



March 27, 2019

Ms. Erika Li  
Department of Finance  
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Sacramento, CA 95814

Mr. Lloyd Pellman  
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*And Parties, Interested Parties, and Interested Persons (See Mailing List)*

**Re: Decision**

*Central Basin Municipal Water District Governance Reform, 17-TC-02*  
Water Code Sections 71265, 71266, and 71267;  
Statutes 2016, Chapter 401 (AB 1794)  
Central Basin Municipal Water District, Claimant

Dear Ms. Li and Mr. Pellman:

On March 22, 2019, the Commission on State Mandates adopted the Decision denying the Test Claim on the above-entitled matter.

Sincerely,

Heather Halsey  
Executive Director

COMMISSION ON STATE MANDATES  
STATE OF CALIFORNIA

<p><b>IN RE TEST CLAIM</b></p> <p>Water Code Sections 71265, 71266, and 71267; Statutes 2016, Chapter 401 (AB 1794)</p> <p>Filed on September 20, 2017</p> <p>Central Basin Municipal Water District, Claimant</p>	<p>Case No.: 17-TC-02</p> <p><i>Central Basin Municipal Water District Governance Reform</i></p> <p>DECISION PURSUANT TO GOVERNMENT CODE SECTION 17500 ET SEQ.; CALIFORNIA CODE OF REGULATIONS, TITLE 2, DIVISION 2, CHAPTER 2.5, ARTICLE 7.</p> <p><i>(Adopted March 22, 2019)</i></p> <p><i>(Served March 27, 2019)</i></p>
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**DECISION**

The Commission on State Mandates (Commission) heard and decided this Test Claim during a regularly scheduled hearing on March 22, 2019. Kevin Hunt appeared on behalf of the Central Basin Municipal Water District (claimant). Chris Hill appeared on behalf of the Department of Finance (Finance).

The law applicable to the Commission’s determination of a reimbursable state-mandated program is article XIII B, section 6 of the California Constitution, Government Code sections 17500 et seq., and related case law.

The Commission adopted the Proposed Decision to deny the Test Claim by a vote of 7-0, as follows:

<b>Member</b>	<b>Vote</b>
Lee Adams, County Supervisor	Yes
Keely Bosler, Director of the Department of Finance, Chairperson	Yes
Mark Hariri, Representative of the State Treasurer	Yes
Jeannie Lee, Representative of the Director of the Office of Planning and Research	Yes
Sarah Olsen, Public Member	Yes
Carmen Ramirez, City Council Member	Yes
Yvette Stowers, Representative of the State Controller, Vice Chairperson	Yes

## **Summary of the Findings**

This Test Claim alleges reimbursable state-mandated activities and costs arising from Statutes 2016, chapter 401, which added sections 71265, 71266, and 71267 to the Water Code, effective January 1, 2017. The test claim statute requires the Central Basin Municipal Water District (claimant) to expand its board of directors from its current five members (also known as directors) to eight members, until the election of November 8, 2022, after which the board would be composed of seven members. The claimant's general manager is also required to notify the district's water purveyors (purveyors) and provide a 60-day period during which the purveyors may nominate individuals for appointment to the board. In addition, the statute establishes minimum qualifications for appointed board members and limits benefits provided to the board members. The goal of the test claim statute is to protect consumers and "improve the District's effectiveness as a water wholesaler by enhancing the technical knowledge of the Board and by encouraging the participation of the water retailers that are responsible for water delivery directly to the customers."<sup>1</sup> The claimant seeks reimbursement for the costs of the appointment process for the additional board members, capital improvements to its facilities, and increased overhead costs due to the required expansion of the governing board.

Prior to the enactment of the test claim statute, the claimant had been under increased scrutiny as news reports highlighted its misuse of public funds, inappropriate contracting and employment practices, and several pending lawsuits. The Bureau of State Audits proceeded to review various aspects of the claimant's operations between July 2010 and June 2015, and in December 2015, issued an audit report recommending special legislation to modify the claimant's governance structure so as to ensure the claimant's accountability to its customers.

This Test Claim was timely filed, pursuant to Government Code section 17551, on September 20, 2017 which is within 12 months of the January 1, 2017 effective date of the test claim statute.

To be eligible for reimbursement under article XIII B, section 6, a local agency must be subject to the taxing and spending limitations of articles XIII A and XIII B of the California Constitution. In this case, reimbursement is not required under article XIII B, section 6, however, because there is no evidence that the claimant receives any proceeds of taxes subject to the appropriations limit of article XIII B and, therefore, is not eligible to claim mandate reimbursement under section 6. Article XIII B, section 9(c) specifically provides that special districts that existed in 1977-78 and did not share in ad valorem property taxes, or were created later and are funded entirely by "other than the proceeds of taxes", which precisely describes the claimant, are not subject to the appropriations limit.

Although the claimant is theoretically able to impose special taxes pursuant to Article XIII C, section 2(a) of the California Constitution and certain provisions in the Municipal Water Act of 1911, there is no evidence in the record that it has ever done so. In fact, all evidence in the record indicates that the claimant's revenues derive solely from its authority to collect fees and

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<sup>1</sup> Exhibit G, AB 1794 – Assembly Bill - Bill Analysis, August 19, 2016, [https://leginfo.ca.gov/faces/billAnalysisClient.xhtml?bill\\_id=201520160AB1794](https://leginfo.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201520160AB1794), accessed October 31, 2018, page 5.

assessments and grants.<sup>2</sup> Moreover, Proposition 218 does not convert claimant’s fees, assessments, or charges into “proceeds of taxes” subject to the appropriations limit of article XIII B, section 8, nor do expenditures of fees imposed pursuant to Proposition 218 trigger the reimbursement requirements of article XIII B, section 6 as appropriations of such fees are not “appropriations subject to limitation.” Therefore, there is no substantial evidence in the record to support a finding the claimant has eligibility for subvention of funds within the meaning of article XIII B, section 6.

Accordingly, based on this record, the Commission denies this Test Claim.

## COMMISSION FINDINGS

### I. Chronology

01/01/2017	Water Code sections 71265, 71266, and 71267, as added by Statutes 2016, chapter 401, become effective.
09/20/2017	The claimant filed the Test Claim. <sup>3</sup>
03/14/2018	Commission staff determined that the Test Claim was incomplete, because the claimant was not eligible for subvention, and returned it to the claimant.
03/27/2018	The claimant filed an appeal of the Executive Director’s decision to deny jurisdiction over the Test Claim. <sup>4</sup>
03/30/2018	The Executive Director issued a Notice of Test Claim Filing, which mooted the appeal of the executive director’s decision, requesting comments on the Test Claim and evidence that the claimant had ever collected taxes. <sup>5</sup>
04/27/2018	The Department of Finance (Finance) filed comments on the Test Claim. <sup>6</sup>
04/30/2018	The California Special Districts Association (CSDA) filed comments on the Test Claim. <sup>7</sup>

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<sup>2</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 19-20; Exhibit G, Central Basin Municipal Water District Adopted Operating Budget & Capital Improvement Projects/Grant Projects Budget, Fiscal Year 2016-17 (July 2016), [https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17\\_FINAL\\_0.pdf](https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17_FINAL_0.pdf), accessed December 14, 2018, pages 10-13.

<sup>3</sup> Exhibit A, Test Claim.

<sup>4</sup> Exhibit B, Appeal of Executive Director’s Decision.

<sup>5</sup> Exhibit C, Notice of Test Claim Filing.

<sup>6</sup> Exhibit D, Finance’s Comments on Test Claim.

<sup>7</sup> Exhibit E, CSDA’s Comments on Test Claim.

11/19/2018 Commission staff issued the Draft Proposed Decision.<sup>8</sup>  
01/22/2019 The claimant filed a request for postponement of hearing and change in representation which was approved for good cause.

## II. Background

This Test Claim alleges that Water Code sections 71265 through 71267, enacted by Statutes 2016, chapter 401 impose reimbursable state-mandated increased costs resulting from activities required of the claimant.

