Water Rates, Prop. 218 and 26 Litigation, and Other Developments in the Law of Municipal Revenues

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Current Developments in the Law of Municipal Revenues

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by

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I. Introduction

Municipal finance is not getting any simpler and recent months have produced new developments in the Legislature and the courts involving a broad range of municipal revenues. We focus on just four here — transactions and use ("sales") taxes, utility users taxes, water rates, and sewer rates.

II. Transactions and Use ("Sales") Taxes

Revenue and Taxations Code sections 7285.9 et seq. authorize California cities, with voter approval, to supplement the 1 percent Bradley-Burns Uniform Local Sales and Use Tax with "transactions and use taxes" in increments of one-eight percent of taxable transactions. Section 7251.1 of that law, however, caps all city and county transaction and use taxes at 2 percent. A number of questions about that cap are unanswered, like what happens if two taxes are approved at the same election that, together, take a community over the cap? Does one or the other prevail? Are they prorated? Los Angeles County recently collected less than all of its voter-approved park and recreation tax in some communities to respect the limited "headroom" under the 2 percent cap in those communities. Long Beach is now litigating whether its tax automatically returned to its full amount when voters reduced a Los Angeles County housing tax. (*Long Beach Reform Coalition v. City of Long Beach*, Los Angeles Superior Court No. 25 STCP 00471, filed Feb. 6, 2025.) These unanswered questions will eventually require legislative answers but, for now, the affected local governments seem to be finding negotiated solutions, mostly avoiding litigation.

A. Exceptions to the 2 Percent Cap on Local Taxes

Many Los Angeles County and Bay Area communities are at or near the 2 percent cap, leading the Legislature to make exceptions. Many of these justify their application to one or a few communities despite our Constitution's preference for general legislation by referencing "unique fiscal pressures" on the benefited communities. Article IV, section 16 of the California Constitution[1] states:

> (a) All laws of a general nature have uniform operation.
>
> (b) A local or special statute is invalid in any case if a general statute can be made applicable.

Some of the recent bills allowing exceptions include 2024's AB 1256 (Humboldt County transportation programs); SB 335 (Santa Clara County general tax, Ventura County transportation tax); and, SB 862 (Santa Cruz County transportation tax). Such statutes have been litigated, questioning whether special legislation can be justified and whether the taxes which relied on them actually come within their terms.

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[1] Unspecified references to "articles" are to the California Constitution.

Alameda County Taxpayers Association v. County of Alameda (2025) 108 Cal.App.5th 524, review pending, rejected a challenge to a general transactions and use tax, concluding ballot materials' references to homeless services were not sufficient to make this a special tax; the ballot materials were not so false and misleading as to violate due process, empowering the court to invalidate the tax; the tax did not violate the 2 percent cap given a statutory exception; and, that exception was not invalid special legislation. The last point is of most interest given that it is also raised in *Silicon Valley Taxpayers Association v. City of Campbell,* Santa Clara Superior Court Case No. 25 CV 455853 (filed Jan 6, 2025) and *Lester v. Cooper*, Contra Costa Superior Court Case No. MSN 20-1173 (filed Aug. 17, 2020).

Alameda County Taxpayers rejected the special legislation claim in broad language that will support a demurrer in the Campbell and Contra Costa County cases:

> In both bills, the Legislature found "unique fiscal pressures" in the specified localities warranted the exemptions from the state sales tax cap. Authorizing additional taxes for certain localities is rationally related to the purpose of alleviating unique fiscal pressures in those localities. That the Legislature did not identify the specific fiscal pressures, as the Association complains, is of no moment: the relevant analysis is whether "any state of facts can reasonably be conceived which would sustain a statutory classification." (*Watson, supra*, 63 Cal.2d at p. 833, 48 Cal.Rptr. 481, 409 P.2d 481.) The Association also argues the fact that the bills identify more than one locality means the localities cannot be unique. The Legislature could reasonably determine that certain localities face fiscal pressures not faced by the state's remaining localities. The Association provides no authority for its contentions that a bill exempting an existing tax is reviewed with

> greater scrutiny than one exempting a future tax, or that the absence of sunset provisions renders the bills unconstitutional.
>
> "Here, the Legislature identified a reasonable and rational basis for the need to enact legislation directed only to [the County and certain other localities]… . The Legislature has the authority to determine the best method for resolving state fiscal issues, and it is not for the court to second-guess its determination." (*White, supra*, 88 Cal.App.4th at p. 307, 105 Cal.Rptr.2d 714.)

(*Alameda County Taxpayers, supra*, 108 Cal.App.5th at p. 517, abridgements by court.)

The petitioner unsuccessfully sought publication and rehearing before the Court of Appeal. It petitioned for Supreme Court on March 13, 2025 and the County is preparing to answer that petition as this paper is written. Review is unlikely because the law in this area is settled. Petitioner effectively seeks error correction, which is rarely a persuasive basis for review in the California Supreme Court.

B. Tax-Rebate Agreements

Some communities have entered into agreements with retailers, especially internet vendors, to rebate a substantial fraction of the Bradley-Burns 1-percent tax in exchange for the vendor's agreement to report all sales as having occurred in the contracting community. This can create a very large windfall for the contracting government, a big tax break for the vendor, and a loss of revenues to the communities that had previously benefited from taxes on those transactions. Such agreements are controversial and have generated litigation. (E.g., *City of Fontana v. California Department of Tax and Fee Administration* (2017) 17 Ca.App.5th 899 [rejecting challenge by Fontana, Lathrop and San

Bernardino to Ontario agreement affecting taxes on sales of medical supplies from warehouses located in those three cities].)

The controversy has led to legislative attention, most recently 2024's AB 2854, which adopted Revenue & Taxation Code section 7213 to require any local agency which benefits from such an agreement to post to its website information about the agreement including: the parties, the amount rebated since its execution, the execution date, any sunset date, the rebate percentage and any commission paid to a third party. The posting is due annually by April 30th. Every city and county which does not have such a rebate agreement must report that fact to the California Department of Tax and Fee Administration (CDTFA) by April 30th of each year, too. CDTFA is then required to compile and post the data to its website. Failure to report to CDTFA (even of the non-existence of such an agreement) or to post the required information is punishable by a fine of $1,000 per day for the first 180 days of non-reporting and $4,000 per day for the balance of the reporting year.

The statute is intended to daylight these agreements and allow State policymakers to understand their consequences for California's sales tax revenues. It is also intended as a precursor to more substantive legislation to rein in such agreements and especially commissions to those who brokered such deals, but that is complicated by the fact that some small cities are very heavily dependent on these agreements.

III. Utility Users Taxes

Utility users taxes have generated litigation lately, too, testing two questions:

- can voters approve a transfer from utility rate proceeds to a city's general fund as a general tax notwithstanding Proposition 218's prohibition on the use of utility rate proceeds for non-utility purposes? (Cal. Cost., art. XIII D, § 6, subd. (b)(2); and,

- can voters approve a general tax on water, sewer and trash services, or are such UUTs limited to special taxes by article XIII D, § 3's closed list of permissible impositions on property or "as an incident of property ownership"?

The general fund transfer question has been answered differently by three published cases to date. *Wyatt v. Sacramento* (2021) 60 Cal.App.5th 373, 383 upheld Sacramento's voter-approved general fund transfer from its utilities as "at least akin to a tax," which voters might approve under article XIII C, section 2. Shortly thereafter, *Lejins v. City of Long Beach* (2021) 72 Cal.App.5th 303 reached the opposite result. *Lejins* purported to distinguish *Wyatt*, but seems to disagree with it:

> In this regard, the matter before us is distinguishable from *Wyatt v. City of Sacramento* (2021) 60 Cal.App.5th 373, 274 Cal.Rptr.3d 710, a recent Third District Court of Appeal case on which the City relies in support of its contention a city's voter-approved general tax on utility services, to fund transfers to the city's general fund, does not violate article XIII D. In *Wyatt*, Sacramento argued—and the Court of Appeal concluded Sacramento proved—a voter-approved mandatory 11 percent tax Sacramento imposed on utilities' revenues was a cost of providing services that the utilities could pass on to ratepayers without violating article XIII D, section 6, subdivision (b). (*Wyatt*, at pp. 378, 380, 383, 274 Cal.Rptr.3d 710.) We express no opinion on whether *Wyatt* was correctly decided. We note only that *Wyatt*'s analysis is inapplicable to the case before us because the City

> here never argued, and there is nothing in the record indicating, the Measure M transfers and/or surcharge were in any way related to the costs of providing water and sewer services.

(Lejins, supra, 72 Cal.App.5th at p. 323–324.) Sacramento did not argue in *Wyatt* that its general fund transfer represented costs of utility service either, of course, only that once voters approved the tax, the utility was obliged to pay it and it was a "cost" of service allowable under Proposition 218 for that reason — just as Bradley-Burns sales taxes borne by utilities are.

Most recent in this series is *Palmer v. City of Anaheim* (2023) 90 Cal.App.5th 718, which concluded that a voter-approved transfer from Anaheim's power utility did not violate Proposition 26. Proposition 218 does not apply to electric rates by virtue of article XIII D, section 3, subdivision (b). Its reasoning was simple — Proposition 26 defines "taxes" which require voter approval and voters had approved the charter provision authorizing the general fund transfer in *Palmer* as a tax. This question recurs in a suit Riverside is defending that may soon reach the Court of Appeal. (*Simpson v. City of Riverside*, Riverside Superior Court Case No. RIC 1906168 (filed Dec. 19, 2019).)

Beck v. City of Canyon Lake, 4th District Court of Appeal case number D083322 (unpublished decision filed Mar. 20, 2025) affirmed a judgment invalidating that city's general UUT on water and sewer services as violating Proposition 218's article XIII D, section 3, subdivision (a), which states:

> Property Taxes, Assessments, Fees and Charges Limited. (a) No tax, assessment, fee, or charge shall be assessed by any agency upon any parcel of property or upon any person as an incident of property ownership except:

(1) The ad valorem property tax imposed pursuant to Article XIII and Article XIII A.

