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The Impact of *Koontz* on Exactions and Environmental Mitigation in California

*By Michael H. Zischke and Daniel K. Kolta**

I. INTRODUCTION

Takings cases are inherently controversial, because they implicate the power of government to take property from landowners and developers who are applying for permission to developer their land. For property rights advocates, exactions—conditions imposed by local governments to mitigate for potential impacts of a development project—often seem like acts of government coercion. This is particularly true when it appears a local agency is exacting property or money for a benefit that is perceived as not directly related to a proposed project. Local government advocates, however, view exactions as a critical tool for ensuring that developers fully mitigate projects rather than externalizing those impacts such that the community must bear the impacts or pay to ameliorate them.

It is thus no surprise that the U.S. Supreme Court's most recent decision on the issue, *Koontz v. St. Johns River Water Management District*[1], provoked

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strong statements from the justices themselves, and strong reactions from a number of commentators. One op-ed piece commentator in the *New York Times* reacted, "It's hard to fathom that the framers of the Constitution would call this either fairness or justice."[2] *Koontz* is an important property rights case, and it was decided by a strongly divided court, with 5 justices in the majority and 4 dissenting. In our view, however, its impact is likely to be more modest than hoped for by some or feared by others.

First, the majority decision, authored by Justice Alito, held that a government violates the Takings Clause of the Fifth Amendment of the U.S. Constitution when it demands a landowner sign over a property interest before it will approve a permit application, the landowner refuses to comply, and the governmental body then denies the permit. Second, the majority concluded that monetary exactions are subject to the same scrutiny as real property exactions under the *Nollan*[3] and *Dolan*[4] "nexus" and "rough proportionality" tests. Both holdings are a victory for property rights advocates, although in practice it is not clear that the decision will work any fundamental change in the way exactions and environmental mitigation requirements are developed in California. To evaluate the impact of *Koontz* on land use law in California, it is necessary to review the primary takings cases that lead up to the current decision.

II. BACKGROUND—THE TAKINGS CONTEXT

A. *Nollan* and the Nexus Requirement

In *Nollan v. California Coastal Commission*, a 1987 decision by Justice Scalia, the Court required an "essential nexus" or connection between an agency's legitimate police power purpose and the dedication requirements that a public agency imposes on a development project to advance that purpose.[5] The legitimate police power purpose in *Nollan* was the California Coastal Commission's interest in providing the public with visual access to the beach. The Commission determined that expansion of the Nollans' beachfront home would block ocean views. To offset this impact, the Commission required the Nollans to grant a public easement for lateral access across the beach in front of the home. The Court found, however, that there was no essential nexus between the agency goal of visual access through the home and this dedication requirement in front of the home because the lateral access across the beach "utterly" failed to further the goal of providing a view to the beach through the property. Accordingly, requiring the dedication of this unconnected or unrelated easement constituted a Fifth Amendment taking.[6]

B. *Dolan* and the Rough Proportionality Requirement

The 1994 *Dolan v. City of Tigard* decision by Justice Rehnquist tells us how strong the required nexus or connection must be, and who bears the burden of proof that the nexus or connection is sufficiently close. In *Dolan*, the Court evaluated dedication requirements imposed by the city of Tigard, Oregon in approving building permits to expand Florence Dolan's plumbing and electric supply store. The city required Dolan to dedicate 10 percent of her property, which was located alongside a creek, for flood protection. The city also required Dolan to dedicate a 15-foot strip of land for a pedestrian and bicycle pathway. The city adopted findings to support its imposition of these dedication requirements, but the findings were general and conclusory. For example, the city found that it was "reasonable to assume the customers and employees of the future uses of the site could utilize a pedestrian/bicycle pathway adjacent to this development for their transportation and recreational needs."[7]

The *Dolan* court held these findings were insufficient to support the dedication requirements.[8] The Court ruled that there must be a "roughly proportional" relationship between the impact of a project and a dedication requirement imposed to offset or mitigate that impact.[9] This rough proportionality standard was, in some ways, similar to the "reasonable relationship" between project impacts and conditions of approval that California courts had previously required.[10] The Court, however, deliberately chose a different phrase based on a concern that a reasonable relationship test would involve the same minimal scrutiny as the "rational basis" standard in equal protection cases.[11] In addition, the Court ruled that the public agency must make an "individualized determination" to demonstrate that the required rough proportionality exists, and that the agency bears the burden of

showing that this proportionality exists.[12] The Court's holding effectively shifted the burden of proof for imposing an exaction onto the agency. This shifting of the burden was probably even more important than the Court's delineation of the new rough proportionality standard.

C. *Ehrlich*—Nollan and Dolan applied in California

In *Ehrlich*, a developer planned to build a multi-unit residential condominium on his property, on which he had previously operated a private tennis club and recreational facility. The city of Culver City found that there was a shortage of recreational facilities in the city and required the developer to pay a mitigation fee of $280,000 as a condition for approval of his project. The city also imposed a $33,200 "art in public places" fee in lieu of placing art on the development site.

Ehrlich foreshadowed one of the key holdings in *Koontz*, as the *Ehrlich* court held that heightened scrutiny may apply to monetary exactions. The court in *Ehrlich* found an important distinction between the sports fee and the arts fee, however. The sports fee was imposed as a condition of approval on Ehrlich's particular project; it was not a fee otherwise generally charged to developers or property owners in the city. In contrast, Culver City adopted the public art requirement as an ordinance of general applicability and applied this art fee across the board to broad classes of development projects.[13] A plurality in *Ehrlich* characterized the art fee as "more akin to traditional land-use regulations imposing minimal building setbacks, parking and lighting conditions, landscaping requirements, and other design conditions such as color schemes, building materials, and architectural amenities."[14] Thus, the court held that *Nollan* and *Dolan*'s "essential nexus" and "rough proportionality" tests applied to the sports fee because of that fee's unique application to the specific project at issue, but that the art fee need only meet the "rational basis" standard typically used by courts in analyzing state actions under the Fourteenth Amendment.

