A Layered Cake for the Bay Delta: On Financing a Bay Delta Restoration Program

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I am going to focus today on the constitutional limits on fees, charges and tax limitations – a sort of menu of options – and leaving aside the more obvious tried and true sources of state and federal funds including from general tax supported bond financing. I'm also setting aside the very important role of contractual arrangements. I'm also I am assuming that we have some sort of regional government that has been given the statutory authority to adopt fees, charges and taxes within the limits of the state constitution – in particular Proposition 218.

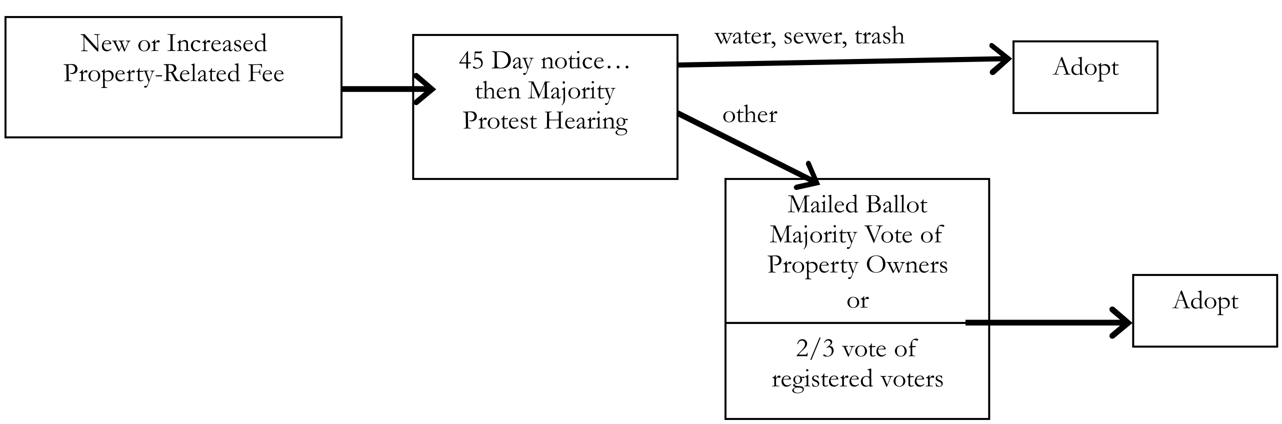
I'm going to take a sort of layered approach, looking at what may be legally possible given the stack of financing needs at hand here. These tools are currently generally available to cities and counties and some to some special districts if there is specific authorization in state law.

Layer #1: Water & Sewer Service Fees. Including water quality.

On the first tier let's examine the funding of essential services to property. Property related fees under Prop 218 include fees for ongoing, physical delivery of essential services to property. [*Bighorn-Desert View Water Agency v. Virjil* (2006) 39 Cal.4th 205, pp. 215-17.] In this layer we can stack costs of retail water services including distribution and treatment to properties within the jurisdiction of the agency. When imposed for water service, a property related fee requires a 45 day notice and a public hearing with a majority protest procedure – no election or property owner vote. A fee may not exceed the estimated reasonable cost of providing the service or facility for which it is charged.

Layer #2: Flood Control and Storm Drainage Fees.

Flood control and storm drainage are essential services to property and can be funded by property related fees, but, unlike water and sewer and trash services, require a vote procedure in addition to the majority protest procedure for adoption. So this is our second layer: essential services other than water: including flood control and storm drainage. Services in this layer require the same 45 day notice, hearing and majority protest procedure, PLUS approval by a mailed ballot majority vote of property owners (one vote per parcel) OR 2/3 vote of registered voters in the jurisdiction.



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A proposed state constitutional amendment in the Legislature, SCA12 (Torlakson 2007) would ask state voters to approve a change in Prop 218 permitting inclusion of "storm drainage" or "urban runoff" with sewer in XIIID§6(c) exceptions to vote requirement. A similar bill, ACA10 (Harman 2003) died and prospects for SCA12 are not good.

To the extent that these fees aren't set at full cost recovery – perhaps because of willingness to pay or taking into account mitigations or the Ramsey economic principles that the PPIC report discusses, the balance of funding could not come from other fee payers – it would have to come from taxes or intergovernmental sources.

Also, note that these fees would be imposed on public agencies (who could also participate in the approval process).

Layer #3: Benefit Assessments

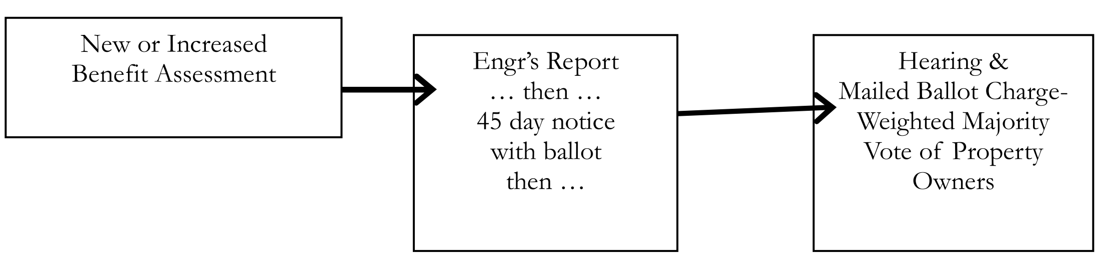
Another way to fund flood control and drainage – and possibly some regional open space and ecosystem restoration programs is through benefit assessments. While a property related fee is imposed to fund essential services to property, an assessment is imposed to fund special benefit to property.

