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David P. Lanferman
Direct Dial: (650) 320-1507
E-mail: dlanferman@rutan.com

January 24, 2018



**VIA FEDEX and E-Mail (to counsel of record)**

The Honorable Chief Justice Tani G. Cantil-Sakauye,
and the Honorable Associate Justices
SUPREME COURT OF CALIFORNIA
350 McAllister Street
San Francisco, CA 94102

**Re:** ***California Building Industry Association v. State Water Resources Control Board***
**Case No. S226753**

**Petitioner's Supplemental Brief – New Authorities**
Set for Oral Argument: 10:00 a.m. February 6, 2018

To the Honorable Tani G. Cantil-Sakauye, Chief Justice of California, and to the Honorable Associate Justices of the Supreme Court of California:

## INTRODUCTION

Petitioner California Building Industry Association ("CBIA") respectfully submits this Supplemental Brief pursuant to Rule 8.520(d) of the California Rules of Court, to assure that relevant new authorities are called to the Court's attention prior to the oral argument now scheduled for February 6, 2018. The new authorities cited in this Supplemental Brief only became available recently, after the filing of the Petitioner's Reply Brief on December 30, 2015, and are relevant to issues raised in this case.

This Court's recent decisions in *City of San Buenaventura v. United Water Conservation District* (2017) 3 Cal.5th 1191, and *Jacks v. City of Santa Barbara* (2017) 3 Cal.5th 248, in particular are closely on point and (along with other new authorities cited below) clearly demonstrate the necessity for reversal of the appellate court's erroneous decision in this case.

## I. *JACKS v. CITY OF SANTA BARBARA* (June 29, 2017) 3 Cal.5th 248:

This Court's decision in *Jacks*, *supra*, traced the repeated expansion of restrictions on taxes and fees in California, as well as the case law distinguishing "fees" from "taxes." The Court concluded that the plaintiff, challenging a city surcharge on utility receipts, had adequately alleged

that the city had failed to show that its surcharge was reasonably related to the value of the utility franchise to be sustained as a "franchise fee" and could be challenged as an invalid "tax" requiring voter approval under Proposition 218.

The Court in *Jacks* cited *Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 875-876, and emphasized that *Sinclair* had held that, in order to be deemed valid as regulatory fees, as distinguished from invalid taxes, the purported fees must be shown to be reasonably related to the cost of the particular regulatory activity for which the fees are charged and fairly allocated "to those who generate" that cost. (3 Cal.5th at 261):

> With respect to costs, we explained in *Sinclair Paint, supra 15 Cal. 4th 866, 879* , that Proposition 13's goal of providing effective property tax relief is promoted rather than subverted by shifting costs to those who generate the costs. (See *San Diego Gas & Electric Co. v. San Diego County Air Pollution Control Dist. (1988) 203 Cal.App.3d 1132, 1148.*) However, if the charges exceed the reasonable cost of the activity on which they are based, the charges are levied for unrelated revenue purposes, and are therefore taxes. (*Sinclair Paint, at pp. 874, 881.*)
>
> In sum, restricting allowable fees to the reasonable cost or value of the activity with which the charges are associated serves Proposition 13's purpose of limiting taxes. .... If a state or local governmental agency were allowed to impose charges in excess of the special benefit received by the payor or the cost associated with the payor's activities, the imposition of fees would become a vehicle for generating revenue independent of the purpose of the fees. Therefore, to the extent charges exceed the rationale underlying the charges, they are taxes. (*Jacks, supra*, at p. 261, [emph. added].)

*Jacks* re-emphasized this key aspect of the Court's – pre-Proposition 26 -- jurisprudence on allowable "fees" (see, pp. 267-268): "*[R]egulatory fees* were allowed where the fees reflected bear a "reasonable relationship to the social or economic 'burdens' that [the payor's] operations generated." (*id. at p. 876*; see *Pennell v. City of San Jose (1986) 42 Cal.3d 365, 375*).

## II. *CITY OF SAN BUENAVENTURA v. UNITED WATER CONSERVATION DISTRICT* (December 4, 2017) 3 Cal.5th 1191 ["*UWCD*"]:

*UWCD* confirms that under Proposition 26 -- as well as under pre-Proposition 26 case law on regulatory fees – the agency imposing purported fees must show that its charges satisfy two [2] distinct requirements in order to be sustained as valid "regulatory fees" rather than "taxes." (*UCWD,* at p. 1210 [emph. added].)

