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IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

Citizens for Fair REU Rates, et al.
Plaintiffs and Appellants

vs.

City of Redding, et al.
Defendants and Respondents

SUPREME COURT
FILED

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Deputy

REPLY BRIEF

Review of a Published Decision of the
Third Appellate District, Case No. C071906

Reversing a Judgment of the Superior Court of
the State of California for the County of Shasta,
Case No. 171377 (Consolidated with Case No. 172960)
Honorable William D. Gallagher, Judge Presiding

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INTRODUCTION

The City of Redding's Opening Brief demonstrated that the payment in lieu of taxes (PILOT) appropriated by its annual budgets and transferred from the Redding Electric Utility (REU) to the City's general fund is legislation that predates 2010's Proposition 26 and therefore survives it. In opposition, Appellants Citizens for Fair REU Rates (Citizens) fail to establish the prima facie case required to challenge government revenues for three reasons:

- Citizens assume, but do not establish, the essential fact on which they build their case — that the PILOT is funded by electric rates — even though the trial court found the contrary with record support.
- They misapprehend the record.
- They assume without argument that Proposition 218 authorities control construction of Proposition 26 despite the different language and intent of the two measures on points material here.

Accordingly, this Court ought to affirm the trial court's ruling

for the City on the grandfathering theory. Alternatively, this Court should affirm the trial court's ruling on its further conclusion, reflected in Justice Duarte's dissent below, that even if

Proposition 26 applied here, the City's PILOT is reasonable in fact and as a matter of law.

LEGAL DISCUSSION

I. STANDARDS OF REVIEW AND BURDENS OF PROOF

The parties are largely in agreement that this Court reviews legal issues and the administrative record de novo. (Defendants and Respondents' Opening Brief (OB) at p. 12; Plaintiffs and Appellants' Answer Brief (Ans.) at p. 15.) However, Citizens overlook that Proposition 26 did not alter the distribution of responsibility between trial and appellate courts. Citizens continue to bear the duty to demonstrate error in the trial court and to identify record support for their claims on appeal.

As the Fourth District Court of Appeal recently confirmed in *Moore v. City of Lemon Grove* (2015) 237 Cal.App.4th 363, 368 (*Lemon Grove*), affirming transfer of sewer service fees to a city's general fund, an appellate court "presume[s] that the appealed judgment is correct." "Even when we exercise our independent judgment in reviewing the record, we do not decide disputed issues of fact and our review 'is limited to issues which have been adequately raised and supported in [the appellant's] brief.'" (*Ibid.* [internal citations omitted].)

Morgan v. Imperial Irrigation Dist. (2014) 223 Cal.App.4th 892, 913 (*Morgan*) explains an “appellant must frame the issues for us, show us where the superior court erred, and provide us with the proper citations to the record and case law”

Further, Citizens may not merely observe the City’s duty to produce a record in support of its rate-making and budgets. It must make a prima facie case the City’s electric rates exceed the reasonable cost of service on account of the PILOT. Only then does the burden shift to the City to demonstrate otherwise on a competent record. Citizens conceded as much in their opening brief to the trial court. (2 CT 541 [“Certainly, a plaintiff fee-payer challenging a local government charge as an unlawful disguised ‘tax’ must allege a prima facie case to initiate the action”].)

Citizens initially “bear[] the burden of proof to establish a prima facie case showing that the fee is invalid.” (*California Farm Bureau Federation v. State Water Resources Control Bd.* (2011) 51 Cal. 4th 421, 436 [construing Prop. 13]; see also *California Building Industry Association v. State Water Resources Control Board* (2015) 235 Cal.App.4th 1430, 1451 [same].) *Morgan* confirms the rule in the context of Proposition 218:

Therefore, although we use a de novo standard of review here, we do not transform into a trial court. ... [W]e do not find it sufficient for an appellant to merely claim the respondent should not have been successful at

trial and then the burden shifts to the respondent to prove its case in its entirety again.

(*Morgan, supra*, 223 Cal.App.4th at p. 913.) So, too, in *Lemon Grove* — another Proposition 218 case:

The agency charging the fee or charge has the burden of demonstrating compliance with these requirements. The question whether a fee or charge violates article XIII D is subject to de novo review. We presume that the appealed judgment is correct. Even when we exercise our independent judgment in reviewing the record, we do not decide disputed issues of fact and our review “is limited to issues which have been adequately raised and supported in [the appellant’s] brief.”

(*Lemon Grove, supra*, 237 Cal.App.4th at pp. 368–369 citations omitted.)

Because Citizens fail to make a prima facie case that the City’s electric rates exceed the reasonable cost of service, this Court should affirm the trial court’s decision. However, even if the Court finds

~~Citizens made a prima facie case, the City can bear its burden on this~~
record, as demonstrated below.

II. CITIZENS MISREAD THE RECORD

A. Citizens Assume Without Evidence that the December 2010 Electric Rates Fund the PILOT

Citizens' Answer Brief is premised on an unsupportable assumption — that the electric rates set on December 7, 2010 fund the PILOT. Because this is untrue, their entire argument fails.

