

Date of Hearing: June 9, 2021

ASSEMBLY COMMITTEE ON LOCAL GOVERNMENT

Cecilia Aguiar-Curry, Chair

SB 323 (Caballero) – As Amended March 17, 2021

SENATE VOTE: 34-1

SUBJECT: Local government: water or sewer service: legal actions.

SUMMARY: Establishes a 120 day statute of limitations on judicial challenges to water and sewer rates. Specifically, **this bill:**

- 1) Specifies that any judicial action or proceeding to attack, review, set aside, void, or annul an ordinance, resolution, or motion adopting a fee or charge for water or sewer service, or modifying or amending an existing fee or charge for water or sewer service, shall be commenced within 120 days of the effective date of the ordinance, resolution, or motion.
- 2) Provides that any action pursuant to this bill by a local agency or interested person shall be brought in accordance with validating proceedings established in Chapter 9 (commencing with section 860) of Title 10 of Part 2 of the Code of Civil Procedure, except that the time limits of 1) above shall apply.
- 3) Specifies that this bill does not apply to any fee or charge for water or sewer service for which another statute establishes a specific time and procedure for bringing judicial action or proceeding to attack, review, set aside, void or annul a fee or charge of that type.
- 4) Provides that this bill shall only apply to a fee or charge for water or sewer service that has been adopted, modified, or amended after January 1, 2022.

EXISTING LAW:

- 1) Establishes procedural and substantive requirements for the imposition of property-related fees and charges, including requirements for notice, a public hearing, the calculation of the fee or charge and the use of revenue; subjects such fees and charges to voter approval, but specifically excludes water and sewer fees and charges from this requirement.
- 2) Provides a procedure for seeking a tax refund, which must be commenced not later than one year after the accrual of the cause of action.
- 3) Establishes procedures governing validation actions that provide a 60 day period in which a public entity or any interested person may sue to determine the validity of a governmental act.

FISCAL EFFECT: None.

COMMENTS:

- 1) **Bill Summary and Author's Statement.** This bill establishes a 120 day statute of limitations for any lawsuit that challenges an ordinance, resolution, or motion adopting a fee

or charge for water or sewer service, starting from the effective date of the fee or charge. This 120 day period only applies to fees or charges adopted by local agencies after January 1, 2022. SB 323 requires challenges to be brought under the existing statutes for validation suits, except that the 120 day time period in SB 323 applies to any action initiated under the bill. The Association of California Water Agencies (ACWA) is the sponsor of this bill.

According to the author, “The COVID-19 pandemic has put strain on many essential businesses, including ones that the public depends on for basic needs. Public utilities, such as water and sewer service providers have experienced a reduction in the number of consumers who are able to pay for their services. Yet because of Governor Newsom’s Executive Order prohibiting water shutoffs, water agencies have continued to service every customer regardless of their ability to pay, which has made water districts’ revenue and financial planning more unpredictable. In light of this new financial strain, another long standing issue comes into focus that needs to be addressed- the lack of a time line for rate challenges. Other public utility agencies, such as electricity providers, have a 120-day statute of limitations for challenges to rates or charges that have been in effect for decades. This is because lawsuits arising years after rates were adopted create unstable funding for the agency. This statute of limitations has not been extended to water agencies yet, and the inability to plan for such claims effects funding necessary to supply safe drinking water, upgrade and improve aging infrastructure, and operate effectively. That is why I have introduced SB 323, which would require an interested party to bring an action within 120 days after the local water agency adopts the new rate. By allowing customers to bring challenges within a reasonable – but limited – period of time, this proposal would balance the interests of ratepayers with those of public water and sewer agencies and end the current piecemeal character of existing law.”

- 2) **Financing Water Infrastructure.** Local governments in California provide most water related services in the state which include water service, sewer service, flood control, and storm water management. A Public Policy Institute of California (PPIC) report, *Paying for Water in California*, outlines four sources of funding currently used for water in California: a) Fees, which include water and waste water bills, property assessments or fees, developer or connection fees, and permitting fees; b) Taxes, which include both general and special taxes, including parcel taxes; c) Fines and penalties, which include excessive pumping on groundwater or directly to customers in violation of rationing restrictions during drought emergencies; and, d) Bonds, which include general obligation and revenue bonds. Local agencies frequently point to the series of constitutional reforms, Proposition 13 (1978), Proposition 218 (1996), and Proposition 26 (2010), that have made it increasingly more difficult to generate the necessary revenue to fund the costs of providing water and other essential services.
- 3) **Proposition 218.** Proposition 218 distinguishes among taxes, assessments, and fees for property-related revenues, and requires certain actions before such revenues may be collected. Counties and other local agencies with police powers may impose any one of these options on property owners, after completing the Proposition 218 process. Special districts created by statute, however, must have specific authority for each of these revenue sources.