Prior to the enactment of the test claim statute, the claimant had been under increased scrutiny as news reports highlighted its misuse of public funds, inappropriate contracting and employment practices, and several pending lawsuits.<sup>9</sup> In October 2014, the County of Los Angeles Department of Public Works issued a report criticizing the district and exploring the steps necessary to dissolve it, though the report recommended an audit rather than dissolution.<sup>10</sup> At the request of the Joint Legislative Audit Committee, the Bureau of State Audits proceeded to review various aspects of the claimant's operations between July 2010 and June 2015, and in December 2015, issued an audit report recommending special legislation to:

. . . preserve the district as an independent entity but modify the district's governance structure. In doing so, the Legislature should consider a governance structure that ensures the district remain accountable to those it serves; for example, the district's board could be changed from one elected by the public at large to one appointed by the district's customers.<sup>11</sup>

Generally, the test claim statute revises the composition of the claimant's board of directors, establishes minimum qualifications for appointed board members, and limits benefits provided to the board members.

To provide some context for how the test claim statute fits into the state's effort to improve the operations of the claimant, a brief discussion of the claimant's history follows.

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<sup>8</sup> Exhibit F, Draft Proposed Decision.

<sup>9</sup> Exhibit G, AB 1794 – Assembly Bill - Bill Analysis, August 19, 2016, [https://leginfo.ca.gov/faces/billAnalysisClient.xhtml?bill\\_id=201520160AB1794](https://leginfo.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201520160AB1794), accessed October 31, 2018, page 8.

<sup>10</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 39-40.

<sup>11</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 42.

### **A. The Creation and History of the Claimant.**

The Municipal Water District Act of 1911 (1911 Act), Water Code sections 71000 et seq., authorized “the people of any county or counties, or of any portions thereof, whether such portions include unincorporated territory only or incorporated territory of any city or cities, or both such incorporated and unincorporated territory” to organize a municipal water district in order to “acquire, control, distribute, store, spread, sink, treat, purify, recycle, recapture, and salvage any water, including sewage and storm waters, for the beneficial use or uses of the district, its inhabitants, or the owners of rights to water in the district.”<sup>12</sup> The 1911 Act authorized municipal water districts to levy property taxes, and to impose special taxes pursuant to Article 3.5 of the Government Code.<sup>13</sup> The authority to levy general purpose property taxes however, has since been eliminated by an amendment to California Constitution - Article XIII C, section 2(a), made by Proposition 218, which restricted the authority of special districts to impose taxes only to special taxes. Municipal water districts may also impose standby “assessments or availability charges” on land within their jurisdiction, in an amount not to exceed \$10 per acre.<sup>14</sup>

In 1952, pursuant to the 1911 Act, the residents of southeastern Los Angeles County voted to establish the claimant, Central Basin Municipal Water District, to mitigate the overpumping of groundwater in the area.<sup>15</sup> In 1954, the claimant became a member agency of the Metropolitan Water District of Southern California (Metropolitan), an agency that was formed to bring imported water to the greater Los Angeles region.<sup>16</sup> The claimant “purchases imported water from Metropolitan for sale to retail water suppliers, including cities, other water districts, mutual water companies, investor-owned utilities, and private companies within the district’s boundaries. Those water retailers in turn provide water to residents and businesses within their respective service areas.”<sup>17</sup> In this manner, the claimant acts to secure water reliability for more

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<sup>12</sup> Water Code, sections 71060, 71610(a).

<sup>13</sup> Water Code, sections 72090, 72090.5.

<sup>14</sup> Water Code, sections 71630, 71631.

<sup>15</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 9.

<sup>16</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 15.

<sup>17</sup> Exhibit G, Senate Committee on Appropriations Analysis of AB 1794, August 1, 2016, [https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill\\_id=201520160AB1794](https://leginfo.legislature.ca.gov/faces/billAnalysisClient.xhtml?bill_id=201520160AB1794), accessed November 1, 2018, pages 7, 15.

than 1.6 million people in Los Angeles County, spanning a range of 27 cities, three unincorporated areas, 40 water retailers, and one water wholesaler.<sup>18</sup>

The audit report issued by the Bureau of State Audits (BSA) states that in fiscal year 2014-2015, the claimant's total revenues were from the following sources: sales of imported water (81% of total revenues); sales of recycled water (7% of total revenues); revenues from standby charges, which are parcel assessments imposed on landowners and used by the claimant to pay its debt service costs on water recycling facilities and the purchase of its headquarters building (6% of total revenues); grant funding (5% of total revenues); and other revenues from deliveries of treated water, investment income, and other miscellaneous sources (1% of total revenues).<sup>19</sup> The claimant's operating budget for fiscal year 2016-2017 identifies the same revenue sources.<sup>20</sup>

Prior to the enactment of the test claim statute, the claimant's 227 square-mile service area was governed by a board of five publicly elected directors, with voters in each of the five divisions of the service area electing one director to serve a four-year term.<sup>21</sup> No limits existed on the number of terms a board member could serve.<sup>22</sup>

**B. The Bureau of State Audits Found Numerous Failures by the District's Board of Directors to Provide for the Effective Management and Efficient Operation of the District.**

The BSA reviewed various aspects of the claimant's operations between July 2010 and June 2015, and in its December 2015 audit report, made the following key findings regarding the claimant and its board:

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<sup>18</sup> Exhibit G, Central Basin Municipal Water District Adopted Operating Budget & Capital Improvement Projects/Grant Projects Budget, Fiscal Year 2016-17 (July 2016), [https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17\\_FINAL\\_0.pdf](https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17_FINAL_0.pdf), accessed December 14, 2018, page 8.

<sup>19</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 19-20.

<sup>20</sup> Exhibit G, Central Basin Municipal Water District Adopted Operating Budget & Capital Improvement Projects/Grant Projects Budget, Fiscal Year 2016-17 (July 2016), [https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17\\_FINAL\\_0.pdf](https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17_FINAL_0.pdf), accessed December 14, 2018, pages 10-13, 43.

<sup>21</sup> Exhibit G, Central Basin Municipal Water District Adopted Operating Budget & Capital Improvement Projects/Grant Projects Budget, Fiscal Year 2016-17 (July 2016), [https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17\\_FINAL\\_0.pdf](https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17_FINAL_0.pdf), accessed December 14, 2018, page 8.

<sup>22</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 17.

- The board’s poor leadership, decision-making and oversight hindered the district’s ability to meet its responsibilities.<sup>23</sup>
  - Six different individuals had served as chief executive and five different individuals and one financial services firm have served as the finance director or an equivalent position.<sup>24</sup>
  - The board had an ineffective structure for investigating complaints regarding its members’ or district staff’s violations of laws and district codes related to ethics.<sup>25</sup>
  - Until recently, the board had not approved a strategic plan for several years and it did not require the district to create a long-term financial plan—the district had endured revenue shortfalls for years, had averaged a \$2.9 million operating deficit in three of the past five fiscal years and had suffered two credit rating downgrades.<sup>26</sup>
  - Because of the board’s inaction and poor decisions, the district was paying more for less general liability and employment practices liability insurance coverage.<sup>27</sup>
- The board violated state law by creating a legal trust fund without adequately disclosing it to the public. It also allowed its outside legal counsel to make

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<sup>23</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 21.

<sup>24</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 22-25.

<sup>25</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 25-28.

<sup>26</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 28-35.

