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7

AGENDA REPORT Consent | Information

June 4, 2018

TO: San Diego Commissioners
FROM: Keene Simonds, Executive Officer
SUBJECT: Commission Counsel Memorandum |
Tax Fairness, Transparency, and Accountability Act of 2018

SUMMARY

The San Diego Local Agency Formation Commission (LAFCO) will receive a memorandum from Commission Counsel summarizing a pending citizens' statewide initiative that proposes to limit the authority of local government to impose new revenues. The initiative is titled the Tax Fairness, Transparency and Accountability Act of 2018 and – among other items – would expand the definition of taxes and voting requirements therein. The memorandum is being presented to the Commission for information.

DISCUSSION

This item is for San Diego LAFCO to receive a memorandum from Commission Counsel on the pertinent details of a pending citizens' initiative: Tax Fairness, Transparency and Accountability Act of 2018. The memorandum is attached and has been prepared at the request of the Executive Officer given the initiative's potential and substantive impact on local government and ability to fund municipal services; the latter of which directly affects LAFCO and its various State directives.

ANALYSIS

See the attached memorandum.

ALTERNATIVES FOR ACTION

This item is being presented for information only.

San Diego LAFCO

June 4, 2018 Regular Meeting

Agenda Item No. 7 | Commission Memorandum: Tax Fairness, Transparency, and Accountability Act of 2018

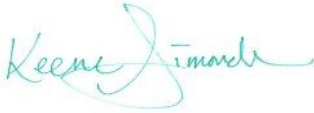
RECOMMENDATION

It is recommended San Diego LAFCO receive the item; no formal action necessary.

PROCEDURES

This item has been placed on the San Diego LAFCO's agenda as part of the consent calendar. A successful motion to approve the consent calendar will include taking affirmative action on the staff recommendation unless otherwise specified by the Commission.

Respectfully,



Keene Simonds
Executive Officer

Attachment:

- 1) Commission Counsel Memorandum | Tax Fairness, Transparency and Accountability Act of 2018

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MEMORANDUM

TO: Keene Simonds
Executive Officer
San Diego LAFCO

FILE NO: 49021.0001

FROM: Michael G. Colantuono, General Counsel
Holly O. Whatley, Asst. General Counsel
John L. Jones II, Asst. General Counsel

DATE: May 5, 2018

RE: Tax Fairness, Transparency and Accountability Act of 2018

INTRODUCTION

As promised, we write to summarize the “Tax Fairness, Transparency and Accountability Act of 2018” — an initiative the California Business Roundtable is circulating for the November 2018 ballot. Its goal — as with Propositions 13, 62, 218, and 26 before it — is to limit the authority of government to impose revenue measures. It eliminates the distinction between general and special taxes, requiring two-thirds voter approval for both, and treating all but a few exempt revenues as special taxes. The initiative broadens the definition of “tax” to include “[e]very levy, charge, or exaction of any kind imposed, adopted, created, or established by local law,”¹ which includes “any ordinance, resolution, ruling, opinion letter, or other legal authority or interpretation adopted, enacted, enforced, issued, or implemented by a local government.”² It applies to both general law and charter cities, as well as to counties, special districts and the State.³

¹ Tax Fairness, Transparency and Accountability Act of 2018 (“Initiative”), § 7 (Cal. Const., art. XIII C, § 2(a), as amended.)

² Initiative, § 6 (Cal. Const., art. XIII C, § 1, subd. (f), as amended).

³ Initiative, § 6 (Cal. Const., art. XIII C, § 1, subd. (b), as amended).

As of late February 2018, the proponents have gathered 25% of the 585,407 signatures needed to place the initiative on the November ballot.⁴ The circulation deadline is July 25, 2018 — enough time for the measure to qualify. The initiative has the backing of the California Business Roundtable and funding from the American Beverage Association. The League of California Cities has formed a committee to oppose the initiative.

