

MEMORANDUM OF LAW

DATE: February 14, 1992

TO: Governance Advisory Group

FROM: City Attorney

SUBJECT: Applicability of Rider Decision to the San Diego Area
Wastewater Management District, Senate Bill 1225

This office has been asked to review the applicability of Rider v. County of San Diego, 1 Cal. 4th 1 (1991) to the proposed San Diego Area Wastewater Management District, Senate Bill 1225 (Killea). We preface our analysis of Rider with a brief historical perspective.

BACKGROUND

Proposition 13

In June 1978, California voters passed article XIII A of the California Constitution (Proposition 13) to address escalating property values and rapidly rising residential property tax assessments.

Article XIII A "consists of four major elements, a real property tax rate limitation (Section 1), a real property assessment limitation (Section 2), a restriction on state taxes (Section 3), and a restriction on local taxes (Section 4)." *Amador Valley Joint Union High Sch. Dist. v. State Bd. of Equalization*, 22 Cal. 3d 208, 231 (1978).

Section 1 of article XIII A limited all ad valorem property taxes which could be imposed by state or local governments to one percent (1%) of assessed value. Section 2 provided that reassessments be limited to two percent (2%) per year from the date the property was purchased. The single exception to the tax rate and assessment adjustment limitation was for taxes levied for the repayment of voter-approved indebtedness if approved prior to July 1, 1978. Cal. Const. art. XIII A, Section 1(b)(1).

In addition, and of particular importance to our analysis, article XIII A, section 4 provided that cities, counties, and special districts upon a two-thirds vote could under certain circumstances impose special taxes. Although phrased in permissive terms, section 4 has been interpreted as a limitation on the ability of local governments to impose other new taxes to replace property tax revenues lost under sections 1 and 2 of article XIII A. (See discussion and citations that follow.)

In 1986, article XIII A was amended to permit additional property taxes to pay for "any bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978, by two-thirds of the votes cast by the voters voting on the proposition." Cal. Const. art. XIII A, Section 1(b)(2).

An extensive body of case law interpreting article XIII A and the 1986 amendment has developed, and it is in this legal context that oral

argument was heard in the case of *Rider v. County of San Diego*.

ANALYSIS

The Rider Case

The San Diego County Regional Justice Facility Financing Agency ("Agency") was created by legislative act (Gov. Code Section 26250 et seq.) in 1987. The act empowered the Agency, which was given no other taxing authority, to adopt an ordinance imposing a supplemental sales tax of one-half (1/2) of one (1) percent and provided for an election to approve the tax ordinance by a simple majority. Tax revenues would finance the construction of justice facilities within San Diego County.

The sales tax ordinance was approved by a bare majority, 50.8 percent, of the County's voters in June 1988. A group of County taxpayers filed suit to challenge the validity of the tax, asserting that it violated the two-thirds vote requirement of article XIII A, section 4 and Government Code sections 53720-53730.

The trial court found in taxpayers' favor, concluding "the tax constituted a deliberate and unavailing attempt to circumvent section 4 and its requirement of two-thirds voter approval of special taxes imposed by special districts such as the Agency." *Rider* at 6.

The Court of Appeal reversed the trial court's judgment. Though it agreed with the trial court that the Agency was "an empty shell through which the Board of Supervisors . . . can exercise its discretion," the appellate court found itself bound by an earlier decision which held article XIII A, section 4 inapplicable to districts such as the Agency, which have no property taxing authorization. *Rider* at 6.

Special District Issues

Prior to the *Rider* decision, the California Supreme Court in *Los Angeles County Transportation Com. v. Richmond*, 31 Cal. 3d 197 (1982) found that the Los Angeles County Transportation Commission ("LACTC"), which was authorized to impose a sales tax once the measure was approved by a majority of the county's voters, was not a 'special district.' *Richmond* at 205-207. The court reasoned that since section 4 of article XIII A was intended to restrict the ability of local taxing agencies to impose new taxes to replace property tax revenues lost due to the tax rate and reassessment restrictions of Proposition 13, only those 'special districts' authorized to levy property taxes were contemplated in section 4. *Richmond* at 206. LACTC had no authority to impose property taxes and therefore could not be deemed a 'special district' subject to the limitations of article XIII A, section 4.

