



LEAGUE OF  
**CALIFORNIA**  
**CITIES**

April 17, 2024



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Strengthening California Cities  
through Advocacy and Education

# Threats to Local Fiscal Sustainability, and What You Need to Know

April 17, 2024



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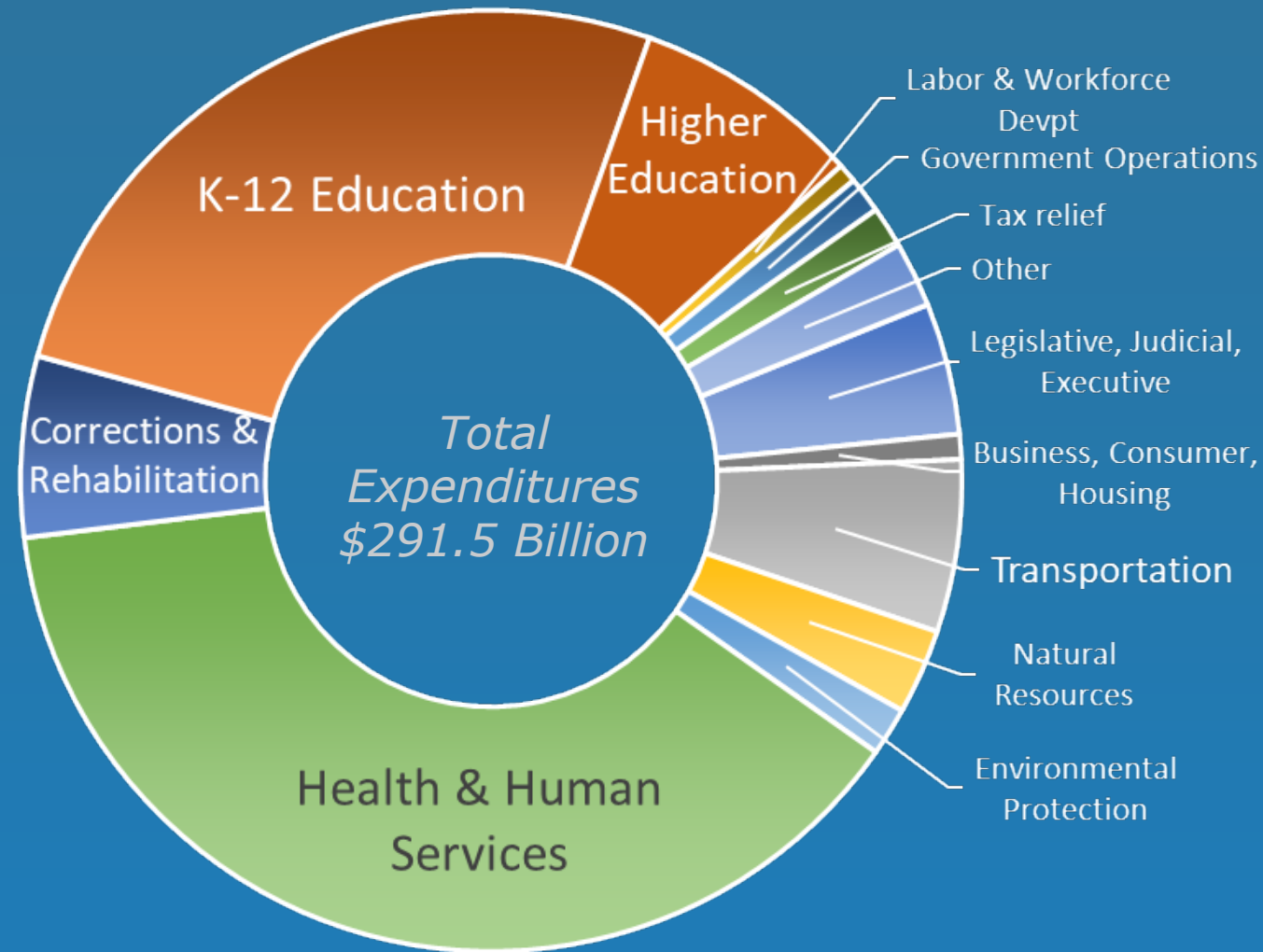
*CaliforniaCityFinance.com*