> [T]he language of Proposition 26 is drawn in large part from pre-Proposition 26 case law distinguishing between taxes subject to the requirements of article XII A, on the one hand, and regulatory and other fees, on the other. (See *Jacks v. City of Santa Barbara (2017) 3 Cal.5th 248, 262...* (*Jacks*). We described this distinction in *Sinclair Paint, supra, 15 Cal. 4th 866 ....* Accordingly, we concluded, a fee does not become a tax subject to article XIII A unless it "'exceed[s] the reasonable cost of providing services ... for which the fee is charged.'" ... We further explained that "'the basis for determining the manner in which the costs are apportioned'" should demonstrate that "'charges allocated to a payor bear a fair or reasonable relationship to the payor's burdens on or benefits from the regulatory activity." (*Id. at p. 878*, quoting *San Diego Gas & Electric co. v. San Diego County Air Pollution Control Dist. (1988) 203 Cal.App.3d 1132, 1146.*)
>
> Proposition 26 codified both requirements. (See Cal. Const. art. XIII C, § 1, subd. (e) [to prove fee is not a tax, "local government bears the burden of proving. . . that 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," and "that the amount is no more than necessary to cover the reasonable costs of the governmental activity"].)[1]

*UWCD* involved a city's challenge to certain disputed "fees" [groundwater pumping charges]. The first part of this Court's decision affirmed that the charges were not "property-related service fees" subject to Cal. Const., article XIII D, but were instead subject to constitutional review under article XIII C, as amended by Proposition 26. In the second part of the decision, the Court applied those standards to the disputed fees and concluded that the appellate court's analysis had been incomplete and in error, because it considered only one [1] of the two [2] critical, constitutional, requirements that governments must satisfy in order to demonstrate that their fees or charges are not, in fact, "taxes."

The appellate court in *UWCD* – much like the appellate court in this case – had erroneously considered only whether the fees being charged "in the aggregate" were no more than necessary to cover the reasonable overall costs of the government's regulatory program. The Court explained (*UWCD*, at pp. 1211-1213) that the appellate court had failed to adequately consider the second, equally-vital, requirement – that the government must also separately demonstrate that it had used a reasonable method for fairly allocating the costs of the regulatory program among fee payers proportional to their burdens on or benefits from the program for which the fees were imposed.

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[1] Proposition 26 included a similar provision explicitly describing the burden on the State or state agencies – like SWRCB – to demonstrate that "a levy, charge, or other exaction is not a tax." (Cal. Const. art. XIII A, section 3(d).)

"Although the Court of Appeal declared both requirements satisfied, its analysis addressed only the first." (*Id.*, at 1211.) So, too, in this case.

Moreover, this Court's decision in *UWCD* (at p. 1213) explains that the Court's decision in *California Farm Bureau Federation v. State Water Resources Control Board* (2011) 51 Cal.4th 421, 436-437, 441, did not alter the analytical framework for regulatory fees established in *San Diego Gas & Electric v. San Diego County APCD* (1988) 203 Cal.App.3d 1132, which in turn the Court had "adopted" in *Sinclair Paint, supra.* Those cases held that, while the Water Board need not show that its fees are allocated "proportionally" to costs "on an individual basis," the Board must nevertheless meet its constitutional obligation to demonstrate that the Board's schedule of fees provides "a fair, reasonable, and substantially proportionate assessment of all costs related to the regulation of affected payors" (*UWCD* at p. 1213, quoting *Farm Bureau*, 51 Cal.4th at p. 442.) The decision in *UWCD* thus confirms that the appellate court in this case, as well as the Water Board, misread the *Farm Bureau* decision. Rather than applying the constitutionally-required scrutiny and the "burden" on the Board to justify the its admittedly skewed allocation of its costs, the appellate court erroneously "deferred" to the Water Board's post-hoc justifications for the disproportionate schedule of fees which admittedly "subsidized" other classes of fee payors at the expense of storm water permittees. Accordingly here, as in *UWCD*, p. 1213, "this [fair allocation of costs] is in essence the same question that the Court of Appeal in this case missed."

Even before Proposition 26 was adopted, or even if it were deemed not applicable to the quasi-legislative enactment of the fees in this case, the decision in *UWCD* again confirms that the burden should have been on the respondent Water Board to prove that its fees were fairly and reasonably allocated and were proportionate to the regulatory cost generated by the class of permittees on whom the fees were imposed. The appellate court here, however, erroneously assumed that it was petitioner's burden to show the contrary, i.e., to prove a negative, and glossed over the record evidence – including the Board's own Staff Reports -- that clearly called out the repeated overcharging of storm water permittees in order to "subsidize" the costs of the Board's seven other distinct regulatory programs for other classes of fee payors. *UWCD* (p. 1213-14) makes clear that this was error:

> But the [pre-Proposition 26] case law did not suggest that the constitutionality of a fee for a government service, for example, depended solely on whether the fees collected, in the aggregate, exceeded the aggregate amount necessary to provide the service to affected payors. (See *id. at p. 950* [distinguishing regulatory fees from "other types of user fees" that are "easily correlated to a specific, ascertainable cost"]. Nor did the cases suggest that the constitutional framework was otherwise indifferent to allegations that a government agency lacked any reasonable basis for charging a higher fee to some payors that others.

