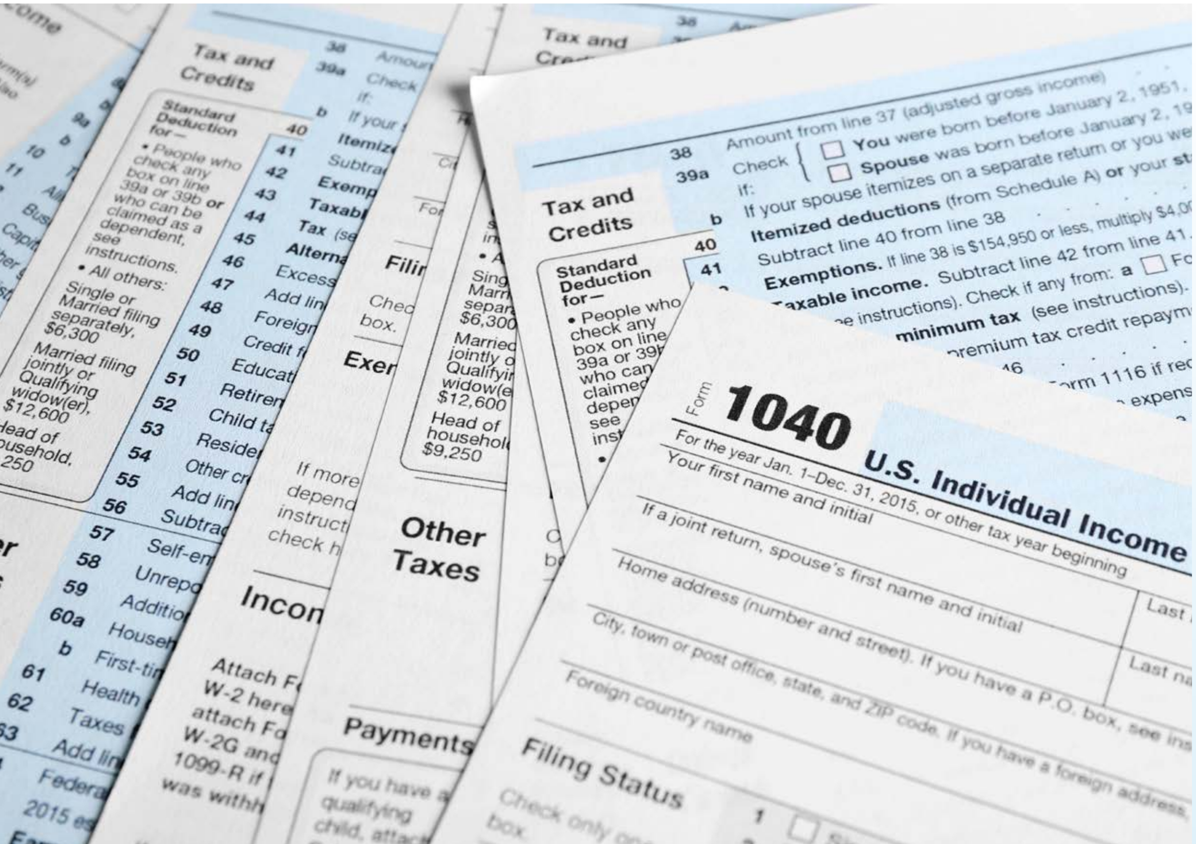

Chapter 2

TAXES

A tax is a monetary imposition by a government on persons or property for the purpose of raising revenue to support the purposes of the government.[1] In contrast to an assessment or a fee, a tax need not be levied in proportion to specific benefit to a person or property. Fees or charges will be considered taxes to the extent they exceed the reasonable cost of the service, commodity, or facility for which they are imposed.

California cities do not have an inherent power to tax. Charter cities are given the power to tax pursuant to Article XI, Section 5 of the California Constitution and may levy taxes for municipal purposes without specific authorization from the Legislature. As authorized in state statute, a general law city, with certain exceptions, may levy any tax that a charter city may levy.[2] State law may set certain limits and procedures and may exempt certain activities from taxes levied by general law cities. These laws apply to charter cities in matters that the courts have determined are of statewide concern.

"The nation should have a tax system that looks like someone designed it on purpose."

— WILLIAM SIMON

General and Special Taxes

The passage of Proposition 13 in 1978 created a distinction between "general" and "special" taxes. Proposition 218, in 1996, further defined and established procedures for general taxes.[3]

A *general tax* is a tax imposed for general governmental purposes, the proceeds of which are deposited into the General Fund. A majority vote of the electorate (those voting on the measure) is required to impose, extend, or increase any general tax.

» An election on a general tax must be consolidated with a regularly scheduled general election of city council members except in cases of emergency, declared by a unanimous vote of the city council.[4]

» Single-purpose special districts (special purpose districts) may not impose general taxes.

	General Tax	Special Tax
Use of Revenues	• Unrestricted	• Specific purpose
Governing Body Approval	• General law cities: two-thirds • Charter cities: majority • Counties: two-thirds • Transactions and Use Taxes: two- thirds See section 2.03 of this chapter.	• Majority
Voter Approval	• Majority	• Two-thirds
Other Rules	• A general tax election must be consolidated with a regularly scheduled general election of members of the governing body, unless an emergency is declared by unanimous vote (among those present) of the governing body.	• Special tax funds may legally be deposited into a special account or the general fund, but should be deposited into a separate account according to best practices and accounting standards. The taxing agency must publish an annual report that includes 1) the tax rate; 2) the amounts of revenues collected and expended, and 3) the status of any project funded by the special tax.[5]

A special tax is a tax that is collected and earmarked for a specific purpose and deposited either into a separate account or the General Fund. A two-thirds vote of the electorate is required to impose, extend, or increase any special tax.