<sup>27</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 35-38.



payments from this \$2.75 million fund without ensuring funds were used appropriately.<sup>28</sup>

- The district inappropriately avoided competitively bidding 11 of the 20 contracts we reviewed and it used amendments to extend and expand contracts—over a three-year period, it executed a total of 134 amendments to 65 contracts, increasing the total cost of the associated contracts from roughly \$14 million to nearly \$30 million.<sup>29</sup>
- The district did not follow best practices in managing its contracts—most of the contracts reviewed lacked critical elements of a scope of work and the district paid certain consultants before the work was performed.<sup>30</sup>
- The district spent funds on purposes unrelated to its mission, such as lavish board member installation ceremonies, that likely constituted prohibited gifts of public funds.<sup>31</sup>
- The district hired some unqualified staff, created a new position without proper approval, and incurred unnecessary expenses. The audit noted four hires in which the district did not comply with its policies, two of which resulted in legal disputes and another caused the district to incur unnecessary expenses.<sup>32</sup>
- Some of the benefits given to board members may have been too generous—a \$600 monthly automobile or transportation allowance, a \$200 monthly allowance

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<sup>28</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 45-49.

<sup>29</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 49-56.

<sup>30</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 56-60.

<sup>31</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 60-63.

<sup>32</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 65-70.

for personal communication devices, and up to \$2,000 per month for health benefits, even though they were not full-time employees.<sup>33</sup>

The audit report also noted that because the board is publicly elected, it is not directly accountable to the district's customers – the various entities to which the district sells imported and recycled water.<sup>34</sup> The report recommended that the Legislature:

[S]hould pass special legislation to preserve the district as an independent entity but modify the district's governance structure. In doing so, the Legislature should consider a governance structure that ensures the district remain accountable to those it serves; for example, the district's board could be changed from one elected by the public at large to one appointed by the district's customers.<sup>35</sup>

### **C. The Test Claim Statute**

The test claim statute, Statutes 2016, chapter 401 (AB 1794) became effective on January 1, 2017, adding sections 71265, 71266, and 71267 to Division 20, Part 3 of the California Water Code, changing the composition of the district's board, establishing minimum qualifications for appointed directors, and limiting benefits of directors.

Section 71265 defines "large water purveyor" as "a public water system that is one of the top five purveyors of water as measured by total purchases of water from the CBMWD for the three prior fiscal years", and "relevant technical expertise" as "at least 5 years of experience in a position materially responsible for performing services relating to the management, operations, engineering, construction, financing, contracting, regulating, or resource management of a public water system." It also defines a small water purveyor as a public water system (as defined in the Health and Safety Code), and clarifies that sections 71265-71267 apply only to the claimant, the Central Basin Municipal Water District.

Section 71266 changes the composition of the claimant's board of directors. The board currently has five directors, each one popularly elected from their respective divisions inside the district, pursuant to Water Code section 71250. Section 71266 requires that three additional directors be added to the board, with these directors appointed by the district's water purveyors, in accordance with section 71267. The new eight-member board would then be responsible, before the election of November 8, 2022, to divide the district into four divisions, in a manner so as to

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<sup>33</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 70-80.

<sup>34</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 40.

<sup>35</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), "Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities," <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, page 42.

equalize the population in each division, pursuant to Water Code section 71540 (in accordance with Section 22000 of Division 21 of the Elections Code.) The eight-member board would exist until the election of November 8, 2022, after which the board would consist of seven directors – the four elected ones, and the three appointed by the water purveyors. Section 72166 reads:

(a) Except as provided in subdivision (c) and notwithstanding any other provision of this division, the board of directors of the district shall be composed of seven directors as follows:

(1) Four directors, one director elected for each division established pursuant to subdivision (d) by the voters of the division. Each director shall be a resident of the division from which he or she is elected. An election pursuant to this paragraph shall be in accordance with the Uniform District Election Law (Part 4 (commencing with Section 10500) of Division 10 of the Elections Code).

(2) Three directors appointed by the water purveyors of the district in accordance with Section 71267.

(b) The district shall be subject to Section 84308 of the Government Code.

(c) Until the directors elected at the November 8, 2022, election take office, the board of directors shall be composed of eight directors as follows:

(1) Five directors in accordance with Section 71250.

(2) Three directors appointed by the water purveyors of the district pursuant to Section 71267.

(d) The board of directors shall divide the district into four divisions in a manner as to equalize, as nearly as practicable, the population in the respective divisions pursuant to Section 71540.

Section 71267 requires the claimant’s general manager to notify all its water purveyors that the district is seeking three new appointed directors for the board, and provide a 60-day period during which nominations for such appointment will be accepted. All individuals nominated must possess “relevant technical expertise” as defined in section 71265. The three appointed directors shall be selected every four years – one by all large water purveyors from the nominees therefrom, one by all cities that are water purveyors of the district, from the nominees of the cities, and one by all the district’s water purveyors, from any nominee. Section 71267 prohibits all three appointed directors from being employees or representatives of large water purveyors, cities, or small water purveyors. Each appointed director must live or work within the district, may not hold elected office, may not hold more than one-half percent ownership interest in any entity regulated by the Public Utilities Commission, and may not hold more than one consecutive term of office on the board. Appointed directors are eligible for compensation for up to ten meetings per month and certain benefits pursuant to the district’s administrative code, but are not eligible for communication or car allowances. Section 71267 reads:

(a) The general manager of the district shall notify each water purveyor of the district and provide a 60-day period during which the district will accept nominations for appointment of individuals to the board of directors.

- (b) Individuals nominated for appointment to the board of directors shall demonstrate eligibility and relevant technical expertise.
- (c)(1) The three directors appointed by the water purveyors shall be selected by the water purveyors of the district every four years as follows:
- (A) One director shall be selected by all large water purveyors from the nominees of large water purveyors. Each large water purveyor shall have one vote.
  - (B) One director shall be selected by all cities that are water purveyors of the district from the nominees of cities. Each city shall have one vote.
  - (C) One director shall be selected by all of the water purveyors of the district from any nominee. The vote of each purveyor shall be weighted to reflect the number of service connections of that water purveyor within the district. If the selection of a director under this subparagraph would result in a violation of paragraph (2), the first eligible candidate receiving the next highest number of votes shall be selected.
- (2) The appointment of directors pursuant to paragraph (1) shall not result in any of the following:
- (A) The appointment of three directors that are all employed by or representatives of entities that are all large water purveyors.
  - (B) The appointment of three directors that are all employed by or representatives of entities that are all cities.
  - (C) The appointment of three directors that are all employed by or representatives of entities that are all small water purveyors.
- (3) Each nominee for director who receives the highest number of votes cast for each office described in paragraph (1) is appointed as a director to the board of directors and shall take office in accordance with Section 71512. The general manager shall collect the votes and report the results to the water purveyors. Votes for an appointed director are public records.
- (d) Each appointed director shall live or work within the district.
- (e) In order to ensure continuity of knowledge, the directors appointed at the first purveyor selection shall classify themselves by lot so that two of them shall hold office until the selection of their successors at the first succeeding purveyor selection and one of them shall hold office until the selection of his or her successor at the second succeeding purveyor selection.
- (f)(1) The term of a director appointed pursuant to subparagraph (A) of paragraph (1) of subdivision (c) is terminated if the appointed director no longer is employed by or a representative of a large water purveyor.
- (2) The term of a director appointed pursuant to subparagraph (B) of paragraph (1) of subdivision (c) is terminated if the appointed director no longer is employed by or a representative of a city.

(3) The term of a director appointed pursuant to subparagraph (C) of paragraph (1) of subdivision (c) is terminated if the appointed director no longer is employed by or a representative of a water purveyor.

(g)(1) An appointed director shall not do any of the following:

(A) Hold an elected office.

(B) Hold more than 0.5 percent ownership in a company regulated by the Public Utilities Commission.

(C) Hold more than one consecutive term of office on the board.

(2) An appointed director shall be subject to all applicable conflict-of-interest and ethics provisions and shall recuse himself or herself from participating in a decision that could have a direct material benefit on the financial interests of the director.

(h) A vacancy in an office of appointed director shall be filled in accordance with the selection process described in subdivisions (a) to (c), inclusive.

(i)(1) An appointed director shall be eligible for all of the following:

(A) Reimbursement for travel and conference expenses pursuant to the Central Basin Municipal Water District Administrative Code.

(B) Compensation for up to 10 meetings per month at the per meeting rate provided by the Central Basin Municipal Water District Administrative Code.