## III. OTHER RECENT AUTHORITIES ON FEES:

***San Diego County Water Auth. v. Metropolitan Water Dist.*** **(2017) 12 Cal.App.5th 1124:**

The First Appellate District, Div. 3, held that a "water stewardship fee" charged to encourage conservation was unlawful under both the Water Code and the common law, because the District failed to show that its fee was based on "costs incurred" or costs of service.

***Newhall County Water Dist. v. Castaic Lake Water Agency*** **(2016) 243 Cal.App.4th 1430:**

The Second Appellate District, Div. 8, held that the Water Agency could not, consistent with Cal. Const., art. XIII C, base its wholesale water charges to four retail purveyors on their use of groundwater, because the Agency did not provide groundwater to the purveyors. Fees could not be charged for services not provided to the fee payors. Proposition 26 required the Agency to allocate its costs by a method "that bears a reasonable relationship to the payor's burdens on or benefits from the Agency's activity." (243 Cal.App.4th at 1446.)

On behalf of the Petitioner, CBIA, we sincerely appreciate the Court's consideration of these additional authorities.

Very truly yours,

RUTAN & TUCKER, LLP

David P. Lanferman

DPL:mtr

cc: See attached Proof of Service and Service List

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## CERTIFICATE OF COMPLIANCE

The text of this Supplemental Brief consists of 1,806 words as counted by the Microsoft Word 2013 word-processing program used to generate this Brief.

Dated: January 24, 2018

RUTAN & TUCKER, LLP

By: _____

DAVID P. LANFERMAN
Attorneys for Petitioner
CALIFORNIA BUILDING INDUSTRY ASSOCIATION

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# PROOF OF SERVICE

## STATE OF CALIFORNIA, COUNTY OF SANTA CLARA

I am employed by the law office of Rutan & Tucker, LLP in the County of Santa Clara, State of California. I am over the age of 18 and not a party to the within action. My business address is Five Palo Alto Square, 3000 El Camino Real, Suite 200, Palo Alto, CA 94306-9814. My electronic notification address is mrespicio@rutan.com.

On January 24, 2018, I served on the interested parties in said action the within:

**PETITIONER SUPPLEMENTAL BRIEF**

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I declare under penalty of perjury that the foregoing is true and correct.

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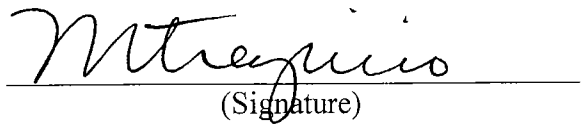
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**SERVICE LIST**

***California Building Industry Association v. State Water Resources Control Board, et al.***

**Supreme Court of California Case no. S226753**

| | |
|---|---|
| Tiffany Yee<br>Deputy Attorney General<br>California Department of Justice<br>1515 Clay Street, 20th Fl.<br>Oakland, CA 94612<br>tiffany.yee@doj.ca.gov | Attorneys for<br>Defendant/Respondent<br>**State Water Resources Control Board** |
| Robert E. Asperger<br>Office of the Attorney General<br>1300 I Street<br>Sacramento, CA 94244-2550<br>bob.asperger@dog.ca.gov | Attorneys for<br>Defendant/Respondent<br>**State Water Resources Control Board** |
| Theresa A. Dunham<br>SOMACH SIMMONS & DUNN<br>500 Capitol Mall, Suite 1000<br>Sacramento, CA 95814<br>tdunham@somachlaw.com | Attorneys for<br>(Amicus Curiae)<br>**The California Dairy Campaign**<br>**The Milk Producers Council**<br>**Western United Dairymen** |
| Hon. Curtis E.A. Karnow<br>San Francisco County Superior Court<br>400 McAllister St.<br>San Francisco, CA 94102 | Case No. CGC-11-516510 |
| Court of Appeal of the<br>State of California<br>First Appellate District, Division Two<br>350 McAllister St.<br>San Francisco, CA 94102 | Case No. A137680 |