KEY PROVISIONS

According to the Legislative Analyst, the expanded “definition of taxes and increase[d] vote thresholds for certain taxes and fees ... makes it harder for local governments and initiative proponents to increase local revenues.”⁵ The Legislative Analyst also wrote that “[r]oughly half of recently enacted sales, business, hotel, and utility general tax measures would have failed if the measure’s increased vote threshold requirements were in effect, suggesting that the reduction in local tax revenue could be substantial.”⁶ These limitations are not limited to newly enacted taxes. The initiative also affects any taxes regularly adjusted or renewed.

a. **Invalidation of Proposition 218 precedents.**

The initiative claims that legislative and judicial decisions have undermined Prop. 218.⁷ It takes direct aim at *Schmeer v. County of Los Angeles* [10-cent paper bag fee is not a tax because not remitted to the county].) (“*Schmeer*”),⁸ *California Cannabis Coalition v. City of Upland* (initiative general tax not limited to general election ballot by Prop. 218) (“*Upland*”),⁹ and *California Chamber of Commerce v. State Air Resources Board*

⁴ MuniServices, *Policy Update: Local Ballot Initiatives* (Mar. 14, 2018)

<<https://www.avenuinsights.com/2018/03/15/local-ballot-measures-considerations-for-california/>> (last viewed Apr. 15, 2018).

⁵ Legis. Analyst’s Off., letter to Attorney General Xavier Becerra re A.G. File No. 17-0050, Amendment No. 1 (Jan. 11, 2018) p. 3 <<https://oag.ca.gov/initiatives/active-measures>> (“LAO Letter”) (last viewed April 15, 2018).

⁶ *Ibid.*

⁷ Initiative, §§ 2(b) – 2(c).

⁸ *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310.

⁹ *California Cannabis Coalition v. City of Upland* (2017) 3 Cal.5th 924.

(2017) 10 Cal.App.5th 604 (AB 32 cap-and-trade fees not a tax, but voluntary payment for valuable right to pollute) (“*Chamber of Commerce*”).¹⁰

The initiative addresses *Schmeer* by clarifying that a levy, charge, or exaction retained by and payable to a private party is a tax, if the local agency limits the use of the proceeds.¹¹ *Upland* is expressly overruled. Initiative tax proposals are subject to the same two-thirds-voter-approval requirement and other requirements as are taxes proposed by local legislative bodies.¹²

The proponents undermine *Chamber of Commerce*, too. That case identified two “hallmarks” of a tax: (i) it is compulsory and (ii) the taxpayer need receive nothing of value in return for paying the tax. This initiative would eliminate the Prop. 26 exception excluding payments voluntarily made in exchange for a benefit or service received.¹³ That action will undermine the first prong of the *Chamber of Commerce* analysis.

b. **Expanded Definitions**

Under the initiative, “extend” now “includes, but is not limited to, doing any of the following with respect to a tax, exempt charge, or Article XIII D assessment or property related fee: lengthening its duration, delaying or eliminating its expiration, expanding its application to a new territory or class of payor, or expanding the base to which its rate is applied.”¹⁴ This has at least two consequences of note. First, any future annexation would require a separate two-thirds vote before any existing city taxes can be collected there. This effectively overrules *Citizens Ass’n of Sunset Beach v. Orange County Local Agency Formation Com’n*¹⁵ and may prevent most inhabited annexations. That case held Prop. 218 did not apply upon annexation to prevent a city from collecting all of its pre-annexation taxes in the annexation area.¹⁶

¹⁰ *California Chamber of Commerce v. State Air Resources Board* (2017) 10 Cal.App.5th 604.

¹¹ Initiative, § 6 (Cal. Const., art. XIII C, § 1, subd. (h)(1), as amended).

¹² Initiative, § 6 (Cal. Const., art. XIII C, §§ 1, subd. (b), 2, subd. (e), 5).

¹³ Initiative, § 6 (Cal. Const., art. XIII § 1, subd. (e)(1)).

¹⁴ Initiative, § 6, Initiative, § 6 (Cal. Const., art. XIII C, § 1, subd. (g)).

¹⁵ (2012) 209 Cal.App.4th 1182.

¹⁶ *Id.* at 1189–1190.