The trial court concluded “there is no evidence that the PILOT is paid out of customers['] rates.” (3 CT 741.) As the Opening Brief explained in detail (at pp. 35–39) the record amply supports this conclusion. (See, e.g., IV AR, Tab 145, p. 831 [Fiscal Year 2010–2011 budget] and Attachment 1 [legible copy];¹ *id.* at p. 873 [2010 audit showing PILOT of \$6,055,950]; XIII AR, Tab 205, p. 2975 [Fiscal Year 2012–2013 budget showing wholesale revenues of at least \$12.6 million per year and miscellaneous income of at least \$6.9 million per year].) Citizens do not dispute the PILOT can be funded three times over from unrestricted revenues without drawing upon retail rate proceeds.

Citizens offer three kinds of “support” for their claim the PILOT is funded by the rates challenged here. First, they make bare assertions of the claim without citation to the record or any other

¹ Duplication of the AR obscured much of page 831. A legible copy is attached to this Brief as Attachment 1 pursuant to California Rules of Court rules 8.520(b) and 8.204(d.)

authority. (See Ans. at pp. 3, 12, 20, 24, 25, and 26.) Second, Citizens offer a single citation to the trial court's statement of decision — to a page that does not speak to how the PILOT is funded. (Ans. at p. 6, citing 3 CT 736.) Rather, as the trial court states elsewhere in that statement of decision: “there is no evidence that the PILOT is paid out of [a] customer's rates.” (3 CT 741.)

Finally, Citizens cite boilerplate language in the City's rate-making resolutions stating electric rates “obtain funds necessary to maintain such intra-City transfers as authorized by law.” (Ans. at p. 12, citing IV AR, Tab 163, p. 1041, § 3.) Citizens assume the resolutions' references to “transfers” must mean the PILOT, but provide no basis for that assumption. (See, e.g., Ans. at pp. 26–27.) However, they also observe that the electric utility reimburses the City's general fund via a “cost allocation plan” for shared overhead and general services — such as facility rent, insurance, the services of the City Attorney, etc. (Ans. at pp. 27–28, 30.) Thus, the boilerplate Citizens cite could as easily refer to cost allocation as to the PILOT — the reference is not proof retail rates fund the PILOT.

Furthermore, as demonstrated by the City's Opening Brief, the records here establish that the December 2010 power rate increases were unneeded to fund the PILOT, which was fully funded by earlier rates (OB at pp. 16, 41; see IV AR, Tab 159, pp. 1030–1034 [Nov. 19, 2010 staff report]; IV AR, Tab 166, pp. 1065–1098) and that the PILOT can be funded from revenues other than the proceeds of

retail rates. (OB at pp. 35–36; see IV AR, Tab 145, p. 831; IV AR, Tab 149, p. 873; XIII AR, Tab 205, p. 2975.)

In sum, the essential factual premise of Citizens’ Answer Brief is simply unsupported on this record. The Answer Brief is therefore entirely unpersuasive.

B. Citizens Repeat a Claim Debunked in the Court of Appeal that the City Increased the PILOT in 2010

As they did in the Court of Appeal, Citizens raise a factual argument they did not make in the trial court. Citizens claim the City changed the PILOT formula in 2010 to include the electric utility’s share of assets held by joint powers agencies, citing an attachment to the City Council resolution adopting the 2011–2013 budget. (Ans. at p. 10; Appellants’ Opening Brief in the Court of Appeal (AOB) at p. 26.) However, as the City explained then, Citizens did not make this factual argument in the trial court. (Respondents’ Brief to the Court of Appeal (RB) at pp. 23–24, citing RT 71–73, 198–199.) Instead, Citizens acknowledged at trial that the calculation was last amended in either “2005 or 2007,” and in any event, has not changed “in the recent years.” (RT at pp. 198–199.)

While Citizens discussed changes in PILOT calculation several times at trial, including accounting for the electric utility’s interest in assets held jointly with other utilities, it never disputed that the

PILOT has been unchanged since before the 2010 adoption of Proposition 26. (RT at pp. 198–199.) Citizens cannot now present a factual argument never raised in the trial court. (*McDonald's Corp. v. Bd. of Supervisors* (1998) 63 Cal.App.4th 612, 618 [“The existence of this factual question prevents the County from raising this theory for the first time on appeal”].) For this reason, this Court should disregard this argument.

Moreover, the Court of Appeal properly rejected this contention on its merits. The Court of Appeal’s recitation of facts acknowledges that the most recent amendment of the PILOT followed “adoption of a two-year budget in June 2005, [when] the City Council adopted the PILOT into its current form by including the value of joint-venture assets in which the Utility has a share in the asset base to which the 1% [PILOT] is applied.” (*Citizens for Fair REU Rates v. City of Redding* (2015) 182 Cal.Rptr.3d 722, 726.)

Thus, were this Court to consider the point, Attachment A to the 2011–2013 budget resolution (XI AR, Tab 203, p. 2469), and the in-lieu computations from the City’s budgets for fiscal years ending 2006 through 2009,² show only what counsel acknowledged at trial:

² The in-lieu computations are attached as Exhibits D and E to the Motion for Judicial Notice in Support of Respondents’ Brief filed in the Court of Appeal. (MJN in Support of Resp. Brief.)

the PILOT increases as utility assets increase.³ The PILOT has worked that way for 25 years. (RB at p. 25.)