The court viewed the sports fee as an example of "regulatory leveraging," which occurs when a property owner and a regulatory agency strike a land use "bargain" in which the agency approves a project in return for the owner's "surrender of benefits which *purportedly* offset the impact of the proposed development."[15] The court characterized the fee as "leveraged" because the city was imposing the fee based on a legal argument that the city could deny Ehrlich's requested change in zoning. In such situations where leverage may be used to make excessive exactions, the "essential nexus" and "rough proportionality" tests are necessary to prevent unconstitutional takings.

However, the justices in *Ehrlich* disagreed over the basis for distinguishing between "leveraged" fees subject to *Nollan* and *Dolan*, and other fees not subject to such heightened scrutiny (the court was divided on many points in Ehrlich, and in addition to the majority opinion, there were three opinions concurring in full or in part). In upholding the art fee, four out of seven justices focused primarily on the traditional aspect of the art fee, comparing it to the types of design and aesthetic regulation that have long been held to be valid exercises of a city's police power to regulate for the public welfare.[16] The three other justices based their approval of the art fee predominantly on the fact that it was a fee required by an ordinance of general applicability, rather than an individualized fee imposed in response to a particular project.[17] These different holdings left unclear whether there is a 'bright line' test for determining when *Ehrlich* applies to a fee or exaction, a problem that would resurface in the *Koontz* decision.

III. THE *KOONTZ* DECISION

Koontz involved an 11-year fight waged between Coy A. Koontz, Sr. and his son Koontz, Jr. and the St. Johns River Water Management District over the development of a 14.9-acre property. Koontz, Sr. sought to develop 3.7 acres, offering to deed to the District a conservation easement on the remaining 11 acres. The District considered the 11-acre conservation easement to be inadequate, and instead informed Koontz, Sr. that it would only approve construction if he agreed to one of two concessions. Either Koontz, Sr. reduce the size of his development to one acre and deed the remaining land to the District, or agree to hire contractors to make improvements to District-owned land several miles away from his property. Believing these mitigation demands to be excessive as compared to the environmental effects that his development project would have caused,

Koontz, Sr. filed suit in state court. After the trial court and state appellate court ruled in favor of Koontz, Sr., holding that the District's mitigation demands were excessive, the Florida Supreme Court determined that *Nollan* and *Dolan* were distinguishable. The Florida Supreme Court concluded that *Nollan* and *Dolan* do not apply when a governmental entity denies an application because the applicant refuses to make concessions, and that the two decisions are only applicable to demands for an interest in real property, not to demands for money. Coy Koontz, Jr.[18] then petitioned for review by the U.S. Supreme Court, and the Court reversed the Florida Supreme Court's decision.

First, the *Koontz* majority, joined by the dissent, held that regardless whether the government approves a permit on the condition that the applicant concede a property interest, or denies a permit because the applicant refuses to do so, *Nollan* and *Dolan* apply with equal force.[19] According to the majority, a contrary rule "would enable the government to evade the limitations of *Nollan* and *Dolan* simply by phrasing its demands for property as conditions precedent to permit approval."[20]

The second question, whether monetary exactions are subject to the nexus and proportionality tests, divided the Court 5–4. The majority expressed concern that without the *Nollan* and *Dolan* tests, local governments wishing to exact an easement could simply give the owner a choice of either surrendering the easement or making a payment equal to the easement's value.[21] Emphasizing that surrender of the easement or equal cash value are functionally equivalent, the majority concluded that monetary exactions must satisfy the nexus and rough proportionality requirements.[22]

Justice Kagan, writing for the dissent, warned that the majority's holding will make it difficult for local governments to make any exaction without being subject to the scrutiny of the nexus and rough proportionality requirements, impairing the ability of local governments to mitigate new project impact.[23] The dissent asserted that the majority's distinction between monetary exactions and taxes is amorphous and difficult to apply, particularly because the majority fails to provide "even a word about how to make the distinction that will now determine whether a given fee is subject to heightened scrutiny."[24] Justice Kagan admonished the majority for leaving lower courts to guess at the proper distinction, invoking *Ehrlich* to suggest the majority should have created a bright line rule, for example as between ad hoc fees and generally applicable fees.[25] Justice Kagan also noted that the Court has held that requiring companies to spend money is not a taking, and that this precedent should have determined the outcome of the case.[26] Justice Kagan concluded, "the majority threatens the heartland of local land-use regulation and service delivery, at a bare minimum depriving State and local governments of 'necessary predictability.'"[27]

The majority responded to the dissent's critique by stating its decision does not impede the power of local governments to impose property taxes, user fees, and similar laws and regulations.[28] The majority insisted that "teasing out the difference between taxes and takings is more difficult in theory than in practice."[29] With that, the majority dismissed the issue, stating that it has little trouble distinguishing between taxes and takings.[30]

IV. IMPACT ON EXACTIONS AND MITIGATION REQUIREMENTS IN CALIFORNIA

The question dominating much of both the majority and the dissent is whether the majority's decision extends the Takings Clause in a manner that will fundamentally change how local governments impose exactions. Cities and towns impose many kinds of permitting fees every day. A government entity may charge a fee to enhance parks every time it issues a building permit, or it may do the same only for major residential projects. Similarly, a government entity might seek a monetary exaction for every new project that has an impact on traffic or pollution, or it might only seek such an exaction for projects with a particularly significant effect on one or both of these. A city or town may want to refrain from seeking substantial exactions from a developer proposing a highly desirable project, and may instead pursue large monetary fees from a deep-pocket developer that stands to make substantial profit from its proposed development. Ultimately, governments often resort to

creative approaches to confronting unique local challenges.

From this type of calculus comes an array of different types of monetary exactions, some of which may not survive *Nollan/Dolan* scrutiny, if applied. The *Koontz* majority clearly states that taxes and user fees are not subject to *Nollan/Dolan* heightened scrutiny, but in practice it is not always clear when the nexus and rough proportionality requirements apply, and when they do not apply. Some initial thoughts on this and other questions raised by the decision are set forth below.