(2) Any special tax receiving a two-thirds vote pursuant to Section 4 of Article XIII A.

(3) Assessments as provided by this article.

(4) Fees or charges for property related services as provided by this article.

The Court also adopted *Lejins*' "distinction" of *Wyatt*.

Petitioners persuaded the trial court that, because water and sewer service charges are fees for a property-related service, a tax on those charges violates this provision of the Constitution unless approved by two-thirds of voters as a special tax under Proposition 13. But Proposition 218's ballot arguments and impartial analysis assured voters that utility taxes on water would continue post-Proposition 218 so long as voters approved them. A petition for review is due April 29, 2025. The ruling is unpublished, but its logic would invalidate the taxes of four counties and nearly 100 cities raising hundreds of millions of dollars. Absent review, copycat litigation is likely.

IV. Ratemaking

Ever since the Supreme Court made clear that retail water rates are property-related fees subject to Proposition 218, they have been often litigated, typically by plaintiffs' contingency counsel suing for refunds (and attorney fees) on behalf of a class of all rate payers. Such cases call for independent judgment review of legislative ratemaking. (*Silicon Valley Taxpayers' Assn., Inc. v. Santa Clara County Open Space Authority* (2008) 44 Cal.4th 431, 450 [independent judgment review of assessment under Prop. 218); *Hill RHF Housing Partners, L.P. v. City of Los Angeles* (2021) 12 Cal.5th 458, 482 [assessment levy is legislation].) This makes outcomes unpredictable. And, if refunds are available, and fees for class counsel, too, there will be many such suits — especially against the State's largest municipal utilities with the potential for multi-million-dollar payouts. Predictably, litigation abounds. We review some of the more recent decisions to aid ratemakers' counsel in containing risk.

Capistrano Taxpayers Assn., Inc. v. City of San Juan Capistrano (2015) 235 Cal.App.4th 1493 invalidated that City's tiered water rates, i.e., rates which increase with the amount of water used to encourage conservation, because the record on which rates were made did not plainly show that the amount charged in each tier recovered only the cost to serve water in that tier. As the decision occurred in the midst of historic drought, it garnered worldwide attention and a wave of litigation followed.

Coziahr v. Otay Water District (2024) 103 Cal.App.5th 785, review denied, is the most recent of these. This was a class-action challenge to tiered water rates imposed by a district which serves territory along the international border south and east of San Diego. At one level, *Coziahr* is just an application of *Capistrano*'s "show your math" rule — decided against the District because its tiered rates were not sufficiently justified by its ratemaking record. On another, though, it is very troubling. It rejected the approach to tiered rates recommended by the American Water Works Association's M-1 Manual — the most-cited authority on ratemaking — that looks to so-called "peaking factors" (ratios of the volume of water a customer or customer class uses in a peak hour, day, or month as compared to that customer's or class's average use). Although ratemaking is necessarily based on reasonable estimates of future expenses, this Court demanded "actual data" regarding costs the District incurred to provide water in each tier of use. It stated that reasonable estimates will not suffice. That standard will invite litigation and may discourage use of tiered rates even though the Legislature has passed laws in each of the last two years (discussed below) encouraging such rates because conservation is a necessity in our desert state. The Court of Appeal upheld an award of $18 million in refunds against Otay (remanding for its recalculation), rejecting argument that money awards are not authorized under Proposition 218.

Howard Jarvis Taxpayers Association v. Coachella Valley Water District (2025) 108 Cal.App.5th 485, review pending, was a class-action challenge to rates this agency charges to deliver raw water for irrigation via its canal system. It distinguishes urban irrigators (e.g., golf courses and homeowners' associations) from farmers and charges only the former the very high cost of supplemental water supplies under the Quantification Settlement Agreements which settled rights to Colorado river water among California agencies. Its rationales for doing so were farmers' historical use of and payment for the water (rejected in the trial court and not reasserted on appeal, although the decision states otherwise) and that urban development is driving the need for new supplies, while agricultural use is declining slowly as farmland is developed.

The trial court invalidated the rates despite evidence the District uses tax proceeds to subsidize rates below cost for all payors. It allowed standing even though the domestic ratepayers for which HJTA sued did not pay the raw-water rates — they bore some of their economic incidence via rates for domestic water service which benefit from groundwater replenishment with canal supplies. It concluded the duty to pay under protest imposed by Heath & Safety Code section 5472 did not apply because the statute references cities and counties, but not special districts like CVWD. It awarded $17 million in refunds and $4 million of that in fees to petitioner's counsel and enjoined the District to comply with Proposition 218 as to future ratemaking, threatening to turn future disputes into contempt proceedings in that case rather than new suits.

The Court of Appeal affirmed on every point but the last. Like *Otay*, it can be viewed as merely a record case and not precedent for rates made on other records. It refused to apply Government Code section 54958.5's new prohibition on refunds without much explanation, stating only that this statute effective January 1,2025 was "not before" the Court. But its holdings on standing, the duty to pay under protest, and the availability of refund remedies may not be so easily dismissed. CVWD's petition for review is pending as this paper is written and raises these questions for review:

- Does *Zolly v. City of Oakland* (2022) 13 Cal.5th 780 authorize challenge under Propositions 218 or 26 to a use of the proceeds of domestic water rates without showing that the use causes rates to exceed the reasonable cost of service, notwithstanding *Webb v. City of Riverside* (2018) 23 Cal.App.5th 244 and *Citizens for Fair REU Rates v. City of Redding* (2018) 6 Cal.5th 1?
- May a customer challenge under Proposition 26 a water rate that is less than the cost of service, due to subsidies from discretionary revenues, because other customers pay even less? Put differently, does Proposition 26 empower courts to independently review an agency's application of discretionary revenues to rate subsidies?
- Are refunds available under Propositions 218 and 26 by implication or common law development, despite California Constitution, article XIII, section 32's requirement of statutory authority for refunds of government revenues?
- Does federal due process require a monetary refund in rate challenges under Propositions 218 and 26?

The Supreme Court's decision to grant or deny review is due May 9, 2025 unless the Court extends that time, as it commonly does.

Patz v. City of San Diego, 4th DCA Case No. E083543 (tentative opinion issued Mar. 12, 2025). This was originally filed under one pleading with *Coziahr*, but the cases were bifurcated. San Diego had no more success than Otay, and the trial court entered a judgment invalidating its tiered rates and awarding almost $80 million in refunds, plus attorney fees. In a tentative ruling issued on March 12, 2024, a Riverside panel of the Court of Appeal affirmed the trial court's conclusion that the city's tiered rates were not supported by its record, but applied Government Code section 53759.1, subdivision (b) to overturn the refund award, remanding to the trial court to allow the remedy the statute calls for — a credit to the single-family residential class in a subsequent ratemaking. This same Division of the Fourth District refused to apply that statute to the *HJTA v. Coachella Valley Water District* case discussed above. Argument is set for May 6, 2025 and, of course, the Court is not bound to follow its tentative.

V. Water and Sewer Ratemaking

A. Tiered Water Rates

The 2015 decision in *Capistrano* discouraged water agencies from using tiered water rates. Environmental advocates and others favor such rates because they encourage conservation. This led Assemblywoman Papan (D-San Mateo), recently a Millbrae Councilmember, to introduce two bills in successive years to encourage such rates. First is 2023's AB 755, which adopts Water Code sections 390 and 390.1 to require a cost-of-service analyses (COSAs) for water rates prepared after January 1, 2024 to identify the top 10 percent of customers by demand and identify any costs associated with serving them. Identifying a cost caused by a customer class and not isolating that cost to that class in rate design implies an improper cross-subsidy of rates — i.e., cost-shifting from those customers to others. However, the statute refers to the top 10 percent of all **customers**, not the top 10 percent of any **customer class**. In many agencies, the largest users will be non-residential and a COSA can easily explain that costs associated with serving those users are not best allocated to them, but to customer classes such as commercial, industrial, single-family, etc. — as is industry-standard practice. Thus, the bill requires a little thought about these issues when preparing a COSA and adopting new rates, but may not unduly control rate design.

2024's AB 1827 seeks to facilitate tiered water rates by stating that a COSA can consider any or all of higher water demand, maximum potential water use, and projected peak water use in allocating costs to customers who use more water than others. It responds to trial court rulings in *Patz* and particularly *Coziahr* which adopted the plaintiffs' draft statement of decision declaring that tiered rates and use of peaking factors more generally (i.e., measures of the extent to which a water user class's peak use exceeds its average use) are necessarily unreasonable and violate Proposition 218 (Cal. Const., art. XIII D, § 6, subd. (b)(3)) unless the agency has time-of-use data. That reasoning is absurd: water ratemakers have been using peaking factors for decades and time-of-use data is a novelty available only to the largest and best-funded utilities. Thus, if time-of-use data is required, nearly all agencies must abandon a decades-old ratemaking practice and many adopted rates are inadequately supported. But nothing in Proposition 218 suggests votes intended that maintaining long-standing, industry-standard ratemaking practices would be deemed unreasonable. The bill adopts Government Code section 53750.6 and states that it is declaratory of existing law. *HJTA v. Coachella* found the statute inapplicable and no other court has yet applied it.

B. Exhaustion of Remedies; Litigation on the Record

Last year's AB 2257 (Wilson, D-Suisun City), sponsored by the Association of California Water Agencies (ACWA), makes two helpful changes to the Proposition 218 Omnibus Implementation Act. First, it authorizes agencies to require those who challenge new or increased fees, charges, or assessments for water or sewer services to exhaust administrative remedies before suit. That requires litigants to inform an agency, in writing, of the legal theories of suit along with a protest under Proposition 218's procedures for property-related fees or assessments. If they do not, they cannot sue. If they do, they can sue only on the issues they (or, perhaps, another objector) raised.