Furthermore, Attachment A to the 2011–2013 budget resolution does not support Citizens’ belated contention that “the City changed its concepts of ‘assets’ and changed its formula for the PILOT.” (Ans. at p. 11; see also AOB at p. 26). Attachment A does not show how the PILOT was calculated for any year other than fiscal year 2010–2011. Careful review of Attachment A shows the City’s consistent methodology for calculating the PILOT. (See RB at pp. 25–27 [explaining calculation of the value of appreciating assets and demonstrating that budget attachments reflect this consistent methodology].)

Attachment A to the 2011–2013 budget resolution distinguishes appreciating assets (e.g., land) from depreciating assets (e.g., vehicles). The far left column of line 14 of Attachment A totals the values of appreciating assets still in service in fiscal year 2010–2011. The fact they appear there does not mean these values

³ As discussed below, this does not amount to an “increase” for purposes of Proposition 218, which does not apply to electric rates in any event. (Gov. Code § 53750, subd. (h)(2)(B) [defining “increase” for purposes of Articles XIII C and XIII D]; Art. XIII D, § 3, subd. (b) [“For purposes of this article, fees for the provision of electrical or gas service shall not be deemed charges or fees imposed as an incident of property ownership”].)

were first calculated in that year, as Citizens assume. Joint powers agency assets are treated as non-appreciating because acquisition data are on the joint powers entities' books, not the City's. Budget attachments for prior years reflect this consistent methodology, with joint powers authority assets accounted for every year just as reflected in Attachment A to the 2011–2013 budget. (See RB at pp. 26–27; MJN in Support of Resp. Brief, Exhs. D and E.) Therefore, Citizens' belated claim that the PILOT was amended in 2010 to include the value of joint powers agency assets is simply wrong.

Thus, the claim is unsupported by the record and should be disregarded, even should this Court be inclined to entertain this arcane factual inquiry for the first time on appeal.

C. Citizens Make, for the First Time in this Litigation, a New Claim of Error by the City

Some two and a half years into this litigation, Citizens “take us a bit into the weeds” to argue for the first time that the City’s briefs mistakenly transposed the respective methodologies employed by the City and the Board of Equalization in a recitation of amendments to the PILOT calculation before the 2010 adoption of Proposition 26. (Ans. at p. 9.) The City indeed stated in its Opening Brief that a 1999 R.W. Beck study “noted the State Board of Equalization assessed multi-county utility property for property taxation using original, rather than the depreciated, asset values; but

the City's PILOT then did not. (III AR, Tab 119, p. 664 (1st ¶).)" (OB at p. 8.) Citizens correctly note that the R.W. Beck study states that the Board of Equalization used depreciated asset values rather than original. (Ans. at p. 9.) This was indeed a transposition error in the City's brief, albeit an inconsequential one.

Citizens are not correct, however, in denying that the City amended the PILOT in the 2001–2003 budget "to bring [it] in line with property tax methodologies" used by the Board of Equalization. (See III AR, Tab 126, pp. 693–694; OB at p. 9.) Thus the City's briefs have correctly stated throughout this litigation the more important point — that the City had amended its PILOT in 2001 to match the Board of Equalization's methodologies.⁴ Furthermore, the only fact needed for present purposes is that the City has not

⁴ The City explained in its trial brief that the PILOT is calculated the same way as the property tax, including an annual 2% escalation cap, based on the book value of REU's assets. (3 CT 630, fn. 12.) The City explained in its brief to the Court of Appeal that "[u]pon adoption of its 2001–2003 budget, the City Council adjusted the PILOT to comply with the State Board of Equalization's methodology" (RB at p. 7, citing III AR, Tab 126, pp. 693–694; III AR, Tab 134, p. 738.) The City made the same argument in its Opening Brief here. (OB at p. 9, citing 2 CT 530 (last ¶); MJN in Support of Resp. Brief, Exh. D [PILOT calculation for fiscal years ending in 2006 and 2007].)

amended the PILOT formula since 2005. (2 CT 530 (last ¶); see also MJN in Support of Resp. Brief, Exh. D.) The precise details of the PILOT methodology are not relevant to the inquiry whether the PILOT is grandfathered; whatever they may be, they are grandfathered.

Citizens evade this question to argue the PILOT is transferred to the City's general fund while the property tax it mimics is shared among the City, County, school and other special districts. (Ans. at pp. 39-40.) Again, the point is true, but immaterial. The City was free in the pre-Proposition 26 legal environment to legislate the PILOT to ensure that the economic activity represented by the electric utility supports public services approximately as an investor-owned utility would. That the distribution of those funds differs from the distribution of a property tax may be of policy concern, but it is of no legal moment here.

In any event, regardless of whether the PILOT perfectly matches the property tax or makes good public policy, the PILOT as it is implemented today existed before voters adopted Proposition 26 and is therefore grandfathered by it.

III. THE PILOT DOES NOT EXCEED THE REASONABLE COST OF SERVICE

A. Proposition 218 and Proposition 26 Impose Different Cost of Service Standards

Citizens argue “[t]he constitutional requirements for compliance with Proposition 26 are no less ‘substantive’ than those for Proposition 218.” (Ans. at p. 17.) Indeed. However, the two requirements state different cost limitations for the revenue measures they regulate. That there are some similarities between the two does not permit unthinking resort to authorities under Proposition 218 to construe Proposition 26. Authorities applied by analogy must be applied with care and only to the extent the analogy holds true to the constitutional text.

