

April 7, 1999

REPORT TO THE HONORABLE
MAYOR AND CITY COUNCIL

City of San Diego v. Robert McCarty, et al.
San Diego Sup. Ct., Case No. 714746

Edward Teyssier v. City of San Diego
San Diego Sup. Ct., Case No. 721202

These cases involved challenges under the California Constitution to the City's Rental Unit Business Tax. The defendant and cross-complainant in the first case was Robert McCarty, who owns residential rental property at 1346 29th Street and at 401-423 East Juniper Street. The plaintiff in the second case was Edward Teyssier, who owns residential rental property and purports to be a taxpayer advocate. This Tax generates over \$5 million annually for the general fund.

The cases started when a City collections investigator brought a routine small claims action against McCarty to collect \$2,436 in rental taxes for the period 1992 through 1997. McCarty appeared and challenged the validity of the tax. Under Code of Civil Procedure section 86(a)(1), this challenge stripped the Municipal Court of jurisdiction, and the City's case was dismissed. Collections consulted with the City Attorney's Civil Enforcement Unit and, due to McCarty's standing in the apartment owner's community and the likely spread of refusals to pay the tax, a decision was made to refile the matter in Superior Court, and to pursue collection of the taxes due. The case was assigned to Judge David C. Danielsen.

Defendants appeared through attorney Norman Blumenthal, of Blumenthal, Ostroff and Markham. The City was unaware that, at this same time, Mr. Blumenthal was preparing the case against the City for Mr. Teyssier and his group. Defendant McCarty filed a cross-complaint, again challenging the validity of this tax, alleging it was unconstitutional, pursuant to California Constitution Article XIII, as a non-ad valorem property tax,. The cross-complaint sought a refund, declaratory relief, an accounting, and imposition of a constructive trust. Defendants also began extensive discovery efforts, including the deposition of Jack Sturak, the retired deputy director who had administered the Tax.

Mr. Blumenthal then filed the case of *Teyssier v. City of San Diego* on June 3, 1998. The *Teyssier* case differed from *McCarty* because it included a challenge to the tax based on California Constitution Article XIID (Proposition 218). This case was assigned to Judge S. Charles Wickersham.

McCarty filed a motion for summary judgment seeking the court's confirmation that the Tax is an unconstitutional property tax, imposed on property owners solely because they own the property. Judge Danielsen denied the motion, confirming the City's contention that the tax is an excise tax, not a property tax, rightfully imposed on property owners who rent their properties.

The parties proceeded to trial in the *McCarty* action on October 22, 1998, before Judge

Danielsen. The City, through testimony and documentary evidence, introduced evidence to establish a prima facie case in support of the allegations in its Complaint. Defendants introduced no evidence to refute or controvert the City's evidence, but continued the argument that, despite the judge's ruling, the Tax was a property tax and unconstitutional. They also made a motion to amend their cross-complaint at that time to allege that the Tax was also unconstitutional under California Constitution Article XIID.

On February 25, 1999, Judge Danielsen issued his final ruling, again declaring that the City's Rental Unit Business Tax is a constitutional excise tax, imposed on property owners who choose to rent out their property. Judgment was entered on behalf of the City, and defendants were ordered to pay the City for the taxes, interest to date, and collection costs.

In the *Teyssier* action, both the Plaintiff and the City filed motions for summary judgment that were heard on January 19, 1999. Plaintiff's motion also sought to have his case declared a class action for the purpose of recovering all such taxes paid by all holders of rental property. Plaintiff's primary argument was that the Tax is a "fee or charge" imposed "as an incident of property ownership" which would be invalid without an appropriate vote pursuant to Article XIID. On February 25, 1999, Judge Wickersham granted the City's motion, ruling that the Tax is not a "fee or charge" under Article XIID and that it otherwise complies with Article XIII A.

Deputy City Attorney Grant Richard Telfer handled the *McCarty* case and Deputy City Attorney James M. Chapin handled the *Teyssier* case on behalf of the City of San Diego.

Respectfully submitted,

CASEY
GWINN
City Attorney

JMC:vtc:Civ.
RC-99-4