The *Rider* court has now refined the definition of 'special district' to include "any local taxing agency created to raise funds for city or county purposes to replace revenues lost by reason of the restrictions of Proposition 13." *Rider* at 11. The *Rider* court reasoned that "*Richmond's* limitation of the term 'special district' to those districts possessing property tax power is unworkable as applied to

districts formed after the adoption of Proposition 13, because . . . no such agencies possess that power." Rider at 11. Further, the court found strong evidence that the Agency was created to raise revenues for county purposes, thereby circumventing the strictures of section 4.

An 'essential control' test which would afford grounds for reasonably inferring an intent to circumvent Proposition 13 was outlined by the Rider court.

In determining whether such control exists, a variety of considerations may be relevant, including the presence or absence of (1) substantial municipal control over agency operations, revenues or expenditures, (2) municipal ownership or control over agency property or facilities, (3) coterminous physical boundaries, (4) common or over-lapping governing boards, (5) municipal involvement in the creation or formation of the agency, and (6) agency performance of functions customarily or historically performed by municipalities and financed through levies of property taxes.

Rider at 11-12.

We are unconvinced, despite Assemblyman Peace's analysis of the Rider decision, attached as Enclosure 1, that application of any of the factors in the 'essential control' test would jeopardize the status of the San Diego Area Wastewater Management District.

The purpose in creating the San Diego Area Wastewater Management District is to provide greater decision-making control for the thirteen (13) member agencies over policies and procedures in the regional management of wastewater and its byproducts. The wastewater system is currently under the sole ownership and control of the City of San Diego. The public entities which contract with the City of San Diego through the existing joint powers agreement for the collection, treatment, transportation, and disposal of their wastewater have a limited voice in the operation of the system.

As is currently contemplated, ownership of system facilities and property would be transferred to the district provided the district agrees to assume all of the City of San Diego's system-related contractual obligations. Control of the wastewater system would pass to the district's member agencies. In Rider, the County of San Diego "retained substantial control over operations and expenditures" of the Agency and "required compliance with the County's master plan." Rider at 9. Such substantial control by the City of San Diego or any other district member is not foreseen nor is it in any way provided for by the proposed legislation.

The physical boundaries of the proposed district would be defined

by the service areas of the thirteen (13) member agencies. In Rider, the Agency's boundaries are coterminous with those of the County.

The district will be governed by a twenty (20) member board; the governing body of each member agency will appoint a board member or members who may be either elected or appointed officials of the member agency making the appointment. Any motion, resolution, or ordinance before the board requires a majority vote for approval unless the ordinance under consideration pertains to the issuance of revenue bonds. In that instance a two-thirds vote for approval is required to enact the ordinance. The Agency, on the other hand, included two (2) County Supervisors and the Sheriff of San Diego County among the seven (7) Agency directors giving the County extensive control and influence over the small Agency board.

With regard to municipal involvement in the formation of the district, the City of San Diego, as the current sole owner of the wastewater system, has been instrumental in the proposed creation of the district. However, the impetus for the district's formation, came from other public entities whose representatives appeared before the San Diego City Council demanding that the City establish a means by which they could meaningfully participate in wastewater system decision-making functions.

Subsequently, the City Council created a Governance Advisory Group, composed of representatives of the contracting agencies as well as representatives of the City and County of San Diego and the San Diego County Water Authority, which was responsible for recommending an appropriate form for participatory management of the wastewater system. The group collectively conceived and endorsed the enabling legislation for the San Diego Area Wastewater Management District, Senate Bill 1225.

And, finally, the district has no generic authority to finance, through levies of property taxes or sales taxes, functions historically performed by municipalities, except in conformance with Proposition 13's standard of a two-thirds voter ratification.

