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Government Code § 6103

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

Citizens for Fair REU Rates, et al.
Plaintiffs and Appellants
vs.
City of Redding, et al.
Defendants and Respondents.

Fee Fighter LLC, et al.
Plaintiffs and Appellants
vs.
City of Redding, et al.
Defendants and Respondents.

PETITION FOR REVIEW

Of a Published Decision of the
Third Appellate District, Case No. C071906

Reversing a Judgment of the Superior Court of
the State of California for the County of Shasta,
Case No. 171377 (Consolidated with Case No. 172960)
Honorable William D. Gallagher, Judge Presiding

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To the Honorable Chief Justice and Associate Justices of the California Supreme Court:

The City of Redding respectfully petitions for review of a published opinion of the Court of Appeal.

QUESTIONS FOR REVIEW

1. Does Proposition 26 — California Constitution, article XIII C, section 1, subdivision (e)[1] — retroactively invalidate earlier local legislation that increases the cost of a government service? If so, does that retroactive effect turn on the legislation's form (e.g. charter provisions, ordinances, resolutions, or budget provisions)?

2. Is a payment in lieu of property taxes (PILOT) imposed on a City's electric utility for the benefit of its general fund necessarily a reasonable cost of service under article XIII C, section 1, subdivision (e)(2) because it equals the tax an investor-owned utility would pay under Proposition 13 (Cal. Const., art. XIII A, § 1) and because rates which may fund it are significantly lower than rates of a neighboring investor-owned utility approved by the Public Utilities Commission?

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[1] All references to articles in this Petition are to the Constitution.

3. Are prices in wholesale power markets "imposed" under article XIII C, section 1, subdivision (e)(2) notwithstanding that those who pay such prices are sophisticated entities with substantial market power?

4. Does the statutory remedy for a violation of 1986's Proposition 62 apply to a PILOT lawful when enacted but later found to violate Proposition 26?

INTRODUCTION

This case presents an opportunity to answer significant questions pending in many lower courts considering Proposition 26. That 2010 initiative amendment to our California Constitution newly defines all revenue measures "imposed" by local governments as taxes requiring voter approval, with seven stated exceptions. (Cal. Const., art. XIII C, § 2, subd. (e).) It defines revenues imposed by the State as taxes requiring two-thirds approval of each legislative chamber, with five exceptions worded nearly identically to those provided for local government. (Cal. Const., art. XIII A, § 3, subd. (b).)[2]

Over Justice Duarte's dissent, the published opinion of the Third District ("the Opinion") applies Proposition 26 to invalidate a

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[2] There are very minor differences between article XIII C, section 1, subdivisions (e)(1) – (5) and XIII A, section 3, subd. (b)(1) – (5). None is material here.

payment in lieu of taxes ("PILOT") first legislated by the Redding City Council in 1988 and last amended in 2005. This case raises important issues under Proposition 26, including:

- whether the measure prospectively invalidates earlier legislation affecting the cost of government services,
- the meaning of "reasonable cost of service" — which also appears in Proposition 218 (art. XIII D, § 6, subd. (b)(1) & (b)(3))— and
- remedies for violation of either measure.

Further, although this Court does not review mere error, the published Opinion contains numerous factual and legal errors — uncorrected on denial of competing petitions for rehearing. It has already been criticized by the Second District. (*Jacks v. County of Santa Barbara* (Feb. 26, 2015, No. B253474) ___ Cal.App.4th ___ ("*Jacks*").) These facts counsel against delaying review to allow these issues to further develop in the lower courts. Absent review, the Opinion will mislead lower courts, the State, and local governments and waste public resources in duplicative litigation affecting many agencies — including 42 listed in footnote one to Justice Duarte's dissent which collectively represent the entire public power industry in California and which serve the great majority of its people.

The Opinion elevates form over substance by hinging its conclusion on the City's adoption of the PILOT by budget resolution rather than ordinance. Accordingly, under the Opinion, application

of Proposition 26 depends on the form rather than the substance of earlier legislation. The Opinion assumes — without analysis of the language or intent of the City's legislation — the PILOT was temporary because it was included in recurring budget resolutions, despite uncontroverted evidence the City Council intended the PILOT to be permanent. This overlooks the canon of construction that re-adoption of legislative language is construed to continue earlier legislation, not to re-adopt it. The Opinion concludes the PILOT expired with the budget in effect on Proposition 26's effective date. Thus the Opinion invents a new rule of legislative formalism that will have widespread impacts for both State and local governments; for the construction of Proposition 26 and related Propositions 13, 62 and 218; and for the application of other constitutional amendments or preemptive legislation.

The Opinion's conclusion also disserves the plain intent of voters to grandfather pre-Proposition 26 legislation. By the Opinion's logic, many state and local laws that increase utility costs by subsidizing rates for the poor and the elderly — or requiring safety or environmental protections — do not survive Proposition 26, despite ballot argument assurances to the contrary.

The Opinion also clouds the meaning of "reasonable cost of service" under Proposition 26. (Cal. Const., art. XIII C, § 1, subds. (e)(1) – (3).) The Dissent concludes a PILOT is a reasonable cost of publicly-owned utility service, just as privately-owned

utilities pay property taxes under Proposition 13. The Opinion holds otherwise, and erroneously concludes the PILOT itself must recover costs paid by the electric enterprise fund, as opposed to the cost of municipal services provided by the general fund.

The case also asks: under what circumstances is a charge for a government benefit or service "imposed" so as to trigger Proposition 26 — or Proposition 218, which uses the same term? The Opinion erred in finding that wholesale transactions between sophisticated entities with multiple power sources are subject to the same cost-of-service limitations of Proposition 26 as retail rates paid by customers who have no practical alternative to the City's utility. This published holding will have widespread impact on public power — effectively ceding that market to private parties unconstrained by Proposition 26.

Finally, this case presents the first opportunity to consider remedies under Proposition 62.

These questions are vital to the State and local governments alike. Moreover, each is pending in many lower courts. Review will allow this Court to authoritatively resolve these questions for the benefit of litigants, courts, and policymakers through California.

STATEMENT OF FACTS

From 1971 to 1988, the City implemented an operating transfer from Redding Electric Utility ("REU") to the City's general fund. This was a fixed amount established by budget; unlike a

PILOT, which is calculated like a property tax as a percentage of the value of utility assets. (II AR Tab 37, p. 358; II AR Tab 42, pp. 379–380; III AR Tab 111, p. 640.)[3] The transfer was intended to compensate the general fund for benefits and services to the utility (for which a private utility would pay via property taxes and franchise fees for use of public rights of way) in addition to services not provided to a private utility, such as billing, finance, and fleet maintenance. (II AR Tab 37, p. 358; I AR Tab 5, p.133.)

The City Council replaced the operating transfer with a PILOT upon adoption of the FY 1988–1989 budget. (II AR Tab 28, p. 319; III AR Tab 111, p. 640.) The PILOT was initially calculated by valuing REU's property, subtracting depreciation, and multiplying the result by Proposition 13's one percent property tax rate. (II AR Tab 42, p. 380.) The PILOT was amended to reflect evolving accounting practices three times — in 1991 (II AR Tab 70, pp. 446–447; II AR Tab 72, p. 450), 2001 (III AR Tab 126, pp. 693–694; III Tab 134, p. 738), and in 2005 (2 CT 530). The City has since implemented the PILOT without change.

In December 2010, the City Council adopted Resolution No. 2010-179 to increase electric rates by 7.84 percent, effective January 2011, and by another 7.84 percent effective December 2011. (IV AR Tab 163, p. 1041.) Although the utility's costs to generate

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[3] Citations to the Administrative Record are in this form: [Volume] AR Tab [#], p. [#].

electricity had increased significantly in earlier years; the City deferred rate increases, depleting reserves. (III AR Tab 140, pp. 797–800; IV AR Tab 159, p. 1031.) As a result, reserves fell significantly and staff warned that failure to raise raises would harm REU's credit rating and increase its borrowing costs. (IV AR Tab 165, p. 1060; IV Tab 166, p. 1077–1078.) Staff also recommended rate increases to reflect escalating costs and to honor bond covenants to maintain rates and cash reserves sufficient to ensure debt repayment. (IV AR Tab 158, p. 1028; IV AR Tab 159, pp. 1031–1033.)

The 2010 rate increases did not change the PILOT in any way. (IV AR Tab 163, p. 1041.) Nor were those increases necessary to fund the PILOT — REU's non-rate revenues are three to four times the PILOT amount. (IV AR Tab 145, p. 831; IV AR Tab 149, p. 873.) Thus, the PILOT can be funded from non-rate revenues. (IV AR Tab 145, p. 831; IV AR Tab 149, p. 873; XIII AR Tab 205, p. 2975.)

PROCEDURAL HISTORY

A. Two Writ Petitions

On February 4, 2011, Citizens for Fair REU Rates, an unincorporated association, sued the City and City Council of Redding (collectively, "City") in mandate and for declaratory and injunctive relief (Case No. 171377, "Rate Case"), alleging rates adopted by Resolution No. 2010-179 are "taxes" requiring voter

approval under Proposition 26 due to their inclusione of the PILOT. (1 CT 2.)

On August 29, 2011, Feefighter, LLC, a for-profit entity owned by Citizens' counsel, filed a second suit (Case No. 172960, "Budget Case") alleging Resolution No. 2011-111, which adopted the City's FY 2011–2013 budget, illegally reflected PILOT revenues and therefore violated Proposition 26. (2 CT 498.)

B. Trial Court Proceedings

The Superior Court tried the Rate Case November 8, 2011, ruling for the City. (3 CT 709.) The court concluded the PILOT was neither created nor altered by the December 2010 rate increase; Proposition 26 therefore does not apply to the PILOT, and cannot invalidate the rate increase. (3 CT 711.)

The court consolidated the two cases on February 2, 2012. (3 CT 719.)

On July 13, 2012, the Court issued judgment for the City in both cases. (3 CT 750.) The trial court concluded Proposition 26 does not apply retroactively to the PILOT, adopted in 1988. (3 CT 736, 739.) The trial court also concluded the PILOT is a lawful cost of service not displaced by Proposition 26. (3 CT 734-737.)[4]

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[4] A copy of the June 22, 2012 Memorandum of Decision is attached to this brief pursuant to California Rules of Court, rule 8.504, subd. (e)(1)(B).

Citizens for Fair REU Rates and Feefighter, LLC (collectively, "Citizens") appealed both judgments on August 20, 2012. (3 CT 760.)

C. The Opinion

The Opinion accepts the trial court's conclusion that Proposition 26 does not apply retroactively to local government charges adopted before its November 2010 effective date. (Opinion at p. 3.)[5] However, the Opinion determined the PILOT was subject to annual reauthorization by the City Council (*ibid.*),[6] and thus the PILOT grandfathered by Proposition 26 was the one adopted by the FY 2009–2011 budget — except any PILOT increase that may have resulted from the December 2010 rate increase. (Opinion at pp. 19–20.) The Opinion is thus ambiguous as to whether the PILOT became subject to Proposition 26 with the December 2010 rates (*ibid.*) or the June 2011 budget adoption. (Opinion at p. 19.) The City's petition for rehearing noted the ambiguity — to no effect. (Petn. for Rehg. at pp. 9–10.)

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[5] As required by California Rules of Court, rule 8.504, subd. (e)(1)(A), copies of the Opinion and the Dissent are attached to this brief, along with the Order Denying Rehearing.

[6] The Opinion contains a factual error on this point, in that the City's budgets are adopted every two years. This error was brought to the Court of Appeal's attention in the City's Petition for Rehearing. The modified Opinion maintains the error.

The Opinion concludes the PILOT reflected in FY 2011–2013 and subsequent budgets is new, post-Proposition 26 legislation and therefore a tax requiring voter approval unless the City demonstrates it is limited to cost of service as article XIII C, section 1, subdivision (e)(2) requires. (Opinion at p. 20.) The Opinion declines to address whether the PILOT reflects a reasonable cost to the City for services to REU, and remands that issue for trial. (Opinion at pp. 20–23.) Citizens' petition for rehearing objected to that remand to no avail. (Citizens Petn. for Rehg. at pp. 2–12.) Finally, the Opinion rejected the trial court's factual finding that the PILOT is funded by non-rate revenues, without explanation why the PILOT must be viewed as funded by rates. (Opinion at p. 14.) The Opinion rejected the City's contention that prices for its wholesale power sales are not "imposed" under Proposition 26. (Opinion at p. 14.) The City unsuccessfully sought rehearing on this issue, too. (Petn. for Rehg. at pp. 10–11.)

D. The Dissent

Justice Duarte dissented ("Dissent"), agreeing with the Opinion's conclusions the PILOT was readopted after November 2010 and therefore subject to Proposition 26. (Dissent at p. 2.) However, she concluded the PILOT is a "reasonable" cost allowed by article XIII C, section 1, subdivision (e)(2) because it reflects the property tax on private utilities limited by Proposition 13. (Dissent at p. 2.) As property taxes may be funded by rates of regulated

private utilities, a public utility may do the same under Proposition 26. (Dissent at p. 4.) The Dissent finds "legally-compelled" the trial court's conclusion the PILOT is a reasonable cost of service under article XIII C, section 1, subdivision (e)(2). (Dissent at pp. 4–5.)

E. Denial of Both Petitions for Rehearing

Both parties sought rehearing. The City identified factual errors, misstatements of the City's arguments, and errors of law. Citizens objected to remand and to the conclusion the PILOT models the property tax. The Court of Appeal denied both petitions on February 19, 2015 and ordered the Opinion modified to address one of the City's legal arguments and to correct a typographical error, but without change in judgment. This timely Petition follows.

I. REVIEW IS NECESSARY TO RESOLVE IMPORTANT QUESTIONS AFFECTING THE STATE AND ALL LOCAL GOVERNMENTS

The Opinion addresses important questions that affect every legislative body's power to make or maintain revenue measures under Propositions 13, 218, and 26. It misstates settled law, the facts of the case, and misinterprets Proposition 26. Review is necessary to correct these errors. Moreover, this Court should not await further appellate authority before addressing these questions, because the Opinion provides lower courts inappropriate guidance on pressing public finance matters affecting not only the public power industry,

but **all** state and local rate-making. Thus the Opinion's errors must be corrected now to avoid unnecessary disruption and litigation that may take years to resolve.

A. Guidance Is Needed on Retroactive Application of Proposition 26

Nearly all publicly owned utilities provide general fund support like that challenged here. (See Brief of Amicus Curiae California Municipal Utility Association ("CMUA Brief") at pp. 6–7; See also Dissent at p. 1, fn. 1.) Such transfers are so common the Legislature requires:

> All city-owned electric utilities shall report on the periodic bill the amount expected to be transferred from the utility to the general fund, and to any special funds, of the city on a no less than annual basis.

(Pub. Util. Code, § 9606.)