The Constitution defines a fee (or charge) as any levy other than an ad valorem tax, special tax, or assessment that is imposed by a local government on a parcel or on a person as an incident of property ownership, including a user fee for a property-related service. The fee

imposed on any parcel or person cannot exceed the proportional cost of the service that is attributable to the parcel. Prior to imposing or increasing a property-related fee, the local government is required to identify the parcels, mail a written notice to all the property owners subject to the fee detailing the amount of the fee, the reason for the fee, and the date, time, and location of a public hearing on the proposed fee. No sooner than 45 days after mailing the notice to property owners, the agency must conduct a public hearing on the proposed fee. If a majority of owners of the identified parcels provide written protests against the fee, it cannot be imposed or increased by the agency.

Additionally, Article XIII D, Section 6, subdivision (c) of the California Constitution, provides election requirements, stating, “Except for fees or charges for sewer, water, and refuse collection services, no property-related fee or charge shall be imposed or increased unless and until that fee or charge is submitted and approved by a majority vote of the property owners of the property subject to the fee or charge or, at the option of the agency, by a two-thirds vote of the electorate residing in the affected area.” The election for the fee is required to be conducted no less than 45 days following the public hearing.

The definition of "water" under the Proposition 218 Omnibus Implementation Act is significant because the election requirements are on fees for services other than water, sewer, and trash services. Determining the services that fall within the definitions of "water" and "sewer" services has been the subject of litigation. An appellate court decision in *HJTA v. City of Salinas* (2002) found that a city's charges on developed parcels to fund storm water management were property-related fees, and were not covered by the exemption for sewer or water services. A subsequent appellate court decision in *Griffith v. Pajaro Valley Water Management Agency* (2013) relied on the definition of "water" in the Proposition 218 Omnibus Implementation Act narrowly construing an earlier decision in *HJTA v. City of Salinas*, which did not apply the Act's definitions to a storm water charge dispute. The Griffith decision found that a groundwater augmentation charge is a fee for "water service.”

- 1) **Proposition 218 Procedures.** The Legislature enacted the Proposition 218 Omnibus Implementation Act to translate many of Proposition 218's requirements into statutory definitions and procedures [SB 919 (Rainey), Chapter 38, Statutes of 1997].

Before a local government can charge a new property-related fee, or increase an existing one, Proposition 218 requires local officials to:

- a) Identify the parcels to be charged.
- b) Calculate the fee for each parcel.
- c) Notify the parcels' owners in writing about the fee, the reason for imposing or increasing it, the basis for calculating the fee, and the date of a public hearing on the proposed fee.
- d) Hold a public hearing to consider and count protests at least 45 days after mailing the notice.
- e) Abandon the fees if a majority of the parcels' owners protest.

- 4) **Requirements on Fees.** New or increased property-related fees cannot exceed the proportional cost of service to each parcel. They also generally require a majority-vote of the affected property owners, two-thirds registered voter approval, or weighted ballot approval by the affected property owners.

However, Proposition 218, and subsequently clarified by Proposition 26, exempts various local fees from some or all of its requirements, including the following:

- a) Exclude fees for electric and gas service from the definition of property-related fees. These fees are still subject to Proposition 26's requirements that fees be limited to the reasonable cost of providing the service and bear a fair or reasonable relationship to the benefits received.
 - b) Establish development fees, such as the fees that water and sewer agencies charge when a new user connects to their systems (known as "connection fees" and "capacity charges") as a separate category of fee not subject to Proposition 218's requirements on fees or taxes.
 - c) Exempt property-related fees for sewer, water, or refuse collection services from Proposition 218's voter approval requirements. However, all the other procedural requirements in Proposition 218 and the Omnibus Implementation Act apply to fees for water, sewer, and refuse collection services.
- 5) **Validation Procedures.** The Legislature has long recognized that certain actions taken by state and local agencies would suffer or be rendered ineffective if subject to protracted adjudication. Code of Civil Procedure sections 860 through 870.5, known as the "validation statutes," establish an expedited procedure for challenging certain government acts. Under these procedures, once a public agency takes an action, a complaint must be filed within 60 days. Notice of the claim must be served on all interested parties by publication, and a challenge under these provisions receives calendar preference. If no challenge is brought within 60 days, the action is deemed valid and becomes immune from attack. Courts have concluded the 60 day period is reasonable given the important purposes of the validation statutes, which include "the need to limit the extent to which delay due to litigation may impair a public agency's ability to operate financially." (*California Commerce Casino, Inc. v. Schwarzenegger* (2007). "We recognize the statutory period of limitation for commencing a validation action is extremely short but it is not unique in its brevity. 'What constitutes a reasonable time is a question ordinarily left to the Legislature, whose decision a court will not overrule except where palpable error has been committed.'")