Will Koontz fundamentally change exactions and mitigation practice in California? Probably not. *Ehrlich* already applied *Nollan/Dolan* scrutiny to mitigation fees, or at least to "nontraditional" mitigation fees imposed on an ad hoc basis. Also, both the Mitigation Fee Act[31] and the California Environmental Quality Act Guidelines[32] require agencies to justify most land use exactions and mitigation requirements.

Koontz may push local governments to do more to justify the nexus and proportionality of monetary exactions, although in practice that push may largely have already occurred given the holdings in *Ehrlich* and the above-mentioned statutory and regulatory requirements. The use of environmental impact reports to provide the required nexus justification and proportionality analysis may expand a bit. These are likely to be modest changes, however, consistent with existing land use and planning practice in California. Agencies that properly justify their exactions and conditions of approval should be no more at risk for takings claims under Koontz than they were previously.

The most fundamental aspect of *Koontz*, in fact, may be that is maintains (and to some limited extent, expands) the *status quo* under *Nollan*, *Dolan*, and *Ehrlich*. And that may be precisely why environmental advocates react so strongly against the decision; *Nollan* and *Dolan* have never been accepted by many of them. If one views all of these cases as simply requiring local agencies to show their work and provide sound planning justifications that link project conditions to project impacts, however, *Koontz* is primarily a decision that affirms existing principles.

Will Agencies Seek to Rely on Agreements in Place of Imposed Exactions? One reaction to the potential of takings claims is to seek voluntary agreements to provide facilities or funding. To the extent *Koontz* may increase takings claims (which seems uncertain), it may lead to more use of consensual agreements. Cities and counties could seek to obtain some exactions through development agreements, which as voluntary contracts are not subject to takings clause liability.[33] Other agreements outside the statutory development agreement context, including reimbursement agreements, could also be used when there is concern that an exaction may not pass *Nollan/Dolan* muster.[34]

How Will California Courts Apply Koontz? The answer to this question may come more quickly than usual (at least in comparison to the relatively glacial pace of takings jurisprudence generally). On September 11, 2013, the California Supreme Court agreed to review a decision by the Sixth District Court of Appeal relating to the justification required for inclusionary housing ordinances.[35] The Court of Appeal held that inclusionary housing ordinances are valid if they are "reasonably related" to a "legitimate public purpose."[36] The homebuilders had argued, and the trial court agreed, that the City of San Jose failed to demonstrate a sufficient nexus between the inclusionary housing requirements and the impact of building new, market-rate housing. The case could be an interesting early example of how a court grapples with takings principles now that *Koontz* has been added to the lineup of precedents, and the case may offer the California Supreme Court a chance to determine how bright the lines should be when courts evaluate nexus and rough proportionality requirements.

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Endnotes

1 133 S.Ct. 2586 (2013).

2 J. Escheverria, *A Legal Blow to Sustainable Development*, The New York Times (June 26, 2013).

3 *Nollan v. Cal. Coastal Comm'n*, 483 U.S. 825, 107 S.Ct. 3141 (1987).

4 *Dolan v. City of Tigard*, 512 U.S. 374, 114 S.Ct. 2309 (1994).

5 *Nollan*, 483 U.S. at 836.

6 *Id.* at 837-42.

7 *Dolan*, 512 U.S. at 381.

8 *Id.* at 395-96.

9 *Id.* at 398.

10 See *Associated Home Builders, Inc. v. City of Walnut Creek*, 4 Cal.3d 633 (1971).

11 *Dolan*, 512 U.S. at 391.

12 *Id.* at 391, 398.

13 *Ehrlich v. City of Culver City*, 12 Cal.4th 854, 862 (1996).

14 *Id.* at 866.

15 *Id.* at 867-68.

16 *Id.* at 886 (Arabian, Lucas, and George, JJ.), 912 (Werdegar, J. joining).

17 *Id.* at 902 (Mosk), 903 (Kennard and Baxter, JJ.).

18 Coy A. Koontz, Jr. continued this case after his father died, and he was the petitioner in the U.S. Supreme Court challenge.

19 *Koontz*, 133 S.Ct. at 2595.

20 *Id.*

21 *Id.* at 2599.

22 *Id.*

23 *Id.* at 2607 (Kagan, J., dissenting).

24 *Id.* at 2607-08.

25 *Id.* at 2608. In fact, it is not entirely clear that *Ehrlich* established such a bright line. One possible reading of the various opinions in *Ehrlich* is that an exaction must meet two tests in order to avoid heightened scrutiny under *Nollan* and *Dolan*. First the fee must regulate an area of traditional land use, and second, the fee must be one of general applicability. Another possible reading is that there is a bright line, and that line is whether the fee is one of general applicability, or an *ad hoc* negotiated fee. *See* Zischke and Spaulding, *Development Fees and Environmental Mitigation in California After* Ehrlich v. Culver City, 14 Cal. Real Prop. Jnl. 4, p. 1 (Fall 1996).

26 *Id.* at 2605-06 (citing *E. Enters. v. Apfel*, 524 U.S. 498, 118 S.Ct. 2131 (1998).

27 *Id.* at 2609 (citing *Apfel*, 524 U.S. at 542).

28 *Id.* at 2601-02.

29 *Id.* at 2601.

30 *Id.* at 2602.

31 Gov't Code §§ 66000-22.

32 Cal. Code Regs. tit. 14, §§ 15041, 15126.4(a)(4).

33 Gov't Code §§ 65864-65869.5

34 For an expanded discussion of this and related points, see the excellent commentary on the *Koontz* case by Bill Abbott and Glen Hansen on the Abbott & Kinderman land use blog. http://blog.aklandlaw.com.

35 *California Building Industry Association v. City of San Jose*, California Supreme Court Case No. S212072.

36 *Cal. Building Indus. Ass'n v. City of San Jose*, 157 Cal.Rptr.3d 813 (2013).