Electric utilities must also comply with many other legislatively imposed costs, including environmental regulation, safety requirements, and greenhouse-gas-reduction goals. Most were legislated before Proposition 26's adoption in 2010, but — because that measure limits rates for public services to the cost of service — continued vitality of these laws depends on whether Proposition 26 applies to pre-existing legislation.

It is plain that Proposition 26 is not retroactive as to local governments.[7] All four judges to review this case — the trial court, the majority and the dissent — agree on this point. (3 CT 736, 739; Opinion at p. 17, citing *Brooktrails Township CSD v. Board of Supervisors* (2013) 218 Cal.App.4th 195, 205–207; see also Dissent at p. 2, fn. 2.) However , it is less clear whether rate-making after Proposition 26 may account for costs to comply with legislation that predates it — the facts here. Thus, the State and all local governments need guidance as to the continuing validity of those earlier laws.

Grandfathered costs under Proposition 26 are disputed in many lower courts. To cite but two significant examples:

- 2006's A.B. 32, the greenhouse gas law, is subject to a Proposition 26 challenge to fees imposed by the California Air Resources Board to implement the law. (See Motion for Judicial Notice ("MJN"), Exh. A at pp. 44–64[8] [Opening Brief in *California Chamber of*

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[7] Article XIII A, section 3, subdivision (c) provides limited retroactivity as to the State. Article XIII C, section 1, subdivision (e) provides no similar language as to local government — suggesting no retroactivity as to local government was intended.

[8] Citations to the MJN exhibits are to Bates-stamped pagination, not original document pagination (e.g., MJN00044–MJN00064).

Commerce v. California Air Resources Board, Third District Court of Appeal Case No. C075930]; see also MJN, Exh. B at pp. 132–137 [Appellant's Opening Brief in *Morning Star Packing Co. v. California Air Resources Control Board*, Third District Court of Appeal Case No. C075954.)

- California's gun registration fees under Penal Code section 28225 are challenged as exceeding the cost of regulation under art. XIII A, § 3, subd. (b)(3). (MJN, Exh. C, at p. 155 [2nd Amended Complaint in *Bauer v. Harris*, E.D. Cal. Case No. 11 CV 01440].)

Thus, guidance on the scope of Proposition 26 will assist resolution of important questions pending in lower courts, secure uniformity of decisions among the appellate courts, and save myriad governments fees to litigate these and the cases predicted by the Dissent's footnote one.

Application of Proposition 26 to legislatively-imposed costs that predate it would prohibit using rate revenue to fund:

- programs to reduce greenhouse gases under 2006's A.B. 32 (Health & Saf. Code §§ 38550–38551);
- "green" power development (Pub. Util. Code § 387.5);
- solar energy mandates (Pub. Resources Code §§ 25780 et seq.);

- renewable energy mandates (Pub. Util. Code § 399.11); and,
- discounted rates for the poor and elderly.

(IV AR Tab 142, p. 817; IV AR Tab 145, p. 830; IV AR Tab 148, pp. 869–870.)

In short, any government agency that has legislatively mandated costs to achieve public policy goals beyond the cost of generating, transmitting, storing and distributing power — or the comparable costs of other government services — needs guidance whether that legislation survived Proposition 26. Thus Proposition 26's retroactivity is of wide-spread and immediate importance and affects dozens of laws of pressing social and environmental import.

B. Guidance Is Needed on the "Reasonable Costs" Standard of Articles XIII A and XIII C and the "Proportionate Cost" Standard of Article XIII D

Article XIII A, section 3, subdivision (b)(2) and article XIII C, section 1, subdivision (e)(2) refer identically to "reasonable costs" of services. However, there is yet no case interpreting that Proposition 26 standard. Proposition 218 imposes an analogous burden on property related fees via article XIII D, section 6, subdivisions (b)(1) and (b)(3).

Proposition 26's "reasonable cost" requirement could be the Proposition 13 standard applied in *Sinclair Paint Co. v. Board of*

Equalization (1997) 15 Cal.4th 866. That case and its progeny recognize that the distinction between a regulatory fee and a special tax turns on whether a payor's charge bears a fair and reasonable relationship to that payor's burdens on or benefits from the regulated activity. (*Id.* at p. 878, citing *San Diego Gas & Electric Co. v. San Diego County Air Pollution Control Dist.* (1988) 203 Cal.App.3d 1132, 1145–1146.) The few cases interpreting Proposition 26 to date have noted that its article XIII A, section 3, subdivision (d) and final, unnumbered paragraph of article XIII C, section 1, subdivision (e) are paraphrases of *Sinclair Paint*. (See, e.g. *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310, 1326 [citing *Sinclair Paint* to construe Proposition 26].) However, Proposition 26 was a reaction to *Sinclair Paint* and intended to alter its rule in some respects. (*Id.* at p. 1322; see also 1 CT 276 [legislative analyst's summary of Prop. 26].)

Thus, if the *Sinclair Paint* reasonableness standard applies under Proposition 26, as *Schmeer, supra,* Cal.App.4th 1310 suggests — and Justice Duarte would hold here — charging Redding's electric utility for general governmental services via a PILOT measured by the property tax investor-owned utilities pay is "fair and reasonable," and the PILOT is a lawful cost of service. (Dissent at pp. 4–5.)

What constitutes adequate record evidence showing rates do not exceed the proportional cost of services as demanded by

Proposition 218 (art. XIII D, § 6, subd. (b)(3)) confounds rate makers and courts. Because Proposition 26 was intended to build upon Proposition 218 (*Schmeer, supra,* 213 Cal.App.4th at p. 1322), the two are in pari materia and decision here will assist resolution of Proposition 218, too.

Proposition 218 disputes abound as well, and include:

- *City of Palmdale v. Palmdale Water Dist.* (2011) 198 Cal.App.4th 926 [insufficient record to show tiered retail water rates reflect proportional cost of service];
- *Capistrano Taxpayers Assn. v. City of San Jan Capistrano* [4th DCA No. G048969, testing same issue] (MJN, Exh. D at p. 163 (Appellant's Opening Brief));
- *Glendale Coalition for Better Government v. City of Glendale* [L.A. Super. Ct. No. BS153253, testing same issue] (MJN, Exh. E at p. 252 (Complaint));
- *Sweetwater Authority Ratepayers Association, Inc. v. Sweetwater Authority* [San Diego Super. Ct. No. 37-2014-00029611-CM-MC-CTL, testing same issue] (MJN, Exh. F at p. 280 (Complaint));
- *City of San Buenaventura v. United Water Conservation District* [2d DCA No. B251810, testing the same issue as to groundwater augmentation charges] (MJN, Exh. G at p. 302 (Respondent's Brief));

- *Great Oaks Water Co. v. Santa Clara Valley Water District* [Sixth Appellate District Case No. H035885, same] (MJN, Exh. H at p. 452 (Amicus Brief));

Capistrano, Ventura, and *Great Oaks* were submitted by separate panels of the 2nd, 4th and 6th District Courts of Appeal since December.

Further, a very recent decision construes Article XIII C, section 2's requirement for voter approval of "taxes" as applied to a city's franchise fee on a private power utility. *Jacks, supra,* ___ Cal.App.4th ___. It is significant here for a further reason — it expressly criticizes and declines to follow the Opinion as to Proposition 218's application to charges associated with electric service. (*Id.*, Slip Op. at 5 & fn. 4.)

These four Proposition 218 cases — *Capistrano, Ventura, Great Oaks,* and *Jacks* — will all be decided within a few weeks and it seems unlikely these decisions can inform one another. This creates a risk of confusing, uncoordinated decisions. Thus, review here can inform developments under Proposition 218, too, to the extent Articles XIII C and XIII D impose similar cost-of-service requirements.

C. Guidance Is Needed as to When Revenue Measures Are "Imposed" so as to Trigger Propositions 218 and 26

Propositions 218 and 26 apply to revenue measures "imposed" by government. (Cal. Const., art. XIII C, § 2 and

art. XIII D, § 6 [Prop. 218]; Cal. Const., art. XIII A, § 3 and art. XIII C, § 1, subd. (e) [Prop. 26].) The meaning of that term is therefore crucial to governments' authority to fund services. However, there is little case authority on this issue, the text is silent, and legislative history opaque. *Citizens Ass'n of Sunset Beach v. Orange County Local Formation Com'n* (2012) 209 Cal.App.4th 1182 ruled that "impose" as used in Proposition 218 "refers to the first enactment of a tax, as distinct from an extension through operation of a process such as annexation". (at p. 1194) That framework is unhelpful as to other disputes under Proposition 218.

Litigants commonly cite *Ponderosa Homes, Inc. v. City of San Ramon* (1994) 23 Cal.App.4th 1761 which interprets "impose" as used in the Fee Mitigation Act (Gov. Code § 66000 et seq.): "The phrase 'to impose' is generally defined to mean to establish or apply by authority or force, as in 'to impose a tax.'" (*Ponderosa Homes, supra,* 23 Cal.App.4th at p. 1770.) Under this view, voters' intended Propositions 26 and 218 to reach only fees which government requires someone to pay, either by "authority or force," or by the absence of alternatives to the service for which a fee is charged.

The Opinion concludes Redding's retail power customers lack viable alternatives to its electric service, despite the City's reference to solar, wind and other sources. (Opinion at p. 13.) However, the Opinion goes further to apply Proposition 26 to voluntary transactions between sophisticated wholesale power customers —

like Enron and other public- and investor-owned utilities — which participate in a free market for power, and choose to purchase it from REU on terms negotiated at arm's length. (Opinion at p. 14.) The trial court concluded the PILOT was not funded from retail rates, but could be funded three times over from wholesale revenues —which are not subject to constitutional limitations. (See 3 CT 741 [trial court Memorandum of Decision].) The Opinion rejected that finding without analysis, suggesting it is irrelevant. (Opinion at p. 14.)

The Opinion's refusal to distinguish retail from wholesale rates dramatically expands the reach of Propositions 218 and 26, far beyond what the text or legislative history of either supports. It does so without citation to authority or detailed analysis. Nor is there any indication the voters who enacted Propositions 13, 218, and 26 sought to protect voluntary, wholesale customers of publicly-owned enterprises. While Redding might need protection from the likes of Enron, the reverse is hardly true and cannot have been the concern of voters who adopted Propositions 218 and 26.

This published Opinion will have repercussions throughout California. Extending Propositions 218 and 26 to commercial enterprises that purchase surplus power from REU and other public utilities will force those utilities to unnecessarily lower wholesale rates, raising costs for retail customers — the antithesis of what

those measures intended. If this profound and unexpected conclusion is the law, this Court should say so.

Precisely because the Opinion lacks meaningful analysis on this point, lower courts and utility policy makers lack guidance how to apply it. As revenue measures are commonly pledged to serve debt to fund expensive capital facilities that have useful lives of many years, uncertainty is fatal to the efficient operation of California's service enterprises. Bond lawyers do not give clean opinions on doubtful law and bond markets impose a risk premium for the resulting uncertainty. This Court can and should dispel this uncertainty for the benefit of every public utility in our state and the millions who depend on them for essential services.

D. Guidance Is Needed on Remedies for Invalid Government Revenue Measures

Citizens seek double recovery — they sue for refunds under the Government Claims Act (Gov. Code § 905 et seq.) **and** for a writ to mandate reduction of property taxes payable to the City under Proposition 62, a 1987 statutory initiative (Gov. Code § 53020 et seq.). (See AOB at pp. 31–32.) No published case or — to the knowledge of counsel for both parties here who together have many decades of experience in public finance disputes — any other case has ever applied this property tax reduction remedy. Nor does the Opinion address it, instead remanding the issue for decision if Redding is unable to prove the PILOT reflects the cost of services its

general fund provides REU. Review here would allow guidance on this important issue, too.

Although no published appellate authority squarely addresses remedies for violation of Propositions 218 or 26, one recent case provides helpful dicta. (See, e.g. *Water Replenishment District of Southern California v. City of Cerritos* (2013) 220 Cal.App.4th 1450, 1464 [applying "pay first, litigate later rule" and observing that likely remedy upon final judgment is refund of difference between fee paid and what lawful fee would have been].) In general, however, Proposition 218 authorities are silent as to monetary relief. Examples from this Court are:

- *Silicon Valley Taxpayers Ass'n, Inc. v. Santa Clara County Open Space Authority* (2008) 44 Cal.4th 431, 457–458 (invalidating open space assessment);
- *Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal.4th 205, 217 (invalidating water-rate initiative).

Government Code section 53728 requires a county auditor-controller to withhold from a city's share of property tax equal to the proceeds of a tax collected in violation of Proposition 62's requirement of voter approval post-August 1985. (Gov. Code, § 53727.) This remedy is unworkable here.

Proposition 62, largely supplanted by Proposition 218, required voter approval of local "taxes" without altering the pre-existing common law definition of the term, which did not

encompass utility charges. (*Hansen v. City of San Buenaventura* (1986) 42 Cal.3d 1172, 1182 [water rates not taxes even though non-city customers charged more than cost of service].) Moreover, utility rates were understood not to be taxes when Proposition 62 was adopted in 1986. (*Arcade County Water Dist. v. Arcade Fire Dist.* (1970) 6 Cal.App.3d 232, 240 ["A charge for services rendered is in no sense a tax."].) Nor was a PILOT a "tax" before adoption of Proposition 218 (as to water and sewer utilities) and Proposition 26 (as to electric and gas utilities). (*Howard Jarvis Taxpayers Ass'n v. City of Fresno* (2005) 127 Cal.App.4th 914, 927 ["An exaction imposed on any particular ratepayer in an amount established in the discretion of the utility department is not an exercise of the city's taxing power" despite *Oneto v. City of Fresno* (1982) 136 Cal.App.3d 460 [upholding same PILOT under Prop. 13].) Thus, the PILOT was not a "tax" when Proposition 62 was adopted and nothing in that measure indicates intent to change that rule, as Propositions 218 and 26 later did.

In addition, the remedy required by Proposition 62 is ill-defined. It does not require a county auditor-controller to reduce the 1 percent property tax authorized by Proposition 13 (art. XIII A, § 1); nor does it state how property taxes withheld from an offending city should be allocated. No law specifies what becomes of property taxes withheld under Government Code section 53728. Is it a windfall to the county? Escheat to the State? Become a windfall to all

taxing agencies other than the offending city? Clearly, a county may not simply keep the taxes because that would violate Proposition 13's directive that "[t]he one percent (1%) tax [is] to be collected by the counties and apportioned according to law to the districts within the counties." (Art. XIII A, § 1, emphasis added.)

Thus, a significant issue left unresolved by the Opinion is the appropriate remedy for violation of Proposition 218 or Proposition 26.

II. REVIEW IS NECESSARY TO CORRECT SIGNIFICANT ERRORS IN A PUBLISHED APPELLATE DECISION

Although this Court does not grant review merely to correct error, review should be granted to address significant legal errors in a published decision that will bind lower courts and constrain the State and local governments.