The requirements for the local remedy (best clarified by ordinance or resolution) are many, but most restate existing law. New requirements are that an agency must state in hearing notices that an exhaustion requirement applies and must respond in writing to every substantive comment made in objection to a proposed rate, charge, or assessment. This will require some work and last-minute comments (common in CEQA disputes) will slow down ratemaking, but adopting a local policy to clarify and maximize the exhaustion requirement ought to be a priority for every local water or sewer provider.

AB 2257 also provides that Prop. 218 challenges to water and sewer charges, fees, and assessments are litigated on the agency's record of its ratemaking — discovery is not permitted on the merits of such disputes. This is what many public lawyers understood to be the law, but we have been litigating the point and not always winning it. So, this is a helpful change. In addition, the statute defines the contents of a ratemaking record, ending disputes on that subject, too. These rules took effect in January 2025 without local action.

The statute adopts Government Code section 53759.1 (exhaustion) and 53759.2 (litigation on the record). To date, only the tentative ruling in *Patz v. San Diego* applies them. The statute's uncodified findings state the "act establishes a 'clearly defined machinery for the submission, evaluation, and resolution of complaints by aggrieved parties' (see *Plantier v. Ramona Municipal Water Dist.*, *supra*, 7 Cal.5th at p. 384, citing *Rosenfield v. Malcom* (1967) 65 Cal.2d 559, 566)."

C. Statutory Bar on Refunds in Proposition 218 Challenges

SB 1072 (Padilla, D-Chula Vista) states that refund remedies are not permitted in Proposition 218 challenges to property-related fees, including those for water, sewer and trash service. If a challenge to a fee determines that one class of customers or another, or all customers, have been overcharged, the necessary repayment is to be accomplished in the next ratemaking. This will prevent the multimillion-dollar refunds *Coziahr, Patz* and *HJTA v. Coachella* awarded, threatening the finances of providers of vital utility services. Such refunds wipe out agency reserves, which have to be refunded by rate increases, so this is all a very expensive way of shifting money from ratepayers' left pocket to their right – generating defense costs and large fee awards to plaintiffs' counsel, too. Orders that rates be corrected will be sufficient to protect ratepayers and to enforce Prop. 218. Indeed, this was how limits on revenue measures were enforced until the advent of class action claims in the last decade.

The statute adopts Government Code section 53758.5, the gist of which is:

> If a court determines that a fee or charge for a property-related service, including water, sewer, and refuse collection, violates Section 6 of Article XIII D of the California Constitution [i.e., Proposition 218], then the local agency shall, in the next procedure to impose or increase the fee or charge, credit the amount of the fee or charge attributable to the violation against

the amount of the revenues required to provide the property-related service unless a refund is explicitly provided for by statute.

A statement the measure was declaratory of existing law was deleted in the Legislature, but the bill should apply to rates made previously in any event. Courts apply the law in effect when judgment is entered, unless doing so would "result in manifest injustice or there is statutory direction or legislative history to the contrary." (*Woodland Hills Residents Assn., Inc. v. City Council* (1979) 23 Cal.3d 917, 931, citing *Bradley v. School Bd. of City of Richmond* (1974) 416 U.S. 696, 711.) And even if judgment has entered and a case is on appeal, the reviewing court "must dispose of the case under the law in force when its decision is rendered." (*Governing Board v. Mann* (1977) 18 Cal.3d 819, 831.)

"It is well established that a plaintiff has no vested property right in a particular measure of damages, and that the Legislature possesses broad authority to modify the scope and nature of such damages." (*American Bank & Trust Co. v. Community Hospital* (1984) 36 Cal.3d 359, 368; see also *Fein v. Permanente Medical Group* (1985) 38 Cal.3d 137, 159; *Werner v. Southern California Associated Newspapers* (1950) 35 Cal.2d 121, 129.) "All statutory remedies are pursued with full realization that the legislature may abolish the right to recover at any time." (*Callet v. Alioto* (1930) 210 Cal. 65, 67–68.)

Moreover, SB 1072 represents "a considered legislative judgment as to the appropriate reach of the constitutional provision." (*Greene v. Marin County Flood Control & Water Conservation Dist*. (2010) 49 Cal.4th 277, 291.) It therefore "enjoys significant weight and deference by the courts." (*Ibid*., citing *Pacific Legal Foundation v. Brown* (1981) 29 Cal.3d 168, 180.) And, like a court, the Legislature interprets Propositions 218 and 26 as they were adopted in 1996 and 2010, respectively. Retroactivity is not an issue.

D. Stormwater and Sewer Fees

The cost of complying with Regional Water Quality Control Board mandates under the federal Clean Water Act's National Pollutant Discharge Elimination System (NPDES) has become unsustainably expensive. Proposition 218, as interpreted in *Howard Jarvis Taxpayers Ass'n v. City of Salinas* (2002) 98 Cal.App.4th 1351 requires majority property-owner approval, or two-thirds registered-voter approval, of fees for water quality and flood control programs. (Cal. Const., art. XIII D, § 6, subd. (c).) *Salinas* read Proposition 218's exception from that rule for fees for "sewer, water, and refuse collection services" (*ibid*.) to limit "sewer" to sanitary sewer fees.

Environmental advocates who persuaded the regional boards to impose the expensive water quality mandates have recognized the need to help local governments fund compliance. This led to 2017's SB 231 (Hertzberg, D-San Fernando Valley) which amended Government Code section 53750, subdivision (k) to define the "sewer" services fees which are partially exempt from Proposition 218 to include storm, as well as sanitary, sewers. It also adopted Government Code section 53751 to explain the Legislature's disagreement with *Salinas*. One trial court accepted that reasoning and refused to follow Salinas. (*Gluck v. City and County of San Francisco*, 1st DCA Case No. A170087.) The appeal has been fully briefed and awaiting argument since October 30, 2024, so argument is likely soon.

However, the Third District Court of Appeal, while noting that SB 231 postdated the dispute before it, nevertheless disagreed with it and provided a more intellectually rigorous justification for *Salinas*' interpretation of Proposition 218. (*Department of Finance v. Commission on State Mandates* (2022) 85 Cal.App.5th 535.) The decision concluded that, because of the voter-approval requirement, local governments do not have the power to adopt stormwater fees. Accordingly, many of the provisions of the 2007 NPDES permit for the County of San Diego and the cities within it are unfunded state mandates requiring the Legislature to fund their costs or to suspend the mandate. Interestingly, the Court of Appeal noted that many stormwater permit programs amount to removing waste from waterways and might therefore be funded by a fee for "refuse collection services" exempt from Proposition 218's election requirement, and subject only to its 45-day noticed majority-protest proceeding, with which we have become familiar.

In light of these developments, cities may rely on one or more of these options to fund stormwater mandates:

- use general funds;
- charge appropriate portions of the stormwater budget to other city programs which burden the system — like water, sewer and trash services;
- recover a portion of the stormwater budget from a fee for "refuse collection services" in the form of efforts to prevent trash from entering receiving waters or removing it from them;
- seek property-owner or voter approval of a stormwater fee under article XIII D, section 6, subdivision (c); or
- seek voter approval of a general or special tax under article XIII C, section 2.

Dessin, LLC v. City of Sacramento, 3rd DCA Case No. C100644 is a challenge to a fee for combined sewer and storm sewer services imposed after a property-owner election under Proposition 218's article XIII D, section 6, subdivision (c). This reverse validation challenge argued that the measure should have failed because the margin of victory was provided by the city's own properties and those of other government agencies, of which there are many in our capital city. The trial court ruled for City and the petitioners appealed. The appeal is fully briefed and awaiting argument as of March 3, 2025. Argument is likely late this year.

VI. Conclusion

Further developments are, of course, inevitable. City Attorneys should monitor new developments in the courts, the Legislature, and in the communities we serve.

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Our File No. 99904.0114

Current Developments in the Law of Municipal Revenues:

Regulatory Fees After *Sutter's Place, Inc. v. City of San Jose;*
What's Bubbling with Soda Taxes; &
Development Impact Fee Update – Cases and Statutes

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I. Regulatory Fees After *Sutter's Place, Inc. v. City of San Jose* (2024) 104 Cal. App. 5th 855

Holding: Regulatory fees under Proposition 26 cannot cover the full cost of a regulatory program. Instead, fees must be limited to specific activities enumerated in Cal. Const., art. XIII C, § 1, subd. (e)(3): "issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof."

The Sixth District also found San Jose properly divided its regulatory costs equally between two licensed cardrooms, since both could operate the same number of tables. The appellate court interpreted Proposition 26's exceptions to the definition of a tax very narrowly—treating the measure as if it were a statute passed by the Legislature, rather than a voter initiative, which precedent requires to be interpreted more flexibly in light of voters' apparent intent rather than in a strict way informed by the canons of statutory construction.

As a result, local governments may no longer be able to fund regulatory programs through regulatory fees alone. Any unrecoverable costs may need to be subsidized by other sources, like the general fund, which are often already overextended. Since the California Supreme Court declined to review or depublish the decision, this interpretation remains binding law—unless a future Court of Appeal is persuaded to issue a contrary decision and the Supreme Court elects to resolve the conflict.

Sutter's Place also reaffirms earlier case law that allows agencies flexibility in how they distribute regulatory costs among the entities they regulate, as long as the allocation is reasonable. An equal split was acceptable here even if one club or the other made greater demands on the City's staff in a given year. Additionally, it confirms that if a court invalidates certain costs recovered through a Proposition 26 charge, the appropriate remedy is not a full refund. Instead, the refund should be the difference between what the fee payer paid and what they should have been charged in compliance with Proposition 26 to cover the agency's valid costs.

Facts/Background: Sutter's Place, Inc., operating as Bay 101 Casino, and M8trix are San Jose's only two cardrooms. Each is licensed to operate 49 tables and is open 24 hours per day, year-round. San Jose imposes three charges on each: a voter-approved special tax that varies with a cardroom's income; a licensing fee of about $1,500 per year; and a regulatory fee, which varies annually based on the City's projected enforcement and regulation costs.