*The California Local Government Finance Almanac*



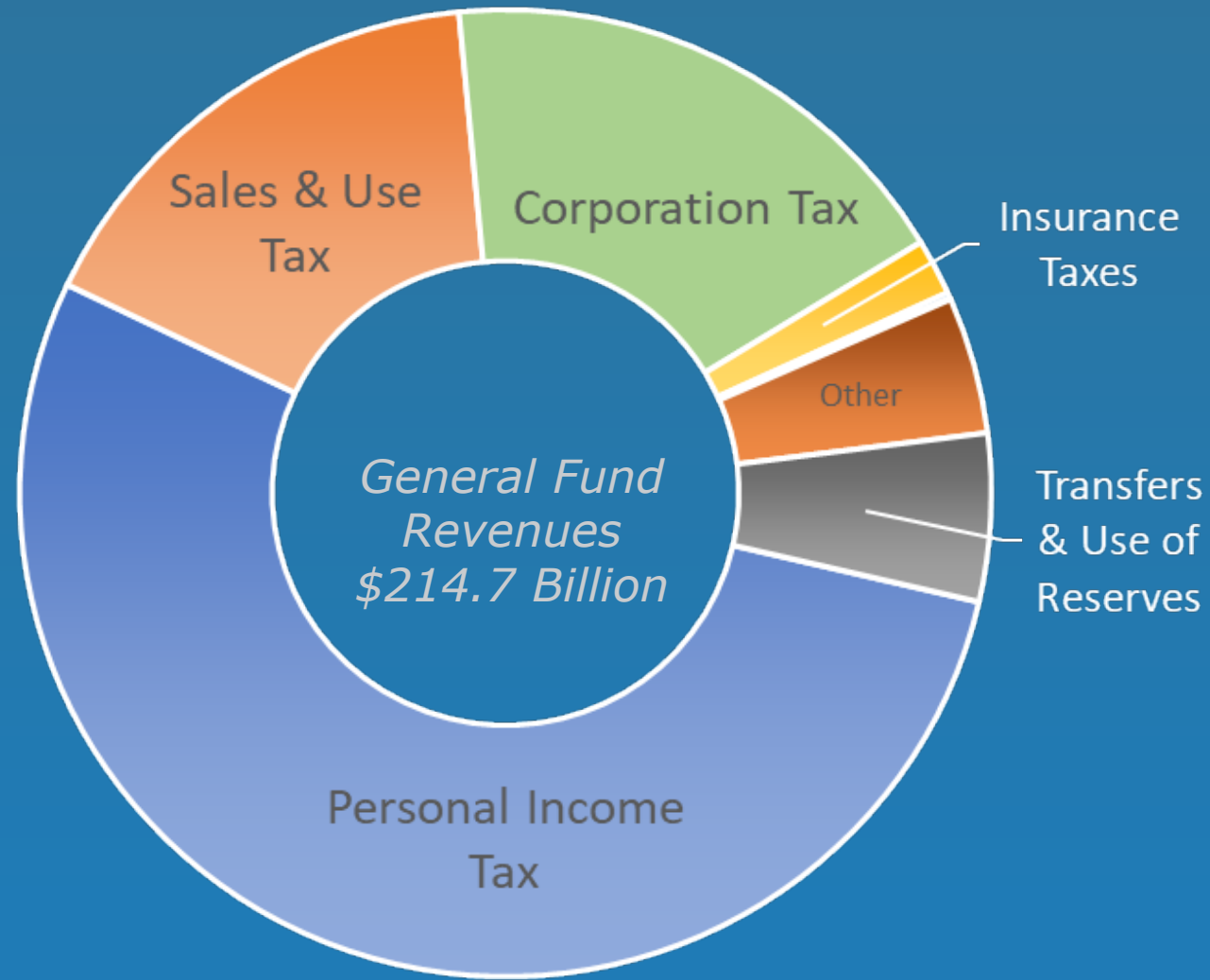
# The California State Budget

## Governor's Proposed Budget January 2024

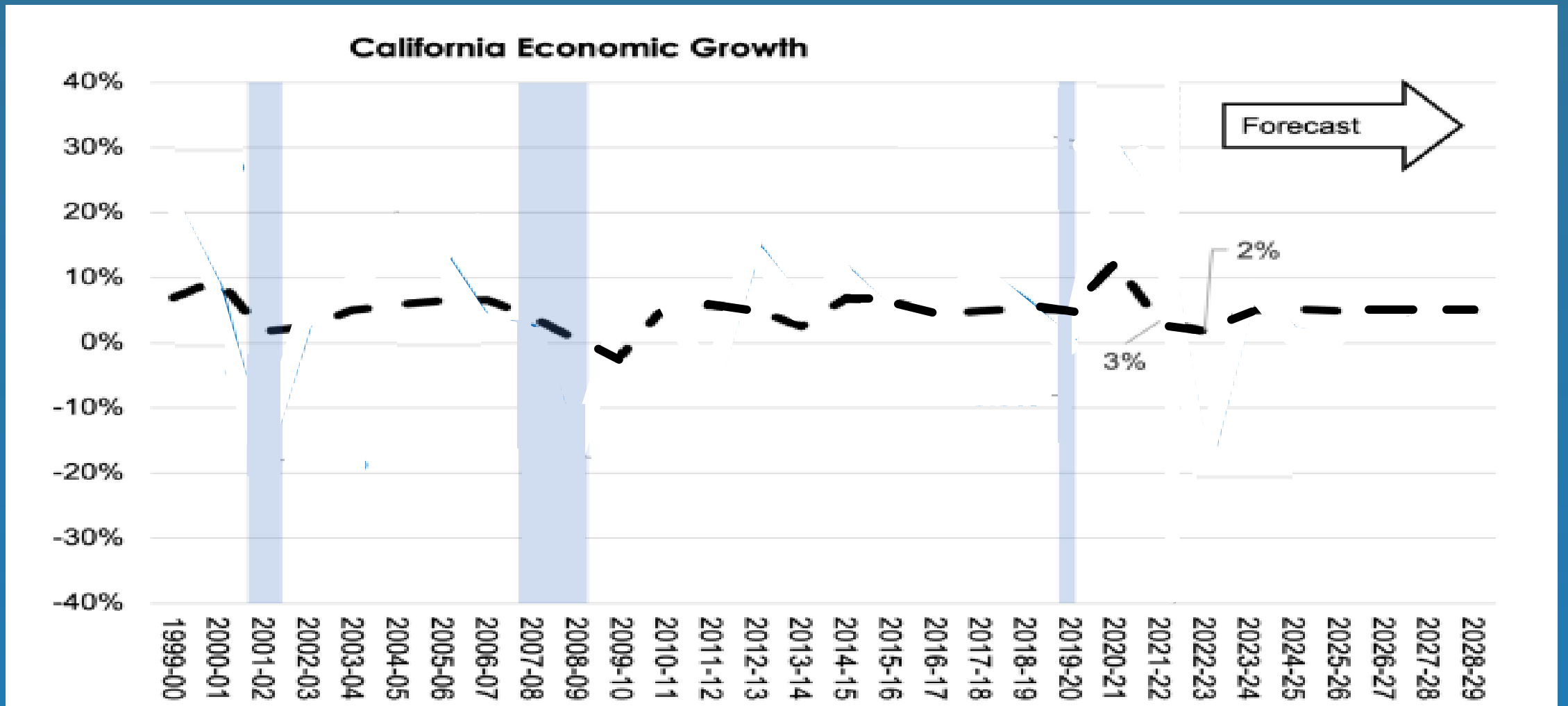


# The California State Budget

## Governor's Proposed Budget January 2024



# “A Story of Correction and Normalization”

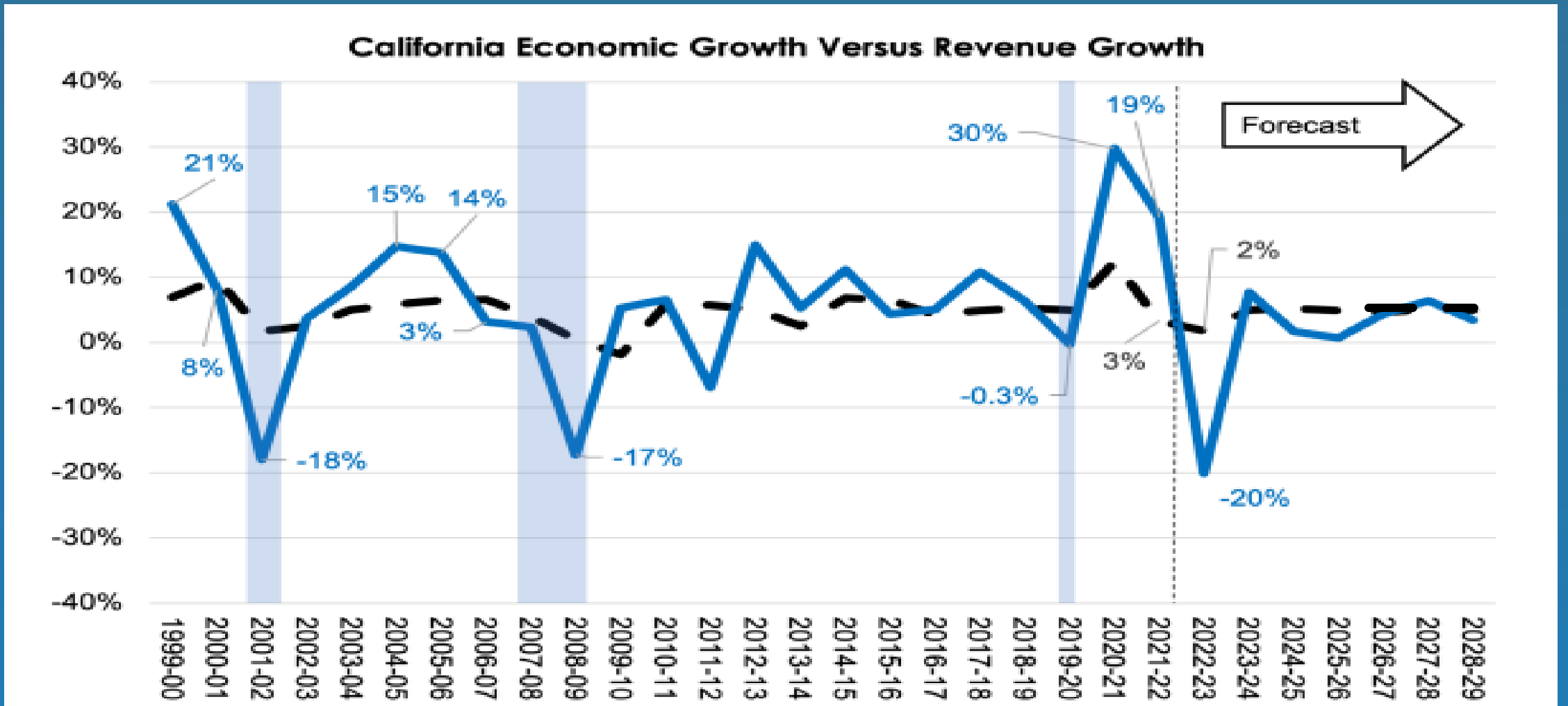