A. Proposition 26 Does Not Retroactively Invalidate the PILOT

The Opinion and Dissent agree Proposition 26 is not retroactive. (Opinion at p. 17; Dissent at p. 2, fn. 2.) However, neither correctly characterizes the legislation by which the City adopted the PILOT or identified any reason to treat budgetary resolutions adopting and maintaining a PILOT differently from ordinances or other resolutions. Properly understood, the PILOT was intended to be permanent.

1. Proposition 26 does not apply to earlier legislation

Proposition 26 was adopted November 2, 2010 to amend the California Constitution to provide the first legislative definition of the "taxes" for which voter approval is required by Propositions 13 (art. XIII A, § 4) and 218 (art. XIII C, § 2). Proposition 26 includes a limited retroactivity clause for state taxes, but not for local taxes. (Compare art. XIII A, § 3, subd. (b) with art. XIII C, § 1, subd. (e).) Thus, it lacks the necessary "express language of retroactivity" to overcome the presumption of prospective application. (*Myers v. Philip Morris Co.* (2002) 28 Cal.4th 828, 844; see also *Gikas v. Zolin* (1993) 6 Cal.4th 841, 852 ["*Expressio unius est exclusio alterius*. The expression of some things in a statute necessarily means the exclusion of other things not expressed"].) Accordingly, Proposition 26 applies only to local legislative actions affecting fees, charges and taxes taken on or after November 3, 2010.[9]

Legislative history supports this conclusion. The Impartial Analysis informed voters the measure would apply only prospectively: "[M]ost other fees or charges in existence at the time of the November 2, 2010 election would not be affected unless ... [t]he ... local government later increases or extends the fees or charges." (1 CT 277 [City's RJN, Exh. J].) The argument in favor of

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[9] Constitutional amendments take effect the day after approval. (Art. XVIII, § 4.)

Proposition 26 disclaims any retroactive effect, assuring voters it would have no impact on environmental laws, consumer protection laws, or other public policies. (1 CT 279–280.) The framers apparently feared retroactivity would reduce the likelihood of voter approval. That the voters who narrowly approved Proposition 26 also rejected Proposition 24 to suspend A.B. 32's greenhouse gas law suggests that was an accurate view of voter sentiment.

Thus, both the text and the legislative history of Proposition 26 demonstrate it was not intended to apply retroactively. (*Brooktrails, supra,* 218 Cal.App.4th at pp. 206–207.)

2. Redding's PILOT is prior legislation that survived adoption of the FY 2011–2013 budget

The trial court found the PILOT had been a component of REU's budget for over 20 years when Proposition 26 was adopted in November 2010. (3 CT 736, 739). The trial court also found the December 2010 rate increase did not affect the PILOT, which was funded by other revenues. (3 CT 736–737.) The record supports these findings. (IV AR Tab 163, p. 1041; IV AR Tab 145, p. 831; IV AR Tab 149, p. 873; IV AR Tab 145, p. 831; IV AR Tab 149, p. 873; XIII AR Tab 205, p. 2975.) The trial court concluded the PILOT survives Proposition 26. (See 3 CT 737.)

The Opinion and Dissent agree the PILOT was adopted by legislation and that Proposition 26 does not apply to legislation predating it. (Opinion at p. 19; Dissent at p. 2, fn. 2.) Both the

Opinion and Dissent err, however, in concluding the PILOT expires with each biennial budget.

General law cities like Redding have no duty to adopt a budget at all — much less to do so in any particular form — and one resolution may legislate appropriations limited to a fiscal year, enact permanent fiscal policies like the PILOT, or both. (Gov. Code § 53901 [alternate reporting in absence of budget].) The 1988 adoption of the PILOT by a budget resolution was legislation. (See *Scott v. Common Council* (1996) 44 Cal.App.4th 684, 698 [budget legislation subject to narrow judicial review].)

The canons of statutory construction apply to interpretation of municipal legislation. (*City of San Diego v. Shapiro* (2014) 228 Cal.App.4th 756, 789 [interpreting city charter and Props. 13 and 218]; *C-Y Development Co. v. City of Redlands* (1982) 137 Cal.App.3d 926, 929 [ordinances]; *City and County of San Francisco v. Cooper* (1975) 13 Cal.3d 898, 911 [municipal ordinances and resolutions "are clearly legislative in nature"].) Thus, interpreting Redding's fiscal legislation is an ordinary question of statutory construction that begins with the language of the measure and seeks to accomplish legislative intent. (*People v. Allegheny Casualty Co.* (2007) 41 Cal.4th 704, 708–709.) This the Opinion did not do.

The central task is to ascertain the intent of the City Council to effectuate its purpose. (*Schmeer, supra,* 213 Cal.App.4th at p. 1316.) Legislative intent is evidenced first and foremost by the words of the

legislation — the City's resolutions involving the PILOT. (*Ibid.*; *Renee J. v. Superior Court* (2001) 26 Cal.4th 735, 754.) Only if legislative language is vague or ambiguous may a court consider extrinsic evidence of intent. (*Schmeer, supra,* 213 Cal.App.4th at p. 1317.) In addition, subsequent legislation can — in some circumstances — demonstrate legislative intent. (*Southern California Edison Company v. Public Utilities Commission* (2014) 227 Cal.App.4th 172, 191 [legislative authority for PUC's public goods charge evidenced by subsequent, related legislation which did not displace it].) The question, therefore, is: what did the City Council intend when it adopted the PILOT in 1988 and amended it most recently in 2005 — a temporary fiscal policy or a continuing revenue transfer?

When first adopted in 1988, the PILOT replaced an earlier, ongoing operating transfer. (See I AR 4, pp. 119–124 [Jan. 7, 1987 Finance Director Memorandum]; II AR 37, p. 358, pp. 379–380 ["city's long standing policy of transferring funds from its water, sewer, solid waste and electric systems to the General Fund in amounts characterized as 'In Lieu Taxes.'"]; III AR 111, p. 640 [Jan. 18, 1999 City Attorney Memorandum re: In Lieu Taxes].) As the City implemented the PILOT in every year from 1988 to those litigated here, it periodically acknowledged the PILOT's ongoing effect. (See, e.g. II AR 70, pp. 446–447 [1992 Finance Director memorandum].) These record references demonstrate the City's

understanding that the PILOT is permanent and intended to continue beyond any biennial budget.

The City Council's recognition of the PILOT in every budget since 1988 evidences its intent to maintain the PILOT as ongoing policy. When the Council wished to change the PILOT, it has done so expressly, most recently in 2005. (2 CT 530.) Moreover, it is a fundamental canon of statutory construction that amending part of a law but restating another does not reenact the part restated:

> Where a section or part of a statute is amended, it is not to be considered as having been repealed and reenacted in the amended form. **The portions which are not altered are to be considered as having been the law from the time when they were enacted**; the new provisions are to be considered as having been enacted at the time of the amendment; and the omitted portions are to be considered as having been repealed at the time of the amendment.

(Gov't Code § 9605 (emphasis added); see, e.g., *State Dept. of Public Health v. Superior Court of Sacramento County* (Feb. 19, 2015, Case No. S214679, ___ Cal.4th ___, 2015 WL 690809 at p. *14; *Garat v. City of Riverside* (1991) 2 Cal.App.4th 259, 288 fn. 21[applying rule to local legislation], disapproved on other grounds by *Morehart v. County of Santa Barbara* (1994) 7 Cal.4th 725, 743 fn. 11.)

The City adopted its FY 2011–2013 budget on June 22, 2011 by Resolution No. 2011-111. (XI AR 203, pp. 2466–2469.) This budget is the subject of the second of the mandate actions here. Resolution No. 2011-111 reconfirmed "previously approved legislative direction of the present and former City Councils to employ cost accounting formulas and methodologies carried forward from budget to budget including ... a payment-in-lieu of property tax (PILOT) from the Redding Electric Utility (REU) to the General Fund ... ." (XI AR 203, p. 2466.) This recognizes the PILOT as a continuing legislative act; it does not create it anew. Thus, when Proposition 26 was adopted, the PILOT had been permanent legislation for over 22 years, and it has not since been newly adopted or increased so as to trigger Proposition 26. (Cf. *AB Cellular LA, LLC v. City of Los Angeles* (2007) 150 Cal.App.4th 747 ["a change of administrative methodology" constituted tax "increase" requiring voter approval under Prop. 218].)

The Opinion does not interpret the City's resolutions, but summarily concludes the PILOT expires with each budget. (Opinion at p. 18.) The Opinion supports this conclusion by noting the "record shows changes to the method of calculating the PILOT were made in 1992, 2002, and 2005." (Opinion at p. 18.) However, no law or logic holds that amendments by themselves demonstrate the impermanence of the amended legislation, especially when the expressed intent of the legislative body is to the contrary. By that

standard, nearly every California statute is intended to be temporary because most have been amended since adoption.

Furthermore, the Opinion cites no language from Resolution No. 2009-61 (adopting biennial budget for FY 2009–2011) or Resolution No. 2011-111 (adopting biennial budget for FY 2011—2013) stating the earlier resolution expired or that a later budget repealed and replaced the earlier. The Opinion simply assumes the PILOT is "reenacted" with each budget. (See Opinion at p. 18.) However, as all budget resolutions maintain the same language regarding the PILOT, the Opinion disregards the well-established canon of construction that legislation which readopts prior language is read to continue it, not to reenact it. (See *In re White* (2008) 163 Cal.App.4th 1576, 1581–1582 [unchanged provisions interpreted as continuously in force], citing *Bear Lake & River Waterworks & Irrigation Co. v. Garland* (1896) 164 U.S. 1, 11–12.)

As the trial court correctly recognized, the reenactment theory does not comport with Proposition 26's intent either:

> Proposition 26 was not intended to require an election every time a local government adopts a budget that includes pre-existing components so long as that budget does not impose new or increased fees or charges or change the manner in which those fees are calculated. ... The adoption of Resolution 2011-111 adopting the City of Redding's budget, that included the budget of

REU and the PILOT, does not impose, extend, or increase a tax, and Proposition 26 does not apply.

(3 CT 739.)

The Opinion cites only one case for its reenactment theory — *Barratt American Inc. v. City of Rancho Cucamonga* (2005) 37 Cal.4th 685 — which has been applied by only one other reported case and only in the specific context of land use statutes of limitations. (See *Arcadia Development Co. v. City of Morgan Hill* (2008) 169 Cal.App.4th 253, 261–262.) These cases reflect their statutory contexts and do not abandon the rule that restating legislation continues it rather than legislates it anew.

The Opinion thus renders Proposition 26 retroactive by concluding the viability of a revenue measure depends on the form of legislation which enacted it, rather than legislative intent. This draws an illogical distinction between PILOTs established by budget resolution and those by ordinance or charter provision. The application of Proposition 26 cannot turn on accidents of legislative form, as legislative meaning does not.

3. Retroactive invalidation of Redding's PILOT imperils other legislation

The Opinion suggests the PILOT would survive Proposition 26 if it had been enacted by ordinance, but articulates no standard for other forms of legislation that survive it. Thus, the State and local governments cannot know whether Proposition 26

retroactively invalidates other rate components that reflect earlier legislative concern for issues other than service cost. For example, as noted above, the Opinion threatens REU's discounted rates for the poor and the elderly — as well as a wide variety of public goods charges. (IV AR Tab 142, p. 817; IV AR Tab 145, p. 830; IV AR Tab 148, pp. 869–870.) Although many of these costs are imposed by statute, and presumably satisfy the Opinion's standard for legislative permanence, the Opinion does not confirm that safe harbor or provide logic for it. Thus the Opinion invites additional litigation, as rate challengers seek to identify which legislative forms are permanent and which transitory.[10]

Moreover, while local legislation governing the public is typically adopted by ordinance to facilitate enforcement, internal governance policies — like budgets — are often adopted by resolution. Yet the Opinion suggests the Council was required to predict the coming of Proposition 26, and to use a specific form of legislation to enact and amend its PILOT to survive the measure.

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[10] The Public Utilities Commission interpreted Proposition 26 narrowly to allow its own pre-Proposition 26 Electric Program Investment Charge — which replaced A.B. 1890 after the sunset of that public goods charge legislation — to survive Proposition 26. (CPUC Decision 13-01-016 at 3–4.)

Surely these important policy choices cannot depend on an accident of form and a failure of such unlooked-for prescience.

The law has long held the intent of the legislative body governs legislative construction and adherence to that rule here would avoid these consequences, and would allow current laws and policies affecting public utility rates to remain in place until those laws change.

B. The PILOT Complies with Proposition 26

As the trial court found, the PILOT was intended to defray the costs to the City for the use of its rights of way, police and fire protection of utility assets, and other services and benefits the City provides REU and to avoid penalizing the general fund for the City's decision to municipalize electric service. (See 3 CT 736; II AR Tab 37, p. 358.) Thus the City established the PILOT to approximate the 1% tax an investor-owned utility pays for the same benefits. Such transfers were common when the Redding City Council first adopted the PILOT in 1988. (See I AR Tab 4, pp. 119–124; I AR Tab 5, pp. 133–135.) As Justice Duarte concluded in her Dissent, the PILOT's purpose and rate are reasonable as a matter of law. (Dissent at p. 2.)

Furthermore, even if the PILOT were newly established, the mere existence of the PILOT does not mean REU's retail electric rates exceed the cost of service and therefore constitute taxes under Proposition 26. As the trial court found, "there is no evidence that

that the PILOT is paid out of customers' rates." (3 CT 741.) This is because REU has multiple sources of revenue, including:

- The challenged retail rates;
- proceeds of wholesale transactions, the prices of which no one has challenged and which are not "imposed" so as to be subject to Proposition 26;
- interest on investments; and
- grants and donations.

(IV AR Tab 145, p. 831; XIII AR Tab 205, p. 2975.)

It is undisputed that REU's non-retail sources of revenue exceed the PILOT by more than three times. (XIII AR Tab 205, p. 2975; XIII AR Tab 205, p. 2975.) Therefore, even if REU's compliance with the PILOT is not a cost of service that may be funded by rates, the PILOT nevertheless survives Proposition 26 because it is funded by non-rate revenues.

Finally, the trial court's findings that the December 2010 rate increase neither funded nor affected the PILOT are supported by the record and Appellants offered nothing to contradict them. The Opinion acknowledges this finding of fact and provides no factual or legal rebuttal, but merely overrules it. (See Opinion at p. 14.) The Opinion therefore erred in reaching a contrary conclusion without support in the record or in law. Review is warranted to correct this error in a published appellate decision addressing these issues of statewide concern for the first time.