The validation statutes were originally devised in order to speedily validate local government bonds and provide certainty to prospective bondholders, but these statutes have since been applied in a variety of contexts, including certain types of fees and charges, in order to support the fiscal stability of public agencies. While validation proceedings are typically reserved for financial matters, they also extend to actions under the Cortese-Knox-Hertzberg Local Government Reorganization Act related to changes in the organization, reorganization and sphere of influence of local governments. Similarly, state law requires anyone who wishes to challenge an ordinance, resolution, or motion setting rates for electric service, establishing water or sewer connection fees and capacity charges, or setting the cost of

zoning and building permits to file the lawsuit within 120 days of the effective date of the measure imposing the fees or charges.

- 6) **Court Determinations.** Statutes of limitations provide important certainty for local governments that rely on rates to fund their operations, build infrastructure, and provide reliable service to the public. The existing statutes of limitations for water and sewer connection fees and electric rates have been tested in court and found to be sufficient. Specifically, the Supreme Court found in *Utility Cost Management v. Indian Wells Valley Water District (2001)* that because of the extensive fiscal analysis and public review requirements on connection fees and capacity charges, "...a diligent plaintiff should be able to discover, within the statutory period, whether a cause of action exists. Tolling might of course be appropriate during the period a public utility is processing a request for information prior to disclosure, but we think a broader application of the discovery rule would be directly at odds with the legislative intent to give public utilities certainty with respect to the enforceability of their fee ordinances and resolutions. (§ 54999, *subd. (a)*; *San Marcos II, supra*, 190 Cal.App.3d at pp. 1085-1086, 235 Cal.Rptr. 827.) If a plaintiff could challenge fee legislation any number of years after the legislation was adopted simply by taking advantage of the discovery rule and without any allegation that critical information was withheld, then public utilities would be left in a continuous state of fiscal uncertainty, which ultimately would only increase costs for consumers."

Additionally, the Fourth District Court of Appeals subsequently determined that the 120 day statute of limitations established for electric rates applied even in a situation where a violation of Proposition 218 and 26 was alleged, and noted, "Permitting this case to move forward and seek refunds of electric service charges more than two years after Riverside's decision would place the municipal utility in a state of fiscal uncertainty, which is what the statute of limitations was intended to prevent." (*Webb v. City of Riverside (2018)* SB 323 proposes to apply these same time limits and procedures to water and sewer rates for the same purpose of enhancing fiscal certainty and stability. SB 323 also incorporates some additional safeguards, including to ensure that the bill only applies to rates adopted in the future.

- 7) **Recent Water Rate Litigation.** Unlike connection fees and capacity charges, the ongoing rates that customers pay on their water and sewer bills are not subject to a 120-day statute of limitations. Instead, a one-year statute of limitations applies, with an important caveat: under the doctrine of "continual accrual," courts treat each water or sewer bill that is improperly charged as a new violation. As a result, the clock on the statute of limitations restarts with each new payment of an allegedly incorrect amount, meaning that rates can be challenged years after the ordinance imposing them was adopted.

On February 19, 2020, a class action lawsuit was filed against 81 water agencies throughout the state alleging that their practice of charging ratepayers for the costs associated with supplying water for fire protection violates Proposition 218. Specifically, the complaint argued that this practice results in water agencies charging ratepayers for more than the cost of service to their parcel and imposes costs on property owners for general governmental services that are available to the public at large in substantially the same manner as they are available to property owners. Water agencies see it differently: they argue that the benefit of fire hydrants accrues to the property owners because hydrants are positioned and used to fight structure fires, not wildland or other types of fires that are unrelated to a specific

property. This case influenced legislative action to clarify that fire hydrants and the water provided by them are a component of water service [SB 1386 (Moorlach), Chapter 240, Statutes of 2020]. Some ordinances under the class action lawsuit date back to 2016, meaning that the plaintiffs didn't initiate litigation until four years after the rates were adopted in some cases.