Source: California Dept of Finance , Governor's Proposed Budget January 2024

— California Economy (Personal Income)

Previous U.S. recessions

# “A Story of Correction and Normalization”



Source: California Dept of Finance , Governor’s Proposed Budget January 2024

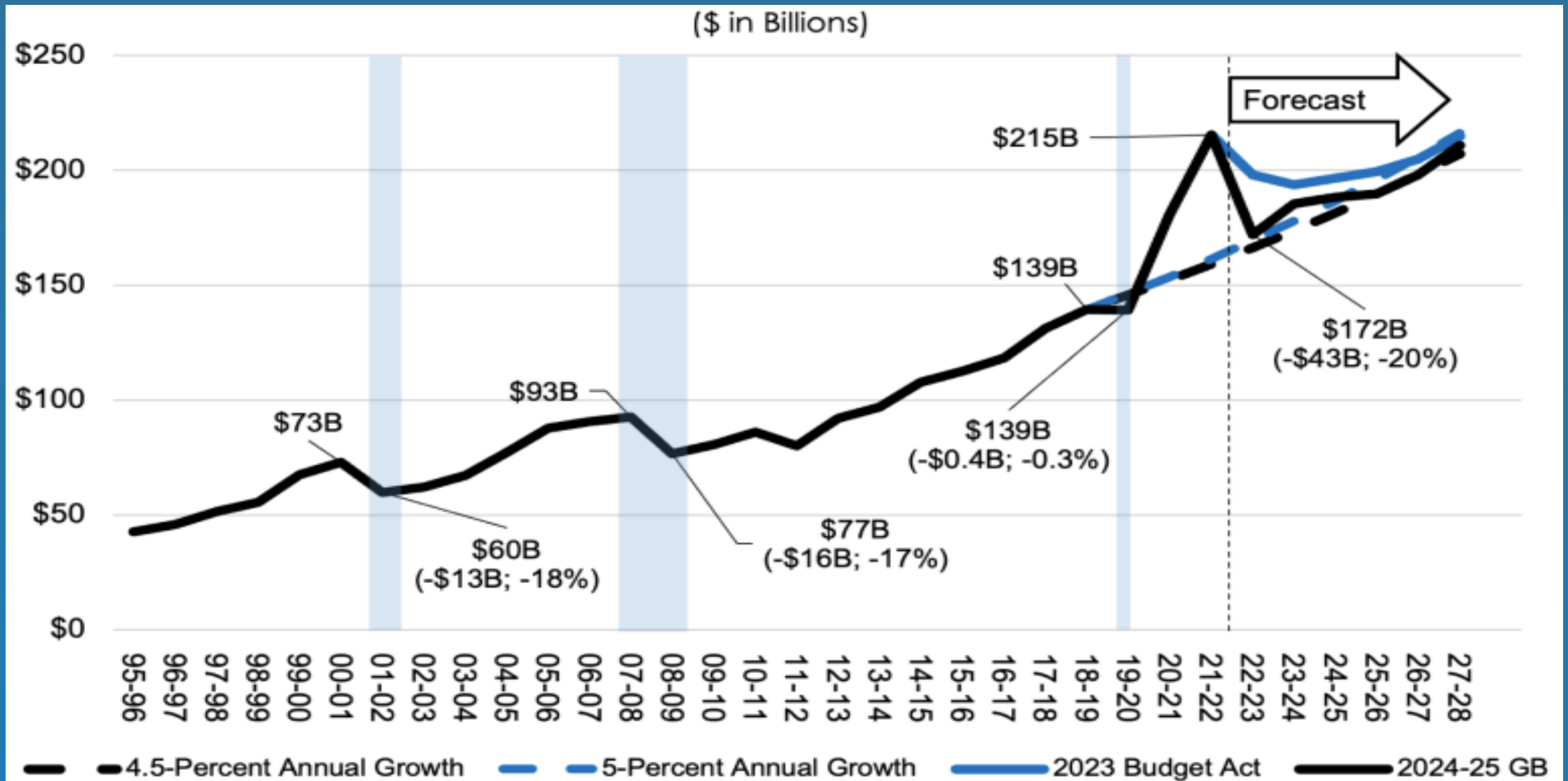
— California Economy (Personal Income)