CONCLUSION

This case merits review to resolve the retroactive application of Proposition 26 to local legislation, the application of Propositions 218 and 26 to wholesale market transactions, interpretation of the "reasonable cost of service" standard common to both Propositions 218 and 26, and appropriate remedies for violation of those measures. Moreover, many pending disputes in lower courts will benefit from review here, which would provide guidance on issues of concern to the State, all local governments, the 38 million Californians they serve and those who litigate public finance issues. For all these reasons, the City respectfully submits that this case warrants review.

DATED: March 2, 2015

COLANTUONO, HIGHSMITH & WHATLEY, PC

MICHAEL G. COLANTUONO
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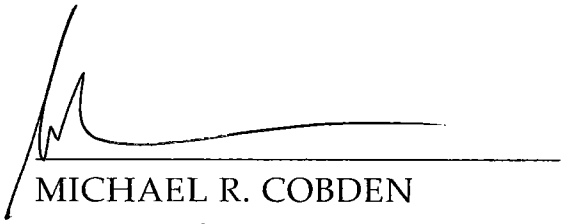
Attorneys for Petitioner
CITY OF REDDING

CERTIFICATION OF COMPLIANCE WITH CAL. RULES OF COURT, RULE 8.504(D)

Pursuant to Rule 8.504, subdivision (d) of the California Rules of Court, the foregoing Petition for Review contains 7,861 words (including footnotes, but excluding the tables and this Certification) and is within the 8,400 word limit set by the rule. In preparing this Certification, I relied upon the word count generated by Microsoft Word 2010.

DATED: March 2, 2015

COLANTUONO, HIGHSMITH & WHATLEY, PC



MICHAEL R. COBDEN
Attorneys for Petitioner
CITY OF REDDING

ATTACHMENT 1

(Cal. Rules of Court, rule 8.204(d))

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

(Shasta)

CITIZENS FOR FAIR REU RATES et al.,

Plaintiffs and Appellants,

v.

CITY OF REDDING et al.,

Defendants and Respondents.

C071906

(Super. Ct. Nos. 171377, 172960)

APPEAL from a judgment of the Superior Court of Shasta County, William D. Gallagher, Judge. Reversed with directions.

McNeill Law Offices and Walter P. McNeill for Plaintiffs and Appellants.

Colantuono & Levin, Colantuono, Highsmith & Whatley, Michael G. Colantuono, Amy C. Sparrow and Michael R. Cobden for Defendants and Respondents

Braun Blaising McLaughlin Smith, C. Anthony Braun and Justin C. Wynne for California Municipal Utilities Association as Amicus Curiae on behalf of Defendants and Respondents; Jarvis, Fay, Doporto & Gibson, Benjamin P. Fay and Rick W. Jarvis for League of California Cities and the California State Association of Counties as Amicus Curiae on behalf of Respondent, City of Redding.

California voters adopted Proposition 13 in 1978 (Cal. Const., art XIII A, added by Prop. 13, as approved by voters, Primary Elec., June 6, 1978)[1] to require -- among other constitutionally implemented tax relief measures -- that any "special taxes" for cities, counties, and special districts be approved by two-thirds of voters. (Art. XIII A, § 4.) In 1996, voters adopted Proposition 218 (art. XIII D, added by Prop. 218, as approved by voters, Gen. Elec., Nov. 5, 1996 (Proposition 218)), with one of its aims being "to tighten the two-thirds voter approval requirement for 'special taxes' and assessments imposed by Proposition 13." (*Brooktrails Township Community Services Dist. v. Board of Supervisors of Mendocino County* (2013) 218 Cal.App.4th 195, 197 (*Brooktrails*).) To this end, Proposition 218 added article XIII C to require that new taxes imposed by a local government be subject to two-thirds vote by the electorate. (Art. XIII A, § 4; art. XIII C, § 1, as approved by voters, Gen. Elec., Nov. 5, 1996; see also 2B West's Ann. Cal. Codes (2013) pp. 362-363.) Article XIII C was amended by the voters in 2010 when they passed Proposition 26. (Art. XIII C, § 1, amended by Prop. 26, as approved by voters, Gen. Elec., Nov. 2, 2010 (Proposition 26).)

Proposition 26 added subdivision (e) to section 1 of article XIII C, broadly defining "tax" to include "any levy, charge, or exaction of any kind imposed by a local government." (Art. XIII C, § 1, subd. (e).) Subdivision (e) incorporated seven exceptions to this definition of tax. (*Ibid.*) The second exception is the subject of this appeal and provides that "tax" does not include "[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.*" (Art. XIII C, § 1, subd. (e)(2), italics added.) Section 1 of article XIII C further provides that "[t]he local government bears the burden of

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1 Undesignated references to articles are to the California Constitution.

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. XIII C, § 1 [last para.].)

This case calls us to consider whether Proposition 26 applies to a practice by the City of Redding (Redding) of making an annual budget transfer from the Redding Electrical Utility (Utility) to Redding's general fund. Because the Utility is municipally owned, it is not subject to a one percent ad valorem tax imposed on privately owned utilities in California. (Art. XIII, § 3, subd. (b), adopted by voters, Gen. Elec., Nov. 5, 1974.) However, the amount transferred between the Utility's funds and the Redding general fund is designed to be equivalent to the ad valorem tax the Utility would have to pay if privately owned. Redding describes the annual transfer as a payment in lieu of taxes (PILOT). The PILOT is not set by ordinance, but is part of the Redding biennial budget.

Plaintiffs in this case (Citizens for Fair REU Rates, Michael Schmitz, Shirlyn Pappas, and Fee Fighter LLC) challenge the PILOT on grounds it constitutes a tax for which article XIII C requires approval by two-thirds of voters. Redding responds the PILOT is not a tax, and if it is a tax, it is grandfathered-in because it precedes the adoption of Proposition 26.

We conclude the PILOT constitutes a tax under Proposition 26 for which Redding must secure two-thirds voter approval unless it proves the amount collected is necessary to cover the reasonable costs to the city to provide electric service. We reject Redding's assertion the PILOT is grandfathered-in by preceding Proposition 26's adoption. As a budget line item, the PILOT is subject to annual discretionary reauthorization by Redding's city council. The PILOT does not escape the purview of Proposition 26

because it is a long-standing practice.[2] Because the trial court concluded the PILOT was reasonable as a matter of law, we reverse and remand for an evidentiary hearing in which Redding has the opportunity to prove the PILOT does not exceed reasonable costs under article XIII C, section 1, subdivision (e)(2).

BACKGROUND

Redding's PILOT

The facts of this case are undisputed.[3] Redding owns a municipal utility to provide electric service for residents and commercial businesses within the city. The Utility owns property to generate and transmit electricity. This municipally owned property is not subject to taxation. (See generally, art. XIII, § 3, subd. (b).)

In 1987, Redding's director of finance proposed a PILOT to transfer funds from the Utility to the city's general fund. The director of finance noted 17 other cities regularly made PILOT transfers and a PILOT in Redding "would generate $1,531,622.45 for the General Fund." However, the proposal included a cautionary statement contained in a legal advisory letter to the Northern California Power Agency, a consortium of municipal electric utilities including Redding's Utility. The legal advisory letter concluded that so long as the internal fund transfer had a rational basis or was equal to or less than market rates, there was little risk of invalidation. However, the letter also warned of "a real possibility that rates which produce revenues in excess of cost of

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2 PILOTs are not uncommon among California municipalities. (See, e.g., *Howard Jarvis Taxpayers Assn. v. City of Fresno* (2005) 127 Cal.App.4th 914, 917 (*Fresno*) [noting PILOTs used in Fresno since 1957 charter provision and 1967 ordinance].) We do not consider or address the validity of any PILOT other than the one presented in this case.

3 Given the undisputed nature of the facts and sufficiency of the appellate record, we deny all pending motions for judicial notice.

service will require a two thirds vote of the affected electorate to be valid under Propositions 13 and 62, or that such excess revenues will be subjected to the expenditure limitations of Proposition 4."

Redding adopted the PILOT in 1988.

As noted above, California voters adopted Proposition 26 in the general election November 2, 2010. The next month, in December 2010, Redding passed a resolution (No. 2010-179) increasing electric rates by 7.84 percent effective January 2011, and an additional 7.84 percent effective December 2011. There is no line item in the electric bills sent to the Utility's customers that reflects the PILOT.

The First Action

On February 4, 2011, plaintiffs filed a petition for writ of mandate and complaint for declaratory and injunctive relief. Plaintiffs' first petition and complaint focused on Resolution No. 2010-179, which the Redding City Council passed in December 2010 to increase the Utility's rates. One of the stated purposes for the Resolution was "to obtain funds necessary to maintain such intra-City transfers as authorized by law." Plaintiffs alleged the new rates incorporated the PILOT charge (about $6,000,000), which did not reflect "any particular costs or expenses incurred" to provide electric service, but was "purely extra revenue." They alleged that because the PILOT was an invalid tax, the rate increase calculated based on the PILOT was also invalid. Plaintiffs asserted the PILOT is an unlawful tax that is "in excess of the reasonable cost of providing services, due to the unlawful incorporation of the PILOT charge and transfer to [Redding]'s general fund."

Redding demurred, raising three general claims: First, Proposition 26 was not retrospective and therefore did not apply to any aspect of the PILOT charge; second, utility rates were not "imposed" because anybody was free to provide their own electricity rather than pay the Utility for a supply; third, a utility charge was not a "tax"

within the meaning of Proposition 62.[4] The trial court denied the demurrer and the case proceeded to a bench trial.

The trial court denied the first petition based on its conclusion the PILOT charge predated and therefore was immune from a Proposition 26 challenge. "The PILOT was an established cost that was not increased or affected by the adoption of Resolution 2010-179 [raising rates]. As the rate increases did not increase the PILOT, the Court finds that the Resolution did not impose or increase any tax, and therefore did not require voter approval."

The Second Action

On August 29, 2011, plaintiffs filed a second complaint, seeking a declaration that a new two-year budget adopted on June 22, 2011, violated Proposition 26. The Redding City Council passed Resolution No. 2011-111 to adopt the biennial budget for the fiscal years ending June 30, 2010, and June 30, 2011. The Resolution explains that "the City Council has approved continuation of the PILOT in every budget since 1988-89. Upon adoption of the [fiscal year] 1992-1993 budget, the City Council amended the PILOT to include the value of capital improvement projects undertaken during the budget year in the asset base to which the 1% [PILOT] is applied. Upon adoption of the [fiscal year] 2002-2003 budget, the City Council further revised the PILOT to adjust the value of assets for inflation in the calculation of the PILOT. Upon adoption of a two-year budget in June 2005, the City Council amended the PILOT into its current form by including the value of joint-venture assets in which [the Utility] has a share in the asset base to which the 1% [PILOT] is applied. The City's practice is to estimate the value of the assets over

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[4] Proposition 62 "is a statutory initiative adopted by the voters at the 1986 General Election. It added a new article to the Government Code (§§ 53720–53730) requiring that all new local taxes be approved by a vote of the local electorate." (*Santa Clara County Local Transportation Authority v. Guardino* (1995) 11 Cal.4th 220, 231.)

the life of a two-year budget and to calculate the PILOT based on that estimate and to correct any variance between the PILOT calculated for the last two-year budget and the actual asset value experienced in that time. Estimates are necessary because the PILOT formula: (i) includes capital projects to be completed in the two future years covered by a [PILOT] and (ii) uses an estimate of inflation during that time." Thus, Redding's biennial budget incorporated "a marked increase" in the PILOT that was "due to the addition of the Unit Six generator . . . ."

Consolidation and Trial Court Decision

By stipulation, the trial court consolidated the two actions. The trial court then issued a memorandum of decision in favor of Redding. The trial court concluded the PILOT transfer was not a new, increased, or extended tax under Proposition 26, and therefore was grandfathered-in. After reaching this conclusion, the trial court went on to address additional issues. In this part of the decision, the trial court also found that "even if" the PILOT fell within Proposition 26's ambit, it could reasonably be argued the PILOT reflected a reasonable cost of providing electric service.

Plaintiffs timely appealed from the ensuing judgment for Redding.

DISCUSSION

I

Proposition 26's Application to Redding's PILOT

We begin by considering whether the PILOT constitutes a tax under Proposition 26. If the PILOT is not a tax under Proposition 26, there is no need to consider whether it is grandfathered-in. Plaintiffs contend the PILOT is a tax because it is not based on any calculation of reasonable costs to Redding for providing electric service. In support, plaintiffs note the PILOT is intended to replicate the tax that would be imposed if the Utility were privately owned.

A.

Standard of Review

The question of "whether impositions are 'taxes' or 'fees' is a question of law for the appellate courts to decide on independent review of the facts." (*Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 874 (*Sinclair Paint*).) Consequently, our review affords no deference to the trial court's conclusions of law. We are, however, not rudderless in our inquiry into the applicability of Proposition 26 to the PILOT in this case. Instead, we aim to construe Proposition 26 to discern the intent of the voters who adopted the initiative. " 'In interpreting a voter initiative . . . , we apply the same principles that govern statutory construction. (See *Horwich v. Superior Court* (1999) 21 Cal.4th 272, 276 (*Horwich*).) Thus, "we turn first to the language of the statute, giving the words their ordinary meaning." (*People v. Birkett* (1999) 21 Cal.4th 226, 231 (*Birkett*).) The statutory language must also be construed in the context of the statute as a whole and the overall statutory scheme [in light of the electorate's intent]. (*Horwich, supra*, 21 Cal.4th at p. 276, [280].) When the language is ambiguous, "we refer to other indicia of the voters' intent, particularly the analyses and arguments contained in the official ballot pamphlet." (*Birkett, supra*, 21 Cal.4th at p. 243.)' (*People v. Rizo* (2000) 22 Cal.4th 681, 685 (*Rizo*).) [¶] In other words, our 'task is simply to interpret and apply the initiative's language so as to effectuate the electorate's intent.' (*Hi–Voltage Wire Works, Inc. v. City of San Jose* (2000) 24 Cal.4th 537, 576 (*Hi–Voltage*) (conc. & dis. opn. of George, C.J.).)" (*Robert L. v. Superior Court* (2003) 30 Cal.4th 894, 900-901.)

B.