- 8) **Policy Considerations.** The Committee may wish to consider the following:
- a) **Consistently, Inconsistent.** Proposition 218 established constitutional protections for ratepayers to ensure that they are not overcharged for the services that they receive. SB 323 limits the time period that taxpayers have to challenge the validity and constitutionality of rates to 120 days. Opponents of the measure argue that this time period is too short to adequately ensure that ratepayers' constitutional rights are protected. If the 120 day deadline passes with no lawsuit, potentially unlawful water and sewer rates could be protected for years. However, connection fees, capacity charges, electric rates, and permit fees are subject to the same 120 day deadline. The Committee may wish to consider if ratepayers should have a longer time to dispute water and sewer rates that they believe violate the Constitution or if they should be treated similarly to other types of rates and fees.
 - b) **Notification.** Some stakeholders believe that more notice of the statute of limitations should be provided. However, the Proposition 218 Omnibus Implementation Act, which the Legislature adopted to add specificity and clarity to the constitutional requirements in Proposition 218, imposes many transparency requirements on local agencies, down to details such as the font size that must be used to denote that the mailed notices contain a ballot to be used in the protest process. Connection fees, capacity charges, electric rates, and permit fees do not need to meet these same requirements. The Committee may wish to consider if additional notification to property owners is warranted or if Proposition 218's notification requirements are sufficient.
- 9) **Prior Legislation.** SB 231 (Hertzberg), Chapter 536, Statutes of 2017, defined "sewer" for the purposes of the Proposition 218 Omnibus Implementation Act.

SB 1298 (Hertzberg) of 2016 would have specified the definition of "sewer" for the purposes of the Proposition 218 Omnibus Implementation Act. SB 1298 died on the inactive file.

AB 1362 (Gordon) of 2015, would have provided a definition for "stormwater" to mean "any system of public improvements, or service intended to provide for the quality, conservation, control, or conveyance of waters that land on or drain across the natural or man-made landscape" in the Proposition 218 Omnibus Implementation Act. AB 1362 would have only become operative if a constitutional amendment was approved by the voters. The introduced version of AB 1362 was subsequently amended into a different issue area to address mosquito and vector control districts.

AB 2403 (Rendon), Chapter 78, Statutes of 2014, expanded the definition of "water" in the Proposition 218 of 1996 Omnibus Implementation Act to mean any system of public improvements intended to provide for the production, storage, supply, treatment, or distribution of water from any source.

SB 919 (Rainey), Chapter 38, Statutes of 1997, enacted the Proposition 218 Omnibus Implementation Act to prescribe specific procedures and parameters for local jurisdictions in complying with Article XIII C and Article XIII D of the California Constitution.

- 10) **Arguments in Support.** The Association of California Water Agencies argues that, “Reliable long-term financial planning is paramount to providing essential government services, like water and sewer. Public water and sewer utility budgets are largely funded by revenue collected through service rates. These rates provide the funding necessary to improve aging infrastructure, build delivery systems, maintain reliable operations, and more. While public water and sewer service providers require financial stability to meet these demands, existing law allows lawsuits that seek refunds or seek to invalidate existing rate structures *years* after rates have been adopted and collected.

“The California State Legislature has recognized the need to minimize fiscal uncertainty for public agencies providing essential government services by creating statutes of limitation for legal challenges to certain fees and charges, such as municipal electric rates and connection and capacity fees assessed by water and sewer agencies. However, existing law offers a piecemeal statutory landscape where statutes of limitation are afforded to fees and charges that fund some essential government services but not others. SB 323 would close this gap in existing law by allowing customers to bring legal challenges to water and sewer rates within a reasonable—but limited—period of time. By following precedent established in existing law, this bill strikes a balance between the interests of ratepayers and the need for public agencies to maintain reliable sources of revenue.

“The impacts of COVID-19 have exacerbated many challenges facing local agencies. The necessary disruptions to in-person work and Governor Newsom’s executive order prohibiting water shutoffs have made water districts’ revenue and financial planning more unpredictable. Now is the time to make existing legal protections consistent and increase predictability for utility providers throughout our State.”

- 11) **Arguments in Opposition.** The Howard Jarvis Taxpayers Association is opposed unless amended and argues that, “While we oppose all attempts to enlarge the universe of government actions that are subject to the validation statutes, there are also fundamental problems with SB 323.