(C) Health insurance benefits, if those benefits are not provided by the director's employer.

(2) An appointed director shall not be eligible to receive communication or car allowances. For purposes of this paragraph, "car allowances" does not include travel expenses incurred as described in paragraph (1).

(3) An appointed director may waive the reimbursement and compensation described in paragraph (1) and may be required to reimburse his or her employer for any compensation received.

### **III. Positions of the Parties and Interested Parties**

#### **A. Central Basin Municipal Water District**

The claimant alleges that the addition of Water Code sections 71265 through 71267 resulted in reimbursable increased costs mandated by the state. The claimant alleges new activities and increased actual costs totaling \$217,948 for fiscal year 2016-2017,<sup>36</sup> as follows:

- 1) Capital improvements to expand the district's board room dais from five to eight seats, and expand the parking lot.

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<sup>36</sup> Exhibit A, Test Claim, page 10. However, on page 8, the claimant states that the actual increased costs for fiscal year 2016-2017 totaled \$181,765.

- 2) Project management to oversee building improvements to the board room and parking lot.
- 3) Executive time and expenses in conducting the appointment process of three additional directors. The General Manager's time was spent on planning, directing, coordinating and overseeing the orientation, nomination and election of water purveyor representatives to the District's Board of Directors.
- 4) Obtaining legal services in the implementation and defense of AB 1794 in two lawsuits.
- 5) Meetings with the water purveyors responsible to appoint the three additional directors during a seven month period from September 2016 to March 2017. Costs were also incurred for meals provided during these meetings.
- 6) Staff time and expenses in conducting the appointment process of three additional directors. Staff members created a database of water purveyors, verified contact information and mailing addresses, drafted a memorandum and nomination forms, and mailed the information to the water purveyors. After the nomination process, staff prepared the ballots and mailed the information. Upon receiving the ballots, staff opened them and documented the results.
- 7) Additional staff time for the implementation of AB 1794. At the request of the Board of Directors, staff was asked to prepare a written report on the implementation process for the test claim statute.
- 8) Compensation, travel and administrative/office expenses (which included expenses for registration and dues, housing and accommodations, meals, photography services, office supplies, and miscellaneous expenses) for the three additional directors.<sup>37</sup>

The claimant also alleges estimated annual costs of \$18,488 for compensation, travel, and administrative expenses for the three new directors, and \$160,371 in legal fees and staff costs to write the election process in the claimant's Administrative Code and expenses incurred in two cases in litigation relating to the test claim statute.<sup>38</sup>

The claimant contends that it is eligible to claim reimbursement because it receives "proceeds of taxes" and is subject to the tax and spend limitations of articles XIII A and B. The claimant relies on documentation from the County of Los Angeles that shows the claimant will receive \$3.3 million for standby charges consistent with the County of Los Angeles' property tax remittance schedule.<sup>39</sup>

The claimant further asserts that nothing in article XIII B, section 6 requires that a claimant must receive property tax revenue to be eligible to claim reimbursement. "In the decades since [*County of Fresno v. State of California*] was issued, not only has there been a complete turnover

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<sup>37</sup> Exhibit A, Test Claim, pages 4-9.

<sup>38</sup> Exhibit A, Test Claim, pages 12-13.

<sup>39</sup> Exhibit A, Test Claim, pages 286, 290.

in the composition of the court but the landscape of local government financing has been changed by the passage of Proposition 218 in November of 1996 . . . .”<sup>40</sup>

In addition, the claimant states that the test claim statute did nothing to add a new service or to expand current services, and instead increased the overhead of the claimant by amending the governing board, as follows:

The District, as a water wholesale agency, purchases both potable and recycled water, and sells it to retail agencies. The implementation of AB 1794 did nothing to add a new service to the services of the District or to expand its current services; the legislation increased the overhead of the District by amending the governing board. It is the expansion of the board and the express procedure for selecting the three new members that is the mandated new program, applicable only to this one water district. As such, the District should be reimbursed by way of approval of its SB 90 test claim.<sup>41</sup>

In its Appeal of Executive Director’s Decision to reject the Test Claim filing finding claimant to be ineligible for subvention, the claimant asserts that article XIII B, section 6 of the California Constitution does not require that the district receive the proceeds of taxes in order to seek reimbursement for its expenses.<sup>42</sup> The claimant further asserts that section 2 of AB 1794 did not require that the district be a recipient of property taxes to seek reimbursement, and also that reimbursement appeared to be mandatory according to the language used therein.<sup>43</sup>

The claimant did not file comments on the Draft Proposed Decision.

### **B. Department of Finance**

Finance urges the Commission to deny this Test Claim.<sup>44</sup> Finance argues that the claimant is ineligible for reimbursement, as it is a local agency financed entirely by fees and other non-tax revenue, and is not subject to the taxing and spending limitations of article XIII B, section 6.<sup>45</sup> Finance further contends that even if the claimant were eligible to claim reimbursement, the activities it performed pursuant to the test claim statute do not qualify for reimbursement, as they do not constitute a new program or higher level of service.<sup>46</sup> Lastly, Finance notes that many of the activities for which the claimant seeks reimbursement were not required by the test claim statute, such as expenses for meals at the installation ceremony for the three new directors

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<sup>40</sup> Exhibit A, Test Claim, page 287.

<sup>41</sup> Exhibit A, Test Claim, page 288. Note that SB 90 refers to a long obsolete Revenue and Tax Code system for providing mandate reimbursement, which was quasi-legislative in nature. We presume that claimant actually intends to seek subvention pursuant to article XIII B, section 6 of the California Constitution and Government Code section 17500 et seq.

<sup>42</sup> Exhibit B, Appeal of Executive Director’s Decision, page 1.

<sup>43</sup> Exhibit B, Appeal of Executive Director’s Decision, page 2.

<sup>44</sup> Exhibit D, Finance’s Comments on the Test Claim.

<sup>45</sup> Exhibit D, Finance’s Comments on the Test Claim, pages 1-2.

<sup>46</sup> Exhibit D, Finance’s Comments on the Test Claim, page 2.

(\$411.53), photographic prints of the new directors (\$211.68), and lunch meetings with the district's water purveyors regarding the nomination of the three new directors (\$1,623.23).<sup>47</sup>

Finance did not file comments on the Draft Proposed Decision.

### **C. California Special Districts Association**

The CSDA, as an interested person under the Commission's regulations,<sup>48</sup> submitted comments on the Test Claim on April 30, 2018.<sup>49</sup> CSDA argues that "reasonable public policy warrants approval" of the Test Claim.<sup>50</sup> CSDA contends that past Commission interpretation of article XIII B, section 6 to protect only tax revenues and not the expenses that are recoverable from sources other than taxes, "fails to account for the ever-increasing series of constraints on the funding available to administer these services."<sup>51</sup> CSDA identifies the following constraints: Proposition 13, which drastically cut property tax revenue by nearly 50 percent, creating a funding deficit for local agencies; and Proposition 218, which imposed restrictions on special districts' authority to collect or increase fees and assessments. CSDA asserts that article XIII B, section 6 is designed "to protect local governments with constitutional funding limitations from shouldering the financial burden of the Legislature's preferred programs."<sup>52</sup> CSDA further asserts that the exclusion of local governments that do not receive property taxes or "proceeds of taxes" is contrary to the plain language of article XIII B, section 6, which provides subvention for all local governments. "The denial for subvention in the case of Central Basin Municipal Water District, and other enterprise special districts, results in the creation of a class of local governments and their citizens that must always bear the cost of state mandates through increased fees, even before clearing the uncertain Proposition 218 voter authorization hurdle for said fee increases, while others deemed as eligible under the current interpretation will see no fee increases."<sup>53</sup>

CSDA did not file comments on the Draft Proposed Decision.

### **IV. Discussion**

Article XIII B, section 6 of the California Constitution provides in relevant part the following:

Whenever the Legislature or any state agency mandates a new program or higher level of service on any local government, the state shall provide a subvention of funds to reimburse such local government for the costs of such programs or increased level of service...