Taxes, Fees, and Exceptions under Proposition 26

Determining whether a levy, charge, or exaction qualifies as a tax or fee often presents a subtle question. As the California Supreme Court has observed, "cases recognize that 'tax' has no fixed meaning, and that the distinction between taxes and fees

is frequently 'blurred,' taking on different meanings in different contexts. (*Russ Bldg. Partnership v. City and County of San Francisco* [(1987)] 199 Cal.App.3d [1496,] 1504; *Terminal Plaza Corp. v. City and County of San Francisco* (1986) 177 Cal.App.3d 892, 905; *Mills v. County of Trinity* (1980) 108 Cal.App.3d 656, 660; *County of Fresno v. Malmstrom* (1979) 94 Cal.App.3d 974, 983–984.) In general, taxes are imposed for revenue purposes, rather than in return for a specific benefit conferred or privilege granted. (*Shapell Industries, Inc. v. Governing Board* (1991) 1 Cal.App.4th 218, 240; *County of Fresno v. Malmstrom, supra*, 94 Cal.App.3d at p. 983 ['Taxes are raised for the general revenue of the governmental entity to pay for a variety of public services'].) Most taxes are compulsory rather than imposed in response to a voluntary decision to develop or to seek other government benefits or privileges. (*Shapell Industries, Inc. v. Governing Board, supra*, 1 Cal.App.4th at p. 240; *Russ Bldg. Partnership v. City and County of San Francisco, supra*, 199 Cal.App.3d at pp. 1505–1506; see *Terminal Plaza Corp. v. City and County of San Francisco, supra*, 177 Cal.App.3d at p. 907.) But compulsory fees may be deemed legitimate fees rather than taxes. (See *Kern County Farm Bureau v. County of Kern* (1993) 19 Cal.App.4th 1416, 1424.)" (*Sinclair Paint, supra*, 15 Cal.4th at p. 874.)

In contrast to taxes that serve to raise general revenue, fees " 'do not exceed the reasonable cost of providing services necessary to the activity for which the fee is charged and which are not levied for unrelated revenue purposes.' " (*Apartment Assn of Los Angeles County, Inc. v. City of Los Angeles* (2001) 24 Cal.4th 830, 843, quoting *Sinclair Paint, supra*, 15 Cal.4th 866, 876 [collecting authority].) A levy, charge, or exaction cannot be considered a fee if "the amount of the fees [bears] no reasonable relationship to the social or economic 'burdens' its operations generated." (*Apartment Assn, supra*, at p. 881.)

The issue of whether the PILOT in this case constitutes a tax or a fee arises only after the adoption of Proposition 26 because Proposition 218 previously excluded fees for gas and electrical service from the voter approval requirement. (Compare art. XIII C, § 1, subd. (e) [definition of "tax" to include "*any* levy, charge, or exaction of any kind imposed by a local government" added by Proposition 26, italics added], with art. XIII D, § 3, subd. (b) [Proposition 218's exemption of electrical and gas service from its provisions].)

Proposition 26 was intended to address taxes disguised as fees. As pertinent to this case, Proposition 26's findings and declaration of purpose state: "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. . . . [¶] . . . [¶] (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 exact 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 . . . 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.' " (Prop. 26, § 1, subds. (b), (c), (e), (f), reprinted at Historical Notes, 2B West's Ann. Cal. Codes (2013) foll. art. 13A, § 3, pp. 296-297; see also *Roseville*, *supra*, 97 Cal.App.4th at p. 645, fn. 17 [noting courts may use ballot summary, arguments, and analysis to construe voter-approved initiatives].)

In short, the question of whether Redding's PILOT constitutes a tax under Proposition 26 turns on whether the PILOT serves to raise general revenue or reflects the reasonable costs to the city to provide electric service.

More specifically, for purposes of this case, whether the PILOT constitutes a tax within the meaning of section 1, subdivision (e), of article XIII C turns on whether the exception in article XIII C, section 1, subdivision (e)(2), applies. This exception asserted by Redding pertains to "[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." The adoption of Proposition 26 shifted the burden of proof regarding the exception's applicability to the local government. (Art. XIII C, § 1, [last para.]) The last paragraph of article XIII C, section 1, provides: "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."

C.

Redding's PILOT

Because the Utility is municipally owned, Redding imposes the PILOT to collect the same amount as would be due under the ad valorem tax on privately owned utilities. Throughout its history, the PILOT has been measured against the ad valorem tax. The PILOT has been adjusted to keep it equivalent to the ad valorem tax. It has not been designed to approximate the reasonable costs of providing electric service in Redding.

The PILOT is calculated as a flat percentage of the Utility's assets. As a flat percentage, the PILOT in this case resembles the in-lieu payment reviewed by this court

in *Howard Jarvis Taxpayers Assn v. City of Roseville* (2002) 97 Cal.App.4th 637 (*Roseville*). In *Roseville*, we considered a challenge to an in-lieu payment at a flat four percent of the annual budgets of three of Roseville's municipal utilities that provided water, sewer, and garbage collection. (*Id.* at p. 648.) In considering the constitutional validity of the in-lieu payment, we acknowledged that "[o]f course," the city could recoup "what it costs to provide such services includ[ing] all the required costs of providing service, short-term and long-term, including operation, maintenance, financial, and capital expenditures." (*Id.* at pp. 647-648.) Even so, we concluded the "fee does not represent costs. It is a flat fee. It is imposed on the utilities' budgets, presumably after their total costs have been accounted for in the budget process. If the budget of a utility increases because of a cost increase unrelated to the in-lieu fee, the in-lieu revenues, as a flat percentage of that increased budget, increase as well. The in-lieu fee is the same percentage applied to each budget, regardless of varying uses of streets, alleys and rights-of-way by the individual utilities. It cannot be said that this flat fee on budgets coincides with these costs." (*Id.* at p. 648.) Like the in-lieu payment at issue in *Roseville*, Redding's PILOT is a flat percentage of the Utility's assets.

The revenues generated by the PILOT are transferred to Redding's general fund. In *Roseville*, the in-lieu payment violated Proposition 218 because the " '[r]evenue from the in[-]lieu franchise fee is 'placed in [Roseville's] general fund to pay for general governmental services. It has not been pledged, formally or informally[,] for any specific purpose.' " (*Id.* at p. 650.) This practice ran "afoul of section 6(b)(2) that '[r]evenues derived from the fee or charge shall not be used for any purpose other than that for which the fee or charge was imposed.' It also contravene[d] section 6(b)(5) that '[n]o fee or charge may be imposed for general governmental services. . . .' " (*Roseville,* at p. 650.) Here, as in *Roseville*, the transfer of the in-lieu payment into the general fund provides

additional support for the conclusion that the payment constitutes a revenue-generating tax.

Redding argues Proposition 26 does not apply because the Utility's rates (including the PILOT component) are not "imposed." Redding reasons that "[e]ven if the PILOT were funded by [electric] rates, no force or authority is involved here -- those who wish to buy energy from [the Utility] pay the PILOT (and other costs argued to be funded by [the Utility's] service rates) only to the extent they use its service. Those who obtain energy in other ways do not. [There are] other alternatives to electric utility service (such as solar, water, wind and geothermal power) . . . ." The trial court rejected the argument, pointing out that while "legally [the Utility] has no monopoly as an electric utility, the reality is that for many people there are no economically viable alternatives. The Court used the example of a tenant who is renting a house or apartment that is served by [the Utility]. While theoretically possible that a tenant who does not wish to use [the Utility] could install an alternate power source, that is simply not a realistic option." We agree. A tax does not lose its revenue-generating character because there is a theoretical but unrealistic way to escape from the tax's purview. The PILOT was imposed under Redding's authority to generate revenue for its general fund.

We also reject Redding's argument that the PILOT was never "imposed" by "force or authority" because the one percent levy was collected in customer bills for electric service. For guidance, we turn to the instructive case of *Howard Jarvis Taxpayers Assn v. City of La Habra* (2001) 25 Cal.4th 809, 823 (*La Habra*). In *La Habra*, the California Supreme Court considered the question of when a tax on utility rates is "imposed." (*Id.* at p. 818.) The city argued the tax was not imposed until the voters approved the levy. (*Id.* at pp. 817-818.) The Supreme Court rejected the proposition that "when a city disregards the approval requirement in imposing a tax, the imposition has never happened and thus may not be challenged." (*Id.* at p. 818.) The *La Habra* court held Proposition

62, which added voter-approval requirements for local taxes, "prohibited the imposition of a general tax 'unless and until such general tax is submitted to the electorate.' (Gov. Code, § 53723.) That command is allegedly violated *each time the City collects its utility tax through the service providers*." (*La Habra*, at p. 823, italics added.) The same reasoning applies here. That the PILOT in this case may be collected through electric service bills does not by itself render Proposition 26 inapplicable.

Redding next argues the PILOT "is a pre-existing legal obligation of [the Utility] and could therefore be funded from rates."[5] In support, Redding notes the Utility's "non-retail revenue is more than three times the amount of the PILOT." This argument seemed to be persuasive to the trial court, which concluded the Utility "has non-rate revenues that exceed the amount of the PILOT, therefore, there is no evidence that the PILOT is paid out of customer's rates." We reject this reasoning. That the Utility has other sources of income is not dispositive. The gravamen of the problem is that, regardless of what else Redding might collect from certain customers, it has imposed a PILOT -- which it may do only with voter approval or if able to show it reflects Redding's reasonable costs of providing electric service.

The PILOT is also not saved from being a disguised tax simply because it is not separately listed on the Utility customers' electric bills. A municipal payment in lieu of taxes was held to violate Proposition 218 even though the in-lieu payment was not separately listed in the utility bills challenged in *Howard Jarvis Taxpayers Assn v. City of Fresno* (2005) 127 Cal.App.4th 914. *Fresno* involved a taxpayer lawsuit that focused on the rates charged by the city's municipal utilities. (*Id.* at p. 917.) By ordinance, the City of Fresno "required each municipal utility to 'pay to the City, in lieu of property and

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5 We address the issue of whether the PILOT precedes the adoption of Proposition 26 in part II, *post*.

other taxes normally placed upon private business,' an amount designated by the council in a master fee resolution. (Fresno Mun. Code, § 4–803.) The fee [was] 1 percent of the assessed value of fixed assets of the utility department or division." (*Id.* at p. 917.) "The overall amount of the in lieu fee [was] 'blended' into the user fees (in a manner not disclosed by the record), so that, for example, a water bill contain[ed] only a single amount due for service; the pass-through of the in lieu fee [was] not separately reflected on the bill. According to the budget of Fresno for the fiscal year 2003–2004 . . . in lieu fees var[ied] as a percentage of the utility divisions' operating budgets, ranging up to 9 percent of the water division's budget and 11 percent of the wastewater division's budget." (*Id.* at p. 918.) The *Fresno* court noted even after Proposition 218, "[c]ities are still entitled to recover all of their costs for utility services through user fees." (*Id.* at p. 922.) "The manner in which they may do so, however, is restricted by another portion of Proposition 218: 'The amount of a fee or charge imposed . . . shall not exceed the proportional cost of the service attributable to the parcel.' (Art. XIII D, § 6, subd. (b)(3).)" (*Fresno,* at pp. 922-923.) Thus, the *Fresno* court held the city needed to "reasonably determine" the "unbudgeted costs of utilities enterprises and that those costs be recovered through rates proportional to the cost of providing service to each parcel" if it chose to charge the in-lieu payment. (*Id.* at p. 923.) In so holding, the *Fresno* court recognized: "Undoubtedly this is a more complex process than the assessment of the in lieu fee and the blending of that fee into the rate structure. Nevertheless, such a process is now required by the California Constitution." (*Id.* at p. 923.)

Despite Redding's insistence it could cover the PILOT costs with non-retail income, the city protests the PILOT is necessary to comply with such costs to the Utility as green power mandates (Pub. Util. Code, § 2854), other renewable energy mandates (*id.* at §§ 399.11, 739.2 & 739.4), and Redding's "pre-Proposition 26 policy requiring discounted power for low-income and senior households." Nothing in Proposition 26

prevents the Utility from recouping its expenses. To the contrary, Proposition 26 expressly excepted from the definition of taxes any charge that "does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege." (Art. XIII C, § 1, subd. (e)(1).) Neither Redding nor its Utility is restrained from recovering the reasonable costs of electricity production and distribution.

Nor is the Utility required to charge a flat rate to all customers to prevent discounted power to low-income and senior households. Variable rate plans, such as for municipal delivery of water, have been upheld against challenge under Proposition 13. (*Brydon v. East Bay Mun. Utility Dist.* (1994) 24 Cal.App.4th 178.) In *Brydon*, a municipal water district imposed a variable rate structure for which the price increased with consumption. This price "structure of the District [was] a response to state mandated water resource conservation requirements." (*Id.* at p. 192.) Even though a rate varied among customers, the *Brydon* court rejected a challenge to the increased payment for greater consumption as a tax for which voter approval was necessary. *Brydon* holds the voter approval requirement "does not apply to every regulatory fee simply because, as applied to one or another of the payor class, the fee is disproportionate to the service rendered." (*Id.* at p. 194.) Thus, the fact that customers of the Utility in this case might pay more because of renewable energy mandates, or some rates might subsidize low-income households, does not violate Proposition 26. However, Proposition 26 prohibits the PILOT from increasing the bill of customers by the same amount as the ad valorem tax on private utilities without voter approval or showing it reflects reasonable costs to the city.

Accordingly, we conclude the PILOT constitutes a tax under Proposition 26 unless Redding proves the amount collected is necessary to cover the reasonable costs to the city to provide electric service. (Art. XIII C, § 1, subd. (e).) We consider whether any portion of the "reasonable costs" exception provided by article XIII C, section 1,

subdivision (e)(2), exempts the PILOT from the voter approval requirement for taxes in part III, *post*.

II

Whether Redding's PILOT is "Grandfathered-in"

We turn to the question of whether the PILOT preexisted the adoption of Proposition 26. Proposition 26 has no retrospective effect as to local taxes that existed prior to November 3, 2010. (*Brooktrails, supra,* 218 Cal.App.4th at pp. 205-207.) However, the parties disagree on whether the PILOT in this case existed prior to the adoption of Proposition 26. Redding contends the PILOT is a set fixture of the Redding budget that is grandfathered-in, i.e., escapes the applicability of Proposition 26 as a preexisting levy. Plaintiffs respond the PILOT is a component of the electric rates that is transferred to the general fund in Redding's biennial budget and is subject to recurring discretionary adoption and adjustment. As we explain, the PILOT may be a familiar part of the Redding biennial budget, but it has not been fixed by ordinance or any other authority. Being subject to the Redding City Council's recurring discretion, it is not grandfathered-in under Proposition 26.

A.

The Trial Court's Retroactivity Finding

There is no dispute the PILOT has not been implemented by ordinance or other law. Indeed, Redding explains that "City staff calculates the PILOT with each budget according to the formula adopted by the City Council. [Citations.] Because the formula relies on estimates, the PILOT is 'trued up' with the adoption of the budgets in odd-numbered years to correct estimates for the previous biennium."

Moreover, the formula itself is periodically adjusted. The trial court found the PILOT's formula has been "refined in 1992, 2002, and 2005." The most notable "refine[ment]" to the PILOT was made in the 2001-2003 budget to "bring it in line with

the State Board of Equalization property tax calculation methodologies." However, it appears undisputed that the PILOT has been adjusted to equate as nearly as practicable to the tax a private utility would have to pay Redding in ad valorem taxes.