Prop. 26 provided seven express and two implied exceptions. The initiative deletes the exception for fees imposed for a privilege or benefit, which could imperil some franchise fees.¹⁷ The measure does retain an exception from the definition of “tax” for fees for the use of property, which will protect some franchise fees.

c. **Earmarking**

The initiative requires any tax for a specific use to identify the purposes for which tax proceeds may be spent and that language must be binding and enforceable.¹⁸ General taxes must state their proceeds may be used “for general revenue purposes.”¹⁹

d. **Retroactivity**

If passed, the initiative will invalidate all local taxes adopted, increased, or extended on or after January 1, 2018 unless they comply with the new law, including the requirement that a general tax mention “general revenue purposes.”²⁰

e. **Exemptions**

The initiative exempts existing school bond (55% vote) construction authority.²¹

IMPACT ON MUNICIPAL REVENUE

a. **Taxes**

The initiative eliminates the distinction between general and special taxes and instead focuses on whether there will be an exaction of **any** sort from a taxpayer. If so, then it is a tax — regardless of the label used to describe it — unless one of the few exceptions applies.²² All revenue measures require two-thirds approval — of voters for

¹⁷ *Jacks v. City of Santa Barbara* (2017) 3 Cal.5th 248, 270–271.

¹⁸ Initiative, § 7 (Cal. Const., art. XIII C, § 2, subd. (f)(1), as amended).

¹⁹ *Ibid.*

²⁰ Initiative, § 7, (Cal. Const., art. XIII C, § 2, subd. (i)(1), as amended).

²¹ Initiative, § 8 (Cal. Const., art. XIII C, § 5, subd. (b), as amended).

²² Initiative, § 2, subd. (f).

taxes and of the legislative body for the few fees which are not made taxes by this measure.²³

Local governments will likely see a substantial decline in revenue if the initiative is approved. The Legislative Analyst noted that local governments may offset some of this lost revenue by greater reliance on “developer fees and other majority-vote revenue sources for the revenue sources subject to a higher vote threshold under the measure.”²⁴

Non-property-based business assessments other than tourism marketing district assessments will require two-thirds voter approval. Because the initiative exempts development impact fees and Tourism Marketing District assessments, but not other business assessments, non-property-based business assessments are likely made taxes requiring two-thirds voter approval.²⁵

b. Statutory and Ordinance Conflicts

If passed, the initiative will amend the California Constitution and overrule contrary statutes and charter city ordinances.

²³ Initiative, § 7 (Cal. Const., art. XIII C, § 2, subds. (a) through (e), as amended).

²⁴ LAO Letter, *supra*, fn. 3 at p. 3.

²⁵ This effectively overrules *Evans v. City of San Jose* (1992) 3 Cal.App.4th 728, 738 (distinguishing non-property based assessments from those on real property).

c. **Fees**

It will be much more difficult to impose a new fee or to increase or extend an existing fee. A legislative body cannot adopt or increase any non-Prop. 218 fees unless two-thirds of that body votes to approve it.²⁶ Even if they do so, the voters can referend the decision with signatures of 5% of the number of voters in the jurisdiction who voted in the last gubernatorial election.²⁷ As gubernatorial turnouts are commonly in the neighborhood of 40 percent, as few as 2 percent of a community's voters will be able to referend a fee. Unlike an initiative, which takes effect after an election result is certified, referenda suspend the targeted legislation immediately. This will make rate stabilization and other reserves vital for the stability and credit-worthiness of water, sewer and other utilities.

The legal threshold for fees has also changed. Now, fees are limited to actual costs — not reasonable costs.²⁸ Further, the legal standard to prevail has changed from preponderance of the evidence (i.e. more likely than not) to “clear and convincing evidence,” which requires a higher degree of proof to defend an agency's revenues.

d. **Fines**

Fines and penalties will not be taxes if imposed to punish a violation of the law pursuant to “adjudicatory due process.”²⁹ It is not clear how demanding that last phrase will be.

CONCLUSION

The goal of the initiative is familiar — to make it more difficult to pass new taxes. The initiative, however, seems to have been drafted to overrule every significant government victory under Propositions 13, 26 and 218 to cast a wide net in terms of potentially benefited industries.

²⁶ Initiative, § 2, subd. (d).

²⁷ *Ibid.*

²⁸ Initiative, § 6 (Cal. Const., art. XIII C, subd. 1(e)(2) through (e)(3), Cal. Const., art. XIII C (i).)

²⁹ Initiative, § 6 (Cal. Const., art. XIII C, subd. 1(e)(4).)

Keene Simonds, Executive Officer
San Diego LAFCO
May 5, 2018
Page 7

If you would like more information regarding the issues discussed in this memo, please contact us.

Keene Simonds, Executive Officer
San Diego LAFCO
May 5, 2018
Page 8

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