— Big Three Revenues

Previous U.S. recessions



# California's Big Three Revenues



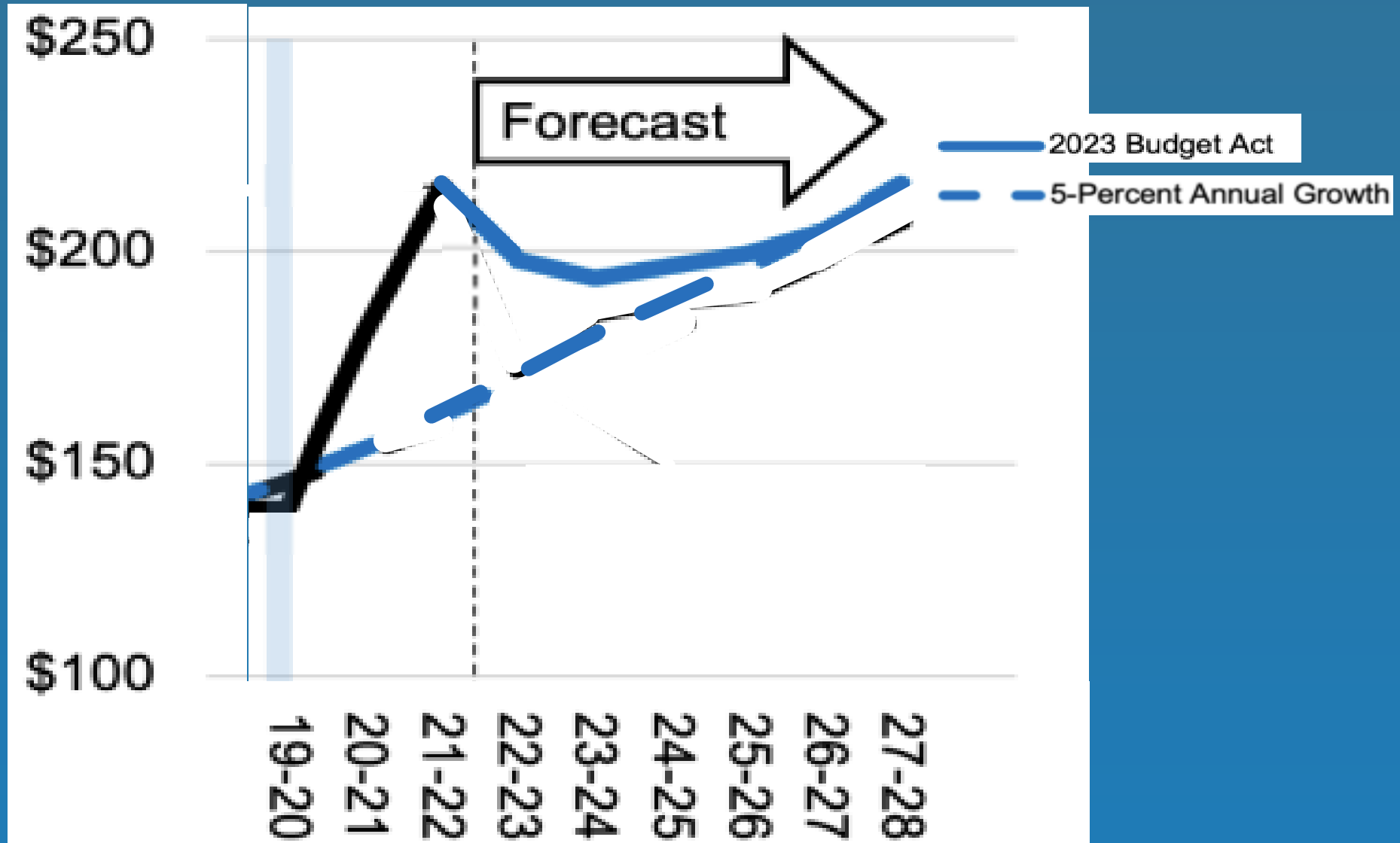
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April 2024





