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REPORT TO MAYOR AND CITY COUNCILMEMBERS

TOURISM MARKETING DISTRICT

INTRODUCTION

On November 26, 2012, the City Council passed a resolution approving a contract with the Tourism Marketing District (“TMD”). Given the fact that the TMD operating agreement has not been signed, funds collected since January 1, 2013, remain with the City and have not been turned over to the TMD. Under the TMD structure which was approved by the City Council and hoteliers who pay the assessment, those funds are to be administered by the TMD. Accordingly, the City Council will need to decide a course of action.

There are three options:

1. The City Council may consider ending the TMD and refunding the money collected;
2. The City Council may consider amending the TMD;
3. The City Council may consider enforcement of the TMD structure as approved.

The last option will be the subject of a closed session meeting on Tuesday, February 26, 2013, and we suggest that it not be discussed at the public session.

What follows is our legal overview of the first two options. Upon direction from the City Council, we will return with more specifics.

I. Ending the TMD and/or the assessment

If the City Council wants to consider rescinding the TMD and the assessment, we suggest that you direct our office to return as soon as possible with legal options to accomplish that.

The Mayor has indicated opposition to the TMD assessment for a number of reasons. For purposes of this memo, we will only address one of the Mayor’s arguments that deals with the

legal issue. The rest would be considered policy issues which we will leave to the City Council to consider.

The Mayor claims the TMD assessment is an illegal tax. Last year, our office and the City Council addressed this issue. We have distributed our July 27, 2012 Memorandum of Law on the topic, which can also be found on our website under Documents/Memoranda of Law. Our office raised concerns regarding legality in light of Proposition 26 due to the very high standard that must be met, but we did not conclude the assessment was illegal, particularly in light of the TMD's lawyers' opinion that they structured the assessment to satisfy the standard. Rather than opine on the legality or refuse to sign off on the assessment, our office suggested that we take steps to protect the City's general fund while allowing the TMD to defend the assessment if that was the will of the Council.

Under California's Constitution, taxes can only be imposed if approved by voters. Fees can be imposed without a vote. The standard for being deemed a fee is very stringent under Proposition 26, approved by voters in 2010. Generally, Prop 26 states it is a fee only if the activities to be funded by the assessment are limited to benefits or services provided directly to the charged businesses and not to others who are not charged.

This is a very difficult standard to meet. Comparing to water ratepayers, you pay for the water you use. That is a fee. Here, the legal payors are the hotels. In order to try and meet that standard, the TMD and its lawyers structured its budget to spend money only on those activities benefiting the payors. There are pending lawsuits as to whether the standard has been met.

Last November, the City Council decided to proceed with the TMD assessment and allow the TMD to defend the assessment's legality, but protect the City from liability and costs. Accordingly, the TMD operating agreement provides that the TMD will defend the City in lawsuits challenging the fee and indemnify the City as to any judgment. Since the operating agreement remains unsigned, those provisions are not in force. Accordingly, our office is defending the pending lawsuits.

As additional protection, even if the operating agreement is signed the funds are not released to the TMD absent further approval of the City Council. Our office has been working with the TMD's lawyers to establish waiver agreements from individual hotels that would allow pro rata release of funds and further protect the City's general fund.

The City now faces multiple lawsuits challenging the assessment and a lawsuit challenging the Mayor's refusal to sign the operating agreement. If the City Council wants to consider rescission of the TMD and assessment, please direct us to return with the appropriate ordinance and we will do so.

II. Amending the TMD

If the City Council wants to consider amending the TMD, we suggest that you direct our office to return as soon as possible with legal options to accomplish that. It should be pointed out that substantive changes would likely require a revote.

As reported by the media, the four requests made by the Mayor before he would sign the TMD contract are as follows: (1) Indemnification for the City should the hotel room levy be found illegal by the courts; (2) more money for the City Treasury; (3) a short-term marketing agreement of one or two years instead of the 39-1/2 years approved late last year by the City Council; and (4) a living-wage requirement for downtown hotels. Each are addressed below:

A. Indemnification for the City should the hotel room levy be found illegal by the courts

An indemnification for the City should the hotel room levy be found illegal by the courts is already in the TMD contract Mr. Filner is refusing to sign.

In addition, the TMD funds would be frozen until waivers are signed further protecting the City's general fund.

B. More money for the City Treasury

This would be illegal. It would certainly eliminate any basis for arguing that the TMD assessment is a fee.

It would be like demanding from water ratepayers that the only way we will continue supplying water is if part of their payment goes to the City's general fund.

C. A short-term marketing agreement of one or two years instead of the 39-1/2 years approved late last year by the City Council

The term of the TMD, the assessment and the operating agreement can all be changed. That would be a policy decision for the City Council. If the term is changed, the TMD would need to be redone and a revote taken.

D. A living-wage requirement for downtown hotels

The TMD is a separate entity from the hotels. Imposition of a living wage is something that can be considered by the City Council by ordinance, but cannot be imposed through an agreement between the TMD and the City.

CONCLUSION

The City Council may consider ending or amending the TMD and the assessment with some legal limits. For example, the City may not extract funds for its general use. If the Council wants to consider ending or amending the TMD and the assessment, we suggest that the Council direct us to return with ordinances for Council consideration. Enforcement of the existing TMD structure is scheduled for closed session on Tuesday, February 26, 2013, and should not be discussed in open session due to pending litigation.

Respectfully submitted,

/s/ Jan I. Goldsmith

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