Proposition 218 defines a benefit assessment imposed on property as "a levy or charge upon real property by an agency for a special benefit conferred upon the real property." [Cal. Const. Art. XIIID § 2(b)] Benefit assessments are charges for public improvements or services that provide a specific benefit to property within a predetermined area. Each parcel in the area is charged according to the benefit received from the improvement. A property can only be subject to a benefit assessment if it is a **specially benefited** by the improvements to be financed. Properties that are **generally benefited** may not be charged.

An analysis ("engineer's report") must be prepared to determine which properties will be specially benefited by the improvements. The analysis includes a description of the improvements to be financed, cost estimates of the improvements, and an assessment diagram mapping the district's boundaries, zones, and parcels. The report identifies the method of allocating the annual assessments to each parcel and the proposed maximum annual assessment per parcel to pay administration or registration costs. Different classes of properties pay different assessment amounts, calculated in proportion to the special benefit received.

A new assessment requires the **approval of a majority of the property owners** who return **mailed ballots** through an assessment ballot proceeding. Voting is **weighed in accordance with the amount of the assessment**. Once created, the assessment applies to all real property within the assessment district, including all new lots and homes built or created. Applicable law: Benefit Assessment Act of 1982 [Cal. Gov. Code §54710 et seq.]

Does regional open space provide special benefit to property owners sufficient to justify assessment financing? Question is currently before the California Supreme Court in *Silicon Valley Taxpayers Assn v. Santa Clara County Open Space Authority*, Case No. S136468. But see precedence in *Not About Water Committee v. Solano County Board of Sups*., 95 Cal.App.4th 982 (2002).



Last year, a proposed state constitutional amendment, ACA 30 (Laird 2006) would have asked state voters to approve a change in Prop 218 permitting assessments for maintenance, operation, repair, relocation, upgrade of flood control levies in existence prior to Nov 6, 1996 (Prop 218) to skip the majority vote property owner mailed ballot election and instead use a majority protest proceeding. ACA30 died on the floor of the Assembly.

Assessments must be calculated as if to impose on public properties – whether they can be compelled to pay or not and these agencies could participate in the approval process. The state and locals likely would have to pay but the federal government cannot be compelled to pay.

As in the case of property related fees, to the extent that these assessments aren't set at full cost recovery – perhaps because of willingness to pay or taking into account mitigations or the Ramsey economic principles that the PPIC report discusses, the balance of funding could not come from other fee payers – it would have to come from taxes or intergovernmental sources.

Layer #4: Development Impact Fees & Utility Connection Fees

The fourth layer applies to costs related to land use development in the region. Local governments may impose development impact fees imposed "as a condition of property development." Development fees are not property related fees under Prop 218. [Cal. Const., Art. XIIID, § 1(b).] Under the Mitigation Fee Act (Cal. Gov. Code §§ 66000-66025), development impact fees must be 1) roughly proportional to the impacts of the project and 2) imposed for purposes related to the impacts of the project. When imposing such a fee or dedication of property, local agencies typically prepare a fee study and tie the charges to their general plan and capital improvement program.

Development fee revenues must be deposited in separate dedicated capital facilities accounts. State law provides specific accounting procedures to ensure that the funds are used properly. Generally, development impact fees may be levied for the construction of capital improvements, but not for the maintenance or operation of public capital facilities or improvements.

Layer #5: Regulatory Fees.

The fifth layer is regulatory fees. Regulatory fees are not subject to Proposition 218. Regulatory fees are imposed to benefit and protect the community, in its entirety, from the deleterious and damaging effects of a particular business or personal enterprise. Regulatory fees are limited to covering the cost of the regulatory program and may not be used for unrelated revenue purposes. The costs funded by the fee may include all those incident to the issuance of the license, permit, investigation, inspection, administration, maintenance, of a system of supervision and enforcement. **The regulatory program may include "measures to mitigate the past, present and future adverse impacts of the fee payers operations."** It does not matter if a regulatory fee does not benefit those charged as long as the fee is commensurate with the burden imposed by the activity of those charged.

Given the authority in state law, regulatory fees may be adopted by majority vote of the governing body.

Layer #6: Taxes.

The sixth layer is taxes. Taxes are of course the obvious / fallback where fees and assessment can't apply – other than state or federal support – the source of which is, of course, essentially … taxes. But here I'm talking about a new source. By contrast to fees and assessments, taxes are simpler to craft and comprehend have simpler legal tests. Taxes have no legal nexus or benefit requirements. But of course they may be more difficult to pass. What sort of taxes might apply here?: perhaps a surtax on water utility bills or a non-ad-valorem parcel tax. Such a tax would be a special tax, requiring 2/3 voter approval if imposed by the local agency. A statewide tax could be imposed by 2/3 vote of each house of the legislature and approval of the Governor – or – a ballot measure approved by a majority of voters statewide.

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You have a complex and challenging task to save the Delta and you face a complex and challenging set of rules for raising the revenues to do so. The product will have to be a finance structure that contains a variety of revenues which will have to be carefully targeted to specific uses. The acceptability and success of this will require a carefully crafted spending plan, forthright consensus building with all the affected interests, transparency and measures to ensure accountability.

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