“Measuring the deadline for challenging a water or sewer fee from the date of its ‘motion’ could create confusion if multiple motions on multiple dates preceded the actual enactment of the rate increase. A ‘motion’ does not enact anything. If a motion is seconded, voted on, and is passed, it can enact an ordinance or resolution. But a motion, standing alone, is just a proposal. HJTA recommends deletion of the word ‘motion.’

“Potential confusion is also created by specifying a 120-day statute of limitations in paragraph (a), but then stating without reservation in paragraph (b) that ‘Any action under this section by a local agency or interested person shall be brought pursuant to [the validation statutes],’ which require challenges to be filed within 60 days. HJTA recommends adding, ‘except that the time limits of subdivision (a) shall apply.’

“Ultimately, HJTA feels validation statutes are an unfair denial of due process. Even the California Supreme Court has acknowledged that they can have the effect of cementing into

law illegal government acts that are then forever insulated from judicial review. That is why, at a minimum, an agency should be required to bring its own validation action within 120 days in order to obtain the protection and give taxpayer's proper notice should action be necessary.”

12) **Double-Referral.** This bill is double-referred to the Judiciary Committee.

REGISTERED SUPPORT / OPPOSITION:

Support

Association of California Water Agencies [SPONSOR]

Alameda County Water District

Amador Water Agency

Aromas Water District

Bella Vista Water District

Bodega Bay Public Utility District

Brooktrails Township Community Services District

California Association of Sanitation Agencies

California Municipal Utilities Association

California Special Districts Association

Calleguas Municipal Water District

City of Brea

City of Fountain Valley

City of Garden Grove

City of Hayward

City of La Habra

City of Oceanside

City of Riverside

City of Roseville

City of Sacramento

City of Santa Ana

City of Santa Monica

City of Santa Rosa

City of Shasta Lake

City of Torrance

City of Tracy

City of Watsonville

Coachella Valley Water District

Corcoran Irrigation District

Cucamonga Valley Water District

Desert Water Agency

Diablo Water District

East Orange County Water District

East Valley Water District

Eastern Municipal Water District

El Dorado Irrigation District

El Toro Water District

Elk Grove Water District

Elsinore Valley Municipal Water District
Foothill Municipal Water District
Fresno Metropolitan Flood Control District
Helix Water District
Hidden Valley Lake Community Services District
Humboldt Bay Municipal Water District
Humboldt Community Services District
Indian Wells Valley Water District
Inland Empire Utilities Agency
Irvine Ranch Water District
Kings River Conservation District
Lakeside Water District
Las Virgenes Municipal Water District
League of California Cities
Los Angeles County Sanitation Districts
Los Angeles County Water District
Mariana Ranchos County Water District
Marin Water
McKinleyville Community Services District
Mercy Springs Water District
Mid-Peninsula Water District
Modesto Irrigation District
Monte Vista Water District
Monterey Peninsula Water Management District
Municipal Water District of Orange County
North Coast County Water District
North Marin Water District
Olivenhain Municipal Water District
Otay Water District
Panoche Water District
Pine Grove Community Services District
Princeton Codora Glenn Irrigation District
Provident Irrigation District
Public Water Agencies Group
Rainbow Municipal Water District
Rancho California Water District
Reclamation District #1500
Regional Water Authority
Root Creek Water District
Sacramento Suburban Water District
San Bernardino Municipal Water Department
San Diego County Water Authority
San Francisco Public Utilities Commission
San Juan Water District
Santa Clara Valley Water District
Santa Clarita Valley Water Agency
Santa Margarita Water District
Scotts Valley Water District
Sonoma County Water Agency

South San Joaquin Irrigation District
South Tahoe Public Utility District
Southern California Water Coalition
Stege Sanitary District
Tahoe City Public Utility District
Tehama Colusa Canal Authority
Trabuco Canyon Water District
United Water Conservation District
Valley Center Municipal Water District
Vista Irrigation District
Walnut Valley Water District
West County Wastewater District
Western Municipal Water District
Westlands Water District

Support if Amended

California Association of Mutual Water Companies
Mesa Water District
Tuolumne Utilities District
Yorba Linda Water District

Opposition

California Association of Realtors [Unless Amended]
Consumer Attorneys of California [Unless Amended]
Howard Jarvis Taxpayers Association [Unless Amended]

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