Proposition 218 demands more of rate-makers than Proposition 26. Both measures limit service fee proceeds to the total cost of service to all who receive it. (Cal. Const., art. XIII D, § 6, subd. (b)(1) [“Revenues derived from the fee or charge shall not exceed the funds required to provide the property related service”]; Cal. Const., art. XIII C, § 1, subd. (e)(2) [“Tax” excludes “A charge imposed for a specific government service or product ... which does not exceed the reasonable costs to the local government of providing the service or product”].) Proposition 218 reinforces its cost-of-service limitation by forbidding use of fee proceeds for other

purposes. (Cal. Const., art. XIII D, § 6, subd. (b)(2) [“Revenues derived from the fee or charge shall not be used for any purpose other than that for which the fee or charge is imposed”].) Finally, and at the heart of Proposition 218, is a proportional cost requirement with only a rough parallel in Proposition 26. (*Id.*, § 6, subd. (b)(3) [“The 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.”].)

Proposition 218’s cost-of-service limitations require someone, presumably the legislative rate-maker, to reasonably attribute service to each parcel. For administrative necessity, this is often done customer-class-by-customer-class, rather than customer-by-customer.⁵ (*California Farm Bureau Federation, supra*, 51 Cal. 4th at p. 437, 446 [class-by-class cost allocation under Prop. 13]; see also *Griffith v. Pajaro Valley Water Management Agency* (2013) 220 Cal.App.4th 586, 600 [same under Prop. 218]; *Lemon Grove, supra*, 237 Cal.App.4th at pp. 374–375 [same under Prop. 218].) A rate-maker

⁵ Some rate-makers have so few customers that there is no need to make rates by class. For example, *Newhall County Water Dist. v. Castaic Lake Water Agency*, Second District Court of Appeal Case No. B257964 (filed Aug. 4, 2014; Reply Brief due Aug. 17, 2015), involves a State Water Project contractor that wholesales water to just four retailers.

must then determine the proportional cost of providing that attributed service to each customer class — allocating the cost of providing that service to all. Finally, the rate-maker must demonstrate its rates do not exceed that proportional cost as to any customer class.

Proposition 26 is less demanding. It requires a rate-maker to demonstrate a service charge is:

imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.

(Cal. Const., art. XIII C, § 1, subd. (e)(2).)⁶ Further, the rate-maker must prove:

that the amount is not more than necessary to cover the reasonable costs of the governmental activity, and that

⁶ This brief applies Proposition 26's exception for government-provided services and products. (Cal. Const., art. XIII C, § 1, subd. (e)(2).) However, it might as easily apply that for government-provided privileges and benefits. (Cal. Const., art. XIII C, § 1, subd. (e)(1).) The distinction between a privilege or benefit and a service or product is not always clear, but the two exceptions impose identical requirements, so the distinction is unimportant.

the manner in which those costs are allocated to a payor bear a **fair or reasonable** relationship to the payor's burdens on, or benefits received from, the governmental activity.

(Cal. Const., art. XIII C, § 1, final unnumbered ¶, emphasis added.)

This text creates four requirements:

1. The "direct-service requirement" — The fee must be for a specific service provided directly to payors.
2. The "no free riders principle" — The service may not be provided to those not charged.⁷

⁷ It is unlikely the voters who approved Proposition 26 intended to forbid free or discounted services. More likely, they intended to forbid such services if funded by other rate-payors. If subsidies or discounts are funded by taxes or other non-rate-revenues, the goals of Proposition 26 to reduce the burden of government on tax-, rate- and fee-payors are met. (IV AR, p. 988 [uncodified § 1 of Proposition 26, "Findings and Declarations of Purpose"]; cf. *Morgan, supra*, 223 Cal.App.4th at 923 ["We find nothing in section 6 that prohibits an agency from charging less than the proportional cost of service. The fees simply cannot exceed the proportional cost"].) Thus, Citizens' bare assertion, without argument, that rate-payors would be harmed by the funding of the PILOT from non-rate revenues fails to persuade. (Ans. at pp. 31–33.)

3. The “total cost limit” — The charge may “not exceed the reasonable costs to the local government of providing the service or product.”⁸
4. The “cost allocation requirement” — Rate-makers must show “the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the government activity.”

(Cal. Const., art. XIII C, § 1, subd. (e) [final, unnumbered para.])

The cost allocation requirement requires something more than the total-cost limit; yet it is not a proportionate-cost-of-service rule comparable to Proposition 218’s article XIII D, section 6, subdivision (b)(3). Rather it codifies this Court’s pre-Proposition 26 case law testing regulatory and other fees under Proposition 13, on

⁸ This is analogous to Proposition 218’s article XIII D, section 6, subdivision (b)(1). It is reinforced by the final unnumbered paragraph of section 1, subdivision (e), which requires a rate-maker to prove a charge “is no more than necessary to cover the reasonable costs of the government activity.” (Cal. Const., art. XIII C, § 1, subd. (e) [final, unnumbered ¶].) This language from the final unnumbered paragraph seems to merely assign the burden to prove — rather than to change — the total cost requirement of subdivision (1)(e)(2).

which both Propositions 26 and 218 build. (OB at p. 33; see *Sinclair Paint Co. v. State Board of Equalization* (1997) 15 Cal.4th 866, 879 quoting *San Diego Gas & Electric Co. v. San Diego County Air Pollution Control Dist.* (1988) 203 Cal.App.3d 1132, 1146 [“to show a fee is a regulatory fee and not a special tax, the government should prove (1) the estimated costs of the service or regulatory activity, and (2) the basis for determining the manner in which the costs are apportioned, so that charges allocated to a payor bear a fair or reasonable relationship to the payors’ burdens on or benefits from the regulatory activity”]; see also, *Schmeer v. County of Los Angeles* (2013) 213 Cal.App.4th 1310, 1321–1322, 1326 [citing *Sinclair Paint* to construe Proposition 26].)