Despite the period adjustments in the Redding budgeting process, the trial court dismissed plaintiffs' challenges on the rationale that the PILOT had been grandfathered-in. The trial court reasoned that "Proposition 26 was not intended to require an election every time a local government adopts a budget that includes pre-existing components so long as that budget does not impose new or increased fees or charges or change the manner in which those fees are calculated. The adoption of Resolution 2011-111 adopting the City of Redding's budget, that included the budget of REU and the PILOT does not impose, extend, or increase a tax, and Proposition 26 does not apply." (Fn. omitted.)

B.

Adoption of PILOT in the Budgetary Cycle

Each budget is a discretionary legislative act made by each city council. (See *Scott v. Common Council* (1996) 44 Cal.App.4th 684, 690-694; *County of Butte v. Superior Court* (1985) 176 Cal.App.3d 693, 698.) The broad legislative discretion with which a city council is imbued stands in contrast to a tax or fee fixed by ordinance. In this case, each PILOT transfer represented a readoption in the discretion of each city council. Indeed, the record shows changes to the method of calculating the PILOT were made in 1992, 2002, and 2005. Consequently, the PILOT cannot be deemed to be grandfathered-in as preceding the 2010 adoption of Proposition 26. (Cf. *Barratt American Inc. v. City of Rancho Cucamonga* (2005) 37 Cal.4th 685 [discussing the "reenactment rule" in a different statutory context]; *Arcadia Development Co. v. City of Morgan Hill* (2008) 169 Cal.App.4th 253, 262-266; see also *La Habra, supra,* 25 Cal.4th at p. 825 ["Cities and counties must eventually obey the state laws governing their taxing

authority and cannot continue indefinitely to collect unauthorized taxes"]; *Advance Medical Diagnostic Laboratories v. County of Los Angeles* (1976) 58 Cal.App.3d 263, 269 [longtime government custom "even if conducted in the best of faith will not make legal what is illegal"].)

The PILOT's regular appearance in Redding's budgetary process does not mean it was a permanent or continuing transfer compelled by ordinance or other non-discretionary authority. As a recurring discretionary part of the Redding biennial budget, the PILOT cannot be said to precede or be grandfathered-in under Proposition 26. And, the PILOT also cannot be said to be the product of legislation for which Proposition 218 provided a savings clause to allow "fees and charges" to be brought into compliance by a certain date. Although Propositions 26 and 218 stand in pari materia -- namely they relate to the same subject (*People v. Honig* (1996) 48 Cal.App.4th 289, 327) -- nothing in either statute grandfathers in the PILOT simply because it has been a customary recurrence in the Redding municipal budget.

As to the two-year budget adopted by Redding on June 11, 2009, we conclude the included PILOT was grandfathered-in because budget adoption preceded the voters' approval of Proposition 26.[6] Even though the PILOT in the 2009-approved Redding budget did not expire until 2011, the PILOT for this budget was not subject to Proposition 26. To the extent Redding continued to collect the PILOT *as authorized in 2009*, Redding does not need to cost justify the PILOT. Nonetheless, the December 7, 2010 increase of the PILOT by Redding does require cost justification under Proposition 26. Rather than being the continuation of a grandfathered-in rate, the December 2010

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[6] Proposition 26 took effect on November 3, 2010, the day after being approved by the voters. (*Brooktrails, supra,* 218 Cal.App.4th at p. 205; 2B West's Ann. Cal. Codes (2013), Credits foll. art. XIII C, § 1, at p. 363.)

increase of the PILOT constitutes a tax under Proposition 26 unless Redding proves the amount collected represents its reasonable costs to provide electric service. Thus, Redding must cost justify the PILOT collected under the 2009 two-year Redding budget to the extent that additional funds were collected based on the December 7, 2010 rate increase.

The PILOT included in the two-year budget adopted by Redding on June 22, 2011, was not grandfathered-in because it was adopted after Proposition 26 became effective in 2010.

III

Is Redding's Pilot a Reasonable Cost?

Proposition 26 gives the local government the opportunity to prove the levy, charge, or exaction amounts to "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. XIII C, § 1 [last para.].) Consequently, we turn to the issue of whether the PILOT reflects Redding's reasonable costs of providing electrical service.

A.

Trial Court Decision

Although Redding is entitled to prove the PILOT reflects only reasonable costs of electric service (Art. XIII C, § 1, subd. (e)), the question arises whether that factual issue has been resolved in this case. We requested supplemental briefing to clarify a portion of the trial court's decision that seemingly makes the finding the PILOT reflected a reasonable cost of providing electric service.

The pertinent portion of the trial court decision falls under the heading, "Additional Issues" for which the court explained: "While not essential to the analysis

and the above conclusion [that grandfathering exempted the PILOT from Proposition 26's purview], the Court finds that the following comments warrant inclusion in a discussion of the issues that came before the Court." Among these, the trial court included a discussion of whether the PILOT reflected the reasonable costs to Redding for providing electric service. The trial court stated:

"Even if the PILOT were part of the utility rates charged to ratepayers, it could reasonably be argued that the PILOT is part of the costs of providing the service. All business enterprises have costs and expenses that are a cost of doing business or a cost of providing the service or product. All businesses are required to pay taxes. Here, the City had the foresight to own and operate its own electric utility. As a result, [Redding] has utility rates that are comparatively lower than many others in the state. If there was a private company providing electric service, that company would be required to pay taxes to [Redding] for the services and benefits [Redding] provides. That expense could be passed on to customers as a cost of providing the service and product, and would not be subject to voter approval. The private utility could charge whatever rates it desired. Requiring [Redding] to put its electric rates out to vote every time a rate increase is necessary (because the rates include items that arguably are not 'directly related' to the cost of providing electricity) cannot reasonably be deemed to be an intended consequence of Proposition 26."

B.

Reasonable Cost to Redding?

Undoubtedly, Redding incurs costs to provide infrastructure and support to the Utility. For example, Redding police protect the Utility property and the Utility's workers. Redding's streets, used by the Utility in its operations, are built and maintained by Redding's general fund. Redding's fire department stands ready to respond if a Utility transformer sparks a fire, or a downed tree cuts a live utility line, endangering Redding's

citizens. The trial court's exploration of the issue of reasonable costs constitutes a conclusion of law rather than a finding of fact. Rather than finding the costs incurred by Redding to provide electric service, the trial court determined the Utility's comparatively low rates necessarily mean the PILOT passes constitutional muster under Proposition 26. We reject this legal conclusion.

We also reject the assertion made by Redding at oral argument that a 1999 letter supplies the facts necessary to determine whether the PILOT reflects the reasonable costs to Redding for providing electric service. The letter was sent by an independent consultant to the director of the Utility to recommend that the PILOT calculation methodology not be changed to lower the amount transferred to Redding's general fund. The consultant's conclusion largely rested on a survey of rates charged by other municipal utilities rather than any examination of costs incurred by Redding in providing electric service. Indeed, Redding conceded that no cost of service analysis has been conducted to determine the reasonable cost of providing electric service.

We disagree with Redding's assertion, in its supplemental brief, that the PILOT comports with Proposition 26 because Redding's electric rates are lower than those paid by others in California. Even if Redding's rates were the lowest in California, Proposition 26 would nonetheless require the PILOT to either reflect the city's reasonable cost of providing electric service or be approved by two-thirds of voters. An unconstitutional tax is not rendered lawful simply by being bundled with otherwise reasonable utility rates.

We decline Redding's invitation to engage in a fact-finding mission to determine whether the administrative record contains enough evidence to cost justify the PILOT for purposes of Proposition 26. As we have explained, the trial court's conclusion that the PILOT passes constitutional muster because the PILOT is equivalent to the ad valorem tax rate applicable to private utilities constitutes a conclusion of law. The possibility that

non-rate revenues exceed the PILOT does not satisfy Proposition 26's requirement that Redding demonstrate the collected tax reflects the reasonable costs of providing electric service. So too, Redding's argument that the Utility's electricity rates are "reasonable" does not prove the PILOT bears a reasonable relationship to the costs of service.

Redding misses the mark when it asserts the administrative record shows that "the December 2010 rates do not exceed the cost of providing electric service to [Utility's] customers." In support, Redding asserts the fairness of the rate-making process and the participation of appellants' counsel in the rate-making process. The fairness of the rate-making process, however, does not address whether the amount of the PILOT reasonably reflected Redding's service costs. Tellingly, Redding cites to public comments in the rate making process rather than any cost study by Redding that shows the dollar amounts expended to provide electricity generation or distribution.

Because findings of fact are the unique province of the trial court, we are unable to supply the factual findings necessary to uphold the PILOT as a reasonable cost under Proposition 26. Our conclusion "reflects an 'essential distinction between the trial and the appellate court . . . that it is the province of the trial court to decide questions of fact and of the appellate court to decide questions of law. . . .' " (*In re Zeth S.* (2003) 31 Cal.4th 396, 405, quoting *Tupman v. Haberkern* (1929) 208 Cal. 256, 262–263.)

Perhaps the PILOT reflects Redding's reasonable cost to provide electric service. However, this factual question has not yet been properly determined by the trial court. The question of whether a particular levy, charge, or exaction reflects a "reasonable cost" to the local government requires a factual rather than legal answer. (*Mills v. County of Trinity* (1980) 108 Cal.App.3d 656, 663 (*Mills*).)

In *Mills*, this court considered whether the two-thirds voter approval requirement applied to fees for county services in processing subdivision, zoning, and other land-use applications. (108 Cal.App.3d at pp. 658-659.) *Mills* held that "the 'special tax' referred

to in section 4 of article XIII A does not embrace fees charged in connection with regulatory activities which fees do not exceed the reasonable cost of providing services necessary to the activity for which the fee is charged and which are not levied for unrelated revenue purposes." (*Id.* at p. 659.) We explained that "[s]ince the trial court held the fees imposed by [the county's charges] constitute a 'special tax' as a matter of law, the factual question whether or not such fees exceed the reasonable cost of the related regulatory activity has never been litigated. On remand that issue must be tried." (*Id.* at p. 663.) Accordingly, the disposition in *Mills* was to "reverse and remand for a factual determination of whether the fees in question are reasonably compensatory for the costs occasioned by the regulated activities." (*Id.* at p. 660.)

In *Sinclair Paint, supra*, 15 Cal.4th 866, the California Supreme Court likewise held reversal and remand was necessary " 'for a factual determination of whether the fees in question are reasonably compensatory for the costs occasioned by the regulated activities.' " (*California Assn. of Professional Scientists v. Department of Fish & Game* (2000) 79 Cal.App.4th 935, 947.) In *Sinclair Paint*, the Supreme Court concluded that "Sinclair should be permitted to attempt to prove at trial that the amount of fees assessed and paid exceeded the reasonable cost of providing the protective services for which the fees were charged, or that the fees were levied for unrelated revenue purposes. [Citation.] Additionally, Sinclair will have the opportunity to try to show that no clear nexus exists between its products and childhood lead poisoning, or that the amount of the fees bore no reasonable relationship to the social or economic 'burdens' its operations generated." (*Sinclair Paint, supra*, 15 Cal.4th at p. 881.)

Following *Mills* and *Sinclair Paint*, we determine remand is necessary to allow the trial court to determine the factual question of whether the PILOT reflects the reasonable

costs borne by Redding to provide electric service.[7] (See *California Farm Bureau Federation v. State Water Resources Control Bd.* (2011) 51 Cal.4th 421, 446 [remand for findings].)

DISPOSITION

The judgment is reversed and the cause remanded for further proceedings consistent with this opinion. Plaintiffs (Citizens for Fair REU Rates, Michael Schmitz, Shirlyn Pappas, and Fee Fighter LLC) shall recover their costs on appeal. (Cal. Rules of Court, rule 8.278(a)(1) & (2).)

HOCH, J.

I concur:

MAURO, Acting P. J.

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[7] Given our conclusion, it would be premature to consider the question of remedy for improperly collected taxes in violation of Proposition 26. (See Gov. Code, § 53728.)

DUARTE, J., Dissenting

The majority opinion requires *every municipal utility* that is charged a payment in lieu of taxes (PILOT), with the insignificant exception of those utilities, if any, that pay PILOTS pursuant to a pre-Proposition 26 ordinance, to prove at a trial the exact cost of providing fire, police, sanitation, streets, and other municipal services, no doubt with competing accounting, municipal finance, and other experts. This result is disruptive, uncertain, and chaotic, and, in my view, is not compelled by Proposition 26 (as approved by voters, Gen. Elec., Nov. 2, 2010).

The resulting disruption will be widespread; I note that amici curiae in support of Redding include the League of California Cities, the California State Association of Counties, and the California Municipal Utilities Association (CMUA).[1]

I perceive this result as unwarranted because, in my view, a PILOT such as Redding's--which actually conforms to the limitations set forth by Proposition 13 (as approved by voters, Primary Elect., June 6, 1987) and implementing laws that are designed to establish "fair" property tax rates--as a matter of law does not "exceed the reasonable costs to the local government of providing the service." (Cal. Const., art. XIII C, § 1, subd. (e)(2).) Therefore, it is not a "tax" as defined by Proposition 26.

Accordingly, I respectfully dissent.

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[1] CMUA electric utility members potentially impacted by the majority decision include the Cities of Alameda, Anaheim, Azusa, Banning, Burbank, Cerritos, Colton, Corona, Glendale, Gridley, Healdsburg, Hercules, Lodi, Lompoc, Los Angeles, Moreno Valley, Needles, Palo Alto, Pasadena, Pittsburg, Rancho Cucamonga, Redding, Riverside, Roseville, Santa Clara, Shasta Lake, Ukiah, and Vernon; also represented are the Imperial, Merced, Modesto, and Turlock Irrigation Districts; the Northern California Power Agency; Southern California Public Power Authority; Transmission Agency of Northern California; Lassen Municipal Utility District; Power and Water Resources Pooling Authority; Sacramento Municipal Utility District; the Trinity and Donner Public Utility Districts; the Metropolitan Water District of Southern California; and the City and County of San Francisco, Hetch Hetchy.

I agree with the majority that Redding's PILOT program is not grandfathered-in, and thus immune from a Proposition 26 challenge, because the PILOT is adopted by each successive city council during the biennial budget process. As the majority explains, this practice, however longstanding, is unlike an ordinance, and each council must consider the potential applicability of Proposition 26 when using the PILOT as one component during the process of setting electricity rates.[2] I also agree with the majority's rejection of Redding's claims that it does not "impose" the PILOT because some customers may be able to generate their own electricity.

I agree that the record does not contain evidence of the *exact* benefits conferred by Redding to its utility--benefits available equally to all other property owners who pay their taxes in conformity with Proposition 13 and related laws. My disagreement flows from the fact that a PILOT, by definition, is designed to equate to the property taxes the utility *would* pay, were it not a municipal utility. The PILOT is a "payment *in lieu* of taxes." (Italics added.) In this case, the trial court found Redding's PILOT budget transfer equated to what a private utility would pay in taxes. Indeed, plaintiffs themselves *pleaded* that Redding's PILOT equals "as closely as possible" the taxes a private utility would pay. Thus, Redding's PILOT equals what a private utility would pay in taxes.[3]

As I shall now explain, in my view, *any* PILOT, whenever adopted, is reasonable as a matter of law if it actually comports with Proposition 13 and implementing laws.