The regulatory fee is split evenly between the two cardrooms. Over the seven years at issue, each paid between $826,871 and $1,012,142 annually. In all but two of those years, the fee revenue fell short of the City's actual regulatory costs.

Sutter's Place sued, claiming the fee was an unconstitutional tax under Proposition 26 and violated due process. It also claimed the regulatory fee violated Proposition 26 in two ways: the fee included costs unrelated to regulatory functions and thus exceeded the City's actual or reasonable costs of administration; and that dividing the fee equally failed to reflect differences in regulatory burden between the two cardrooms, which forced Sutter's Place to bear an unreasonable share of the cost of the regulatory program.

Specifically, Sutter's Place disputed four types of costs that the City sought to recover through its regulatory fee: legislative activity, including work to amend the municipal code and travel to Sacramento to testify before the California Legislature (at card rooms' request); responding to California Public Records Act requests from card rooms and others; City attorney's office staff time spent on litigation (including this case); and tax-monitoring activities. Because these are not among the cost categories in Proposition 26's regulatory fee exception, Sutter's Place argued their inclusion made the fee into a tax requiring voter approval.

The trial court found for the City, stating there was no "specific test" for determining which costs could be included. Therefore, all costs reasonably related to regulation could be included. The trial court also found that the equal fee split between the two licensed clubs bore a fair and reasonable relationship to the respective burdens of each cardroom.

The Sixth District reversed. It held that Article XIII C, § 1(e)(3) of the California Constitution provides a specific test for valid regulatory fees: charges must be limited to the reasonable costs of licensing, inspections, investigations, audits, and related enforcement.

The City's regulatory fee was designed to recover both direct and indirect regulatory costs, including general government functions like CPRA compliance, tax monitoring, amending the municipal code, and litigation. The appellate court found these broader cost categories indirectly related to the regulation exceeded the narrow constitutional exception.

The Sixth District noted that there may be costs associated with operating the cardroom regulation program that cannot be recovered through a regulatory fee under the narrow constitutional exception. The government must show the costs comprising the fee are incurred only for permissible regulatory activities, not just peripherally related to the regulatory program.

The case was remanded for further proceedings. The trial court must determine whether the four disputed cost categories fall outside the permissible scope of Proposition 26. If the fee collected exceeded the City's allowable regulatory costs, Sutter's Place is entitled to a refund of the difference—but not a full refund. If actual allowable costs were higher than the fee charged (as the City contends), no refund is owed.

Analysis: The Sixth District took a narrow view of Proposition 26's regulatory fee exception, limiting recoverable costs to those directly tied to licensing, inspections, investigations, audits, and related enforcement. Based on that reading, the trial court may find that the four cost categories challenged in *Sutter's Place*—legislative activity, CPRA responses that would not be necessary but for the operation of regulated party, litigation, and tax monitoring—cannot be recovered from a regulatory fee.

This decision suggests that indirect costs related to regulation may not be recoverable by a regulatory fee. Those costs may now require support from general fund or other discretionary revenues. Based on the ballot arguments on Proposition 26, this is a shift from how most public lawyers interpreted Proposition 26. Most public lawyers understood that the fees could cover the full cost of regulatory programs, which necessarily require rulemaking, and Public Records Act compliance, and litigation because these are costs associated with licensing, permitting, investigations, and the like. That is certainly what voters were led to expect.

Historically, courts readily found that agencies could recover the full cost of a regulation, including indirect costs, as long as the agency could justify them. Courts have upheld recovery of expenses such as utility impacts,[1] debt service,[2] sewer system management,[3] and housing inspection programs[4] when tied to the cost of service. Drafting and updating regulations had also been considered a legitimate, recoverable expense under the regulatory fee exception.

This decision means that trial courts now face conflicting precedents. Some may follow *Sutter's Place* for Proposition 26 fees, while limiting cases like *Griffith v. Pajaro Valley Water Management Agency,* which allowed indirect cost recovery under Prop. 218, to that measure.

Equal Division of Regulation Fee. Regarding the equal division of the regulation fee, the Sixth District agreed with the trial court, upholding the City's equal cost allocation between cardrooms. The Sixth District also found that substantial evidence supported the trial court's determination that equally allocating the cardroom regulation fee between the two cardrooms was fair and reasonable. It noted that local agencies need not show a precise cost-fee ratio, as Proposition 26 only requires a reasonable basis for cost allocation. The appellate court noted the two cardrooms had similar operations, the same number of licensed tables, and imposed equal burdens on the City's oversight over time, despite varying regulatory attention in a given year.

Refund Limited to Invalid Costs Only. Although Sutter's Place sought a full refund, the Sixth District held that only impermissible costs must be refunded, aligning with earlier Proposition 26 decisions.[5] The court observed that "in all but two of the contested years, the cardroom regulation fee was lower than the defendants' total actual costs." If the trial court finds that the City's allowable costs exceeded the fee charged, no refund is owed. If some charged costs were impermissible, the refund is limited to the difference between what was charged and what could have been lawfully imposed under Proposition 26.

Due Process for Refunds of Regulatory Fees. The trial court rejected plaintiff's claim that its federal constitutional right to due process was violated by the imposition and

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[1] See *Howard Jarvis Taxpayers Ass'n v. City of Fresno* (2005) 127 Cal.App.4th 914, 927
[2] *Griffith v. Pajaro Valley Water Management Agency* (2013) 220 Cal.App.4th 586, 598
[3] *Moore v. City of Lemon Grove* (2015) 237 Cal.App.4th 363, 369
[4] *Griffith v. City of Santa Cruz* (2012) 207 Cal.App.4th 987, 997
[5] *Citizens for Fair REU Rates v. City of Redding* (2018) 6 Cal.5th 1.

implementation of the cardroom regulation fee as an unconstitutional tax imposed without voter approval.

Citing *McKesson Corp. v. Division of Alcoholic Beverages and Tobacco, Dept. of Business Regulation of Florida* (1990) 496 U.S. 18, 32, the Sixth District explained that a valid due process claim arises if a party is denied both the opportunity to challenge a fee and a meaningful remedy for any unlawful taxation. (*McKesson*, at p. 39). If the trial court finds any refund is owed, Sutter's Place is entitled to proceed to trial on its federal due process cause of action.

This reasoning represents a novel application of *McKesson*—a tax case—to regulatory fees. Under the court's logic, any dispute which can be monetized is a federal due process claim. Regulatory fees do not involve federally protected property interests unless the right to do business at all is at stake.

Takeaways: This case is bad news for local agencies, suggesting much more work to be done to impose defensible fees and much greater risk of litigation and large refund awards.

- <u>Full cost recovery may be risky</u>. A fee that includes full cost-recovery of all costs both directly and indirectly related to a regulatory program is now harder to defend. Some general fund support will allow a margin for error.

- <u>To avoid risk, fees must clearly fall within Proposition 26's regulatory fee exception permitted categories.</u> To minimize legal exposure, fees should be limited to the regulatory activities listed in Cal. Con., art. XIII C, § 1, subd. (e)(3):

    - Issuing licenses and permits
    - Performing investigations, inspections, and audits
    - Administrative enforcement and adjudication of those activities

    For costs not plainly within these categories, make findings supported by evidence in the ratemaking record how they relate to the permitted categories and are necessary costs of providing the service for which the fee was adopted.

- If a general fund subsidy is required, document it in ratemaking record.

  Agencies should comply with 2024's AB 2257's procedures to impose a duty to exhaust administrative remedies before suit to limit exposure to suit and give the agency a full opportunity to consider the asserted bases for challenge and make administrative corrections. (Gov. Code §§ 53759.1 and 53759.2). Although that statute applies only to Proposition 218 challenges to utility fees, cities' and counties' police power under California Constitution, article XI, section 7 will allow a broader local exhaustion requirement. Special districts also have such power under article XI, section 9 empowering them to provide utility services and, by implication, to impose fees and fee-making procedures to do so.

- Be clear and specific in your fee resolution. Use your fee-setting resolution as an opportunity to explain how fees support permissible activities instead of generally citing the need for regulation.

- Ensure support for allocation is fair and reasonable. Courts generally defer to how agencies allocate fees among payees, applying a standard similar to rational basis review. As long an agency can show by a preponderance of the evidence that the allocation is fair and reasonable across all payees, it will likely hold.

- Follow legal developments. This area of the law is developing rapidly.

II. What's Bubbling with Soda Taxes

Over the past decade, soda taxes in California have sparked ongoing disputes—from the 2018 passage of Keep Groceries Affordable Act of 2018 ("Groceries Act"), a political compromise to block a harmful revenue initiative, to the recent legal challenge in *Cultiva La Salud v. State,* which invalidated a provision threatening charter cities' sales tax revenues if they enacted soda taxes.

Following that ruling, in the November 2024 election, the City Santa Cruz took on the beverage industry with its Measure Z "Sugar Sweetened Beverage Tax", which was adopted by its voters. While no lawsuit has been filed yet, threats of litigation continue to loom over Measure Z. If "Big Soda" does not challenge Santa Cruz's tax, other charter cities will likely follow, both to raise money and to discourage consumption of what they perceive to be a health risk.

***Cultiva La Salud v. State of California* (2023) 89 Cal.App.5th 868**

Holding: The penalty provision in the Keep Groceries Affordable Act of 2018 (AB 1838), which threatened charter cities with losing sales and use tax revenue if they imposed taxes on sugar-sweetened beverages, is unconstitutional. The penalty provision improperly uses the threat of crippling penalties to deter charter cities from exercising their right to enact local taxes under the home-rule doctrine of the California Constitution.

Facts/Background: Between 2014 and 2016, Berkeley, San Francisco, Oakland, and Albany adopted 1-cent-per-fluid-ounce taxes on the distribution of sodas and other sugar-sweetened beverages, citing the dangers of too much sugar in children's diets. Similar efforts were underway in Chicago and Seattle, as well as Cook County, IL.

