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REPORT TO THE NATURAL RESOURCES AND CULTURE COMMITTEE

APPLICABILITY OF PROPOSITION 218 TO PROPOSED PILOT STUDY ON BUDGET-BASED WATER BILLING

**INTRODUCTION**

At the May 23, 2012 NR&C committee hearing, Councilmember Carl DeMaio inquired as to whether the City would be required to mail Proposition 218 notices in order to conduct a pilot study on budget-based water billing, and bill actual customers according to the budget-based rates.

**ANALYSIS**

**I. REQUIREMENTS OF CALIFORNIA LAW**

**A. Article XIII D, section 6 of the California Constitution**

Proposition 218, or the "Right to Vote on Taxes Act," was adopted by the voters in 1996. Proposition 218 added articles XIII C and XIII D to the California Constitution. Article XIII D generally requires local governments to submit property-related assessments, fees and charges to property owners for approval after receiving a written explanation and the opportunity to attend a public hearing. Cal. Const. art. XIII D, §§ 1-6. The primary purpose of Proposition 218 is to limit and control local government's ability to impose monetary levies on real property. *Richmond v. Shasta Community Services Dist.*, 32 Cal. 4th 409, 414-15 (2004); *Apartment Assn. of Los Angeles County, Inc., v. City of Los Angeles*, 24 Cal. 4th 830, 837 (2001).

Article XIII D, section 6(a)(2) of the California Constitution requires public entities to hold a public hearing to approve any utility rate increases and provide 45 day prior written notice of the public hearing:

The agency shall conduct a public hearing upon the proposed fee or charge not less than 45 days after mailing the notice of the proposed fee or charge to the record owners of each identified parcel upon which the fee or charge is proposed for imposition. At the public hearing, the agency shall consider all protests against the proposed fee or charge. If written protests against the proposed fee or charge are presented by a majority of owners of the identified parcels, the agency shall not impose the fee or charge.

Proposition 218 establishes certain requirements that fees not exceed the reasonable cost of providing the service for which the fee or charge is imposed, and that “[t]he amount of a fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel.” Cal. Const. art. XIII D, § 6(b)(3).

These Proposition 218 requirements will restrict participants in the pilot study to customers who volunteer for the study. Some participants could pay more for water under the pilot study, triggering the 45 day prior written notice and a public hearing. Requiring some customers to pay for water under a rate structure different than other similarly structured customers may also result in disproportional rates. Therefore, participants will need to waive their rights under Proposition 218 to join the pilot study without a Proposition 218 notice, a public hearing, or a guarantee that their water rates will be proportionate to the cost of providing service. Cal Const. art. XIII D, § 6(b) (1-5).

There is also a possibility that participants in the pilot study will pay less than the cost to provide service to them. If a customer is charged more than the proportional cost of the service because participants in a budget-based pilot study are paying less, it is arguably a violation of Proposition 218. The State Legislature clarified Proposition 218 in California Assembly Bill 2882 (2007-2008 Reg. Sess.) (AB 2882), which is discussed below.

#### **B. California Assembly Bill 2882 (2007-2008 Reg. Sess.)**

AB 2882, which water agencies added sections 370 through 374 to the California Water Code (Water Code), authorizes to implement tiered water-rate structures that encourage conservation and reduce the insufficient use of water. Under this structure, as customers consume more water they pay higher “incremental costs”, which are defined in Water Code section 371 (d) as:

“Incremental costs” means the costs of water service, including capital costs, that the public entity incurs directly, or by contract, as a result of the use of water in excess of the basic use allocation or to implement water conservation or demand management measures employed to increase efficient uses of water, and further discourage the wasteful or unreasonable use of water, and may include any of the following:

(1) Conservation best management practices, conservation education, irrigation controls and other conservation devices, and other demand management measures.

Section 371 (d)(1) authorizes water agencies to include the cost of water conservation measures in the cost of water service billed to customers. The proposed pilot study could be considered water conservation measures designed to investigate the effectiveness of alternative

rate models. Thus, even if the participants end up paying less than the actual cost of providing service, we believe it is a permissible water conservation measure.

### **CONCLUSION**

Although the law under Proposition 218 is still evolving, we believe AB 2882 presents the City with reasonable authority for engaging in a pilot study with volunteers to determine the effectiveness of budget-based water rates. Therefore, we believe a volunteer pilot study would fit within the framework of active water conservation issues described in Water Code Section 371(d)(1) as a possible water cost. However, no court has yet addressed this approach vis-à-vis Proposition 218's plain language requiring proportionality to the cost of serving each parcel.

Respectfully submitted,

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