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[2] Although this conclusion is compelled by existing precedent, it seems clear Proposition 26 was not intended to apply to pre-existing municipal charges.

[3] Parts of plaintiffs' briefs appear to contest this, and they contested it at oral argument. However, the point is forfeited both because it contradicts their theory of the case (see *Panopulos v. Maderis* (1956) 47 Cal.2d 337, 340-341), and because they fail to set forth the facts in light of the proper standard of review (see *Foreman & Clark Corp. v. Fallon* (1971) 3 Cal.3d 875, 881).

The trial court stated that because the PILOT equated to what a private utility would pay in taxes, its use in the periodic calculation of electric rates by Redding does not result in an unreasonable charge for providing electric service. In full, this part of the trial court's ruling reads as follows:

> "There are many components of [a] rate payer's bill that are technically not directly related to the cost of providing electrical service. These include costs built in to cover programs mandated by law. It is not a reasonable interpretation of Prop 26 that voters intended that any time electric rates are set, this requires an election and voter approval of those portions of the electric rates.
>
> "Even if the PILOT were part of the utility rates charged to ratepayers, it could reasonably be argued that the PILOT is part of the cost of providing the service. All business enterprises have costs and expenses that are a cost of doing business, including regulatory fees, taxes, and all other items that constitute overhead. These are passed on to customers through pricing and rates and are a cost of doing business or a cost of providing the service or product. All businesses are required to pay taxes. Here, the City of Redding had the foresight to own and operate its own electric utility. As a result . . . [i]t has utility rates that are comparatively lower than many others in the state. If there was a private company providing electric service, that company would be required to pay taxes to [Redding] for the services and benefits [Redding] provides. That expense would be passed on to customers as a cost of providing the service and product, and would not be subject to voter approval. The private utility could charge whatever rates it desired. Requiring [Redding] to put its electric rates out to vote every time a rate increase is necessary (because the rates include items that arguably are not 'directly related' to the cost of providing electricity) cannot reasonably be deemed to be an intended consequence of Proposition 26."

I make two preliminary observations about this ruling.

First, a private utility servicing Redding could *not* "charge whatever rates it desired" as the trial court suggested. The Public Utilities Commission (PUC) has broad regulatory authority, conferred by the California Constitution and relevant statutes. (See *Southern California Edison Co. v. Peevey* (2003) 31 Cal.4th 781, 792 (*Peevey*); 8 Witkin, Summary of Cal. Law (10th ed. 2005) Constitutional Law, §§ 1099-1100, pp. 726-729.) "Statutorily, [the] PUC is authorized to supervise and regulate public utilities and to 'do all things . . . which are necessary and convenient in the exercise of such power and

jurisdiction' ([Pub. Util. Code,] § 701); this includes the authority to determine and fix 'just, reasonable [and] sufficient rates' ([*id.*,] § 728) to be charged by the utilities." (*Peevey, supra*, 31 Cal.4th at p. 792.) "In contrast, *publicly* owned municipal utilities are not regulated by the [PUC] or any other supervising agency [citations] in the absence of a legislative grant of authority . . . . Thus, it is the public entity itself which fixes utility rates pursuant to its independent legislative power." (*American Microsystems, Inc. v. City of Santa Clara* (1982) 137 Cal.App.3d 1037, 1042-1043 (*American Microsystems*).)

Importantly, however, the PUC *considers tax liability* when determining whether a private utility's proposed rates are just and reasonable. (See *Southern California Gas Co. v. Public Utilities Com.* (1979) 23 Cal.3d 470, 474 ["As taxes are part of a utility's cost of service, this expense is borne by the ratepayers"]; *City and County of San Francisco v. Public Utilities Com.* (1971) 6 Cal.3d 119, 122-131; *SFPP, L.P. v. Public Utilities Com.* (2013) 217 Cal.App.4th 784, 795-800.) Thus, although the trial court overstated the power of a private utility to set rates, that fact does not diminish the force of the trial court's point: A private utility would properly claim necessary taxes--including local property taxes assessed within the limits of Proposition 13 and implementing laws--as valid costs of service in its PUC rate-setting applications.

Second, although the trial court used the phrase "it could reasonably be argued" that Redding's PILOT was a valid cost of service, in context the trial court was not merely *hypothesizing* about reasonableness, it was *finding* reasonableness. Just prior to the quoted passage, the trial court stated that *if* the PILOT were the imposition, extension or increase of a tax, "the next issue to be decided" is whether the charges exceeded "the reasonable costs of providing" service. Then the trial court addressed the issue in detail, as fully quoted *ante*. Thus, I interpret this passage as an alternative or secondary finding by the trial court, not mere musings.

In my view, the trial court's finding is not a factual finding based on the evidence, but a legally-compelled finding. Under Proposition 26 a "tax" does *not* include: "A

charge imposed for a specific government service . . . 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 . . . ." (Cal. Const., art. XIII C, § 1, subd. (e)(2).) Further, the local government must show "the amount is no more than necessary to cover the reasonable costs" and that "the manner in which those costs are allocated to a payor bear a *fair or reasonable* relationship" to the benefits received. (*Id.*, § 1, last par., italics added.) Thus Proposition 26 does not compel Redding to charge the utility the *least possible* amount for municipal services, nor to charge customers the *least possible* amount for electricity, as plaintiffs assert.

The electric rates set by Redding may be increased by the PILOT transfer, but that is only one factor the city council considers in setting rates. That is, an increase in the amount of the PILOT (e.g., through acquisition of new property by the utility) does not raise rates; rates are set by the city council. (See *American Microsystems*, *supra,* 137 Cal.App.3d at pp. 1042-1043.) Thus, the PILOT is not of itself a "levy, charge, or other exaction" (Cal. Const., art. XIII C, § 1, subd. (e)) *imposed on ratepayers.*

The question here is whether Redding, exercising its legislative discretion, may determine part of the reasonable costs of its utility to include an amount equal to what Redding would collect in taxes from an equivalent private utility, and consider this amount as "costs" when it considers the many factors that go into setting utility rates. I would answer the question "yes" as a matter of law.

A municipal budget ascertains "the amount of money which must be raised to conduct the affairs of the municipality for the ensuing fiscal year, so that the business of the municipality may be conducted on a balanced budget, and on sound business principles, and, as far as practicable, on the same basis that a successful private business is conducted." (15 McQuillin, Law of Municipal Corporations (3d ed. 2014) Budget Law, § 39:49, fns. omitted.) We have deemed it to be a "fundamental proposition . . . that the adoption of a budget is a legislative function." (*County of Butte v. Superior*

Court (1985) 176 Cal.App.3d 693, 698 (*Butte*); see *Scott v. Common Council* (1996) 44 Cal.App.4th 684, 690-694.) "The budgetary process entails a complex balancing of public needs in many and varied areas with the finite financial resources available for distribution among those demands. It involves interdependent political, social and economic judgments which cannot be left to individual officers acting in isolation; rather, it is, and indeed must be, the responsibility of the legislative body to weigh those needs and set priorities for the utilization of the limited revenues available." (*Butte*, *supra*, 176 Cal.App.3d at p. 699; see *Collier v. City and County of San Francisco* (2007) 151 Cal.App.4th 1326, 1345 [citing this passage of *Butte* with approval].)

Taxation is fundamental to municipal budgeting. Proposition 13--the foundation of future tax and appropriation initiatives, including Proposition 26--ensures "fair" property taxation. (Ballot Pamp., Primary Elect. (June 6, 1978) argument in favor of Prop. 13, p. 58; *id.*, rebuttal to argument against Prop. 3, p. 59, capitalization omitted.) Therefore, if the amount of a PILOT is consistent with Proposition 13 and implementing legislation, the PILOT perforce is fair and reasonable. Proposition 26 was not designed to allow the utility to use Redding's general civic services without paying its "fair share."

By requiring the utility to pay the same amount that a private utility would pay in taxes, Redding recoups the reasonable or--as stated by Proposition 13--"fair" costs incurred in providing electric service. This insures Redding operates "on sound business principles, and, as far as practicable, on the same basis that a successful private business is conducted." (15 McQuillin, *supra*, § 39:49; see also 12 McQuillin, *supra*, § 35:65 ["In setting rates, a city may take into consideration the fact that the property of the utility is not taxed and that other services furnished by the city, such as fire and police protection, are furnished without charge"].)

Accordingly, I would affirm the judgment in favor of Redding.

DUARTE, J.

IN THE

Court of Appeal of the State of California

IN AND FOR THE

THIRD APPELLATE DISTRICT

MAILING LIST

Re: Citizens For Fair REU Rates et al. v. City of Redding et al.
C071906
Shasta County
No. 171377, 172960

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ATTACHMENT 2

(Cal. Rules of Court, rule 8.204(d))

CERTIFIED FOR PUBLICATION

COPY

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

(Shasta)

FILED

FEB 19 2015

Court of Appeal, Third Appellate District
Deena C. Fawcett, Clerk
BY _____ Deputy

CITIZENS FOR FAIR REU RATES et al., Plaintiffs and Appellants, v. CITY OF REDDING et al., Defendants and Respondents.	C071906 (Super. Ct. Nos. 171377, 172960) ORDER MODIFYING OPINION AND DENYING PETITIONS FOR REHEARING [NO CHANGE IN JUDGMENT]

THE COURT:

The opinion filed January 20, 2015, in the above cause is modified as follows:

On page 2, replace the third sentence of the first paragraph with the following: To this end, Proposition 218 added article XIII C to require that new taxes imposed by a local government be subject to vote by the electorate. (Art. XIII A, § 4; art. XIII C, § 1, as approved by voters, Gen. Elec., Nov. 5, 1996; see also 2B West's Ann. Cal. Codes (2013) pp. 362-363.) General taxes may be approved by a simple majority of voters, but special taxes require two-thirds voter approval. (Art. XIII C, § 2, subds. (c) & (d).)

On page 3, replace the first sentence of the second full paragraph with the following: Plaintiffs in this case (Citizens for Fair REU Rates, Michael Schmitz, Shirlyn

Pappas, and Fee Fighter LLC) challenge the PILOT on grounds it constitutes a tax for which article XIII C requires voter approval.

Also on page 3, replace the first sentence of the third full paragraph with the following: We conclude the PILOT constitutes a tax under Proposition 26 for which Redding must secure voter approval unless it proves the amount collected is necessary to cover the reasonable costs to the city to provide electric service.

On page 11, delete the first paragraph.

On page 13, delete the last sentence of the first full paragraph.

On page 19, replace the last sentence of the first full paragraph with the following: Although Propositions 26 and 218 stand in pari materia -- namely they relate to the same subject (*People v. Honig* (1996) 48 Cal.App.4th 289, 327) -- nothing in either constitutional amendment grandfathers in the PILOT simply because it has been a customary recurrence in the Redding municipal budget.

On page 22, replace the second sentence of the second full paragraph with the following: Even if Redding's rates were the lowest in California, Proposition 26 would nonetheless require the PILOT to either reflect the city's reasonable cost of providing electric service or be approved by voters.

On page 25, add the following to the end of footnote 7: We also do not consider whether the PILOT in this case would constitute a general or special tax if it does not reflect the reasonable cost to provide electric service. (Art. III C, § 2, subds. (c) & (d).)

This modification does not change the judgment.

The petitions for rehearing are denied.

MAURO, Acting P.J.

HOCH, J.

IN THE

Court of Appeal of the State of California

IN AND FOR THE

THIRD APPELLATE DISTRICT

MAILING LIST

Re: Citizens For Fair REU Rates et al. v. City of Redding et al.
C071906
Shasta County No. 171377, 172960

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ATTACHMENT 3

(Cal. Rules of Court, rule 8.204(d))

SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF SHASTA

HON. WILLIAM D. GALLAGHER Dept. 9
dw

#171377

CITIZENS FOR FAIR REU RATES,
Plaintiff,

vs.

THE CITY OF REDDING, et al.,
Defendants.

NATURE OF PROCEEDINGS:

MEMORANDUM OF DECISION

This matter came on for trial on April 30, 2012. Walter McNeill appeared on behalf of Plaintiffs, and Michael Colantuono appeared on behalf of Defendants. After consideration of the evidence and arguments of counsel, the Court rules as follows:

This is a case of first impression. Both counsel agree that there are currently no appellate decisions addressing the application of Proposition 26.

Applicable Law

In 1996, California Voters passed Proposition 218, the "Right to Vote on Taxes Act." This act amended the California Constitution to add Article XIII C. Sections one and two read, at the time of the enactment:

"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.

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."

In November 2010, the voters approved proposition 26, which amended Article XIIIC Section 1 by adding subdivision (e), which provides:

> "(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."

Article XIII, Section 2 was not altered by Proposition 26.

Factual and Procedural History

In 1988, the City of Redding adopted a resolution adopting its budget for fiscal year 1988-1989. That budget approved a transfer of funds from the City-owned electric utility (Redding Electric Utility or "REU") to the City's general fund. The budget documents explain that, where cities engage in "enterprise activities" (such as operating their own utility) most cities transfer funds from those enterprise activities proportionate to the taxes that would be paid by the enterprise if it were a private activity and was required to pay taxes to the City. In prior years the City had simply used an operating transfer that was a constant amount each year. A new method was adopted for the 1988-1989 budget. This method called for a Payment In Lieu Of Taxes (PILOT) in an amount based on 1% of REU's fixed assets. The calculation is intended to mimic the amount of taxes that REU would have to pay the City if it were a private enterprise and was required to pay such taxes. The purpose of the PILOT, as with any other taxes paid to the City by private enterprises, was to compensate the City for the numerous benefits and services provided by the City to the enterprise. The PILOT is included in REU's annual budget, and is transferred to the City's general fund. Since the 1988-1989 budget, the annual City budgets have maintained the PILOT, which is calculated the same way each year.

On December 7, 2010, the City adopted increased electric rates for all REU customers by resolution 2010-179. That resolution approved a 7.84% increase effective for the first electric billing cycle of January 2011, and a subsequent 7.84 rate increase for usage beginning on the first day of the billing cycle of December 2011.

Petitioners filed a Petition for Writ of Mandate and complaint for Declaratory and Injunctive Relief on February 4, 2011, contending that this resolution, which increased utility rates, constituted a tax within the meaning of Article XIII C, and was required to be submitted to the voters for approval.

The court denied the Petition, holding that the rate increases adopted pursuant to Resolution 2010-179 did not affect the PILOT. The PILOT was included in the City's

budget, was adequately funded at the rates in effect prior to the adoption of the rate increase. It was therefore an established cost that was not increased or affected by the adoption of Resolution 2010-179. As the rate increases did not increase the PILOT, the

Court found that the Resolution did not impose or increase any tax, and therefore did not require voter approval.