# California's Big Three Revenues

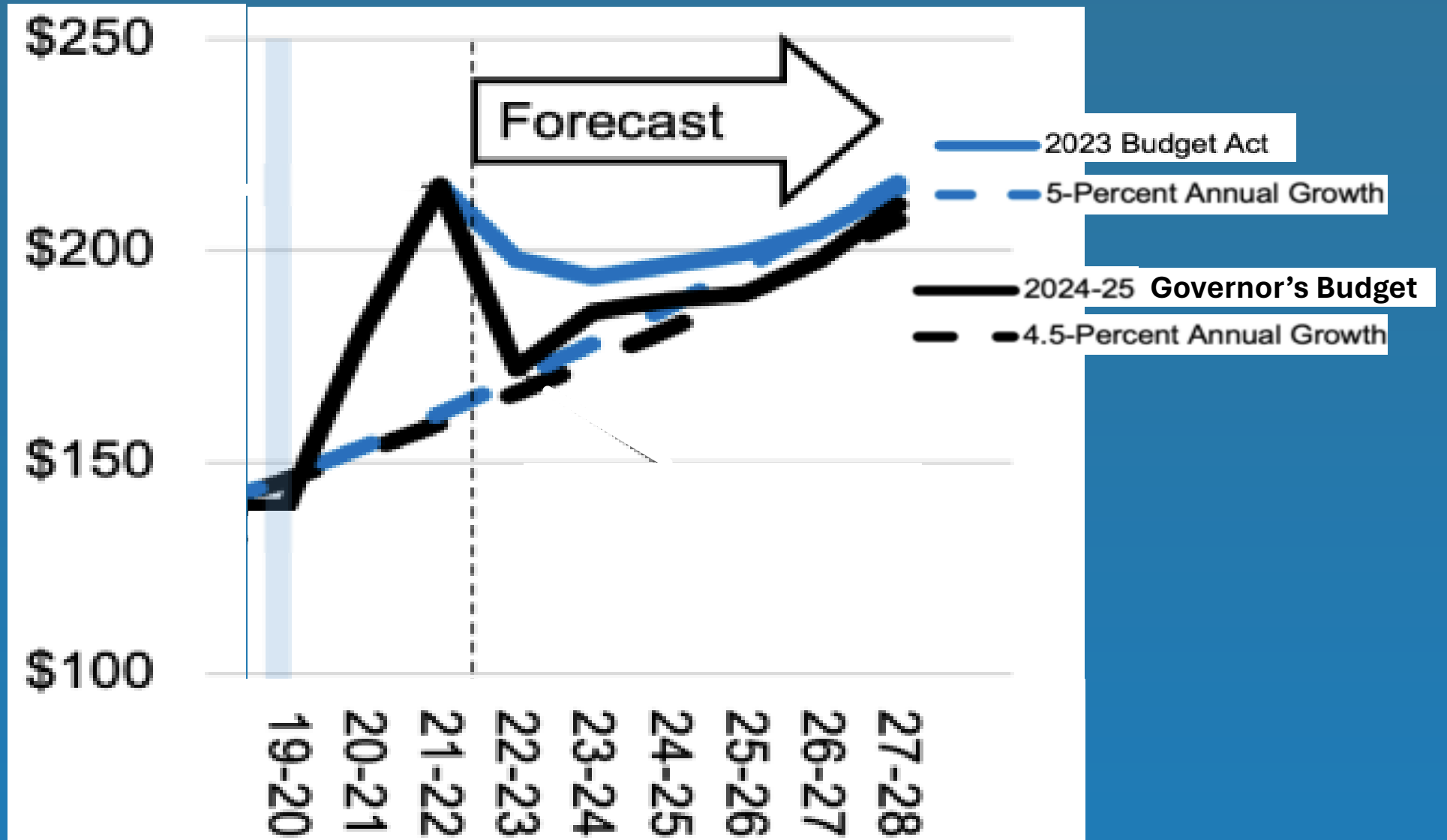


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# California's Big Three Revenues