To stop this trend, the beverage industry contributed generously to the California Business Roundtable's proposed "Tax Fairness, Transparency, and Accountability Act of 2018." This initiative was intended to amend the California Constitution to make nearly all State and local government revenues subject to a two-thirds voter approval and included other restrictive provisions, such as limiting regulatory fees to actual costs.[6] It was a forerunner of a similar Business Roundtable measure excluded from the 2024 ballot by *Legislature of State of California v. Weber* (2024) 16 Cal.5th 237.

To avoid a costly fight to defeat that 2018 initiative, the Legislature passed the Groceries Act in exchange for the initiative proponents' agreement to withdraw the measure. The Groceries Act imposed a 12-year moratorium on new or increased local taxes on carbonated and noncarbonated nonalcoholic beverages. In effect, the State agreed to restrict one type of local government taxing authority to prevent what it perceived as a much larger threat of loss of State and local revenue authority.

[6] Tax Fairness, Transparency, and Accountability Act of 2018 initiative petition: https://www.oag.ca.gov/system/files/initiatives/pdfs/17-0050%20%28Two-Thirds%20Vote%20Requirement%20V1%29.pdf

Specifically, the California Legislature passed AB 1838, labelled the "Keep Groceries Affordable Act of 2018" (Rev. & Tax. Code §§ 7284.8–7284.16). The Groceries Act prohibits charter cities, counties, and other local governments from imposing taxes, fees, or assessments on listed grocery items, including sodas and other sugar-sweetened drinks.

The Act also includes a penalty requiring the California Department of Tax and Fee Administration (CDTFA) to terminate its contract with local agencies that impose taxes on groceries, causing the loss of all sales and use tax revenue (including Bradley-Burns 1 % taxes and any local add-on transactions and uses tax) for any charter city that enacted a tax on sugar-sweetened beverages to test the claim that the Groceries Act was not a matter of statewide concern that could be imposed on charter cities.

The Groceries Act caused several cities to abandon plans to pursue local taxes on sugar-sweetened drinks, including Santa Cruz and Stockton. After the City of Santa Cruz abandoned its pursuits of a soda tax, the nonprofit health group, Cultiva La Salud, along with Santa Cruz City Council Member Martine Watkins, sued the CDTFA, challenging the Groceries Act's penalty provision as unconstitutional as it seeks to bypass charter cities' legitimate authority by imposing a harsh penalty for properly exercising their rights under the home rule doctrine.

Under California's familiar "home rule doctrine,"[7] charter cities may make and enforce ordinances on municipal affairs free from preemption by general laws. A charter city's law on a matter of local concern may only be preempted when it conflicts with a state law addressing a subject of statewide concern, the state law is reasonably related to resolution of that concern, and the state law is narrowly tailored to avoid unnecessary interference in local governance.[8]

Plaintiffs alleged the Legislature knew the home rule doctrine prevented the state from blocking charter cities' right to impose taxes on sugar-sweetened drinks. Thus, instead of enacting an outright prohibition on charter city authority, the Legislature imposed a harsh penalty to deter cities from exercising this right, making it too risky for any charter city to enact a local soda tax. Plaintiffs sought a declaration that the Groceries Act's

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[7] Cal. Const., art. XI, § 5

[8] *State Building & Construction Trades Council of California v. City of Vista* (2012) 54 Cal.4th 547, 555–556

penalty provision was unlawful, an injunction to prevent its enforcement, and a writ of mandate directing the Department not to implement it.

Amicus briefing described this as an example of what academics have called "punitive preemption," by which legislatures not only preempt local legislation, but punish those cities which adopt it — a disheartening retreat from principles of home rule and pluralism.

The Department argued the case was not ripe, and should be decided only after a charter city has enacted a tax triggering the Act's penalty. They also argued the provision penalizes a charter city only when its grocery tax "would **otherwise** be a valid exercise of a of the local government's constitutional powers, **in the absence of the Groceries Act**." Meaning, the penalty would only apply if the Groceries Act is the only reason for finding the tax is prohibited. The Department argued any offending language could be severed to save the rest of the provision.

Finding for Plaintiffs, the trial court found the case ripe for review due to plaintiffs' facial challenge because their petition raised important legal questions that might otherwise remain unanswered, as charter cities may avoid enacting a soda tax fearing the financial risk posed by the penalty provision. Stockton and Santa Cruz did just that after the Groceries Act was adopted. The court found the penalty provision unlawful and deemed it unenforceable because it only penalizes charter cities that validly exercise their constitutional rights under the home rule doctrine. The Department appealed.

Analysis: The Third District affirmed.

<u>Ripe for Review</u>. The appellate court agreed with the trial court's analysis, rejecting the claim that the case should not be reviewed until a local tax was imposed. The court explained that accepting this position would create a situation where laws with potentially unconstitutional provisions could escape judicial scrutiny, as the fear of penalties would prevent cities from challenging them. This approach, the court reasoned, would let the state impose unconstitutional laws with no recourse for affected parties.

The court found that the facts had sufficiently "congealed" to allow for a final ruling on the plaintiffs' facial challenge to the Groceries Act's penalty provision, citing *Vandermost v. Bowen* (2012) 53 Cal.4th 421. The court noted that deferring the case would result in lingering legal uncertainty, particularly because the Groceries Act's penalties that required charter cities to risk loss of their sales and use tax revenues were so severe that no charter city would likely ever enact a soda tax under its terms.

<u>Groceries Act's Penalty Provision Unconstitutional.</u> On the merits, the appellate court rejected the CDTFA's argument that the penalty only applies if the Groceries Act is the only reason a charter city's tax is prohibited. To understand the Act and its penalty provision, the court looked to the Groceries Act's context – the Bradley-Burns Uniform Local Sales and Use Tax Law of 1955, particularly its 1996 amendment.

The appellate court observed that, like the 1996 amendment to the Bradley-Burns Act, section 7284.12 of the Groceries Act reflects the Legislature's concern about preempting charter city taxes. Both laws follow a similar structure: they first prohibit local governments from imposing certain taxes, and then, as a backup, threaten severe penalties if taxes are adopted nevertheless. The court concluded that both laws aim to prevent charter cities from enacting specific taxes, either directly or through the threat of severe penalties if the prohibition is ineffective.

Considering this purpose, the appellate court agreed with the trial court, that section 7284.12 improperly uses the threat of crippling penalties to chill charter cities from exercising their constitutional rights. As the California Supreme Court explained, "[i]f a law has no other purpose than to chill the assertion of constitutional rights by penalizing those who choose to exercise them, then it [is] patently unconstitutional." (*In re King* (1970) 3 Cal.3d 226, 235-236).

<u>Offending Penalty Provision Cannot Be Severed.</u> The appellate court ruled it couldn't sever parts of the penalty provision, as the Department suggested, because doing so would have significantly changed the scope by creating penalties for counties and general law cities, where none were provided by the Legislature. Severance may be used by a court to remove offensive language when the language is grammatically, functionally, and volitionally separable; it is not a tool for creating new penalties the Legislature never intended.

Since the offending provision could not be stricken, the appellate court found the entire penalty provision unlawful and unenforceable. This outcome isn't surprising, given that the Groceries Act's penalty provision clearly targeted expressive activities— framing and adopting local policy – and resort to courts to defend the home rule doctrine. Few courts will tolerate penalties on those who seek judicial assistance. (*San Diego County Water Authority v. Metropolitan Water Dist. of Southern California* (2017) 12 Cal.App.5th 1124.)

Takeaway: The fight for soda taxes and home rule for charter cities is likely not over. In the November 2024 election, Santa Cruz's voters adopted Measure Z. Known as the "Sugar Sweetened Beverage Tax," Measure Z is the first soda tax passed in California since the Groceries Act was enacted in 2018 and after *Cultiva La Salud*.

Measure Z passed despite expensive opposition from the beverage industry lobby. The American Beverage Association has threatened a lawsuit will be filed to challenge Measure Z in the spring of 2025. If filed, the lawsuit would be the first case to challenge a charter city's soda tax after the Groceries Act's penalty provisions were held unconstitutional by the Third District. If Measure Z is not challenged by Big Soda, or it survives a challenge, other charter cities in California are expected to follow.

As of this paper, no challenge has been filed.

III. Development Impact Fee Update – Cases and Statutes

A development impact fee (DIF) is a charge by local governments on developers to cover public facility costs related to their projects (Gov. Code § 66000(b)) and is regulated under the Mitigation Fee Act.

The Mitigation Fee Act (Gov. Code §§ 66000-66025 or "AB 1600") requires local agencies to adopt five-year findings to account for balances of development impact fee proceeds held for more than five years. The findings are to be included in the agency's annual reports and must be filed within 180 days of the end of the fiscal year.

Fees governed by the Act, distinct from taxes or special assessments, must reflect service costs. Imposing a fee requires a nexus study, and annual or five-year reports to demonstrate proper and timely use of funds. If a fee exceeds service cost, it is a special tax, requiring two-thirds voter approval (Cal. Const., Art. XIII A, § 4).

Coming off a busy 2023–2024 Legislative session for development impact fees, these are new statutes and recent cases to be aware of.

County of El Dorado v. Superior Court (2019) 42 Cal.App.5th 620

Holding: Statute of limitations for refund claim under AB 1600 was one year, as the duty to refund fees is a penalty, triggering the statute of Code of Civil Procedure section 340, subdivision (a).

Facts/Background: Property owners, the Austins, sued to recover DIFs under the Mitigation Fee Act levied by the County and its special districts. The Austins alleged that the County did not make the necessary "nexus" findings to justify the continuing need to hold unexpended funds generated from 11 DIFs. The County contended that the statute of limitations barred the action and that the Austins needed to show "prejudice" to recover the fees.

The trial court rejected the County's demurrer regarding the statute of limitations, but upheld the demurrer because the plaintiffs failed to include necessary parties. The County petitioned for writ of mandate.