The enabling legislation for the San Diego Area Wastewater Management District does not contain authority empowering the district to impose property or sales taxes, but it does provide for the imposition of rates, fees, and charges for the use of any facilities owned or operated by the district as well as for services performed by the district.F

As recently as January 9, 1992, the Court of Appeal found that a Major Facilities Charge "was a permissible 'user fee' rather than a 'special tax' subject to the two-thirds vote requirement of article XIII A, section 4, of the California Constitution (Proposition 13)." *Carlsbad Municipal Water District v. Q.L.C. Corp.*, 92 Daily Journal D.A.R. 248 (Jan. 9, 1992). The court reasoned that the Major Facilities Charge was not intended to replace revenues lost by the property tax rate and reassessment limitations imposed by sections 1 and 2 of

article XIII A. The charge was "triggered by the voluntary decision of the developer to develop the 300-unit condominium complex and it is directly tied to the increase in use of water facilities and services likely to be generated by the development." Carlsbad Municipal Water District at 252.

In addition, the district has authority to issue general obligation bonds which would be subject to the provisions of Health and Safety Code Sections 4780 et seq. and Sections 4806 et seq. requiring a two-thirds vote in favor of incurring the bonded indebtedness. Again, in Rider, the Agency's enabling legislation provided for an election to approve a supplemental sales tax to finance the construction of justice facilities by a simple majority vote.

The proposed district is also empowered to issue revenue bonds. Such bonds would be secured by revenues derived from the operation of the wastewater system and would not be backed by any taxing authority of the issuer.

According to the Rider court, "the determination whether a city or county essentially controls a taxing agency is one that necessarily must be made on a case-by-case basis." Rider at 12. Based on the above application of the 'essential control' test, it would appear that the San Diego Area Wastewater District is neither the functional equivalent of the City of San Diego nor could be reasonably inferred under any circumstances to circumvent Proposition 13.

Special Tax Issues

In 1982, the California Supreme Court addressed the meaning of the term 'special tax' as used in article XIII A, section 4. The City and County of San Francisco imposed a payroll and general receipts tax, the proceeds of which were to be used for general revenue purposes. The tax was approved by a majority of the City's voters thereby calling into question whether it was a 'special tax' requiring a two-thirds vote as mandated by article XIII A, section 4.

The 1982 court construed the term "'special taxes' in section 4 to mean taxes which are levied for a specific purpose rather than . . . a levy placed in the general fund to be utilized for general governmental purposes." City and County of San Francisco v. Farrell, 32 Cal. 3d 47, 57 (1982).

The Rider court did not extend the Farrell definition of 'special tax' to limited purpose agencies such as the Agency. "To hold that a tax cannot be deemed a 'special tax' if revenues thereof are deposited in the taxing agency's general fund pulls any remaining teeth from section 4's restriction on special taxes." Rider at 14.

The Rider court formulated an interpretation of section 4 which provides that "a 'special tax' is one levied to fund a specific governmental project or program" and allowed that "under the foregoing principle, every tax levied by a 'special purpose' district or agency

would be deemed a 'special tax'." Rider at 15.

While the proposed district, like the Agency would be a special purpose agency, the district, unlike the Agency, has no taxing authority. As discussed above, San Diego Area Wastewater Management District revenues would be derived from rates, fees, and charges for services performed. General obligation bonds, as approved by district voters, would not allow the district to avoid section 4's supermajority voter approval requirement.

CONCLUSION

At this time, it would be entirely inappropriate to assume that any agency created after the passage of Proposition 13, other than the San Diego County Regional Justice Facility Financing Agency, which has a tax approved by a simple majority vote, is necessarily impacted by the Rider decision.

The ambiguous 'essential control' test will undoubtedly be applied to various local taxing agencies created since 1978. And, depending on the particular facts pertaining to each agency and how narrowly or expansively the court's language is interpreted, some of these agencies may have their tax ordinances subjected to a supermajority vote or their majority approved taxes invalidated. It is our opinion that, at this time, the rule arising from the Rider decision is entirely inapplicable to the proposed San Diego Area Wastewater Management District.

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Enclosure

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