Proposition 26: Defining a Tax by What It Is Not

California voters approved Proposition 26 in November 2010, placing new rules into the California Constitution stating that a government-imposed charge, levy, or exaction of any kind is a tax unless it falls into one of seven express exceptions.

1. **A charge imposed for a specific benefit conferred or privilege granted directly to the payer 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.**

   Specific Benefit Exception examples include restricted neighborhood parking permits and entertainment and street closure permits.

2. **A charge imposed for a specific government service or product provided directly to the payer 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.**

   Government Service or Product Exception examples include user fees for parks and recreation classes, public records copying fees, DUI emergency response fees, emergency medical and ambulance transport service fees, and development application processing fees.

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.**

   Permits and Inspections Exception examples include health and safety permits, building permits, police background checks, pet licenses, bicycle licenses, and permits for regulated commercial activities (such as massage establishments, card rooms, taxicabs, and tow-truck operators).

For exceptions 1 through 3, the fee imposed must not exceed the agency's reasonable costs.

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

   Local Government Property Exception examples include facility room rentals; equipment rentals; park, museum, and zoo entrance fees; golf greens fees; on- and off-street parking; and highway tolls.

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, including late-payment fees, fees imposed under administrative citation ordinances, parking violations, etc.**

   Penalty for Illegal Activity Exception examples include parking fines, code-enforcement fees and penalties, late-payment fees, interest charges, and other charges for violation of the law.

6. **A charge imposed as a condition of property development.**

   Property Development Exception examples include development impact fees, fees imposed by California Environmental Quality Act mitigation requirements, and Quimby Act and park mitigation fees.

7. **Assessments and property-related fees imposed in accordance with the provisions of Article XIII D (Proposition 218).**

   Proposition 218 Exception examples include assessments on real property for special benefit conferred, fees imposed upon a parcel or a person as an incident of property ownership, and fees for a property-related service, such as many retail water and sewer fees.

When is a Tax Imposed, Increased, or Extended?

Under Proposition 218, no local government may impose, extend, or increase any general tax until such tax is submitted to the electorate and approved.[6]

A tax is *imposed* when the local tax ordinance is adopted, and each time a tax is collected.[7] Extend means a decision by an agency to extend the stated effective period for the tax or fee or charge, including amendment or removal of a sunset provision or expiration date.[8]

A tax is *increased* when an agency either 1) increases the rate used to calculate the tax or 2) revises the methodology by which the tax is calculated if that revision results in an increased amount being levied on any person or parcel.[9] A tax is not increased if 1) it is imposed at a rate no higher than the maximum rate previously approved or 2) is adjusted in accordance with a schedule of adjustments, including a clearly defined formula for inflation that was adopted prior to November 6, 1996.[10] However, a tax that is calculated by using a percentage is increased when it is adjusted for inflation even if the voters approve the tax.[11]

Initiative Special Taxes

In September 2020, the California Supreme Court denied review of an appellate court decision in *City and County of San Francisco v. All Persons Interested in the Matter of Proposition C*. The First District Court ruled that the two-thirds voter approval requirement for local special taxes enacted by Proposition 13 in 1978 applies only to taxes proposed by a government body and not to initiatives placed on the ballot by local citizens.

San Francisco's Proposition C was a November 2018 measure placed on the ballot by voter initiative petition. The measure increased taxes on some businesses, with the proceeds dedicated to housing and homeless services and programs. The ballot measure received 61% of the vote and was deemed approved by the San Francisco City Attorney based on the interpretation of another California Supreme Court decision, *California Cannabis Coalition v. City of Upland* (2017).

The Upland case addressed the issue of whether a measure, qualified for the ballot by citizen petition, that imposes a general tax on cannabis businesses must follow the state constitutional rules of Proposition 218. Specifically, the court considered whether such a tax could be enacted through a special election rather than requiring a general election as Proposition 218 would typically require for general taxes. The court found that Proposition 218's requirement for general elections applies only to general taxes imposed by local governments, not to taxes that are qualified for the ballot via initiative. In doing so, the court clarified that local initiative special taxes are to be treated differently than taxes proposed by a local governing body.

"The power of taxing people and their property is essential to the very existence of government."

— JAMES MADISON, U.S. PRESIDENT

Additional Aspects of Municipal Taxation in California

A local tax can be reduced or repealed by initiative unless it supports bonded debt. Many taxes can be imposed or increased by initiative as well.

Certain types of local taxes are specifically preempted by state law. These include taxes on cigarettes, soda, alcohol and personal income.[12]

State law provides various additional procedural requirements for the enactment of some taxes.

If a local agency wants to collect a previously approved tax at a rate lower than was authorized by the voters, the agency should make it very clear in its official actions that the rate is being "suspended" for a certain period of time and not being permanently lowered. An agency that collects a previously approved tax at a rate lower than was authorized by the voters without a statement clarifying the intent and purpose of the suspension may trigger a Proposition 218 vote requirement when it begins collecting the tax at the previously approved rate.[13]

For More Information:

Proposition 218 Implementation Guide, League of California Cities, 2025 edition.

California Municipal Law Handbook, Chapter V, League of California Cities.

Proposition 26 Implementation Guide, League of California Cities, 2011 edition. **www. cacities.org/Prop26Guide**.

Applying Proposition 26