Thus, while Proposition 218 requires a rate-maker to show a fee is **proportionate** to the cost of service attributable to a parcel or customer class; Proposition 26 requires only that total service cost be allocated among payors in a manner that is “**fair or reasonable**” when compared to payors’ respective burdens on or benefits from the government service. This was the basis for Justice Duarte’s dissent below, concluding the PILOT meets Proposition 26’s standard because it is a fair and reasonable allocation of service cost among rate payors. (182 Cal.Rptr.3d at p. 741.) This Court should conclude likewise.

B. Fresno and Roseville Do Not Aid Citizens

Citizens cite *Howard Jarvis Taxpayers Association v. City of Roseville* (2002) 97 Cal.App. 4th 637 (Roseville) and *Howard Jarvis Taxpayers Association v. City of Fresno* (2005) 127 Cal.App.4th 914 (Fresno) to support their claim the 2010 electric rates challenged here exceed the cost of service. (Ans. at pp. 25, 27, 32.) However, those cases are unhelpful here for three reasons.

First, as Citizens concede, those cases apply Proposition 218, not Proposition 26. (Ans. at p. 25.) As discussed above, the proportional-cost-of-service requirement of Propositions 218 is substantially more demanding than the cost-allocation requirement Proposition 26. Proposition 218 authorities construing its proportional-cost requirement are of limited utility in construing the “fair or reasonable” cost allocation requirement of Proposition 26.

Second, Proposition 218 is retroactively applicable to property related fees legislated before its adoption and maintained after July 1, 1997. (Cal. Const., art. XIII D, § 6, subd. (d) [“Beginning July 1, 1997, all fees or charges shall comply with this section”].) No comparable language appears in Proposition 26, which is plainly not

retroactive as to local government. (*Brooktrails Township Community Services Dist. v. Bd. of Supervisors of Mendocino County* (2013) 218 Cal.App.4th 195, 205). The contrast is especially telling because Proposition 26 amends Proposition 218 and is therefore in pari materia with it. (*Gately v. Cloverdale Unified School Dist.* (2007) 156

Cal.App. 4th 487, 494 [“Statutory provisions that are in pari materia, i.e., related to the same subject, should be construed together as one statute and harmonized if possible”].) Because Proposition 26 does not displace pre-existing legislation as Proposition 218 did, and because Proposition 218 excludes power rates from its reach (Cal. Const., art. XIII D, § 3, subd. (b)), *Fresno* and *Roseville* apply law that does not control here.

Third and finally, even if *Fresno* and *Roseville* applied as a matter of law, they are also distinguishable on a critical fact: in both cases it was undisputed that the local government funded a general fund transfer from the challenged retail rates. (*Roseville, supra*, 97 Cal.App.4th at p. 638; *Fresno, supra*, 127 Cal.App.4th at p. 918.) As demonstrated above, that is not true here. Therefore these cases do not help Citizens.

IV. THAT THE PILOT IS TRANSFERRED TO THE GENERAL FUND DOES NOT MAKE IT A TAX

Citizens argue the “PILOT component of the increased electric rate is collected for ‘general revenue purposes’ — a fact which makes it a ‘tax.’” (Ans. at p. 21.) The argument proves too much.

Accounting treatment of revenues is not determinative. For example, Proposition 26 also exempts from its definition of “taxes” fees for the use of government property (Cal. Const., art. XIII C, § 1, subd. (e)(4)), and fines and penalties (*id.*, subd. (e)(5)). Such charges

routinely fund local governments' general funds: "Most revenue from fines and forfeitures may be expended for any legal municipal service." (Coleman, *The California Municipal Revenue Sources Handbook* (2014 ed.) p. 107.)⁹ Similarly, "[r]evenues from rental or use of city property and/or resources" are "[u]nrestricted unless indicated otherwise by agreement." (*Id.* at p. 109.)

Moreover, case law is plain that — even under the more demanding proportional-cost-of-service requirement of Proposition 218 — funds which flow to a general fund in reimbursement for services provided by that fund¹⁰ are not made taxes by that fact. For instance, *Fresno* and *Roseville* allowed utility fund transfers to general funds to reimburse proven costs of services to the utilities. (*Fresno, supra*, 127 Cal.App.4th at p. 926; *Roseville, supra*, 97 Cal.App.4th at pp. 650–651.) Thus, even the cases Citizens cite refute their overly broad claim.

Lemon Grove made this point plain:

[the city] may place in its general fund the revenues derived from a cost-based in-lieu franchise fee to pay

⁹ The cited pages of this resource are provided for the Court's convenience as Exhibit A to the accompanying Motion for Judicial Notice.

¹⁰ This may include equipment, access to rights of way, police and fire protection of utility assets, etc.

for the street, alley and right-of-way costs attributed to the water, sewer and refuse utilities.

(*Lemon Grove, supra*, 237 Cal.App.4th at pp. 376–77, quoting *Roseville, supra*, 97 Cal.App.4th at p. 650, abridgement by *Roseville court*.)