Analysis: On interlocutory review, the County argued that a one-year statute of limitations for penalties and forfeitures applied, and that the plaintiffs did not show prejudice as Government Code section 65010required . The Court of Appeal agreed, ruling that a one-year statute of limitations applied. Since the mandatory damages the plaintiffs sought were in addition to any actual harm they suffered, they were a penalty, subject to the one-year limitations period under Code of Civil Procedure section 340(a).

The appellate court rejected the County's argument that the trial court's action resulted in the invalidation of the county's fees and therefore was not permissible under Government Code section 66022, imposing validation's 60-day bar on such disputes. Instead, it was properly characterized as a refund action based on the County's failure to make timely nexus findings justifying retention of fees. The claim could proceed—at least as to payments made within the statute of limitations—under the continuous accrual doctrine. The County's demurrer was overruled, since the plaintiffs could recover fees for the one-year period preceding each breach. Each fee collected without proper findings constitutes a new breach, resetting the statute of limitations for that collection. While the statute of limitations did not completely bar the action, it limited the recovery.

The appellate court also ruled the requirement in Gov. Code section 65010's requirement of prejudicial error was not applicable to the Austins' AB 1600 claim. The appellate court denied the County's petition for writ of mandate.

Takeaway:

- Statute of limitations to challenge DIFs is one-year
- Suit can be filed to challenge the sufficiency of annual and five-year findings, so the statute limits remedy, but not litigation exposure
- AB 1600 findings are burdensome, but statutorily sufficient and compliant annual and five-year findings are necessary to protect your agency

This case helpfully limits *Walker v. City of San Clemente* (2015) 239 Cal.App.4th 1350 which had ordered refund of all fees collected since inception of a fee.

Hamilton & High, LLC v. City of Palo Alto (2023) 89 Cal.App.5th 528, review denied

Holding: A fee a paid voluntarily in-lieu of providing all the parking a developer's project required was also subject to AB 1600. The court ordered the city to refund the fees because it had not spent them for the purposes for which they were collected in the allowed time and had not adopted adequate findings to support retention.

Facts/Background: In 2013, the Plaintiffs received entitlements for a mixed-use building, conditioned to provide 40 parking spaces. They opted to pay fees $906,900 in lieu of constructing 16 spaces. The City Council certified an EIR for a parking garage to timely spend those funds, but members of the public and some Councilmembers questioned the need for more parking rather than parking demand management.

In January 2019, the City issued five-year findings required by AB 1600 for the period that included Plaintiff's 2013 in-lieu parking payment. However, because the City contended this in-lieu fee was not governed by AB 1600, those five-year findings did not cover the developer's fee.

The Developer asked for a refund, which the City denied in February 2020. The City adopted five-year findings related to the parking fund in May 2020.

Less than two weeks after the City issued its findings, the developer sued to recover the $906,900 in unspent in-lieu parking fees, paid 7 years earlier. The developer argued that the City did not provide timely findings as mandated under the AB 1600. The City contended that (1) the in-lieu parking fees were not subject to AB 1600's reporting requirements; (2) the fees were not included in the City's 2019 report because they had not yet been held for five years; (3) the action was barred by the one-year statute of limitations; and (4) the May 2020 findings complied with the AB 1600 reporting requirements.

The trial court ruled for the City, concluding the case was not filed within one-year statute of limitations under *County of El Dorado v. Superior Court* (2019) 42 Cal.App.5th and AB 1600 did not apply because the fees were paid voluntarily, rather than "imposed" by the City. The developer appealed.

Analysis: The Court of Appeal reversed, concluding that the claim did not accrue until the City rejected the refund demand — without identifying a deadline for the refund demand. The appellate court also concluded AB 1600 applied because the fees were a condition of development (even though the developer paid them rather than provide on- or off-site parking), the City's belated five-year report did not satisfy the requirement to prepare it within 6 months of the end of a fiscal year, and that Government Code section 65010(b) did not require the developer to prove prejudice resulting from the delay in findings. The court directed the trial court to order the City to refund the unexpended fees.

In-lieu fees had not been understood to be subject to AB 1600, because they are a voluntary alternative to providing project improvements to meet zoning standards. Thus, local agencies have rarely made the AB 1600 one- and five-year findings as to in-lieu fees.

Before *Hamilton* these fees were analyzed under the regulatory takings standard of *Ehrlich v. City of Culver City* (1996) 12 Cal.4th 854, which had upheld a fee in lieu of public art included in a project against a takings challenge. *Ehrlich* analysis requires much the same justification as AB 1600 to **establish** a fee, but does not require the money to be spent by a deadline, nor does it require annual and five-year reports.

This is crucial because in-lieu fees rarely support -identified projects and are often held until an opportunity arises to use them effectively. Unless the Legislature enacts a statutory solution, cities may want to reconsider accepting fees instead of requiring developers to meet development standards, such as providing required parking or public art. While developers would lose some options in this scenario, cities would mitigate their risk. *Hamilton* also seems to criticize the holding of *El Dorado*, although it does not formally disagree with it.

Takeaway: In light of this decision, agencies are advised to:

- Require a recorded agreement, perhaps a development agreement, with a developer who chooses to pay a fee rather than meet zoning standards by which it expressly waives application of AB 1600 and any right to a refund of the fee.
- Adopt AB 1600 findings for in lieu fees, annually and every five years.
- Spend fee proceeds timely.
- Consider eliminating in-lieu fee ordinances in favor of enforcing zoning standards and rely on variances and development agreements to vary those standards if necessary.

This case is reason to renew focus on AB 1600 compliance, especially careful programming of funds and timely, well-drafted findings.

Barajas v. City of Petaluma First District Court of Appeal Case No. A1652 (unpublished)58, review denied (Nov. 13, 2024)

Holding: A two-month delay in filing a required report on development impact fee balances did not entitle plaintiffs to a $36 million refund. AB 1600 mandates that local agencies adopt five-year findings for unexpended development impact fees, but does not require new studies.

Facts/Background: As of June 30, 2018, the City had about $32 million in unexpended impact fee funds for various City facilities and traffic improvements.

On February 25, 2019, City's Council adopted a resolution making its five-year findings using mitigation fee reports from 2003, 2008, and 2012 to support the use of the DIFs. The capital improvement program for fiscal year 2018–2019 identified City's five-year plan for capital improvement projects, including improvements funded with impact fees, as well as other sources.

Adrian Barajas sought declaratory relief for the City's failure to make required five-year findings under AB 1600, and filed a writ of mandate to stop the City from collecting impact fees and to refund all unused DIF as "invalid, void, and illegal."

Barajas argued, inter alia, that the City had violated Gov. Code section 66001(d)(1) because its five-year findings for 2018 were based on studies conducted earlier. The trial court disagreed, ruling that section 66001(d)(1) required the City to make new findings, not conduct new studies, and that the City's findings were adequately supported by evidence. Barajas appealed.

Analysis: The First District affirmed the trial court's rulings, explaining that the purpose of the five-year findings was to show the reasonable relationship between fees and the continuing need for the intended public facilities, not to require new studies every five years. The court found that the City's use of past nexus studies from 2003, 2008, and 2012 met the Act's requirements, as they sufficiently identified the purpose and expected projects for which the fees were retained.

Takeaway:

- Make findings annually and every five-year findings, as required by section 66001(d)(1) establishing the continuation of the need for the capital projects for which the fees were collected
- New studies are not required if earlier studies provide adequate evidence of the nexus between fees and their intended purposes BUT nexus studies must be updated every 8 years (starting 1/1/22) per Gov. Code § 66016.5(a)(8).
- Agencies should be mindful of maintaining up-to-date records and consistently making required annual and five-year findings to avoid disputes.

Sheetz v. County of El Dorado (2024) 601 U.S. 267

Holding: Legislatively adopted fees on new development to mitigate its impacts are subject to the same analysis as similar, one-off or ad hoc permit conditions or exactions. This holding follows the familiar analysis established by *Nollan* and *Dolan*, which require any condition or mitigation measure imposed on development have a logical connection — or "nexus" — to the impact it seeks to address (i.e., a traffic fee should mitigate traffic impacts). Additionally, the condition must be at least "roughly proportionate" in scale to the development's impacts.

AB 1600 already requires a nexus study to support new fees and annual and five-year reports to show the fees bear a reasonable relationship to the purpose for which they're collected, and are properly collected, programmed and/or spent. So, this should be of lesser significance in California. Still the property-rights bar views the case as a significant win.

Facts/Background: George Sheetz proposed a modular home in unincorporated El Dorado County. The County conditioned the building permit on a $23,420 traffic mitigation fee — a legislatively adopted development impact fee required by its general plan for all residential development. Sheetz sued, backed by the property-rights bar.

Sheetz argued the fee violated *Nollan* / *Dolan* because there was no showing that the application of the adopted fee to his modest project could be demonstrated to bear any reasonable relationship to its impacts; i.e., he argued there was no reasonable basis to support that his home could trigger a need for Countywide traffic improvements or that the amount of the fee was commensurate to the traffic demand his home would generate.

He lost in the trial and California appellate courts, which followed precedents holding that *Nollan* / *Dolan* apply only to one-off ad hoc permit conditions and exactions, and not to legislatively adopted, generally applicable, fee programs, like AB 1600 fees. The California Supreme Court denied review, but the U.S. Supreme Court granted certiorari.

The briefing in *Sheetz* raised the possibility the case might threaten impact fees and mitigation measures broadly, but oral argument made clear the Court was not headed there. El Dorado County conceded at argument the only point the Supreme Court would decide — that legislative fees and conditions on classes of developments are subject to the same requirements of nexus and rough proportionality traditionally required under *Nollan* / *Dolan* review.

Analysis: The Fifth Amendment requires just compensation when government action results in a "taking" of private property. One form of taking occurs when a government conditions land-use approvals on fees or exactions (like a DIF) that lack a sufficient connection to the proposed development's impacts. Under the *Nollan* / *Dolan* standard, there must be an essential nexus and rough proportionality between the amount of the fee and the project's impacts. If a DIF meets both of those elements, it is not a "taking" under the Fifth Amendment.