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Message from the Chair

*By Jodi Cleesattle**

SHUTTING DOWN THE GOVERNMENT

In early October, on the fourth day of the federal government's partial shutdown, I listened to an astonishing exchange on the radio. The show was National Public Radio's "Hear and Now" program, where host Robin Young interviews guests about current events. On this day, October 4th, Young was interviewing Diana Reimer, national coordinator for the Tea Party Patriots.

Early in the conversation, Reimer raised a point about the "nonessential" federal workers who have been furloughed—"So, if they're nonessential, then why are they even being paid?" Young responded by noting that many workers deemed nonessential really are essential and that some have been called back to work. She mentioned safety inspectors who were unable to investigate a deadly bus crash in Tennessee, cancer researchers who were called back in so patients could get cancer drugs, and National Weather Service and FEMA employees who were called in to respond to a storm threatening the Gulf Coast. And she asked Reimer her thoughts about such workers.

Reimer's response: "Yeah, I'm sorry. I haven't looked into that enough. I would like to know what nonessential workers are."

Reimer then gave the Tea Party mantra about the country needing less government.

Later, Young asked Reimer if she was concerned about government workers who are being hurt by the shutdown.

Reimer: "I really, I have to apologize. I haven't really given it much thought."

The conversation turned to the incident at the World War II memorial in Washington, D.C., where a Tea Party congressman had excoriated a park ranger because the memorial had been barricaded due to the shutdown. Reimer said she wouldn't have blamed the park ranger in the way the congressman did.

Then, there was this exchange.

Young: "But do you understand why a monument might be closed? The monuments are closed because of fear not of World War II veterans making the trip of a lifetime because they're so elderly, but because of vandalism and graffiti? That's why you have park rangers guarding monuments, and that's why monuments have to be closed when there's a shutdown. There's not enough park rangers to keep ...."

Reimer: "Well, according to the veterans, it shouldn't be closed. And yes, I do understand that, and the monuments do have to be protected."

Young: "But that's government."

Radio silence. Seconds ticked by. Then, finally, from Reimer: "Yeah, well, the government's all over."

I thought about this conversation as I attended the State Bar Annual Meeting a week later, and especially as I watched as the Public Law Section presented the Ronald M. George Public Lawyer of the Year Award to Burk E. "Buck" Delventhal, the Deputy City Attorney who leads the Government Law Division of the San Francisco City Attorney's Office. Delventhal has spent 43 years working in the San Francisco City Attorney's Office, representing the city in cases involving taxation following the passage of Proposition 13, prevailing wage ordinances, bans on cigarette vending machines, bilingual instruction in schools, residency requirements for city employees, and more. He supervised the drafting of all business tax and other revenue increase proposals after the adoption of Prop 13, and he has drafted laws regulating handguns, requiring development fees to benefit public transit, requiring bid

preferences in awarding contracts, and protecting the rights of non-smokers in workplaces, among other issues.

Delventhal is probably the worst nightmare for someone like Tea Party activist Reimer. He's a career public servant, one of those people whom Reimer would deem nonessential. He deals in government regulation. But it's people like Delventhal who help make the city, and its services, run smoothly.

Reimer is right about one thing. Government is all over. Local, state and federal government provide an awful lot of programs that most of us don't think about, at least until we have to, when they—or their absence—directly affect us.

Reasonable people can debate how much regulation is enough or how much government is too much. But when they do, they sure as heck should not find themselves saying, "I haven't looked into that" or "I haven't really given it much thought." Especially when they have shut down the government and thrown the lives of hundreds of thousands of people into limbo.

**Jodi Cleesattle is a Deputy Attorney General in the Employment and Administrative Mandate Section of the Civil Division of the California Department Justice. She works in the DOJ's San Diego office, defending state agencies in employment litigation.*

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Buck Delventhal Honored as 2013 Public Lawyer of the Year

The Public Law Section honored Burk E. "Buck" Delventhal, the Deputy City Attorney who leads the Government Law Division of the San Francisco City Attorney's Office, as the 2013 Ronald M. George Public Lawyer of the Year at an awards reception at the State Bar's Annual Meeting in San Jose on October 11, 2013.

Chief Justice Tani Cantil-Sakauye of the presented the award, which is named after her predecessor on the California Supreme Court. The Chief Justice, in honoring Delventhal, noted that she has a special affinity in her heart to the men and women who dedicate themselves to work in the public sector. In noting that Delventhal has many followers and friends who tell great stories about Buck, the Chief Justice said that she had only one question about honoring him with the award—"What took so long?" The Chief Justice pointed out that Delventhal was not being honored for how long he has engaged in public service, but for how he has served, noting his decency, integrity, wisdom, compassion, and tenacity.

Joining the San Francisco City Attorney's Office directly out of law school in 1970, Delventhal served the City and County of San Francisco for almost 43 years. During the that time, he argued landmark cases in the California Supreme Court, California Courts of Appeal, and the Ninth Circuit, and has been an attorney of record in over 100 appellate cases. In addition to his work in San Francisco's Government Law Division, Delventhal has been active with the California League of Cities and the County Counsel Association, serving as a member of the League's Legal Advocacy Committee for over three decades and also serving on the County Counsels' Association's Legal Oversight Committee.

Chief Justice Tani Cantil-Sakauye congratulates Buck Delventhal

In addition to being named this year's Public Lawyer of the Year, the International Municipal Lawyers Association is awarding Delventhal its highest honor—the Charles S. Rhyne Lifetime Achievement Award. According to the Association, this recognition is bestowed only occasionally and then only upon a truly uncommon individual.

Delventhal's exceptional career as a public lawyer is grounded in his belief in the importance of citizen and public engagement. Delventhal remains "hopeful that people of good will will lend their effort and wisdom to the restoration of majority rule and representative democracy." Delventhal believes that "[t]hat hope lies in citizen engagement" and that "San Francisco's engaged constituents" have provided him with such hope. He notes: "I love public law because it lies at the intriguing crossroads of our democracy. I enjoy helping constituents understand how their government functions. I

From Left to Right: Section Chair Jodi Cleesattle, Chief Justice Tani Cantil-Sakauye, Public Lawyer of the Year Buck Delventhal, Public Lawyer of the Year Co-Chairs Scott Dickey and David Hirsch (incoming Chair of the Section)

derive great pleasure helping representatives fashion legal vehicles to achieve their policy objectives. And I am optimistic about the prospect for better days of governance ahead."