In other words, if fees are properly linked to costs, section 6(b) does not prevent those properly imposed fees from then being placed in a general fund.

(*Lemon Grove, supra*, 237 Cal.App.4th at p. 377.) Therefore transfer of the PILOT to the general fund does not alone prove Citizens' case.

V. THE PILOT IS A REASONABLE COST OF SERVICE AS A MATTER OF LAW

As detailed above, Proposition 26 — like Proposition 13 before it — requires only that costs recovered by service and regulatory fees be reasonable in toto and be “fair or reasonably” apportioned to a payor’s burdens on or benefits from the service or regulation. (Cal. Const., art. XIII C, § 1, subd. (e) [final unnumbered ¶].) The PILOT approximates the 1% tax on investor-owned utilities permitted by Proposition 13 and is therefore “reasonable” under this standard.

This was the thrust of Justice Duarte’s dissent below; although she also noted that the City’s rates are lower than those of PG&E, the rates of which are regulated by the Public Utilities Commission (PUC) to ensure reasonableness. (182 Cal. Rptr. 3d at 737–741.)

Citizens make a straw man of Justice Duarte's point. (Ans. at pp. 30–31.) The City agrees that Proposition 26's "fair or reasonable" cost allocation principle is not measured by the marketplace alone. That rates below investor-owned utility rates approved by the PUC are necessarily reasonable does not mean that rates higher than the investor-owned utility rates are necessarily unreasonable — especially those which are sufficiently cost-justified. Justice Duarte's point was that reasonableness under the Constitution can be demonstrated at least in part by comparison to PUC regulated rates, nothing more. That point remains correct and unremarkable. Common market conditions very likely reflect social attitudes as to what is "fair or reasonable."

Furthermore, reasonableness as understood under Proposition 13 does not forbid a utility to earn a return on its capital investment. *Hansen v. City of San Buenaventura* (1986) 42 Cal. 3d 1172, 1183 interpreted Proposition 13 to allow a municipal utility to include such a return in rates for its water service. That rule does not survive Proposition 218 for the utility services that measure governs, such as water and sewer services. (*Fresno, supra*, 127 Cal.App.4th at pp. 922–923 [cities may still recover costs for utility services through user fees, but the amount charged shall not exceed the proportional cost of service]; *Roseville, supra*, 97 Cal.App.4th at 647–648 [same].) However, as demonstrated above, unlike the more demanding Proposition 218, Proposition 26 maintains Proposition 13's more

permissive standards for the cost-justification and allocation of regulatory and service charges — essentially tracking the two-part analysis this court announced in *Sinclair Paint*. Citizens' contrary claim (Ans. at p. 32) merely assumes — but does not persuade — that Proposition 26 and Proposition 218 are consonant on this point despite their different language and apparent intent.

VI. THE PILOT IS PREEXISTING LEGISLATION UNAFFECTED BY PROP. 26

A. Citizens' Attacks on the Form of Legislation Enacting the PILOT Are Unpersuasive

The City has legislated the PILOT in its budget appropriations consistently for decades. Budgets and the appropriations they authorize are plainly legislative acts. (E.g., *Scott v. Common Council* (1996) 44 Cal.App.4th 684, 698 [mandating council fund city attorney positions required by city charter].) Citizens' Answer Brief does not discuss, much less distinguish, the arguments and authorities the Opening Brief cites for this point (at pp. 16–18). Furthermore, Citizens identify no duty before enactment of Proposition 26 to appropriate funding in any particular form. (See Ans. at p. 4.)

Nor do Citizens identify any duty of the Redding City Council to vote on each budget appropriation individually. (See Ans. at p. 7.) There is, of course, no such rule — as demonstrated by *Scott v. Common Council* and other cases involving appropriations. (E.g.

White v. Davis (2003) 30 Cal.4th 528, 538; see also, OB at pp. 16–27.)

In none of those cases was there evidence that the questioned appropriations were separately legislated. Thus Citizens ask this Court to create new law — that a city must legislate in a particular way — and apply it retroactively, without notice, to strike down a PILOT to which they object on policy grounds. The Court of Appeal erred to accept that invitation, an error this Court need not repeat.

B. The PILOT is a Lawful Cost of Service Predating Proposition 26

In arguing the PILOT does not predate Proposition 26, Citizens state: “the PILOT can at best (for the City) be characterized as a ‘cost’ item for the electric utility that it may recover through the rates as with all other costs of the enterprise.” (Ans. at p. 37.) Precisely so. Indeed, the trial court so concluded. (3 CT 737.) The same is true of myriad other legislative acts that increase the cost of power to customers of the Redding Electric Utility, such as the City’s pre-Proposition 26 policy to provide reduced rates to the poor and elderly; occupational safety and health standards; and other public goods charges.¹¹ All survive Propositions 26 and 218, just as their

¹¹ The term “public goods charge” is defined at length in *Southern California Edison Company v. Public Utilities Commission* (2014) 227

proponents argued. (1 CT 280 [Proposition 26 protects consumer regulations and fees]; 2 CT 349 [Proposition 218 proponents' rebuttal argument: "'Lifeline' rates for elderly and disabled for telephone, gas, and electric services are NOT affected".]) Proposition 218 expressly **excludes** electric rates from its sweep to protect these vulnerable populations. (Cal. Const., art. XIII D, § 3, subd. (b); 1 CT 216 [discussing City's Lifeline and CARES Programs].) Thus, except for water, sewer, and trash rates governed by Proposition 218, PILOTs were a lawful cost of service for electric utilities when Proposition 26 was adopted. As demonstrated above, Redding's PILOT was established legislatively in 1988 and last amended in 2005. It is a legislative act under controlling case law. Citizens admit that Proposition 26 did not take effect until November 2010. (Ans. at p. 2.) Nor did Redding readopt the PILOT after 2010.