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<sup>47</sup> Exhibit D, Finance's Comments on the Test Claim, pages 2-3.

<sup>48</sup> California Code of Regulations, title 2, section 1181.2(j).

<sup>49</sup> Exhibit E, CSDA's Comments on the Test Claim.

<sup>50</sup> Exhibit E, CSDA's Comments on the Test Claim, page 1.

<sup>51</sup> Exhibit E, CSDA's Comments on the Test Claim, page 1.

<sup>52</sup> Exhibit E, CSDA's Comments on the Test Claim, page 2.

<sup>53</sup> Exhibit E, CSDA's Comments on Test Claim, page 2.



The purpose of article XIII B, section 6 is to “preclude the state from shifting financial responsibility for carrying out governmental functions to local agencies, which are ‘ill equipped’ to assume increased financial responsibilities because of the taxing and spending limitations that articles XIII A and XIII B impose.”<sup>54</sup> Thus, the subvention requirement of section 6 is “directed to state-mandated increases in the services provided by [local government] ...”<sup>55</sup>

Reimbursement under article XIII B, section 6 is required when the following elements are met:

1. A state statute or executive order requires or “mandates” local agencies or school districts to perform an activity.<sup>56</sup>
2. The mandated activity constitutes a “program” that either:
  - a. Carries out the governmental function of providing a service to the public; or
  - b. Imposes unique requirements on local agencies or school districts and does not apply generally to all residents and entities in the state.<sup>57</sup>
3. The mandated activity is new when compared with the legal requirements in effect immediately before the enactment of the test claim statute or executive order and it increases the level of service provided to the public.<sup>58</sup>
4. The mandated activity results in the local agency or school district incurring increased costs, within the meaning of section 17514. Increased costs, however, are not reimbursable if an exception identified in Government Code section 17556 applies to the activity.<sup>59</sup>

The Commission is vested with the exclusive authority to adjudicate disputes over the existence of state-mandated programs within the meaning of article XIII B, section 6 of the California Constitution.<sup>60</sup> The determination whether a statute or executive order imposes a reimbursable state-mandated program is a question of law.<sup>61</sup> In making its decisions, the Commission must strictly construe article XIII B, section 6 of the California Constitution, and not apply it as an

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<sup>54</sup> *County of San Diego v. State of California* (1997) 15 Cal.4th 68, 81.

<sup>55</sup> *County of Los Angeles v. State of California* (1987) 43 Cal.3d 46, 56.

<sup>56</sup> *San Diego Unified School Dist. v. Commission on State Mandates* (2004) 33 Cal.4th 859, 874.

<sup>57</sup> *San Diego Unified School Dist. v. Commission on State Mandates* (2004) 33 Cal.4th 859, 874-875 (reaffirming the test set out in *County of Los Angeles v. State of California* (1987) 43 Cal.3d 46, 56).

<sup>58</sup> *San Diego Unified School Dist.* (2004) 33 Cal.4th 859, 874-875, 878; *Lucia Mar Unified School District v. Honig* (1988) 44 Cal.3d 830, 835.

<sup>59</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 487; *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1265, 1284; Government Code sections 17514 and 17556.

<sup>60</sup> *Kinlaw v. State of California* (1991) 54 Cal.3d 326, 333.

<sup>61</sup> *County of San Diego v. State of California* (1997) 15 Cal.4th 68, 109.

“equitable remedy to cure the perceived unfairness resulting from political decisions on funding priorities.”<sup>62</sup>

**A. This Test Claim was Timely Filed Pursuant to Government Code section 17551.**

Government Code section 17551(c) provides that a test claim must be filed “not later than 12 months after the effective date of the statute or executive order, or within 12 months of incurring increased costs as a result of a statute or executive order, whichever is later.” This Test Claim was filed on September 20, 2017, and is therefore timely, as it was filed within 12 months of January 1, 2017, the effective date of the test claim statute.

**B. The Claimant, a Special District, Is Not Eligible to Claim Reimbursement Under Article XIII B, Section 6, Because There Is No Evidence That the Claimant Receives Any Proceeds of Taxes Subject to the Appropriations Limit of Article XIII B.**

**1. To be eligible for reimbursement under section 6, a local agency must be subject to the taxing and spending limitations of articles XIII A and XIII B of the California Constitution.**

The courts have made it clear that the reimbursement requirement in article XIII B, section 6 of the California Constitution must be interpreted in context with articles XIII A and XIII B, which “work in tandem, together restricting California governments’ power both to levy and to spend taxes for public purposes.”<sup>63</sup>

In 1978, the voters adopted Proposition 13, which added article XIII A to the California Constitution. Article XIII A drastically reduced property tax revenue previously enjoyed by local governments by providing that “the maximum amount of any ad valorem tax on real property shall not exceed one percent (1%) of the full cash value of such property,” and that the one percent (1%) tax was to be collected by counties and “apportioned according to law to the districts within the counties...”<sup>64</sup> In addition to limiting the property tax, section 4 also restricts a local government’s ability to impose special taxes by requiring a two-thirds approval by voters.<sup>65</sup>

Article XIII B was adopted by the voters as Proposition 4 less than 18 months after the addition of article XIII A to the state Constitution, and was billed as “the next logical step to Proposition 13.”<sup>66</sup> While article XIII A is aimed at controlling ad valorem property taxes and the imposition of new special taxes, “the thrust of article XIII B is toward placing certain limitations on the

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<sup>62</sup> *County of Sonoma v. Commission on State Mandates* (2000) 84 Cal.App.4th 1265, 1280 [citing *City of San Jose v. State of California* (1996) 45 Cal.App.4th 1802, 1817].

<sup>63</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 486; *Dept. of Finance v. Commission on State Mandates* (2016) 1 Cal.5th 749, 763 [quoting *County of San Diego v. State of California* (1997) 15 Cal.4th 68, 81].

<sup>64</sup> California Constitution, article XIII A, section 1 (adopted June 6, 1978).

<sup>65</sup> California Constitution, article XIII A, section 1 (adopted June 6, 1978).

<sup>66</sup> *County of Placer v. Corin* (1980) 113 Cal.App.3d 443, 446.

growth of appropriations at both the state and local government level; in particular, Article XIII B places limits on the authorization to expend the ‘proceeds of taxes.’”<sup>67</sup>

Article XIII B established an “appropriations limit,” or spending limit for each “entity of local government” beginning in fiscal year 1980-1981.<sup>68</sup> Specifically, the appropriations limit provides as follows:

The total annual appropriations subject to limitation of the State and of each local government shall not exceed the appropriations limit of the entity of government for the prior year adjusted for the change in the cost of living and the change in population, except as otherwise provided in this article.<sup>69</sup>

No “appropriations subject to limitation” may be made in excess of the appropriations limit, and revenues received in excess of authorized appropriations must be returned to the taxpayers within the following two fiscal years.<sup>70</sup>

Article XIII B does not limit the ability to expend government funds collected from *all sources*; the appropriations limit is based on “appropriations subject to limitation,” which means, pursuant to article XIII B, section 8, “any authorization to expend during a fiscal year the *proceeds of taxes* levied by or for that entity.”<sup>71</sup> For local agencies, “proceeds of taxes” subject to the appropriations limit include all tax revenues; proceeds from regulatory charges and fees *to the extent such proceeds exceed the costs reasonably borne by government in providing the product or service*; the investment of tax revenue; and subventions received from the state (other than pursuant to section 6).<sup>72</sup>

However, no limitation is placed on the expenditure of those revenues that do not constitute “proceeds of taxes.”<sup>73</sup> For example, appropriations subject to limitation do not include “local agency loan funds or indebtedness funds, investment (or authorizations to invest) funds of the state, or of an entity of local government in accounts at banks or savings and loan associations or

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<sup>67</sup> *County of Placer v. Corin* (1980), 113 Cal.App.3d 443, 446.

<sup>68</sup> California Constitution, article XIII B, section 8(h) (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990).