Delventhal's colleagues praised his hard work, dedication, and commitment to public service in supporting his nomination for the Public Lawyer of the Year. San Francisco City Attorney Dennis J. Herrera observed that "Buck's consummate professionalism, work ethic, undaunted energy and enthusiasm and abiding dedication to the public sector serve as an inspiration to all of us in this office and should be a beacon for public lawyers throughout the State."

Solano County Counsel Dennis Bunting commented on Delventhal's extensive work with other public agency attorneys noting that, "Buck actually serves two masters, cities and counties. He is the ethical and intellectual muse for both the League of California Cities and the County Counsels' Association of California—equally revered by both."

In addition to mentoring attorneys in the San Francisco City Attorney's Office, he teaches classes in Local Government Law at Hastings College of the Law. Noting his work with young lawyers, former San Francisco City Attorney Louise H. Renne said of Delventhal: "He has mentored and encouraged attorneys from all practice areas in the importance of public sector lawyers and the role they play in Democracy, and has helped them develop into dedicated public lawyers. He has helped many, many law students develop an interest in, and later a career in, public sector law."

Delventhal was surrounded by friends, colleagues, family (including his wife, children, and adoring grandchildren) at the award ceremony. In addition to being known for his public law practice, Delventhal is known for his daily swims (sans wetsuit) in the San Francisco Bay. Delventhal received his B.A.in International Relations from UC Davis in 1965 and his J.D. from UC Hastings College of the Law in 1969.

Justice Cantil-Sakauye with outgoing Public Law Section Chair Jodi Cleesattle

2013 Ronald M. George Public Lawyer of the Year Award, Remarks of Award Recipient Burke "Buck" Delventhal

When I graduated from U.C. Hastings in 1969, law schools did not provide internship programs to help students find their way. While waiting for Bar exam results I clerked for a time in a San Francisco law firm, but found that this path was not for me.

Then I heard about an opening in the San Francisco City Attorney's Office. I knew very little about what the City Attorney did—so, naturally, I immediately applied. And when I was offered and accepted a position as a deputy city attorney, I was so thrilled about the idea of working for the City—a city I have always loved and the birthplace of my father, his parents and grandparents and the place where his great grandparents were married in Old St. Mary's in 1861 and the eventual birthplace of my children and grandchildren—that I did not even think to ask about the salary.

Forty three years later, and despite the dramatic historical and political changes I have seen during that time, I still look forward to coming to work each day in City Hall never knowing what interesting issue awaits me.

Buck Delventhal accepts the Public Lawyer of the Year Award at the State Bar's Annual Meeting in San Jose

I recall as if yesterday reporting for my first day of work to Room 206 of San Francisco City Hall on July 16, 1970. I entered a Dickensian world little changed since the construction of City Hall in 1912. The first person I met was Charlie Conlon, a man of the last hurrah with a heart of gold and an endless trove of stories about the old days. He had been the driver for two City Attorneys preceding the man who appointed me. He was also a pharmacist by profession. Word had it that this occupation and access to medicinal alcohol proved more than convenient for the political establishment during Prohibition. As I arrived each morning he would turn to Paul Holm our office manager who sat next to him, and with a sparkle in his eye ask, "What do you think Paul? Are we going to keep this kid"? as he dusted crumbs from Eppler's pastries off the napkin stuffed into his collar.

Many of the desks in the office still bore the stains of only recently obsolete fountain pen ink; our law clerk entered all the records of cases by hand in big ledgers; the IBM Selectric Typewriter was the latest

innovation and our secretaries still used carbon paper, sometimes as many as six at a time, to avoid the tedium of mimeographing copies. Imagine if you can the laborious task of erasing each of the six copies for every typing error. Needless to say briefs did not get edited to death in those days. And space was limited. Quarters that housed 10 attorneys when City Hall opened in 1912 were bursting at the seams with 35 lawyers only one of whom was a woman.

The opportunity to work for the City has proved rewarding beyond even the quixotic fantasies of my youth. This is the truth. For this the work provides a bounty of intellectual stimulation, extraordinary colleagues and clients, and public engagement with energized and committed San Franciscans.

I have been very fortunate. I owe a great deal to Tom O'Connor, who hired me, to George Agnost, who gave me challenging work when Proposition 13 passed, to Louise Renne, who redefined the City Attorney's role into a national model that seamlessly combined advocacy for public agencies and for the commonweal, and finally to Dennis Herrera, who has built upon that model assembling and inspiring the most diverse, talented and dedicated staff of public lawyers in the nation and developing community outreach programs that make me proud to be a member of his team.

And I owe as much to the talented senior attorneys in the office when I started, some of whom dated back to the 1930s, to my peers and to the generations that followed. My

Steven Mayer (left) and Randy Riddle (right) with Buck Delventhal

colleagues have been invariably and selflessly committed to supporting one another and to serving the public with distinction and excellence.

From today's perspective, those early days of my tenure in public service appear downright halcyon. Perched on the wake of the Culture War of the '60s, City government, in for radical changes not yet apparent, functioned pretty much as it had for nearly a half-century dating back to the Progressive reforms early in the Twentieth Century.

One of the cornerstones of that era was the Local Source Doctrine that equated local autonomy with independent taxing authority. This regime gave cities, counties and school districts control over property taxes. It was the lynchpin of local governance, ensuring local elected leaders the wherewithal to govern.

They enjoyed a luxury, nearly inconceivable today, to:

- Decide what the city, county or school district should do.
- Determine the cost.
- Calculate the property taxes needed to meet that cost after taking into account all other revenues.
- And finally set the tax rate by deciding just how much of a tax burden their constituents could afford.

