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REPORT TO THE HONORABLE MAYOR AND CITY COUNCIL

PROPOSITION 26 REVIEW OF PROPOSED AMENDMENTS TO SAN DIEGO'S
REGULATORY ORDINANCES REGARDING POLICE PERMITS AND NONPROFIT
ENTITIES

INTRODUCTION

The City of San Diego is considering amendments to the San Diego Municipal Code (Municipal Code) which affect the fees recovered for police-regulated activities involving nonprofit entities. Under Council Policy 100-05, City departments identify and recover all reasonable and allowable costs incurred in providing government services, including the costs of police regulation. The Municipal Code requires full cost recovery for police-regulated activities. SDMC § 33.0307.

Proposition 26, passed by the voters in November 2010, amended articles XIII A and XIII C of the California Constitution to provide that a levy, charge, or exaction of any kind imposed, increased, or extended by a local government is a tax unless an exception applies. Exceptions to Proposition 26 include user fees; government service or product fees; regulatory fees; government property entrance fees; fines and penalties imposed by a court or local government; property development impact fees; and assessments and property-related fees governed by Proposition 218.¹ Additionally, regulatory fees should reimburse the government entity for all reasonable direct and indirect expenses incurred. *United Business Commission v. City of San Diego*, 91 Cal. App. 3d 156, 166 (1979).

Currently, some nonprofit entities that engage in certain occupations and businesses are exempt from both paying a fee and obtaining a police permit. The general rule in Municipal Code section 33.0601 is that nonprofit entities are required to obtain a police permit but not pay a fee. The proposed amendments will bring nonprofit promoters and solicitors, and nonprofits who engage in entertainment² into conformance with section 33.0601.

¹ For a fuller discussion of Proposition 26 and its application here, see City Att'y MOL No. 11-3 (Mar. 4, 2011), "Proposition 26 and Its Impact on City Fees and Charges."

² "Entertainment" is defined in Municipal Code section 33.1502. There are approximately seventeen exemptions to the entertainment police permit requirement. SDMC § 33.1504.

QUESTION PRESENTED

When a nonprofit entity³ engages in a police-regulated⁴ activity or industry, can the City of San Diego require the nonprofit entity to get a permit without charging them a fee?

SHORT ANSWER

Yes, so long as the cost of the regulation is not borne by the other fee payers. Any funds allocated to reimburse the Police Department (Department) for the cost of regulating the nonprofit entities activity must come from a source outside of the fee payers. Conversely, if the Department is not reimbursed for the cost of regulation, a court could deem the “fee” system a tax rather than a regulatory scheme because no cost is allocated for entities similarly situated.

ANALYSIS

I. REGULATORY AND PENALTY FEE EXCEPTIONS FROM PROPOSITION 26

Proposition 26 provides that certain government imposed fees are excluded from the definition of a “tax” if they fall into one of the listed, enumerated categories. One such category is the local government regulatory fee. Fees of this type are not taxes if they bear relation to reasonable cost of the government expense in regulating or permitting the activity. Permitted “reasonable regulatory costs” include: (i) issuing permits and licenses; (ii) performing investigations, inspections, and audits; and (iii) administrative enforcement and adjudication. Consistent with that exception, the fees must be limited to the reasonable regulatory costs. Cal. Const. art. XIII C, § (1)(e)(3).

An additional category excludes fines, penalties, or other monetary charges imposed by the judicial branch of government or a local government, as a result of a violation of law. Police-regulated industries may be subject to fines and penalties for lack of compliance with governing regulations, and those fines and penalties will not be considered a tax under Proposition 26. Cal. Const. art. XIII C, § (1)(e)(5).

In order for the City to properly set a fee for the regulation of certain industries or activities there must be a showing that each fee is reasonably based on the amount of government services that are expended in regulating those industries. In *California Farm Bureau v. State Water Resources Control Board*, 51 Cal. 4th 421 (2011), the Court determined that the proportionality is not measured on an individual basis but collectively, considering all rate payers or those regulated. The government entity must show that the fee is related to the overall cost of the governmental regulation. The cost should be captured with reasonable certainty but it need not be finely calibrated to the precise benefit each individual fee payer might derive. *Id.* at 438.

³ A nonprofit entity is one that qualifies under state or federal tax laws as tax-exempt. Such entities currently do not pay a permit fee for police regulation. SDMC § 33.0601.

⁴ A police-regulated activity is one that requires a police permit to engage in that occupation or business, pursuant to Chapter 3, Article 3 of the Municipal Code. Such activities require police regulation to protect the general safety and welfare of the public. SDMC § 33.0101.

II. FEES FOR SAN DIEGO POLICE-REGULATED ACTIVITIES

Municipal Code section 33.0101 provides for the regulation of certain businesses and occupations. These regulated industries and activities are the responsibility of the Chief of Police, who assigns officers⁵ to permit, inspect, and regulate those activities, businesses and occupations. The Municipal Code directs recovery of the cost of such regulation. SDMC §§ 33.0103, 33.0307. Those costs are allocated to each activity or industry, separately, based on cost recovery for the required regulation. Such fees are likely an exception under Proposition 26, Cal. Const. art. XIII C, § 1(e)(3), as an acceptable regulatory cost recovery fee.

Municipal Code section 33.0101(a) states, “The occupations and businesses in The City of San Diego listed in this Article are subject to the City’s police power and are classified as ‘police-regulated.’” “This Article” refers to Chapter 3, Article 3, Division 1 of the Municipal Code. Therefore, if an activity, occupation or business is “regulated” the City has directed the Department to directly recover the cost.