<sup>69</sup> California Constitution, article XIII B, section 1 (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990).

<sup>70</sup> California Constitution, article XIII B, section 2 (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990).

<sup>71</sup> California Constitution, article XIII B, section 8 (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990) [emphasis added].

<sup>72</sup> California Constitution, article XIII B, section 8; *County of Placer v. Corin* (1980) 113 Cal.App.3d 443, 448.

<sup>73</sup> *County of Placer v. Corin* (1980) 113 Cal.App.3d 443, 447.

in liquid securities.”<sup>74</sup> With respect to special districts, article XIII B, section 9 provides a specific exclusion from the appropriations limit as follows:

“Appropriations subject to limitation’ for each entity of government *shall not include*: [¶...¶] (c) Appropriations of any special district which existed on January 1, 1978, and which did not as of the 1977-78 fiscal year levy an ad valorem tax on property in excess of 12 ½ cents per \$100 of assessed value; or the appropriations of any special district then existing or thereafter created by a vote of the people, which is totally funded by *other than the proceeds of taxes*.”<sup>75</sup>

Thus, a special district that existed in 1977-78 and did not share in ad valorem property taxes, or one that was created later and is funded entirely by “other than the proceeds of taxes,” is not subject to the appropriations limit.

In 1980, the year following the adoption of article XIII B, the Third District Court of Appeal, in *County of Placer v. Corin*, found that a local special assessment for the construction of public improvements was not included within the definition of “proceeds of taxes,” and thus the proceeds of that assessment were not required to be included within the budgeted “appropriations subject to limitation.”<sup>76</sup> The court explained that article XIII B’s limitation on the expenditure of “proceeds of taxes” does not limit the ability to expend government funds from *all sources*, but contemplates only the expenditure of “impositions which raise general tax revenues for the entity” as follows:

Under Article XIII B, with the exception of state subventions, the items that make up the scope of “proceeds of taxes” concern charges levied to raise general revenues for the local entity. “Proceeds of taxes,” in addition to “all tax revenues” includes “proceeds ...from ... ‘regulatory licenses, user charges, and user fees (only)’ to the extent that such proceeds exceed the costs reasonably borne by such entity in providing the regulation, product or service...” (§ 8, subd. (c)) ... Such “excess” regulatory or user fees are but taxes for the raising of general revenue for the entity. [Citations omitted.] Moreover, to the extent that

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<sup>74</sup> California Constitution, article XIII B, section 8(i) (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990).

<sup>75</sup> California Constitution, article XIII B, section 9(c) (adopted Nov. 6, 1979; amended by Proposition 111, June 5, 1990); see also, Government Code section 7901(e), a statute which implements and defines terms used in article XIII B, including appropriations subject to limitation, which similarly provides the following: ““Local agency” means a city, county, city and county, special district, authority or other political subdivision of the state, except a school district... The term “special district” *shall not include* any district which (1) existed on January 1, 1978 and did not possess the power to levy a property tax at that time or did not levy or have levied on its behalf, an ad valorem property tax rate on all taxable property in the district on the secured roll in excess of 12 ½ cents per \$100 of assessed value for the 1977-78 fiscal year, or (2) existed on January 1, 1978, or was thereafter created by a vote of the people, and is totally funded by revenues other than the proceeds of taxes as defined in subdivision (c) of Section 8 of Article XIII B of the California Constitution.”

<sup>76</sup> *County of Placer v. Corin* (1980) 113 Cal.App.3d 443.

an assessment results in revenue above the cost of the improvement or is of general public benefit, it is no longer a special assessment but a tax. [Citation omitted.] We conclude “proceeds of taxes” generally contemplates only those impositions which raise general tax revenues for the entity.

. . . Special assessments are not taxes, and are not levied for general revenue purposes. We are unable to find anything in Article XIII B to indicate that “proceeds of taxes” were intended to include special assessment proceeds.<sup>77</sup>

In 1991, the California Supreme Court reiterated that article XIII B was not intended to reach beyond taxation:

Article XIII B of the Constitution, however, *was not intended to reach beyond taxation*. That fact is *apparent from the language of the measure*. It is confirmed by its history. In his analysis, the Legislative Analyst declared that Proposition 4 “would not restrict the growth in appropriations financed from other [i.e., nontax] sources of revenue, including federal funds, bond funds, traffic fines, user fees based on reasonable costs, and income from gifts.” (Ballot Pamp., Proposed Stats. and Amends. to Cal. Const. with arguments to voters, Special Statewide Elec. (Nov. 6, 1979), analysis by Legislative Analyst, p. 16.)<sup>78</sup>

Section 6 was included in article XIII B to require that “[w]henver the Legislature or any state agency mandates a new program or higher level of service on any local government, the State shall provide a subvention of funds to reimburse that local government for the costs of the program or increased level of service...”<sup>79</sup> Article XIII B, section 6 was specifically designed to protect the *tax revenues* of local governments from state mandates that would require expenditure of tax revenues:

Section 6 was included in article XIII B in recognition that article XIII A of the Constitution severely restricted the taxing powers of local governments. (See *County of Los Angeles I, supra*, 43 Cal.3d at p. 61.) The provision was intended to preclude the state from shifting financial responsibility for carrying out governmental functions onto local entities that were ill equipped to handle the task. (*Ibid.*; see *Lucia Mar Unified School Dist. v. Honig* (1988) 44 Cal.3d 830, 836, fn. 6.) Specifically, it was designed to protect the tax revenues of local governments from state mandates that would require expenditure of such revenues. Thus, although its language broadly declares that the “state shall provide a subvention of funds to reimburse ... local government for the costs [of a state-mandated new] program or higher level of service,” read in its textual and historical context section 6 of article XIII B requires subvention only when the costs in question can be recovered *solely from tax revenues*.<sup>80</sup>

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<sup>77</sup> *County of Placer v. Corin* (1980) 113 Cal.App.3d 443, 451-452.

<sup>78</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 487.

<sup>79</sup> California Constitution article XIII B, section 6(a) (adopted Nov. 6, 1979).

<sup>80</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 487 [emphasis in original].

The California Supreme Court most recently recognized that the purpose of section 6 was to preclude “the state from shifting financial responsibility for carrying out governmental functions to local agencies, which are ‘ill equipped’ to assume increased financial responsibilities *because of the taxing and spending limitations that articles XIII A and XIII B impose.*”<sup>81</sup>

Thus, article XIII B, section 6 must be read in light of the tax and spend limitations imposed by articles XIII A and XIII B, and requires the state to provide reimbursement only when a local agency is mandated by the state to expend proceeds of taxes subject to the appropriations limit of article XIII B.

In this respect, not every local agency is subject to the restrictions of article XIII B, and therefore not every local agency is entitled to reimbursement under article XIII B. Redevelopment agencies, for example, have been identified by the courts as being exempt from the restrictions of article XIII B. In *Bell Community Redevelopment Agency v. Woolsey*, the Second District Court of Appeal concluded that a redevelopment agency’s power to issue bonds, and to repay those bonds with its tax increment, was not subject to the spending limit of article XIII B. The court reasoned that to construe tax increment payments as appropriations subject to limitation “would be directly contrary to the mandate of section 7,” which provides that “[n]othing in this Article shall be construed to impair the ability of the state or of any local government to meet its obligations with respect to existing or future bonded indebtedness.”<sup>82</sup> In addition, the court found that article XVI, section 16, addressing the funding of redevelopment agencies, was inconsistent with the limitations of article XIII B:

Article XVI, section 16, provides that tax increment revenues “may be irrevocably pledged” to the payment of tax allocation bonds. If bonds must annually compete for payment within an annual appropriations limit, and their payment depend upon complying with the such limit [*sic*], it is clear that tax allocation proceeds cannot be irrevocably pledged to the payment of the bonds. Annual bond payments would be contingent upon factors extraneous to the pledge. That is, bond payments would be revocable every year of their life to the extent that they conflicted with an annual appropriation limit. The untoward effect would be that bonds would become unsaleable because a purchaser could not depend upon the agency having a sure source of payment for such bonds.<sup>83</sup>

The court therefore concluded that redevelopment agencies could not reasonably be subject to article XIII B, and therefore upheld Health and Safety Code section 33678, and ordered that the writ issue to compel Woolsey to publish the notice.<sup>84</sup>

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<sup>81</sup> *Dept. of Finance v. Commission on State Mandates* (2016) 1 Cal.5th 749, 763 [quoting *County of San Diego v. State of California* (1997) 15 Cal.4th 68, 81].