This process took place every year in every city, county and school district in the state. Indeed, I recall as a young deputy advising the Board of Supervisors that it must include in the City and County's annual composite property tax rate the San Francisco Board of Education's tax rate for that year even though some of the supervisors thought that the school tax rate was too high. The decisions local elected officials made were not always ideal. But the ballot box, including the right of recall, provided the safety valve.

But things started to change in the early 1970s when property values in the state entered a period

of unprecedented growth. The modest house that my wife and I bought in 1973 in San Francisco's Eureka Valley, now known as the Castro, for $30,000 doubled in value in the span of just a couple of years. If I did not know better, I might have convinced myself that the paper gain reflected my own business acumen rather than blind luck. And that growth continued nearly unabated for more than 25 years in all California coastal cities. Homeowners in particular felt the pressure that rapidly rising property values, and correspondingly escalating property taxes, brought to bear. Many of them were seniors who had saved for old age on a fixed income by paying off their mortgages only to find that their frugality was repaid in property taxes that exceeded their former mortgage payments.

While the Legislature fiddled sitting on a multibillion dollar surplus that could have provided relief, Howard Jarvis and Paul Gann read and channeled the public's angst and fashioned a taxpayers' revolt initiative measure in 1978. Proposition 13 capped the property tax rate at 1%, instantly cutting the average rate nearly in half. It also rolled back assessed value, required two-thirds voter approval for special taxes at the local level and a two-thirds vote for the Legislature to raise state taxes. It stripped local governments of their fiscal autonomy and made them increasingly dependent on state largesse that inevitably came with strings attached. It also gave birth to an anti-government movement that has reached far beyond California's borders.

The adoption of Proposition 13 provided me with an extraordinary opportunity. I was still pretty junior in the office and in the world of city attorneys. But I was assigned to handle the City's challenge to Proposition 13 that we filed in the California Supreme Court along with the County of Alameda and Amador Valley Joint Union High School District. San Francisco's claim was that the imposition of a cap on the previously unlimited property tax impaired the City's contract obligations to its employee retirement system.

Public Law Section Executive Committee's Donna Mooney (left), Judy Coxsey-Hirsch and Buck Delventhal listen to the Chief Justice.

In those days we did not conduct moot courts to prepare deputies for oral arguments before appellate courts. Instead I retreated to the dusty bowels of the old law library on the fourth floor of City Hall to escape my telephone. There I spent solitary hours preparing for my argument that would be based on the Contract Clause of the United States Constitution.

I began to get an inkling of the import of the event when the Office of the Court's Clerk called to find out who would be accompanying me to the argument. Upon arriving at the court, I really started to get the jitters when I found TV cameras focused on me. The frontal attack I made that day did not prevail, but the Supreme Court did later hold in a case that I argued on behalf of the City of San Gabriel in 1982 that Proposition 13 could not limit the ability of local agencies to levy property taxes to pay for employee retirement obligations incurred before its passage.

Additional voter initiatives over the ensuing 30 years further curtailed the power of state and local governments to raise revenues while also enshrining in the Constitution state spending mandates for education unlinked to revenue reality. As a result, state and local government have increasingly lost the capacity to deliver basic services and provide for the most needy, many of whom

we now see inhabiting the streets of our cities.

That this dysfunction has promoted mistrust of public officials is no surprise. No longer equipped to raise taxes, they have turned to fees for previously free public services and facilities, and to fines and other regressive funding mechanisms. Even then, many these officials find themselves responsible for overseeing institutions they are effectively unable to govern by striking what they view to be the most equitable balance between taxing and spending.

This core dynamic of popular political cohesion is broken. The prevailing ethos in my youth, an extension of the widely held belief in shared sacrifice for the common good so prevalent in the Great Depression and World War II, is no longer the coin of the realm.

And Proposition 13 inevitably pitted state and local governments against one another in the Legislature, the courts and the ballot box. Burdened by ballot initiative spending mandates and the minority veto power over taxes embedded in the two-thirds vote rule, the legislators looked to city and county property taxes to meet some of their public school funding obligations.

Local governments fought back with their own initiatives, adding more complexity and rigidity to the Constitution's already recondite state and local finance rules and inciting further legislative retaliation. The nettlesome dissolution of redevelopment agencies is only the most recent campaign in this war. This process will continue until Californians muster the political will to fully equip their elected representative with the tools that they need to govern.

Why am I recounting this history? I have been a local public servant through this whole period. I remain hopeful that people of goodwill will lend their effort and wisdom to the restoration in California at both the state and local levels of majority rule and representative democracy.

I have another concern. The people of California need to rethink the initiative process. This invaluable tool of self-government played a key role in the Progressive revolt against the Southern Pacific Railroad's stranglehold on state and local governments in the first decade of the Twentieth Century. But the initiative itself has become an all-too-convenient legislative shortcut for anyone with the financial means to hire signature gatherers.

Not surprisingly, the results have on the whole not improved our governance or the quality of life for Californians. Even Proposition 13's vaunted revolt bestowed the lion's share of its bounty not on homeowners who, on average, sell their homes and face reassessment every seven years, but on proprietors of commercial real estate, mostly corporations, that often hold their property for generations. And of course we are all too aware of the typical inequity of two side-by-side, mirror image houses of equal value except that the person who has owned the home for 30 years pays one-tenth the property taxes that her new neighbors pay.

The solution is not to stifle the initiative process but rather to ensure that the voters understand what they are being asked to approve. The necessarily bland and often unavoidably dense summaries of complex measures in the voter pamphlets cannot give the electorate a broad enough perspective.

Instead, we need a formal process in which a body selected in the same fashion as the California Citizens Redistricting Commission would oversee robust and fair public debates on ballot measures that campaigns would not control. These debates would develop critiques of the strengths, weaknesses and potential consequences of the measures, enhancing the capacity of voters to separate the wheat from the chaff.

Finally I do want to close on hopeful note. That hope lies in citizen engagement. Robert Putnam's incisive book from 2000, *Bowling Alone*, examines public engagement and concludes that it peaked in the United States in 1960 and has been falling ever since. He defines public engagement broadly to include everything from holding public office to participating in a bowling league. He sees public apathy and lack of citizen engagement as threats to our society.