Citizens argue that "re-enactment of the fee resolution" requires a fresh examination of fees under *Barratt American, Inc. v. City of Rancho Cucamonga* (2005) 37 Cal. 4th 685, 704 (*Barratt American*). What Citizens call the "re-enactment rule" from *Barratt American* has been applied in only one other reported case — in the context of statutes of limitations for land use disputes. (See *Arcadia*

Cal.App.4th 172 [PUC-imposed public goods charge did not exceed its statutory authority or constitute a tax under Prop. 26].)

Development Co. v. City of Morgan Hill (2008) 169 Cal.App. 4th 253, 261–262.) The trial court here refused to stretch *Barratt American* so far beyond its intended reach, stating that the case applied to its specific statutory context. (3 CT 739.) This Court should affirm that conclusion.

In *Barratt American*, a city council adopted a comprehensive schedule of fees on development, which this Court held triggered a fresh limitations period to challenge any fee on that schedule, including those unchanged from prior schedules. (*Barratt American*, *supra*, 37 Cal.4th at p. 703.) This Court based its holding on two grounds not present here. First, it relied upon a Government Code section requiring the city to engage in periodic accounting of revenue to reconcile estimates of development impact mitigation fees with actual mitigation costs. Second, this Court relied upon the city’s clear intention to adopt a “new comprehensive fee schedule.” (*Ibid*; see also *Arcadia*, 169 Cal.App.4th at pp. 263–265 [extension of “temporary” land use ordinance triggered fresh statute of limitations].) *Arcadia* applied *Barratt American* because the defendant city there clearly indicated that a land use ordinance — as to which any challenge was time-barred — was temporary, and its extension therefore constituted a “re-enactment.” (*Arcadia*, *supra*, 169 Cal.App.4th at p. 263.)

Thus, both *Barratt American* and *Arcadia* are exceptions to the usual rule that maintaining earlier legislative language in new

enactments continues rather than newly enacts that language. Both are justified by legislative intent contrary to the general rule. That canons of construction must bend to evidence of contrary legislative intent does not make them useless. “[E]very rule has its exceptions.” (*Brainard v. Cotner* (1976) 59 Cal.App.3d 790, 795; see also Scalia and Garner, *Reading Law: The Interpretation of Legal Texts* (2012) p. 59 [“No canon of construction is absolute. Each may be overcome by the strength of differing principles that point in other directions”].)

In stark contrast to *Barratt American* and *Arcadia*, the Redding City Council gave no indication in 2011 of intent that the PILOT be temporary or established anew. To the contrary, the Council made express its intent to continue the PILOT as it has existed for over 20 years:

[I]n light of the adoption of Proposition 26 on November 2, 2010, which precludes certain new fees, levies or charges but is not retroactive as to local governments, the City Council desires to maintain the existing PILOT utilizing the current accounting formula and methodology as last modified in 2005.

(2 CT 531.)

Accordingly, Resolution No. 2011-111 stated the Redding City Council did not legislate the PILOT anew and its intent to maintain the pre-Proposition 26 status quo is express and unmistakable. To

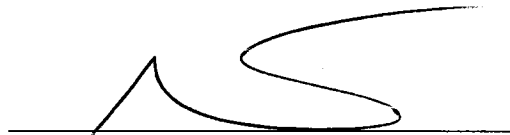
apply *Barratt American* to these facts is to rewrite the Redding City Council's language rather than to implement it. Thus, it is plain that the PILOT predates Proposition 26 and Citizens' terse argument to the contrary simply fails.

CONCLUSION

Citizens' brief fails because it assumes what it must prove and applies Proposition 218 authorities without consideration of the different language and purpose of Proposition 26, which makes those authorities inapt here. Citizens therefore fail to establish a prima facie case sufficient to put the City to its proof that the PILOT is not a tax. Even so, the City can and does demonstrate the PILOT is grandfathered by Proposition 26, is not funded by rates, and the challenged rates would comply with Proposition 26's requirement that charges for government services reflect a reasonable cost of service even if they funded the PILOT. Accordingly, the City respectfully requests that this Court affirm the trial court judgment.

DATED: July 20, 2015

**COLANTUONO, HIGHSMITH &
WHATLEY, PC**



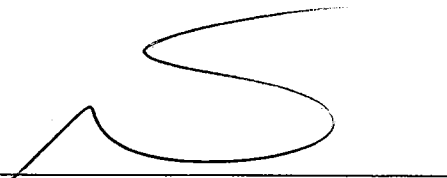
MICHAEL G. COLANTUONO
Attorneys for Respondent City of
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**CERTIFICATION OF COMPLIANCE WITH
CAL. R. CT. 8.520(B) & 8.204(C)(1)**

Pursuant to California Rules of Court, rules 8.520(b) and 8.204(c)(1), the foregoing Reply Brief by Defendants / Respondents City of Redding and City Council of Redding contains 6,067 words (including footnotes, but excluding the tables and this Certificate) and is within the 8,400 word limit set by California Rules of Court, rule 8.520(c). In preparing this certificate, I relied on the word count generated by Word version 14, included in Microsoft Office Professional Plus 2010.

