified contaminated property is sold or otherwise transferred.

(B) In the case in which the remediation of the environmental problems on the qualified contaminated property requires the destruction of, or results in substantial damage to, a structure located on that property, the term "new construction" does not include the repair of a substantially damaged structure, or the construction of a structure replacing a destroyed structure on the qualified contaminated property, performed after the remediation of the environmental problems on that property, provided that the repaired or replacement structure is similar in size, utility, and function to the original structure.

(2) For purposes of this subdivision, "qualified contaminated property" means residential or nonresidential real property that is all of the following:

(A) In the case of residential real property, rendered uninhabitable, and in the case of nonresidential real property, rendered unusable, as the result of either environmental problems, in the nature of and including, but not limited to, the presence of toxic or hazardous materials, or the remediation of those environmental problems, except where the existence of the environmental problems was known to the owner, or to a related individual or entity as described in paragraph (3), at the time the real property was acquired or constructed. For purposes of this subparagraph, residential real property is "uninhabitable" if that property, as a result of health hazards caused by or associated with the environmental problems, is unfit for human habitation, and nonresidential real property is "unusable" if that property, as a result of health hazards caused by or associated with the environmental problems, is unhealthy and unsuitable for occupancy.

(B) Located on a site that has been designated as a toxic or environmental hazard or as an environmental cleanup site by an agency of the State of California or the federal government.

(C) Real property that contains a structure or structures thereon prior to the completion of environmental cleanup activities, and that structure or structures are substantially damaged or destroyed as a result of those environmental cleanup activities.

(D) Stipulated by the lead governmental agency, with respect to the environmental problems or environmental cleanup of the real property, not to have been rendered uninhabitable or unusable, as applicable, as described in subparagraph (A), by any act or omission in which an owner of that real property participated or acquiesced.

(3) It shall be rebuttably presumed that an owner of the real property participated or acquiesced in any act or omission that rendered the real property uninhabitable or unusable, as applicable, if that owner is related to any individual or entity that committed that act or omission in any of the following ways:

(A) Is a spouse, parent, child, grandparent, grandchild, or sibling of that individual.

(B) Is a corporate parent, subsidiary, or affiliate of that entity.

(C) Is an owner of, or has control of, that entity.

(D) Is owned or controlled by that entity.

If this presumption is not overcome, the owner shall not receive the relief provided for in subparagraph (A) or (B) of paragraph (1). The presumption may be overcome by presentation of satisfactory evidence to the assessor, who shall not be bound by the findings of the lead governmental agency in determining whether the presumption has been overcome.

(4) This subdivision applies only to replacement property that is acquired or constructed on or after January 1, 1995, and to property

repairs performed on or after that date.

(j) Unless specifically provided otherwise, amendments to this section adopted prior to November 1, 1988, are effective for changes in ownership that occur, and new construction that is completed, after the effective date of the amendment. Unless specifically provided otherwise, amendments to this section adopted after November 1, 1988, are effective for changes in ownership that occur, and new construction that is completed, on or after the effective date of the amendment.

SEC. 3. (a) Any change in state statute which results in any taxpayer paying a higher tax must be imposed by an act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature, except that no new ad valorem taxes on real property, or sales or transaction taxes on the sales of real property may be imposed.

(b) As used in this section, "tax" means any levy, charge, or exaction of any kind imposed by the State, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of conferring the benefit or granting the privilege to the payor.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the State of providing the service or product to the payor.

(3) A charge imposed for the reasonable regulatory costs to the State incident to issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of state property, or the purchase, rental, or lease of state property, except charges governed by Section 15 of Article XI.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or the State, as a result of a violation of law.

(c) Any tax adopted after January 1, 2010, but prior to the effective date of this act, that was not adopted in compliance with the requirements of this section is void 12 months after the effective date of this act unless the tax is reenacted by the Legislature and signed into law by the Governor in compliance with the requirements of this section.

(d) The State bears the burden of proving by a preponderance of

the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity.

Section 4. Cities, Counties and special districts, by a two-thirds vote of the qualified electors of such district, may impose special taxes on such district, except ad valorem taxes on real property or a transaction tax or sales tax on the sale of real property within such City, County or special district.

Section 5. This article shall take effect for the tax year beginning on July 1 following the passage of this Amendment, except Section 3 which shall become effective upon the passage of this article.

Section 6. If any section, part, clause, or phrase hereof is for any reason held to be invalid or unconstitutional, the remaining sections shall not be affected but will remain in full force and effect.

SEC. 7. Section 3 of this article does not apply to the California Children and Families First Act of 1998.

CALIFORNIA CONSTITUTION  
ARTICLE 13C [VOTER APPROVAL FOR LOCAL TAX LEVIES]

SECTION 1. Definitions. As used in this article:

(a) "General tax" means any tax imposed for general governmental purposes.

(b) "Local government" means any county, city, city and county, including a charter city or county, any special district, or any other local or regional governmental entity.

(c) "Special district" means an agency of the State, formed pursuant to general law or a special act, for the local performance of governmental or proprietary functions with limited geographic boundaries including, but not limited to, school districts and redevelopment agencies.

(d) "Special tax" means any tax imposed for specific purposes, including a tax imposed for specific purposes, which is placed into a general fund.

(e) As used in this article, "tax" means any levy, charge, or exaction of any kind imposed by a local government, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.

(2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.

(3) A charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law.

(6) A charge imposed as a condition of property development.

(7) Assessments and property-related fees imposed in accordance with the provisions of Article XIII D.

The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the

reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity.

SEC. 2. Local Government Tax Limitation. Notwithstanding any other provision of this Constitution:

(a) All taxes imposed by any local government shall be deemed to be either general taxes or special taxes. Special purpose districts or agencies, including school districts, shall have no power to levy general taxes.

(b) No local government may impose, extend, or increase any general tax unless and until that tax is submitted to the electorate and approved by a majority vote. A general tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved. The election required by this subdivision shall be consolidated with a regularly scheduled general election for members of the governing body of the local government, except in cases of emergency declared by a unanimous vote of the governing body.

(c) Any general tax imposed, extended, or increased, without voter approval, by any local government on or after January 1, 1995, and prior to the effective date of this article, shall continue to be imposed only if approved by a majority vote of the voters voting in an election on the issue of the imposition, which election shall be held within two years of the effective date of this article and in compliance with subdivision (b).

(d) No local government may impose, extend, or increase any special tax unless and until that tax is submitted to the electorate and approved by a two-thirds vote. A special tax shall not be deemed to have been increased if it is imposed at a rate not higher than the maximum rate so approved.

SEC. 3. Initiative Power for Local Taxes, Assessments, Fees and Charges. Notwithstanding any other provision of this Constitution, including, but not limited to, Sections 8 and 9 of Article II, the initiative power shall not be prohibited or otherwise limited in matters of reducing or repealing any local tax, assessment, fee or charge. The power of initiative to affect local taxes, assessments, fees and charges shall be applicable to all local governments and neither the Legislature nor any local government charter shall impose a signature requirement higher than that applicable to statewide statutory initiatives.