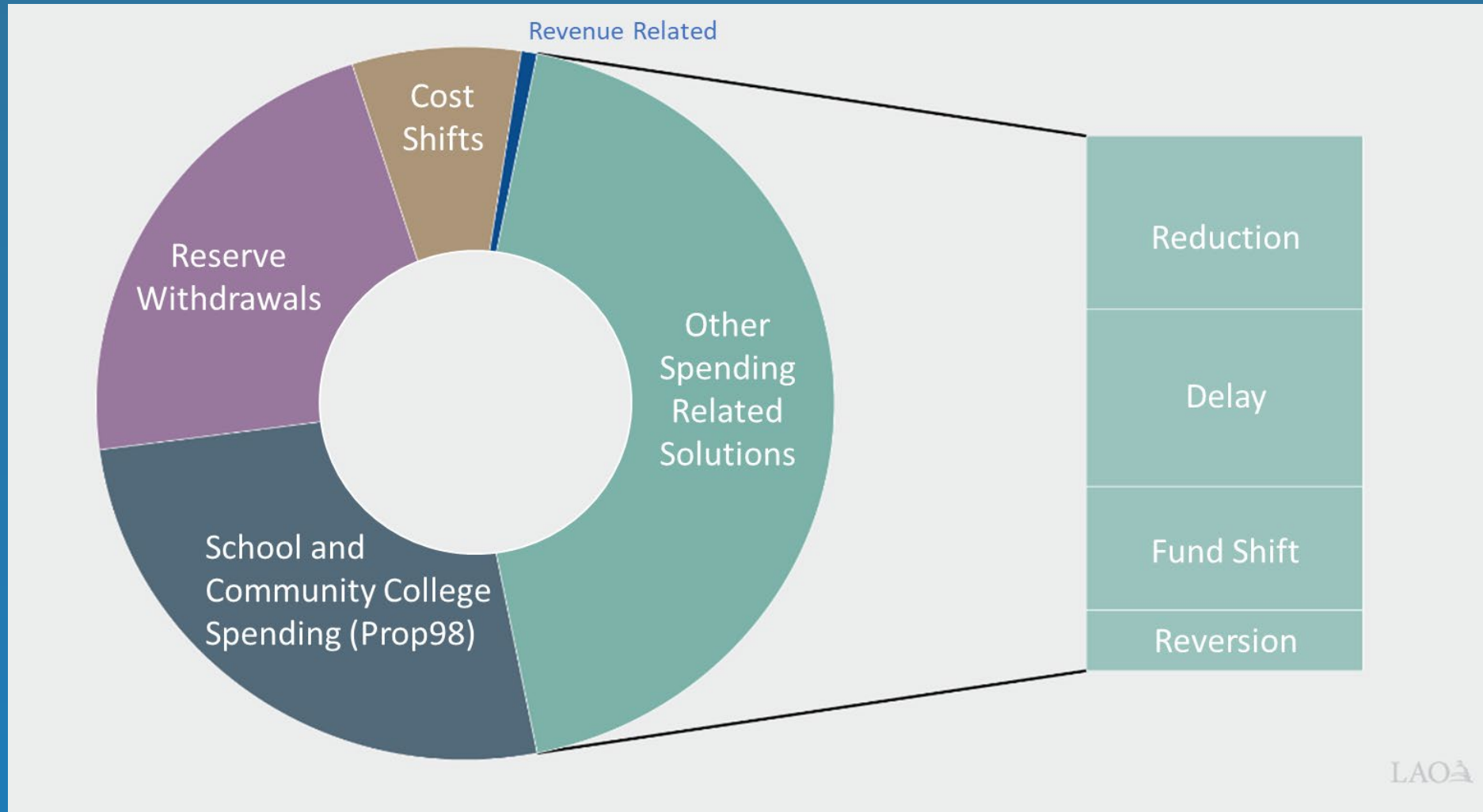
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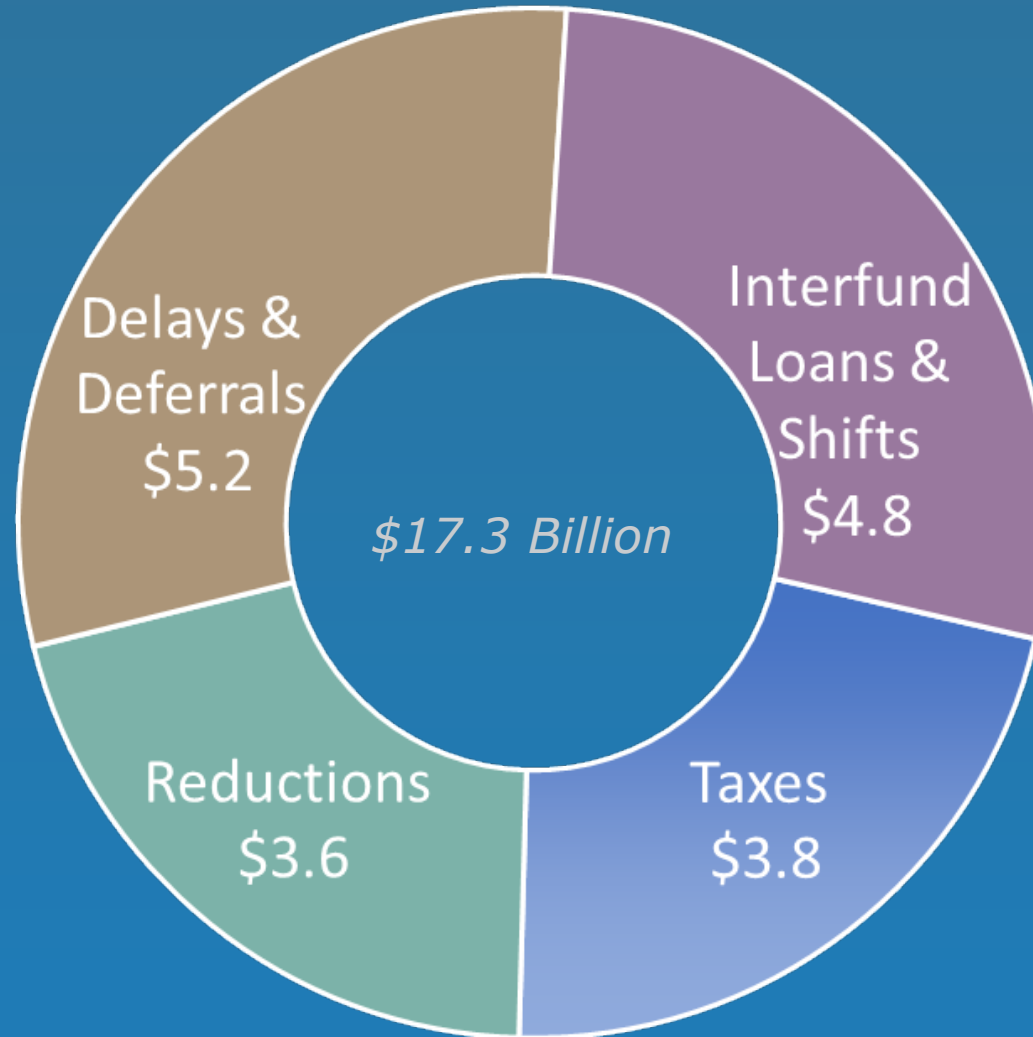


# Governor Proposes \$58 Billion Fix

## Proposed Budget January 2024



# Early Action on April 4 \$17.3 Billion of Solutions



# Some Oft Missed Considerations

- ✓ LAO and DOF count things differently
- ✓ \$ Shortfall numbers are a sum for multiple years
  - Prior year, current year, budget year
- ✓ The budget swings are mostly a reality of our chosen tax structure in California
  - Alternatives: Flatter income tax? Property tax?
- ✓ Interesting/unusual times
  - Pandemic – unexpected economic strength
  - Delayed income tax filings due to disasters



# Risk of State Foisting it's Troubles Onto Cities is Lower Than in the Past

- ✓ State has much stronger reserve levels
- ✓ State can use interfund borrowing as a kind of additional reserve
- ✓ Core city county and special district revenues have strong constitutional protection
- ✓ Unfunded program/cost shifts from state to locals are much more difficult for the state



# ... but Risks Remain and We Must Remain Vigilant Partners

- ✓ Tax exemptions and cost shift proposals
- ✓ Clawbacks
- ✓ Draconian & Impractical State Ballot Initiative Nov 2024



# Draconian, Impractical Ballot Initiative – November 2024

*Initiative #21-0042A1: Limits Ability of Voters and State and Local Governments to Raise Revenues for Government Services. Initiative Constitutional Amendment*

Chokes local tax authority. Requires:

- Requires voter approval for taxes applied to territory that is annexed
- Requires sunset date on all new taxes
- General tax ballot label must say “for general government use”
- Repeals *Upland* exception for initiative special taxes
- Local tax advisory measures are prohibited (the Measure A/B approach).