The Supreme Court held that *Nollan* / *Dolan* applies not only to ad hoc fees imposed through discretionary approvals, but also to generally applicable, legislatively enacted DIFs. It reasoned that courts' focus should be on the result of government action (i.e., requiring money from a developer in exchange for a building permit), not on whether the result is accomplished legislatively or otherwise.

However, the Court declined to decide whether legislative fees must meet the same level of scrutiny as individualized exactions. Justice Kavanaugh's concurrence emphasized this unresolved issue.

Takeaway: While California law did not previously subject DIFs to the heightened scrutiny *Sheetz* now requires, the Mitigation Fee Act requires detailed nexus studies to support such fees.[9] It also requires specific findings connecting each fee to the public facilities they will fund, as well as annual and five-year reports — which address the standards *Nollan* and *Dolan* impose.[10]

Developers also have a short 90-day period to protest the DIFs the City imposes, but only if the City provides notice of that deadline when it imposes the fees.[11] By failing to give this notice, the City waives its protection under this provision.

[9] Gov. Code, § 66016.5(a)(1).
[10] Gov. Code, §§ 66001(a), (d)(1).
[11] Gov. Code, § 66020(d).

The case returns to State court to decide these issues, but there is no further movement as of this writing.

AB 516 (Ramos, D-San Bernardino)

- **Effective** 1/1/24
- **Amends** Gov. Code §§ 66006, 66008, 66023
- **Summary of Changes**
    - Existing law requires annual reports, five-year reports, and auditing on request where DIFs are imposed.
    - AB 1600 now requires annual reports to explain the timeline to construct facilities. Requires agency to inform developer of right to request and receive a mailed notice of the agency's annual report review meeting
    - Also expanded the purpose of periodic auditing and requires the agency to inform developers of their right to request audits

- **Stated Reason for Change -** Enhances transparency and accountability regarding DIFs by increasing public access to information, including the reason for project delays and when construction is expected, and ensures applicants are aware of their rights to ask for an audit and to receive information.

- **Highlights**
    - <u>Annual Report Requirements</u> - Gov. Code § 66006(b)(1) - Additions shown by <u>underline</u>.
        - Annual reports must be made publicly available within 180 days after each fiscal year. Must be presented at the next regularly scheduled public meeting no less than 15 days after making it available. Annual reports must include:
            - Brief description of each type of DIF it imposes.
            - The amount/rate of each DIF.
            - The beginning and ending balance for each DIF fund.
            - Fees collected and the interest earned.
            - Each public improvement on which DIF revenues were expended, the total amount spent on each, and the percentage of that total DIF revenue funded.

- <u>Any subsequent annual report must now note whether construction began by the date estimated in the previous report for these public improvements.</u>
- <u>If construction did not begin, the subsequent annual report must explain the delay and estimated new construction date.</u>

- Expected start date for construction on improvements funded by fees that remain incomplete for which sufficient funds have been collected
- Description for each transfer or loan from a DIF fund, the interest applied to the loaned amount, and the date on which the loan will be repaid
- The amounts of any refunds to property owners, any allocations, <u>and the number of people/entities identified to receive those funds</u>

- <u>Notice Required to Payors</u> **-** Gov. Code § 66006(e) - Agency must tell an applicant/DIF payor of:
  - Their right to ask for an audit under Government Code section 66023
  - Their right to file a written request to receive a mailed notice of the agency's annual report review meeting
  - A link to the location on the agency's website, which includes fee account or fund information for public review

- <u>Auditing Requirements</u> **-** Gov. Code § 66023
  - Any person may ask for an audit of DIF funds.
    - Not required to conduct an audit if already performed one for the same DIF within last 12 months
    - Can be performed by an independent auditor
  - Can require the person asking for the audit to pay a deposit to fund it. If annual reports have not been complete for three consecutive years, agency must pay audit + for each year in which the annual report was not completed

- Audit must examine:
  - Whether the DIF exceeds the amount reasonably necessary to fund the public facilities it is designed to support.
  - When the agency is scheduled to spend the revenue generated by that DIF
  - When those public facilities are scheduled to be completed

AB 1820 (Schiavo, D-Santa Clarita)

- **Effective** 1/1/25
- **Amends** Gov. Code §§ 65940.1 & 65941.1; **Adds** Gov. Code § 65943.1
- **Summary of Changes**
  - Previously agencies required to:
    - Post on its website a current schedule of development fees, exactions, and affordability requirements
    - Accept a preliminary application for a housing development project
    - Request from developers the total fees and exactions associated with a project for which a certificate of occupancy is issued, post it on their websites, and update the website twice a year
  - AB 1820 allows development applicants to request estimate of DIFs to be provided within 30 business days. On project approval, agency must provide a detailed list of estimated fees

- **Stated Reason for Change –** Addresses lack of transparency in DIFs, aims to streamline the development process, and reduce financial risks for developers to allow for more housing.

- **Highlights**
  - <u>Developers Right to Fee Estimates</u> **–** Developers may ask for estimate of fees and exactions at preliminary application and at project approval:
    - Developer may request an estimate in preliminary application (Gov. Code § 65941.1)
      - Agency must provide within 30 business days of submission

        - Applies only to those fees and exactions imposed by local agency, e.g., development impact fees, building permit fees, etc.
        - Estimate is for informational purposes only and not legally binding
    - On project approval, agency must provide detailed list of estimated fees and exactions that will apply to project within 30 business days. (Gov. Code § 65943.1)
        - If a cost recovery method is used to cover administrative costs, must give fee estimates based on the typical fees charged for comparable projects
        - Estimate is for informational purposes only and not legally binding

- <u>Clear Statement Required</u>**—** Cities and counties must request the total fees and exactions from developers at project completion (final inspection or certificate of occupancy), but the request must clearly state that developers are under no obligation to respond and will face no consequences for not responding or for the content of their response. Any information received must be posted online and updated at least twice a year. (Gov. Code § 65940.1)

SB 937 (Wiener, D-San Francisco)

- **Effective** 1/1/25
- **Amends** Gov. Code § 66007
- **Summary of Changes —** Prevents local agencies from requiring payment of impact fees for certain affordable housing projects until the certificate of occupancy or final inspection occurs. Developers must break ground on the project within five years to qualify. Local agencies may collect fees earlier in certain situations.

  Developers may post a performance bond or letter of credit rather than pay cash, though failure to pay cash allows local agencies to place a lien on the land to secure unpaid fees which will likely complicate project financing.

SB 937 creates two rules for collecting development impact fees. Local agencies still cannot require payment of fees or changes on multifamily market-rate residential developments for public improvements until the final inspection or certificate of occupancy, whichever comes first, per Government Code section 66007.

Under SB 937, "designated residential development projects" — which means most affordable residential developments and all market-rate residential developments with 10 or fewer units — will be subject to the new procedure for collecting development impact fees. Fees may no longer be collected upon final building inspection. If the City does not issue a certificate of occupancy, then the final building inspection will serve as the certificate of occupancy.

- **Stated Reason for Change –** To reduce the negative effects of market fluctuations and high interest rates on housing production. It addresses issues such as entitlements expiring before developers can secure funding and the challenge of high development fees during economic hardship.

- **Highlights**
  - <u>Collection of Fees and Charges for Public Facilities — "Designated Residential Development Projects"</u>
    - Under existing law, local agencies may collect development impact fees to mitigate a development project's impact on public infrastructure and facilities.
      - Can only collect on residential projects after a final building inspection or the issuance of the certificate of occupancy, whichever is later
      - Three exceptions – utility service fees, DIF for an established account and proposed construction plan before final inspection or issuance of the certificate of occupancy; or DIF for expenses incurred for public improvements/facilities related to the project
    - Adds "Designated Residential Development Projects," which includes:

    - projects with 100% of units affordable to lower income households,
    - low barrier navigation centers,
    - SB 4 projects (affordable housing projects on land owned by religious or higher education institutions),
    - SB 35 projects (affordable housing projects in multi-family zones),
    - AB 2011 projects (affordable housing projects in commercial zones),
    - projects entitled to a density bonus, or
    - projects that include 10 or fewer residential housing units.
- DIFs may be collected for designated residential development projects on issuance of whichever comes first — the first certificate of occupancy OR the first temporary certificate of occupancy
    - This prohibits collection of DIFs on final building inspections
    - If no certificate of occupancy is issued, final building inspection serves as certificate of occupancy
- Allows DIFs to be collected earlier. Does **not** apply to housing developments if 49% or more units are designated for lower-income households
    - for utility service connection fees (early collection of utility capacity charges is no longer an option);
    - when construction on the development does not begin within five years of building permit issuance;
    - for development impact fees to reimburse the local agency for expenses incurred for public improvements or facilities related to the designated residential development project; or
    - for water, sewer/wastewater, fire, public safety, emergency service, and certain other transportation-related development impact fees for which an account has been established and funds appropriated (e.g. through the adoption of a capital improvement plan).

- Contracts to Pay Outstanding Fees and Charges
    - Existing law allows local agencies to accommodate residential developers without sufficient funds to pay development impact fees by entering into a recorded contract that becomes a lien on the property.
    - SB 937 allows a public officer or employee to execute these contracts on behalf of the agency.
    - Must post a sample version of the contract on agency website if these agreements are made.

AB 2243 (Wicks, D-Oakland)

- **Effective** 1/1/25
- **Adds** Gov. Code § 65912.114(g)
- **Summary of Changes**
    - Part of a larger scheme to expand AB 2011 and SB 6, streamlining housing development in commercial zones and incentivizing retail-to-residential conversions, particularly on larger sites like regional malls.

- **Stated Reason for Change —** To further streamline and expand the Affordable Housing and High Road Jobs Act of 2022 (AB 2011) and the Middle Class Housing Act of 2022 (SB 6) by making it easier for developers to build housing on commercially zoned land, including underutilized malls, and by clarifying certain provisions that proved difficult to interpret.