Through the Municipal Code, the City Council has decided that full cost recovery is essential for regulating certain industries and activities that require police response in excess of normal police services. Charging all police-regulated entities, per regulated activity or industry, will lower the fee for all of those charged since the fee is based on only, and specifically, identifiable time spent regulating the activity. Consequently, if all of the regulated entities are included in the calculation of the fee, then those charged will pay a lower fee. *See also* City Att’y MOL No. 11-3 (Mar. 4, 2011).

However, Chapter 3, Article 3, Division 6 exempts certain entities from paying fees. Specifically, currently exempted entities are any “federal, state, county or municipal organization, or any non-profit organization, organized and qualified under the laws of the United States or California as a tax-exempt organization.” SDMC § 33.0601. The exemption for other government agencies is consistent with the California Government Code. *See* Cal. Gov’t Code § 6100-6110, exempting public officials and public entities from various fees, such as filing fees for any document or paper, fees for service of process by a sheriff or marshal, and no fees for taking of any oath for recovery of property or funds by state and political subdivisions. Presumably, the intent behind these Government Code exemptions is to not tax one government entity to pay another government entity, from the same set of tax payors, for a governmental action.

No specific state statute exists to generally exempt nonprofit organizations from governmental fees, and the intent behind exempting government entities does not apply. Exemptions from this type of fee for nonprofit entities are discussed below.

⁵ “Officers” is used generically to refer to all ranks of both police officers and civilians.

III. NONPROFIT EXEMPTION FROM POLICE COST RECOVERY FEE

A. Nonprofit Exemption is Not a Gift of Public Funds.

When discussing fee waivers and exemptions one must reconcile and analyze its relation to the general prohibition of a “gift of public funds.” A “gift of public funds” is generally prohibited by the California Constitution and San Diego Charter section 93.⁶ However, courts have held it permissible under the California Constitution – Article XVI, section 6, and analogous Charter section 93 – as long as a proper legislative finding is made. The courts have upheld the use of public funds when the expenditure serves a “public purpose.” *California Housing Finance Agency v. Elliot*, 17 Cal. 3d 575, 583 (1976); *County of Alameda v. Carleson*, 5 Cal. 3d 730, 745 (1971); *Sturgeon v. County of Los Angeles*, 167 Cal. App. 4th 630, 637 (2008). A public purpose serves those who may not necessarily be financially independent, or means the “gift” is actually to the public as a whole, not the entity that is receiving the benefit. “In other words, the public purpose exception most frequently occurs in situations where a broad class of people benefit. Additionally, what constitutes a public purpose is a matter for legislative discretion and will not be disturbed so long as it has a reasonable basis. *Board of Supervisors*, 45 Cal. App. 3d at 243.” 2001 City Att’y MOL 148 (01-10; Jun. 27, 2001).

Previously, in 2001 City Att’y MOL 148 (01-10; Jun. 27, 2001), this Office addressed the question of development service permit fee waivers for religious organizations. “. . . [P]ermit fee waivers for religious organizations do not violate either the California or United States constitutions. This analysis, however, depends on the fee waiver falling under the public purpose exception to the state ban on gifts of public funds.” 2001 City Att’y MOL 148, 153 (01-10; Jun. 27, 2001). In that memo, this Office concluded the waiver was permissible with a finding by the legislature that the waiver served a public purpose.⁷

Also, in a separate report from our Office (City Att’y Report 11-10 (Feb. 23, 2011)), we advised that the Mayor and Council have the exclusive authority to set funding levels for City services. With those principals in mind, and the proper legislative finding, the Council could determine that a waiver, or fee reduction, serves a public purpose and therefore will not be construed as an unlawful gift of public funds.

If it is determined that a fee waiver for nonprofits serves an overall public purpose that benefits all citizens of the City, Council should require nonprofits that receive the fee waiver to allow acceptance and participation from all citizens of the City in the regulated activity. This would prohibit discriminatory and private, member only, organizations or events, from receiving a benefit that is intended to benefit all citizens – consistent with previous opinions from this Office. *See also* 1995 City Att’y MOL 113 (95-8; Jan. 24, 1995).

⁶ According to Charter section 93, the credit of the City may only be given to the aid and support of the poor.

⁷ Though at the time of that memo Proposition 26 was not enacted, this Office is now analyzing whether charging a fee to some but not all is essentially a tax on those not charged, in addition to whether it is a gift of public funds to waive those fees.

B. Nonprofit Exemptions Are Defensible Under Proposition 26 So Long As Other Fee Payers Are Not Burdened.

With the passage of Proposition 26, in order to waive regulatory fees a separate funding mechanism must be identified to capture the associated cost. Otherwise, not requiring payment for the police-regulated activity for some undermines the position that the police permit fees fall within the exception for government regulatory fees. Any fee charged to an entity by the government is presumed a tax, unless it falls within a specific exception. The exception would apply equally to all similarly situated, otherwise it does not apply at all. Cal. Const. art. XIII C, § (1)(e). The government cannot say a cost must be recovered for a regulatory action, and yet not charge some of the same entities that are engaged in the same conduct as those that have been charged. Either it is an activity that is regulated, with the associated cost, or it is not.

If all similarly situated activities are not charged in order to recover cost, or the cost is not recovered from another mechanism/fund, then arguably the charged fee is actually just a tax on those charged. The City will either have to charge extra to those fee payors, creating a tax, or, to avoid creating a new tax, pay for those other entities' cost out of a separate City fund.

CONCLUSION

All police permit fees for police-regulated activities, businesses and occupations are based on the reasonable regulatory costs, including issuing permits, performing investigations and inspections, and for the administrative enforcement relating to those activities. A narrow exemption or waiver of that fee may be provided, however a proper legislative finding and proper separate funding source is necessary to avoid conflicts with the taxing provisions of the California Constitution, and to avoid a gift of public funds.

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