# Draconian, Impractical Ballot Initiative – November 2024

*Initiative #21-0042A1: Limits Ability of Voters and State and Local Governments to Raise Revenues for Government Services. Initiative Constitutional Amendment*

## Restricts local fee authority

- Fees by limiting limited “actual cost” of providing the product or service for which the fee is charged. “Actual cost” is defined as the “minimum amount necessary.”
- Fees - including for use of government property - must be “reasonable to the payor”
- Repeals fee for “special benefit” exception to Prop 26 “tax” definition
- Fees must be adopted by legislative body by ordinance, not staff or a commission
- Changes legal standard from “preponderance of the evidence” to “clear and convincing evidence” to prove a fee or charge is not a tax and does not exceed “actual cost.”



# Draconian, Impractical Ballot Initiative – November 2024

*Initiative #21-0042A1: Limits Ability of Voters and State and Local Governments to Raise Revenues for Government Services. Initiative Constitutional Amendment*

Also ...

- Fines require “adjudicatory process”
- No VMT tax or fee as condition of development or occupancy
- Retroactive window: taxes, fees approved after Jan 1, 2022 will sunset in Dec 2025 if not readopted in compliance with the initiative
  - At least \$2 billion of taxes approved in 2022-2024 must be re-adopted in 2025  
New ballot language, new sunsets, new voter thresholds
  - \$ Billions of fees must be readopted to comply in 2025



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# Property Taxes

## **SB 1164 (Newman) Property Taxation: New Construction Exclusion: Accessory Dwelling Units.**

This measure would exempt new ADU construction from property tax assessment for fifteen years from the date of completion or until the property is sold.

**Cal Cities Position:** Oppose

# Property Taxes

## **AB 2647 (Low) Property Taxation: Disabled Veterans' Exemption: Welfare Exemption: Housing for Law Enforcement and Firefighters.**

This measure would expand the property tax welfare exemption by increasing the disabled veterans' exemption to \$869,790 and would allow specified housing for law enforcement officers or firefighters to be eligible for the exemption.

**Cal Cities Position:** Pending

# Sales and Use Tax

## **AB 2274 (Dixon) Taxation: Sales and Use Taxes: Exemption: Tax Holiday.**

This measure would create sales tax exemptions for “qualified school supplies” purchased during the first weekend in August of each year through 2029.

**Cal Cities Position:** Pending

# Sales and Use Tax

## **SB 1494 (Glazer) Local Agencies: Sales and Use Tax: Retailers.**

This measure, as of January 1, 2024, would prohibit a city from entering a sales tax rebate agreement with a retailer. As of January 1, 2030, the bill would make all existing sales tax rebate agreements void and unenforceable.

**Cal Cities Position:** Oppose


# Cannabis Excise Tax

## **AB 3248 (Essayli) Cannabis excise tax: rate reduction**

This measure, as of January 1, 2025, would reduce the cannabis excise tax from 15% to 5%.

**Cal Cities Position:** Pending





**Selected Topics in  
Municipal Finance**  
by  
Matthew C. Slentz, Esq.  
League of California Cities  
City Leaders Summit  
April 17, 2024

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COLANTUONO  
HIGHSMITH  
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# Response to CBRT Measure

*Legislature et al v. Weber*, SCOCA Case No. S281977

- Original writ petition to exclude measure from the ballot arguing
  - Revision, rather than amendment
  - Undermines essential government power
- SCOCA issued order to show cause on 11/29/23, allowing briefing of the merits
- Should be argued in April or May 2024 and decided by ballot-printing deadline of late June 2024

# Response to CBRT Measure

## Cal Cities Amicus Brief:

- Filed on behalf of 9 local government agencies, including Cal Cities and the California State Association of Counties, and Los Angeles and San Francisco
- Expanded on the points made by Legislature, with a focus on the impacts on local government

# Response to CBRT Measure

## Cal Cities Amicus Brief:

- The Measure revises California's constitutional structure
  - CA Constitution provides for home rule and division of power between state and local gov't, and within local gov't
  - Measure requires action by elected legislative body on all levies, robbing them of power to delegate to administrators
  - It also alters the balance of power between State and local gov't by making local gov't dependent on State revenues

# Response to CBRT Measure

## Cal Cities Amicus Brief:

- Measure undermines essential functions of local gov't
  - *Wilde v. City of Dunsmuir* affirmed People's reserved initiative powers cannot undermine essential gov't functions
  - Measure stops local gov't from effectively budgeting because all levies are now subject to referendum
  - "Actual costs" + "clear and convincing evidence" mean setting rates below costs to avoid any surplus
    - Makes it exceedingly difficult to raise necessary revenue

# Response to CBRT Measure

## Cal Cities Amicus Brief:

- Creates significant interpretive issues:
  - Fees for government services or products limited to “actual cost” less other revenues. What counts as “other” revenues?
  - Measure provides a revenue measure is “imposed” each time it is collected. But only elected legislatures may impose an exempt charge. Ratemaking hearing before each bill mailing?
  - Local fines and penalties for a violation of “law” allowed only “pursuant to an adjudicatory due process”
  - Many special districts lack elected boards as required, nor do they have the ability to pass ordinances

# Response to CBRT Measure

## ACA 13 (Ward, D-San Diego)

- Proposed constitutional on November 2024 ballot – affecting CBRT measure if it is also voted in November 2024
- Initiative constitutional amendment imposing supermajority requirements must pass by that supermajority
- So, CBRT measure would require 2/3 voter approval



# Development Impact Fees

*Sheetz v. County of El Dorado* (2022) 84 Cal.App.5th 394, cert. granted SCOTUS No. 22-1074

- \$23,420 traffic impact fee on new house challenged as regulatory taking
- DCA affirmed County's victory, concluding
  - *Nollan / Dolan* analysis does not apply to legislative fees
  - AB 1600 does not require tract-specific analysis
  - Fee reasonably related to traffic impacts