During the first decade of my tenure in the City Attorney's Office, I rarely dealt with public meeting and records issues. Today, our attorneys and those in most other jurisdictions regularly face these issues. In addition, San Francisco voters created an Ethics Commission and a Sunshine Ordinance Task Force to educate

Buck Delventhal and family at the Public Lawyer of the Year Reception.

the public and City officials about and enforce compliance with ethics and sunshine laws. And Chief Justice's Cantil-Sakauye Civics Education Initiative to promote civic awareness, learning, and engagement among our youth provides yet more reason for optimism.

San Francisco's engaged constituents watch public servants carefully and use sunshine laws to hold them accountable. They have batted away institutional barriers that in earlier generations might have impeded such oversight of government. This is a very promising turn of events. An engaged public invigorates government and strengthens its portfolio. This oversight is critical as a democracy in the hands of elected officials, bureaucrats and lobbyists alone is adrift and rudderless, bereft of its vitality.

I have seen the panorama of public life writ large from my perch in City Hall: Former Mayor Jack Shelley's Friday afternoon reminiscences when he would return with our deputies from his duties as the City's lobbyist in Sacramento; Joe Alioto holding court with his Napoleonic, spellbinding grasp of minds and men; George Moscone's disarming bonhomie; Dianne Feinstein's relentless demand for excellence; Art Agnos' principled compassion that cost him dearly; Willie Brown's unparalleled Machiavellian mastery of governance; the tragedy and sorrow of City Hall assassinations and the People's Temple massacre; the joy of victory in the recognition of marriage equality and twice stopping different owners of the Giants from moving the team first to Toronto and then to Jacksonville; the AIDS epidemic and the bathhouse litigation; one recall election and two impeachments all unsuccessful, and one imprisonment of city officials; the introduction of ranked-choice voting and instant run-off elections, local public funding of elections and other attempts to limit the influence of money in local elections; Proposition 187, the 1994 state anti immigrant initiative and the San Francisco's City of Refuge counter point, the explosion of initiatives locally and statewide, the rise and demise of affirmative action; the Loma Prieta Earthquake and the urban rebirth it spawned including a gem of a ball park and the restoration of City Hall to its original splendor; the rise of homelessness; district elections twice over; rent control and condo conversion limits; 49ers and Giants victory celebrations, and on and on and on. It has been an extraordinary era.

It is for these reasons and so many more that I love what I do. I love public law because it lies at the intriguing crossroads of our democracy. I enjoy helping constituents understand how their government functions. I derive great pleasure helping representatives fashion legal vehicles to achieve their policy objectives. And I am optimistic about the prospect for better days of governance ahead.

In conclusion, I would like to express my great appreciation to the People of California and to University of California and Hastings College of the Law for giving me the extraordinary and affordable education that has equipped me to reap the immense rewards of public service. I would also like to thank the City Attorneys who have entrusted in me responsibility for serving the public interest over these many rewarding years. I am honored to receive this award, and most honored to be a public servant.

The Public Law Section
of The State Bar of California

CONGRATULATIONS

Burk E. "Buck" Delventhal

2013 Ronald M. George Public Lawyer of The Year

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Recent Developments in Municipal Bankruptcy

*By Franklin C. Adams**

Since the City of Vallejo filed for bankruptcy in 2008, two other major California cities have filed for Chapter 9 municipal bankruptcy protection. The City of Stockton filed on June 28, 2012, and the City of San Bernardino filed shortly thereafter on August 1, 2012. These cities followed very different routes into Chapter 9, although both cities faced significant obstacles from objecting parties prior to being granted eligibility. These cities' bankruptcy cases have also reinforced the notion that every municipality must meet certain requirements of both State and Federal law in order to be permitted to proceed under Chapter 9 after the petition is filed. This article first describes the procedures that now govern a municipality's eligibility for bankruptcy in California post-Vallejo, before turning to the eligibility paths of San Bernardino and Stockton.

ELIGIBILITY IN CALIFORNIA

A municipality enters bankruptcy by filing a petition, regardless of the basis upon which it believes it is a qualified Chapter 9 debtor. Following the filing, a municipality must set forth its rationale or facts upon which it claims to be an eligible Chapter 9 debtor.[1] Each state has its own system of eligibility for municipalities to file for bankruptcy protection under federal bankruptcy law and procedures.

The eligibility requirements in California are found in the Government Code.[2] Generally, there are two distinct pathways to bankruptcy eligibility—neutral evaluation and declaration of fiscal emergency. These procedures were enacted as part of Assembly Bill 506, effective January 1, 2012.

NEUTRAL EVALUATION

The first pathway to eligibility commences with a confidential neutral evaluation process which is conducted by a neutral evaluator or mediator.[3] Notice is given to all interested parties[4] before this process begins.[5] The invited parties then have 10 business days to respond to the invitation to participate in the evaluation process, but are not required to attend. The time period for the neutral evaluation process may not exceed sixty days absent stipulation of the parties. The process may never exceed ninety days[6].

The Government Code is very particular about the qualifications of the neutral evaluator. The "neutral" must indeed be unbiased and may not impose any settlement on the participating parties. The "neutral" must have experience and/or training in alternative dispute resolution and must either:

1. Have at least 10 years of high-level business or legal practice involving bankruptcy or service as a United States Bankruptcy Judge; or,
2. Professional experience or training in municipal finance and one or more of the following issues areas:
    a. Municipal organization
    b. Municipal debt restructuring
    c. Municipal finance dispute resolution
    d. Chapter 9 bankruptcy
    e. Public finance
    f. Taxation
    g. California constitutional law
    h. Federal labor law.[7]

The costs for the evaluation process are borne by the public entity and the creditors, with each bearing one-half the costs, including the fees of the "neutral" unless otherwise agreed.[8]

The evaluation process ends when one of the following has occurred:

1. The parties execute a settlement agreement;

2. The parties reach an agreement or plan of adjustment that requires approval of the bankruptcy court;

3. The initial sixty day term has expired with no agreement reached and neither party wishes to extend the time period of neutral evaluation;

4. No interested party responded to the invitations to participate; or

5. The fiscal condition of the local public entity deteriorates to the point that a fiscal emergency is declared pursuant to Government Code § 53760.5.[9]

If the evaluation process concludes without resolution or agreement, then Government Code Section 53760.3(u) provides the standard and authority for meeting the State of California's eligibility requirements for filing Chapter 9. This standard does not necessarily meet the United States Bankruptcy Code requirements and proof must still be made in the bankruptcy court of eligibility.