On June 22, 2011, the Redding City Council approved the biennial City Budget for fiscal years ending 2012 and 2013 by adopting Resolution 2011-111. This budget includes the PILOT charge. Plaintiffs filed a second action (Shasta County Superior Court Case Number 172960) on August 29, 2011. The Complaint asserts actions for declaratory and injunctive relief, and seeks refunds of improperly collected fees. Plaintiffs contend that the increased utility rates, with the inclusion of the PILOT, constitute a tax that was imposed without the approval of voters. The parties stipulated to consolidate these actions, and the second matter proceeded to a court trial.

Application of Proposition 26: Proposition 26 amended Article XIIIC Section 1 to further define and clarify what is a "tax." The amendment added subsection (e) to the definitions, stating that a tax means any levy, charge, or exaction of any kind imposed by a local government, except for seven specific categories of fees. The amendment and addition of Subsection (e) also set forth that the burden of proof is on the local government to establish that a levy, charge, or other exaction is not a tax.

Defendants correctly point out that Proposition 26 simply added to the definition of a tax. The Operative section of the statute is contained in Article XIIIC Section 2, which provides that local government may not impose, extend, or increase any tax (general or specific) without voter approval. Therefore, the first step in the analysis is whether the budget resolution, which includes electric rates that incorporate the PILOT, can be said to impose, extend, or increase any tax. If it does not, then voter approval is not required and the amendments to Article XIIIC Section 1 brought about by Proposition 26 simply do not apply.

Whether the PILOT as a component of the electric rates approved by the budget resolution constitutes an increase, extension, or imposition of a tax under Article XIIIC Section 2 is not addressed by Plaintiffs in their opening brief, which addresses whether the PILOT is a tax by the new definitions set forth in Article XIII Section 1(e). In their brief, defendant raises the argument that the PILOT is not "imposed" because imposed implies some measure of force. In reply, plaintiffs counter this argument. (Which will be discussed more fully below). This is essentially the only argument addressed by the parties with respect to the applicability of Article XIIIC Section 2.

There is no detailed argument as to whether the PILOT is an "extension" or "increase" in tax. Defendant contends, and the court agrees that there is no extension of a tax here, as there is no "extension of a revenue measure's effective period, as by repeal of a sunset clause." Government Code Section 53750(e). The Court also agrees that the PILOT does not constitute an "increase" in a tax, in that there has been no change in the method of calculation. Government Code Section 53750(H)(2)(B).

This leaves the analysis as to whether or not the PILOT is "imposed." Defendant contends that the term "imposed" requires an exercise of force or authority, which is not present here because the electric rates are only paid by those who wish to obtain the City's electric power. Defendant essentially argues that no one is obligated to utilize REU's services, as they are free to find some alternate means of obtaining electric power, using the examples of solar, water, wind and geothermal power. The Court advised at the time of the hearing that it was rejecting this argument. While the Court acknowledges that legally REU has no monopoly as an electric utility, the reality is that for many people there are no economically viable alternatives. The Court used the example of a tenant who is renting a house or apartment that is served by REU. While theoretically possible that a tenant who does not wish to use REU could install an alternate power source, that simply is not a realistic option. Therefore, the Court does not agree that the PILOT is not "imposed" simply because no one is forced to purchase their electric power from REU.

The court interprets the term "imposed" in the context of Article XIIIC Section 2 to imply the establishment of a new tax. The Webster's Dictionary definition of "impose" is "to apply or establish by or as if by authority." Its use in the context of Article XIIIC Section 2, which addresses the government's authority to "impose, extend, or increase" any tax, the term "impose" also implies that it is intended to refer to the establishment of new taxes (as "increase" would logically involve an existing tax, and "extend" would also involve an existing tax, such as one whose effective period has been extended).

The text of the law as well as the ballot materials with respect to Proposition 26 contain numerous references that indicate that Proposition 26 was not intended to apply to fees or charges already in place, but was to apply to new or increased taxes. For example, Section One of Proposition 26 sets forth the Findings and Declarations of Purpose contain the following references to new or increased taxes:

Section 1(a): since Proposition 13 was approved, "increases" in state taxes must be approved by 2/3 vote of the Legislature;

- Section 1(b): since Proposition 218 was enacted, "increases" in local taxes must be approved by the voters;
- Section 1(c): despite these limitations, "taxes have continued to escalate";
- Section 1(d): recently, the Legislature "added another $12 billion in new taxes";
- Section 1(e): the Legislature and local governments "have disguised new taxes as 'fees'";
- Section 1(f): this measure defines a tax so that the Legislature and local governments can not circumvent voting requirements "on increasing taxes by simply defining new or expanded taxes as 'fees.'" (Emphasis added).

Similarly, the Ballot materials regarding Proposition 26 (Administrative Record pages 930-933), which contain the Official Title, Summary, and Legislative Analysis of the measure, also contain numerous statements that indicate that Proposition 26 was intended to apply to new or increased taxes, and not to fees or charges already in place. For example:

- Page 930 refers to "higher approval requirements for new revenues" ;
- Page 931 contains references to the manner in which the government can "create or increase a fee", "increasing tax revenues"; the manner in which regulatory fees can be "created or increased"; "revenue proposals"; and "laws that increase taxes";
- Page 932 contains references to "revenue proposals", and also contains the representation that "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. . . . [or] the fees or charges were created or increased by a state law . . . ."; and finally,
- Page 933 indicates that the measure "would make it more difficult for state and local governments to "pass new laws that raise revenues", and that the new higher voter approval requirements would apply to "new laws to create – or extend" fees and charges.

The Court finds that the PILOT was not a new or increased tax. The PILOT was an already existing component of the REU's budget that had been in place for over 20 years. The manner of calculating the PILOT has remained unchanged since 1988. Proposition 26 was not intended to require an election every time a local government adopts a budget that includes pre-existing components so long as that budget does not impose new or increased fees or charges or change the manner in which those fees are calculated.[1] The adoption of Resolution 2011-111 adopting the City of Redding's budget, that included the budget of REU and the PILOT does not impose, extend, or increase a tax, and Proposition 26 does not apply.

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[1] At the trial of this matter, plaintiffs' counsel argued that the "re-enactment rule", as set forth in the case *Barratt American, Inc. v. City of Rancho Cucamonga* (2005) 37 Cal.4th 685 applies, and somehow requires the Court to revisit the legality of each component of the budget resolution. The Court notes that this argument was not raised in any of the trial briefs. The Court also notes that plaintiffs' counsel was counsel of record in the *Barratt* case. Certainly plaintiff's counsel understood the implications of that case, and if it were, in fact, controlling in the present action, would have addressed it in their briefs. Nonetheless, the court has reviewed the *Barratt* case, and finds that it is distinguishable, as it involved a challenge under the "Mitigation Fee Act" to a resolution reenacting building permit and plan review fees. These are fees charged to defray the costs of a specific regulatory program, and not a budget resolution, as in the present case. The fees involved in the *Barratt* case were part of a statutory scheme whereby, if the fee is determined to exceed the cost of providing the regulatory program, any excess is required to be utilized to reduce future fees. No similar statutory scheme is involved here. The *Barratt* case does not involve a claim that the matter was required to be submitted to the voters under Proposition 26. The PILOT was again included in the City's budget as a component of the operating budget of REU, as it had been for over 20 years. The manner of calculating the PILOT did not change, and it was to continue unmodified. Finally, as stated previously, the court finds that Proposition 26 was not intended to require an election every time a local government adopts a budget that includes pre-existing components so long as that budget does not impose new or increased fees or charges or change the manner in which those fees are calculated.

The Court finds in favor of Defendant and against Plaintiffs on plaintiffs' complaint and each cause of action asserted therein.

Additional Issues:

While not essential to the analysis and the above conclusion, the Court finds that the following comments warrant inclusion in a discussion of the issues that came before the Court.

1. Plaintiffs argued at the hearing that the adoption of a budget does not create a fee, and that nothing occurred in the budget process to establish the PILOT as a "fee." Plaintiffs contend that electric rates can only be established by resolution, and the only meaningful action on rates was the adoption of resolution 2010-179 (The December 2010 resolution increasing rates). However, the Court has already ruled on whether Prop 26 required voter approval of the increase in rates, and determined that it did not.

Plaintiffs acknowledged that ordinarily budget resolutions are not subject to attack, and argued that they were not seeking to invalidate the budget but only the language that appeared to ratify the PILOT. If Plaintiffs are contending that the electric rates were not properly established because defendants failed to follow the resolution process, then that would seem to be a different legal challenge, and not one based on voter approval requirements of Proposition 26.

2. Plaintiffs contend that, as electric rates were specifically excluded from the operation of proposition 218, proposition 26 was designed to fill in that gap and to make the voter requirement specifically apply to electrical rates. However, the Court has found nothing in Proposition 26 or the ballot materials to support this. There is no specific reference to utility rates. Instead, these materials make references to taxes that are disguised as fees or charges, which are described as fees imposed for health, environmental and other societal or economic concerns, regulatory programs, or business assessments. Nowhere are utility rates mentioned.

The text of Proposition 26 refers to the types of fees and charges to which Proposition 26 was intended to apply. For example, Section One of Proposition 26 refers to:

- "state personal income taxes, state and local sales and use taxes, and a myriad of state and local business taxes";
- Taxes "to be paid by drivers, shoppers, and anyone who earns an income"; and
- Fees "couched as 'regulatory' but which exceed the reasonable costs of actual regulation" or fees that are "imposed to raise revenue for a new program and are not part of any licensing or permitting program."

The ballot materials (AR 930-933) also contain numerous references to the type of fees and charges to which Proposition 26 was intended to apply, none of which are related to utility rates. For example:

- Page 930 refers to "income, sales, and property taxes" and "fees and charges [that] typically pay for a particular service or program". These are

- described as "user fees", "regulatory fees" and "property charges." These descriptions include examples. None of them are utility rates.
- Page 931 refers to "regulatory fees."
- Page 932 refers to fees and charges "that government imposes to address health, environmental, or other societal or economic concerns", "business assessments", and "user fees, property development charges, and property assessments."
- Page 933 refers to "environmental, health, and other regulatory fees", as well as "business assessments."

The Court does not accept plaintiff's contention that Proposition 26 was enacted to address a gap created after the enactment of Proposition 218, and was specifically intended to include electric utility rates. If it was, then the ballot materials and the statute could have specifically indicated so. They do not.

The court notes that Plaintiffs argued that electric rates were specifically mentioned in the ballot materials. The only reference to electricity is found in the "Argument in favor of proposition 26," which lists "examples" of items to which the government could apply hidden taxes, including electricity. However, the Court finds that the printed arguments in favor of and against ballot measures do not carry any official weight. In fact, the front of the voter's election materials includes a section that says that these arguments are provided by proponents and opponents of the ballot measures, and that "the submitted argument language cannot be verified for accuracy."

Even if the court were to choose to consider these arguments, the Court finds them to be unpersuasive, because they are incorrect and misleading. It should be noted that one of the items listed for which hidden taxes could be applied without Prop 26 is water. This is incorrect and misleading, because this issue was encompassed by Proposition 218, and subsequent to its enactment, PILOT for water services were struck down.

Furthermore, in reviewing the arguments for and against Prop 26, these are replete with references to new or increased taxes and the types of fees to which Prop 26 applies. These arguments indicate that electric utility rates were not contemplated to be within the application of Proposition 26, and, contrary to plaintiff's arguments, it was not the intent for proposition 26 to fill in a perceived gap left by Proposition 218.

3. Defendant contends that the PILOT is not a line item on rate payers' bills, and that REU has non-rate revenues that exceed the amount of the PILOT, therefore, there is no evidence that the PILOT is paid out of customer's rates.

4. Finally, even if the PILOT constitutes the imposition, extension, or increase of a tax, then the next issue to be decided is whether, as defined in Section XIIIC Section 1, the REU rates containing the PILOT constitute a tax because they include charges that exceed the reasonable costs of providing that service. There are many components of an REU rate payer's bill that are technically not directly related to the cost of providing

electrical service. These include costs built in to cover programs mandated by law. It is not a reasonable interpretation of Prop 26 that voters intended that any time electric rates are set, this requires an election and voter approval of those portions of the electric rates.

Even if the PILOT were part of the utility rates charged to ratepayers, it could reasonably be argued that the PILOT is part of the cost of providing the service. All business enterprises have costs and expenses that are a cost of doing business, including regulatory fees, taxes, and all other items that constitute overhead. These are passed on to customers through pricing and rates and are a cost of doing business or a cost of providing the service or product. All businesses are required to pay taxes. Here, the City had the foresight to own and operate its own electric utility. As a result, the City of Redding has utility rates that are comparatively lower than many others in the state. If there was a private company providing electric service, that company would be required to pay taxes to the City for the services and benefits the City provides. That expense could be passed on to customers as a cost of providing the service and product, and would not be subject to voter approval. The private utility could charge whatever rates it desired. Requiring the City to put its electric rates out to vote every time a rate increase is necessary (because the rates include items that arguably are not "directly related" to the cost of providing electricity) cannot reasonably be deemed to be an intended consequence of Proposition 26.

Dated: June 22, 2012

WILLIAM D. GALLAGHER
Judge of the Superior Court

CERTIFICATE OF MAILING

State of California, County of Shasta

I, the undersigned, certify under penalty of perjury under the laws of the State of California that I am a Deputy Court Clerk of the above-entitled court and not a party to the within action; that I mailed a true and correct copy of the above to each person listed below, by depositing same in the United States Post Office in Redding, California, enclosed in sealed envelopes with postage prepaid.

Dated: June 25, 2012

Deputy Clerk

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PROOF OF SERVICE

Citizens For Fair Reu Rates v. City Of Redding
Third District Court of Appeal Case No. C071906
California Supreme Court Case No. S_____

I, Ashley L. Lloyd, declare:

I am employed in the County of Nevada, State of California. I am over the age of 18 and not a party to the within action. My business address is 11364 Pleasant Valley Road, Penn Valley, California 95946. On March 2, 2015 I served the document(s) described as **PETITION FOR REVIEW** on the interested parties in this action by placing a true copy thereof enclosed in a sealed envelope addressed as follows:

SEE ATTACHED LIST

BY MAIL: The envelope was mailed with postage thereon fully prepaid. I am readily familiar with the firm's practice of collection and processing correspondence for mailing. Under that practice it would be deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid at Penn Valley, California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if the postal cancellation date or postage meter date is more than one day after service of deposit for mailing in affidavit.

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on March 2, 2015 at Penn Valley, California.

Ashley L. Lloyd

SERVICE LIST

Citizens For Fair Reu Rates v. City Of Redding
Third District Court of Appeal Case No. C071906

California Supreme Court Case No. S_____

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