DATED: July 20, 2015

COLANTUONO, HIGHSMITH &
WHATLEY, PC



MICHAEL G. COLANTUONO
Attorneys for Respondent City of
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ATTACHMENT NO. I

CITY OF REDDING BIENNIAL BUDGET
FISCAL YEARS ENDING JUNE 30, 2010 AND 2011

Public Benefits Program	Estimated	Adopted	Adopted
Description	FY 2008-09	FY 2009-10	FY 2010-11
Energy Efficiency			
Project Expenses (including labor)	\$ 1,570,000	\$ 1,500,000	\$ 1,500,000
Low Income Assistance			
Project Expenses (including labor)	\$ 480,000	\$ 600,000	\$ 600,000
Research, Development & Demonstration			
Project Expenses (including labor)	\$ 148,000	\$ 150,000	\$ 150,000
Renewable Resources			
Project Expenses (including labor)	\$ 86,000	\$ 50,000	\$ 50,000
TOTAL PBP Charges	\$ 2,284,000	\$ 2,300,000	\$ 2,300,000

Five-Year Financial Plan

The Electric Utility's financial plan for the current year and subsequent five years is summarized in the table below.

FIVE-YEAR FINANCIAL PLAN	Fiscal Years Ending June 30					
	2009	2010	2011	2012	2013	2014
Electric Utility Fund Beginning Balance	40.7	32.2	25.7	18.9	15.0	14.7
Rate Adjustments	7.84%	7.84%	9.10%	9.10%	9.10%	9.10%
Revenues (\$ Mil)						
Retail Electric Sales	86.3	93.4	102.1	110.1	121.6	134.6
Wholesale Electric Sales	26.6	22.7	18.7	12.2	11.7	10.5
Miscellaneous Income	6.1	5.4	5.7	5.9	6.0	6.2
Total	119.0	121.5	126.5	128.2	139.3	151.3
Operating Expenses (\$ Mil)						
Power Supply	85.0	81.4	82.3	80.4	79.8	81.1
O & M	26.0	27.5	28.5	29.4	30.3	31.2
Total	111.0	108.9	110.8	109.8	110.1	112.3
Net Operating Revenue	8.0	12.6	15.7	18.4	29.2	39.0
Total Net Debt Service	5.2	10.0	13.9	13.9	13.9	14.0
Revenue Remaining after Debt Service	2.8	2.6	1.8	4.5	15.3	25.0
Other Revenues & Expenses						
Other Revenues	2.1	1.6	1.2	0.9	0.7	0.7
Reimbursements from Bond Proceeds	6.0	2.0	2.0	4.0	0.0	0.0
General Fund Payback for Land Purchase	0.2	0.2	0.2	0.2	0.2	0.2
Revenue-Funded Capital Projects	-6.5	-5.8	-5.2	-6.0	-6.2	-6.3
In-Lieu Payment to City	-5.2	-6.1	-6.0	-6.1	-6.3	-6.5
Rolling Stock, Major Plant Maintenance	-7.9	-1.0	-0.8	-1.4	-4.0	-5.5
Total	-11.3	-9.1	-8.6	-8.4	-15.6	-17.4
Increase (Decrease) in Funds (\$ Mil)	-8.5	-6.5	-6.8	-3.9	-0.3	7.6
Electric Utility Fund Ending Balance (\$ Mil)	32.2	25.7	18.9	15.0	14.7	22.3
Reserves (as a % of O&M Requirement)	29.0%	23.7%	17.1%	13.6%	13.4%	20.0%
Debt Service Coverage Ratio	1.93	1.42	1.22	1.39	2.14	2.85

PROOF OF SERVICE

Citizens for Fair REU Rates v. City Of Redding
Third District Court of Appeal Case No. C071906
California Supreme Court Case No. S224779

I, Ashley A. Lloyd, declare:

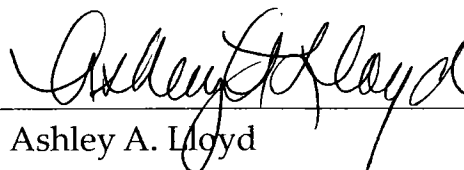
I am employed in the County of Nevada, State of California. I am over the age of 18 and not a party to the within action. My business address is 11364 Pleasant Valley Road, Penn Valley, California 95946. On JULY 20, 2015 I served the document(s) described as **REPLY BRIEF** on the interested parties in this action by placing a true copy thereof enclosed in a sealed envelope addressed as follows:

SEE ATTACHED LIST

BY MAIL: The envelope was mailed with postage thereon fully prepaid. I am readily familiar with the firm's practice of collection and processing correspondence for mailing. Under that practice it would be deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid at Penn Valley, California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if the postal cancellation date or postage meter date is more than one day after service of deposit for mailing in affidavit.

I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on JULY 20, 2015 at Penn Valley, California.



Ashley A. Lloyd

SERVICE LIST

Citizens for Fair REU Rates v. City of Redding
Third District Court of Appeal Case No. C071906
California Supreme Court Case No. S224779

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