<sup>82</sup> *Bell Community Redevelopment Agency v. Woolsey* (1985) 169 Cal.App.3d 24, 31.

<sup>83</sup> *Bell Community Redevelopment Agency v. Woolsey* (1985) 169 Cal.App.3d 24, 31.

<sup>84</sup> *Bell Community Redevelopment Agency v. Woolsey* (1985) 169 Cal.App.3d 24, 33-34.

Similarly, in *Redevelopment Agency of San Marcos v. Commission on State Mandates*,<sup>85</sup> the Fourth District Court of Appeal held that redevelopment agencies were not eligible to claim reimbursement because Health and Safety Code section 33678 exempted tax increment financing, their primary source of revenue, from the limitations of article XIII B:

Because of the nature of the financing they receive, tax increment financing, redevelopment agencies are not subject to this type of appropriations limitations or spending caps; they do not expend any “proceeds of taxes.” Nor do they raise, through tax increment financing, “general revenues for the local entity.” The purpose for which state subvention of funds was created, to protect local agencies from having the state transfer its cost of government from itself to the local level, is therefore not brought into play when redevelopment agencies are required to allocate their tax increment financing in a particular manner...

For all these reasons, we conclude the same policies which support exempting tax increment revenues from article XIII B appropriations limits also support denying reimbursement under section 6... [The] costs of depositing tax increment revenues in the Housing Fund are attributable not directly to tax revenues, but to the benefit received by the Agency from the tax increment financing scheme, which is one step removed from other local agencies’ collection of tax revenues.<sup>86</sup>

In 2000, the Third District Court of Appeal, in *City of El Monte v. Commission on State Mandates*, affirmed the reasoning of the *Redevelopment Agency of San Marcos* decision, holding that a redevelopment agency cannot accept the benefits of an exemption from article XIII B’s spending limit while asserting an entitlement to reimbursement under article XIII B, section 6.<sup>87</sup>

Thus, the courts, with these cases, have drawn a straight line from an agency’s primary sources of funding being exempt from the appropriations limit, to that same agency being ineligible to claim mandate reimbursement under section 6.

Accordingly, to be eligible for reimbursement under article XIII B, section 6, a local agency must be subject to the taxing and spending limitations of articles XIII A and XIII B of the California Constitution and be capable of being forced to expend “appropriations subject to limitation.”

**2. The limitations imposed by Proposition 218 on the local authority to increase assessments, fees, or charges, does not make those revenues “proceeds of taxes” subject to the appropriations limit of article XIII B, or trigger the reimbursement requirements of article XIII B, section 6.**

Despite the analysis above, the claimant and CSDA urge the Commission to consider the restrictions placed on special districts’ authority to impose assessments, fees, or charges by Proposition 218 to be part of the “increasingly limited revenue sources” that subvention under

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<sup>85</sup> *Redevelopment Agency of San Marcos v. Commission on State Mandates* (1997) 55 Cal.App.4th 976).

<sup>86</sup> *Redevelopment Agency of San Marcos v. Commission on State Mandates* (1997) 55 Cal.App.4th 976, 986-987.

<sup>87</sup> *City of El Monte v. Commission on State Mandates* (2000) 83 Cal.App.4th 266, 281-282.

section 6 was intended to protect. The claimant and CSDA would have the Commission broadly interpret and extend the subvention requirement and treat fee authority subject to Proposition 218 as proceeds of taxes, to advance the goal of precluding the state from shifting financial responsibility for carrying out governmental functions onto local entities that are ill equipped to handle the task.

Proposition 218 added article XIII D to the California Constitution in 1996 to place additional limits on the authority of local government to impose or increase assessments, fees, and charges, by imposing voter approval and public notice requirements before raising property-related fees or assessments, and allows for majority written protests to invalidate such fees.

However, nothing in the express language of Proposition 218 expands the scope of article XIII B or draws any direct comparison to the relationship between articles XIII A or XIII B. Had the voters that adopted Proposition 218 intended to link article XIII D with article XIII B, or to broaden the scope of article XIII B to include fees and assessments limited by article XIII D, or to provide relief within article XIII B, section 6 because of the limitations imposed on fees and assessments, they could have expressly provided for such a link. Instead, the voters on Proposition 218 were warned of “[s]hort-term local revenue losses of more than \$100 million annually” and “[l]ong-term local government revenue losses of potentially hundreds of millions of dollars annually.”<sup>88</sup> The proponents of Proposition 218 also noted:

There are now over 5,000 local districts which can impose fees and assessments without the consent of local voters. Special districts have increased assessments by over 2400% over 15 years. Likewise, cities have increased utility taxes 415% and raised benefit assessments 976%, a tenfold increase.<sup>89</sup>

There is no indication in the ballot materials that state mandate reimbursement was intended to supplement or replace the potential revenue lost by imposing public hearing requirements and allowing for written protests to invalidate new or increased water service fees imposed by special districts.

The voters that adopted article XIII B, on the other hand, clearly intended to impose an appropriations limit *only* on tax revenues; they expressed no intention to limit the expenditure of fee or assessment revenues, or to require mandate reimbursement for expenditures that are not “proceeds of taxes.” Indeed, the voters that adopted article XIII B were told explicitly that “[t]he initiative would not restrict the growth in appropriations financed from *other sources of*

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<sup>88</sup> Exhibit G, Ballot Pamphlet, General Election (Nov. 5, 1996) Summary of Legislative Analyst’s Estimate of Net State and Local Government Fiscal Impact of Proposition 218, [https://repository.uchastings.edu/ca\\_ballot\\_props/1138/](https://repository.uchastings.edu/ca_ballot_props/1138/), accessed November 19, 2018 page 72.

<sup>89</sup> Exhibit G, Ballot Pamphlet, General Election (Nov. 5, 1996) Summary of Legislative Analyst’s Estimate of Net State and Local Government Fiscal Impact of Proposition 218, [https://repository.uchastings.edu/ca\\_ballot\\_props/1138/](https://repository.uchastings.edu/ca_ballot_props/1138/), accessed November 19, 2018, page 76.



revenue...”<sup>90</sup> In addition, voters were told that article XIII B “WILL NOT prevent state and local governments from providing essential services...[¶...¶ and] WILL NOT favor one group of taxpayers over another.”<sup>91</sup> Therefore, the voters who adopted article XIII B clearly envisioned user fees and local special assessments would continue to provide funding for essential services, including those only benefiting a small group of property owners or residents.<sup>92</sup> A subsequent decision by the voters to provide a check on the use of fees and assessments does not of itself alter the original intent of article XIII B.

It may be, as the claimant and CSDA assert, that raising additional fee or assessment revenue is made more difficult, both procedurally and substantively, by Proposition 218. But nothing in Proposition 218, either expressly or by implication, broadens the scope and applicability of article XIII B, including section 6, to compel mandate reimbursement for the revenue sources that some speculate Proposition 218 could curtail. To now revise the scope of article XIII B (without Constitutional amendment or legislation) to require mandate reimbursement for expenditures from revenues other than proceeds of taxes would violate the intent of the voters that adopted article XIII B, and the plain language of article XIII B, section 9(c) and Government Code 7901(e), which specifically excludes from the definition of “special district” for purposes of the appropriations limit in article XIII B, a district which is totally funded by revenues other than proceeds of taxes.