- **Highlights**
    - If residential redevelopment in commercial zone demolishes or changes an existing use, DIFs must account for the demolition or change so that the fee amount reflects only to the development's incremental impact on public facilities or services.
    - "Changes an existing use" means no demolition is proposed, but a current office, commercial, or similar use changes to residential use.
    - Demolition credit against DIFs also applies to residential development in commercial corridors.

AB 2430 (Alvarez, D-San Diego)

- **Effective** 1/1/25
- **Adds** Gov. Code § 65915.3
- **Summary of Changes** — The Density Bonus Law requires local agencies to provide development bonuses to housing developers in exchange for projects that include deed-restricted affordable housing units at specified levels. Some agencies charge a monitoring fee to ensure that the affordable units are offered to and occupied by qualifying households. AB 2430 prohibits a local agency from charging a "monitoring fee" on a housing development which satisfies certain requirements. Does not apply to affordable housing projects funded by local governments.

- **Stated Reason for Change —** Eliminates duplicative local monitoring fees. AB 2430 prohibits local agencies from charging a monitoring fee on affordable housing developments built using State Density Bonus Law that are already subject to compliance monitoring by a State housing agency. This change is intended to lower affordable housing development costs by eliminating a duplicate cost. (Note – the level of state oversight leaves room for non-compliance if not overseen at the local level.)

- **Highlights:**

    - <u>No Monitoring Fees On Certain Housing Developments</u> **-** Gov. Code § 65915.3
        - Monitoring fees cannot be charged on housing developments that satisfy all these requirements:
            - Development satisfies all requirements of Density Bonus Law;
            - Development received a "density bonus";
            - 100% of units are affordable;
            - Development is subject to a recorded regulatory agreement;
            - Applicant provides a copy of the recorded regulatory agreement and corresponding tax credit reservation letter;
            - Applicant provides a copy of the monitoring document; and,

- Existing housing developments subject to a monitoring fee that meet these requirements are no longer required to pay it.

- Monitoring Fees Can Still Be Charged Under Certain Circumstances - Gov. Code § 65915.3(d)
    - Monitoring fees may be charged when:
        - An applicant utilizes a local incentive program or accepts a local funding source that results in the development of units with different affordability than what State monitors; or
        - An applicant uses a local incentive program that results in the development of units affordable to and occupied by moderate-income households

AB 2663 (Grayson, D-Contra Costa County)

- **Effective —** 1/1/25 as to Gov. Code § 65906.6
- **Deadline** – Required to post by 1/1/26 every 5 years thereafter
- **Adds —** Gov. Code § 65906.6
- **Summary of Changes -** State law permits local agencies to adopt inclusionary housing ordinances to require a percentage of new residential development be affordable to lower or moderate-income households. Developers must be allowed to pay fees in lieu of providing affordable units. The Mitigation Fee Act requires agencies to post on their website information on how development-related fees are spent. Since housing in-lieu fees do not fall within the Mitigation Fee Act, AB 2663 requires agencies to also post how inclusionary in-lieu fees are spent.

- **Stated Reason for Change** – Per the Legislature, this statute aims to increase transparency in the collection and use of inclusionary housing in-lieu fees, responding to instances where local agencies used affordable housing funds for legal fees related to housing lawsuits. However, considering the decision in *Hamilton & High, LLC v. City of Palo Alto* (2023) 89 Cal.App.5th 528 and the court's application of AB 1600 in-lieu fees, this bill aligns in-lieu fees with reporting requirements annually and every five years in AB 1600.

- **Highlights**
    - Applies only to local agencies that collect inclusionary housing in-lieu fees

- Starting 1/1/26, must post on its website:
  - Annually – the fees collected in the last year and whether those fees are intended to be used for a project.
  - Every 5 years – the fees collected in the past 5 years and the projects on the fees funded.

- **Practice Tip** – In light of the decision in *Hamilton* and the court's application of AB 1600 to in-lieu fees, in-lieu fees must be spent as promptly as AB 1600 fees. We recommend agencies:
  - Require a recorded agreement, perhaps a development agreement, with a developer who chooses to pay a fee rather than comply with zoning standards by which it expressly waives application of AB 1600;
  - Comply with the finding requirements and spend funds promptly;
  - Return funds if the capital project for which fees were collected is no longer pursued; and
  - Consider eliminating in-lieu fee ordinances in favor of enforcing zoning standards and rely on variances and development agreements to vary those standards if necessary.

AB 2553 (Friedman, D-Glendale)

- **Effective — 1/1/25**
- **Amends Gov. Code § 66005.1 & Pub. Res. Code § 21064.3**
- **Summary of Changes –** Companion to AB 3177. Existing law requires local agencies to lower vehicular traffic mitigation fees in areas within a half mile of a "transit station." This change significantly increases the areas in which transit-oriented developments can be developed.

  AB 2553 also requires local agencies to lower traffic impact mitigation fees for "transit priority areas," particularly when a proposed housing project will be in an area with a transit stop expected to be completed within one year of the project's completion and occupancy. It expands the definition of a "major transit stop" to include bus routes with service intervals of up to 20 minutes instead of the 15 minutes which applied previously.

- **Stated Reason for Change** – Promotes development by simplifying development processes and promotes transit-oriented housing by broadening the geographic area eligible for incentives such as reduced traffic impact fees and CEQA exemptions, while also updating the definition of a ”major transit stop.”

- **Highlights**
  - Lower Vehicular Transit Mitigation Fees - Gov. Code, § 66005.1(a)(1) — Agency required to lower these fees in “transit priority areas” if the area’s “major transit stop” is scheduled to be in service before or within one year of completing the affected housing development.

  - New Definition of Major Transit Stop — Pub. Res. Code § 21064.3(c) — Includes bus routes with service intervals of up to 20 minutes or less, instead of the -5 minute standard which previously applied.

AB 3177 (Wendy Carrillo, D-Los Angeles)

- **Effective 1/1/25**
- **Amends Gov. Code § 66005.1**
- **Summary of Changes**
  - Companion bill to AB 2553
  - Existing law allows local agencies to impose an exaction on developers to make a land dedication to improve public facilities. AB 3177 prohibits agencies from imposing a land dedication requirement for widening roads to mitigate traffic, except under specified conditions

- **Stated Reason for Change –** Aimed at decreasing housing costs to increase housing supply. Costs of land dedication to increase roadways drives up the cost of housing and delays its completion. It also uses land for roads, which could be used for more housing units. Road widening has also been shown to increase traffic, not decrease it. Promoting development in transit-rich areas aims to reduce vehicle miles traveled and greenhouse gas emission. It also encourages people to use public transportation.

- **Highlights**

- <u>"Transit Station" is now a "Transit Priority Area"</u>) — Gov. Code, § 66005.1(a)
  - Existing law allows a local agency to impose a "vehicular traffic mitigation fee" on housing development projects.
    - One component of calculating the fee is the rate of automobile trip generation associated with a housing development project.
    - Previously, a lower rate of automobile trip generation was set for projects within a half mile of a "transit station," as defined.
  - "Transit station" was replaced with "transit priority area"
    - "Transit priority area" means an area within one-half mile of an existing or planned "major transit stop," when the stop is scheduled to be completed within one year of completing the housing development project.
    - Uses new definition of "major transit stop" in updated Pub. Res. Code § 21064.3, which includes:
      - An existing rail or bus rapid transit station;
      - A ferry terminal served by either a bus or rail transit service;
      - The intersection of two or more major bus routes with a frequency of service interval of 20 minutes or less during peak commute periods; or
      - Stops designated by the agency's applicable regional transportation plan.
    - Note — "transit priority area" now includes that train stations or stops, such as Amtrak and commuter rail.
- <u>Land Dedications</u> — Gov. Code, § 66005.1(c)
  - Agencies prohibited from imposing a land dedication requirement on housing development projects to widen a roadway if the requirement should mitigate vehicular traffic impacts, achieve an adopted traffic level of service related to vehicular traffic, or achieve a desired roadway width.
  - May impose a land dedication requirement if:

- The affected housing development is not located in a transit priority area and has a linear street frontage of at least 500 feet;
- The agency makes a finding that the requirement is necessary to preserve the public health and safety, including pedestrians, cyclists, and children; or
- The requirement is imposed to construct public improvements, including sidewalk and sewer improvements.

AB 3012 (Grayson, D-Contra Costa)

- **Effective —** 1/1/25
- **Deadline** – Must post tool by 7/1/31 for cities of 500k+; 7/1/32 for smaller cities
- **Adds** Gov. Code § 65940.2 and Health & Safety Code § 50466.6
- **Summary of Changes -** Existing law requires every agency to make its current fee schedule for proposed housing development projects available on its website. AB 3012 goes one step further by requiring agencies to provide a fee estimate tool on their websites for proposed housing development projects. Also requires HCD to create a template for the tool by 7/1/28.

- **Stated Reason for Change —** To address concerns about impact fee transparency and to make information regarding housing impact fees more accessible to the public, requiring local jurisdictions to post relevant information online.

- **Highlights**
  - <u>Fee Estimate Tool</u> — Gov. Code, § 65940.2
    - Must create and post a "fee estimate tool" the public can use to estimate fees and exactions for proposed housing development projects on agency website
    - The tool must calculate:
      - a fee or charge described in the Mitigation Fee Act;
      - a construction excise tax;
      - a special tax levied on new housing units under the Mello-Roos Community Facilities Act of 1982;
      - in-lieu fees for affordability requirements;

            - in-lieu fees for a requirement that project provide public art; and
            - in-lieu fees for dedications of parkland.
        - Agencies not responsible for the accuracy of the estimate
    - <u>Deadlines to Implement Fee Estimate Tool</u>
        - July 1, 2028 for HCD to create a template fee schedule tool
        - Before July 1, 2031 for agencies with a population of greater than 500,000
        - Before July 1, 2032 for agencies with a population of 500,000 or fewer
        - *Practice Tip* – Before developing your own fee estimate tool, check whether a template has been created by HCD.