# Development Impact Fees

*Sheetz v. County of El Dorado, California* (2024) \_\_\_\_ U.S.  
\_\_\_\_ (2024 WL 1588707)

- Decided narrowly, but against the County
- SCOTUS finds the *Nollan/Dolan* requirements for an “essential nexus” and “rough proportionality” also apply to legislatively adopted fee schedules
- Abrogates former California rule, that only “ad hoc” monetary exactions subject to takings analysis
- Remanded to conduct proper analysis

# Franchise Fees

*Jacks v. City of Santa Barbara* (2017) 3 Cal.5th 248

- SCE agreed to increased franchise fee upon PUC authorization for line item on power bills
- DCA found tax requiring voter approval
- Supreme Court remanded: Franchise fee must reflect reasonable value of franchise
  - Reasonable value may be shown by bona fide negotiations, “other indicia of worth”
  - Also reaffirms that valid fees do not become taxes simply because passed on to rate payers

# Trash Franchise Fees

## *Zolly v. City of Oakland* (2022) 13 Cal.5th 780

- Challenge to franchise fee imposed on City solid waste franchisees under Props. 218 and *Jacks v. City of Santa Barbara*
- SCOCA found standing because apartment owners alleged they bore economic incidence of fee; city's claim otherwise could not be tested on demurrer
- Prop. 26 exception for use of property limited to tangible property, not franchise itself
- Fee was "imposed" so as to trigger Prop. 26 b/c established by legal authority
- Oakland can try to prove at trial that haulers get unusual rights in rights-of-way that are proportionate in value to franchise fee

# Trash Franchise Fees

- Tips for protecting this revenue source
  - Avoid controversy if possible
  - Make a record that haulers get rights in rights-of-way that others do not (like the right to place bins in street weekly)
  - Make a record that the value of those rights is at least roughly proportionate to the franchise fee
  - Have a cost-of-service study in your record; consider hiring a consultant, and have a lawyer review it
  - Separately cost regulatory fees (like AB 939 compliance fees)

# Utility Taxes / General Fund Transfers

- *Wyatt v. City of Sacramento* (2021) 60 Cal.App.5th 373
  - Upheld post-218 approval of GFT from water, sewer, and trash utilities to general fund as a general tax
  - Plaintiffs argued Prop. 218 forbids all general UUTs
  - Victory means voters can approve GFTs

# Utility Taxes / General Fund Transfers

- *Lejins v. Long Beach* (2021) 72 Cal.App.5th 303
  - Similar facts as *Wyatt v. Sacramento* – post-218 election to validate GFT from water and sewer utilities
  - Purported to distinguish *Wyatt* in ruling for challengers, but seems to disagree with *Wyatt*
  - Bad fact: tax applied to non-resident customers of water utility, but election in City only

# Utility Taxes / General Fund Transfers

*Palmer v. City of Anaheim* (2023) 90 Cal.App.5th 718

- Voter approval of charter amendment to authorize general fund transfer sufficient to defeat Prop. 26 challenge
- Effectively sides with *Wyatt* over *Lejins* by concluding voter-approved taxes collected from the utility, rather than on customers bills, do not cause rates to exceed cost of service in violation of Propositions 218 and 26
- Plaintiffs did not seek rehearing or review



# Solid Waste Fees

*Padilla v. City of San Jose* (2022) 78 Cal.App.5th 1073,  
review denied

- Class action challenge to collection of delinquent trash fees on tax roll
- Court affirmed trial court conclusion that plaintiffs could not pursue case because they had not paid the fees under protest under HSC 5470 et seq. or to pay first and litigate later
- Powerful defense for water, sewer and trash rates

# *Cal. Cannabis Coalition v. City of Upland* (2017) 3 Cal.5<sup>th</sup> 924

- Voter initiative to regulate medicinal cannabis
- \$75k annual licensing and inspection fee (regulatory fee)
- But . . .
  - Actual cost to the City is \$15k per year
  - Exceeds cost – this is a tax!
- Court suggested Prop 218 applies to “local government” and not to the electorate so maybe 2/3rds voter approval not needed

# Why?

- “No **local government** may impose, extend, or increase any special tax unless and until that tax is submitted to the electorate and approved by a two-thirds vote.” (Art. XIII C, § 2(d).)
- Proposition 13, 218 and 26 do not expressly limit the power of initiative, *Upland* states no implied repeal

# *Upland* & Special Taxes With Majority Voter Approval

*City & County of San Francisco v. All Person Interested in the Matter of Proposition C* (2020) 51 CA5th 703

- Business license tax increase to fund homeless programs got 60% approval
- City filed validation action; HJTA and business groups opposed
- DCA held initiative proposing special tax may pass w/ 50%+1 approval despite
  - Prop. 13
  - Prop. 218
  - City charter
- 5 COA opinions have held the same, despite varying facts

# More on Upland

*Alliance San Diego v. City of San Diego* (2023) 94 Cal.App.5th 419

- Initiative special tax for streets, homeless and Convention Center expansion got just less than 2/3 valid even though ballot materials said 2/3 required
- City waited till post-*Upland* cases decide to declare it passed and authorize debt
- Competing validation actions led to MJOP against City in trial court; DCA reversed; SCOCA denied review
- But remands to try whether service of City-appointed Convention Center Corp. director as initiative proponent invalidates the measure (despite two SF cases on point)

# Water Rates

*Plata v. City of San Jose* (2022) 74 Cal.App.5<sup>th</sup> 736,  
review denied

- *Post-Capistrano* challenge to tiered water rates
- Late payments not subject to Prop. 218 analysis (and get lenient review under Prop. 26)
- Trial court abused its discretion to allow plaintiffs to raise at trial an issue not in Government Claims Act claim or in complaint

# Property Tax

## ACA 1 (Aguiar-Curry, D-Yolo)

- Would amend Prop. 13 to allow 55% voter approval of supplemental property taxes to fund bonds to finance public infrastructure and affordable housing
- On the November 2024 ballot

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