Article XIII B is clear. A local agency that is funding by assessment, fees, and charges, or any combination of revenues “other than the proceeds of taxes” is an agency that is not subject to the appropriations limit, and therefore not entitled to subvention. This interpretation is supported by decades of mandates precedent and is consistent with the purpose of article XIII B. As discussed above, “Section 6 was included in article XIII B in recognition that article XIII A...severely restricted the taxing powers of local governments.”<sup>93</sup> Article XIII B “was not intended to reach beyond taxation...” and “would not restrict the growth in appropriations financed from other [i.e., nontax] sources of revenue...”<sup>94</sup>

Accordingly, the limitations imposed by Proposition 218 on the local authority to increase assessments, fees, or charges, does not make those revenues “proceeds of taxes” subject to the

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<sup>90</sup> Exhibit G, Ballot Pamphlet, General Election (Nov. 7, 1979), Proposition 4, [https://repository.uchastings.edu/cgi/viewcontent.cgi?article=1863&context=ca\\_ballot\\_props](https://repository.uchastings.edu/cgi/viewcontent.cgi?article=1863&context=ca_ballot_props), accessed November 19, 2018 [emphasis added].

<sup>91</sup> Exhibit G, Ballot Pamphlet, General Election (Nov. 7, 1979), Proposition 4, [https://repository.uchastings.edu/cgi/viewcontent.cgi?article=1863&context=ca\\_ballot\\_props](https://repository.uchastings.edu/cgi/viewcontent.cgi?article=1863&context=ca_ballot_props), accessed November 19, 2018.

<sup>92</sup> See, *County of Placer v. Corin* (1980) 113 Cal.App.3d 443, 453; *County of Fresno v. Malmstrom* (1979) 94 Cal.App.3d 974, 981 [Broad reading of appropriations limit creates “Hobson's choice of spending general tax funds either for expenditures to benefit the public at large or for projects to benefit certain individual property owners by funding improvements such as the construction of streets, sidewalks, gutters and sewers.”].

<sup>93</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 487.

<sup>94</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 487.

appropriations limit of article XIII B, or trigger the reimbursement requirements of article XIII B, section 6.

**3. There is no evidence in the record that the claimant receives any proceeds of taxes subject to the appropriations limit of article XIII B and, therefore, claimant is not eligible to claim reimbursement under section 6.**

As indicated above, article XIII B, section 6 requires the state to provide reimbursement only when a local agency is mandated by the state to expend funds subject to the appropriations limit of article XIII B. And, article XIII B, section 9(c) specifically provides that special districts that existed in 1977-78 and did not share in ad valorem property taxes, or were created later and are funded entirely by “other than the proceeds of taxes,” are not subject to the appropriations limit.

The claimant, having been established in 1952, clearly existed on January 1, 1978. Although the claimant is theoretically able to impose special taxes pursuant to Article XIII C, section 2(a) of the California Constitution and certain provisions in the 1911 Act,<sup>95</sup> there is no evidence in the record that it has ever done so. In fact, all evidence in the record indicates that the claimant’s revenues derive solely from its fee authority and grant funds. The 2015 audit report issued by the Bureau of State Audits and the claimant’s operating budget for fiscal year 2016-2017 identify revenues from sales of imported water, sales of recycled water, revenues from standby charges, grant funding, and other revenues from deliveries of treated water, investment income, and other miscellaneous sources.<sup>96</sup> These documents do not identify the receipt of any “proceeds of taxes” as defined in article XIII B, section 8. Although the standby charges are collected with a landowner’s property taxes,<sup>97</sup> the standby charges are not converted to property taxes. Standby charges are, by definition, assessments.<sup>98</sup>

Moreover, special districts are required by law to annually submit financial transaction reports to the State Controller’s Office, which “shall include the appropriations limits and the total annual

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<sup>95</sup> Water Code, sections 72090 and 72090.5.

<sup>96</sup> Exhibit G, Bureau of State Audits (BSA) Audit Report 2015-102 (Dec. 2015), “Central Basin Municipal Water District – Its Board of Directors Has Failed to Provide the Leadership Necessary for It to Effectively Fulfill its Responsibilities,” <https://www.auditor.ca.gov/pdfs/reports/2015-102.pdf>, accessed October 8, 2018, pages 19-20; Exhibit G, Central Basin Municipal Water District Adopted Operating Budget & Capital Improvement Projects/Grant Projects Budget, Fiscal Year 2016-17 (July 2016), [https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17\\_FINAL\\_0.pdf](https://forms.centralbasin.org/sites/default/files/finance/Adopted%20Budget%20for%20FY%202016-17_FINAL_0.pdf), accessed December 14, 2018, pages 10-13, 43.

<sup>97</sup> Exhibit A, Test Claim, page 290.

<sup>98</sup> Water Code section 71630, which states the following: “The district by ordinance may, pursuant to the notice, protest, and hearing procedures in Section 53753 of the Government Code, fix on or before the third Monday of August, in each fiscal year, a water standby *assessment* or availability charge in the district, in any portion thereof, or in any improvement district, to which water is made available by the district, whether the water is actually used or not.”

appropriations subject to limitation.”<sup>99</sup> The Controller’s Last Special District Annual Report showed that claimant had no appropriations subject to limitation.<sup>100</sup> The Controller’s open data site no longer provides information regarding special districts’ reporting on appropriations limits. However, the claimant has neither asserted nor provided any evidence to show that it has reported to the Controller’s Office any appropriations subject to limitation.

Accordingly, the Commission finds that there is no evidence in the record that the claimant receives any proceeds of taxes subject to the appropriations limit of article XIII B and, therefore, is not eligible to claim mandate reimbursement under section 6.

With this conclusion, the Commission does not reach the issues of whether the test claim statute mandates a new program or higher level of service, or results in increased costs mandated by the state within the meaning of Government Code sections 17514 and 17556.

## **V. Conclusion**

Based on the foregoing analysis, the Commission denies this Test Claim.

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<sup>99</sup> Government Code section 12463.

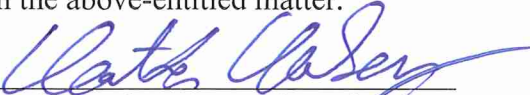
<sup>100</sup> Exhibit G, Excerpt from the State Controller’s Special District Annual Report 2011-2012, [https://www.sco.ca.gov/Files-ARD-Local/LocRep/1112\\_special\\_districts.pdf](https://www.sco.ca.gov/Files-ARD-Local/LocRep/1112_special_districts.pdf), accessed November 19, 2018.



RE: **Decision**

*Central Basin Municipal Water District Governance Reform, 17-TC-02*  
Water Code Sections 71265, 71266, and 71267;  
Statutes 2016, Chapter 401 (AB 1794)  
Central Basin Municipal Water District, Claimant

On March 22, 2019, the foregoing Decision of the Commission on State Mandates was adopted on the above-entitled matter.

  
\_\_\_\_\_  
Heather Halsey, Executive Director

Dated: March 27, 2019

**DECLARATION OF SERVICE BY EMAIL**

I, the undersigned, declare as follows:

I am a resident of the County of Sacramento and I am over the age of 18 years, and not a party to the within action. My place of employment is 980 Ninth Street, Suite 300, Sacramento, California 95814.

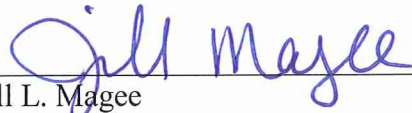
On March 27, 2019, I served the:

- **Decision adopted March 22, 2019**

*Central Basin Municipal Water District Governance Reform, 17-TC-02*  
Water Code Sections 71265, 71266, and 71267;  
Statutes 2016, Chapter 401 (AB 1794)  
Central Basin Municipal Water District, Claimant

By making it available on the Commission's website and providing notice of how to locate it to the email addresses provided on the attached mailing list.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct, and that this declaration was executed on March 27, 2019 at Sacramento, California.



Jill L. Magee  
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**Claim Number:** 17-TC-02

**Matter:** Central Basin Municipal Water District Governance Reform

**Claimant:** Central Basin Municipal Water District

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