DECLARATION OF FISCAL EMERGENCY

The second and only other path to Chapter 9 is declaration of a fiscal emergency. The standard required to declare fiscal emergency is that the local public entity "is or will be unable to pay its obligations within the next 60 days."[10]

In addition, the municipality must adopt a resolution satisfying all of the following requirements before the declaration of fiscal emergency will meet the standards of California Government Code § 53760.5:

1. The resolution must pass by a majority vote of the governing body;

2. There must be a finding that the financial state of the local public entity jeopardizes the health, safety, or well-being of the residents of its jurisdiction or service area absent the protections of Chapter 9; and

3. The municipality must notice and agendize a public hearing on the fiscal condition of the entity and take public comment.

RELATIONSHIP TO FEDERAL BANKRUPTCY CODE

The above requirements have provided the statutory requirements for filing Chapter 9 in California since Assembly Bill 506 was adopted. Prior to that adoption (and in the cases of Orange County and the City of Vallejo), similar state law requirements did not exist. The Bankruptcy Code sets out the federal requirements for eligibility at 11 U.S.C. §109(c), which are mandated in addition to the state requirements.[11] In many aspects, the new requirements imposed by AB 506 find similar counterparts in the federal scheme. For example the Bankruptcy Code requires that the municipality either:

1. Obtain the agreement of at least a majority of claims in each class of creditors;

2. Negotiate in good faith with creditors;

3. Demonstrate that negotiations with creditors would be impracticable; or

4. Reasonably believe that a creditor is about to obtain a transfer of property that would be avoidable under 11 U.S.C. § 547 of the Bankruptcy Code.[12]

Another potential area of overlap is 11 U.S.C. §109(c)(3), which is similar to Government Code § 53760.5 in setting forth an entity's requirements for insolvency due to fiscal emergency.

VALLEJO AS A TURNING POINT

The Vallejo case in some respects represents a turning point in municipal bankruptcies in that it resulted from fiscal challenges facing many municipalities in California, as opposed to improvident investments in an otherwise and relatively stable economy. The Vallejo case revealed two clear developments in municipal bankruptcy law. First, Vallejo's bankruptcy revealed that courts would not allow the use of restricted funds to determine fiscal insolvency. In other words, a fund that is not statutorily available cannot be factored into the determination of the municipality's insolvency. Second, the Vallejo case revealed that collective bargaining agreements of the various unions could be rejected.[13] Prior to 1984, the standard for rejection of an executory contract was whether or not the contract was burdensome on the debtor. Equity favored rejection and merely required that the debtor make reasonable efforts to negotiate a voluntary modification without a likelihood that such negotiations would produce a prompt solution.[14] The 1984 amendments to the Bankruptcy Code changed that standard and required much stricter

standards for rejection of collective bargaining agreements. The stricter standards for rejection of collective bargaining agreements, however, are found at 11 U.S.C. § 1113 and are not incorporated into Chapter 9.[15] As a result, municipalities are not burdened by the stricter standards imposed by 11 U.S.C. § 1113, but must only meet the less restrictive standards set forth in *NLRB v. Bildisco & Bildisco*.[16]

SINCE VALLEJO

With the fallout of Vallejo, there was significant concern in California that many more municipalities would seek Chapter 9 protection. Since the Bankruptcy Code requires any petitioner to meet State standards for admission into Chapter 9,[17] the legislature sought to provide more guidance and set stricter standards for admission into Chapter 9, resulting in Assembly Bill 506, as noted above.

Since Vallejo, the intensity of the battle to gain admittance to Chapter 9 nirvana has, if anything, increased, and the focus on eligibility has persisted. The Chapter 9 case of the City of San Bernardino[18] was filed on August 1, 2012, but the order for relief[19] was not entered until September 17, 2013.[20] Interestingly the order for relief was entered on a motion for summary judgment. In the case of Stockton, the order for relief was entered on April 1, 2013.[21]

ELIGIBILITY PATH OF THE CITY OF SAN BERNARDINO

The City of San Bernardino did not enter bankruptcy through the neutral evaluation process. Rather, declaration of a fiscal emergency provided the city with an expedient path to Chapter 9 protection. Opposition came from the city's unions, bond insurers, and CalPERS, the administrator of the pension and retirement plans of the city employees. That opposition challenged eligibility by contesting both the propriety of the declaration of fiscal emergency and the good faith nature of the filing. The objecting parties argued that the City essentially managed its way into bankruptcy.[22] CalPERS' initial objection raised issues of good faith as well as attacked the City's desire to effectuate a plan of adjustment.[23] CalPERS highlighted the discovery issues that would become a hallmark of this case by asserting that: 1) the City's records were in such disarray as to make it impossible to determine eligibility from the outset of the case; and 2) the City was not operating within its budget and had no unrestricted funds with which to operate.

On September 17, 2013, the Court filed and entered its Statement of Uncontroverted Facts and Conclusions of Law supporting the entry of an order for relief determining, on summary judgment, that the City had met its burden and was eligible for Chapter 9. In making that determination, the Court made some notable findings. For example it found that the City's water department had over $37,000,000.00 in immediately available cash or cash equivalents and that it had net assets of $263 million as of the date of the filing of the petition. However, the Court found that none of those monies or assets were available to be used as general funds or could be borrowed by the City. It found that the City had failed to pay "millions of dollars" in post-petition obligations and had paid pre-petition claims.[24] Notably, along the way, the City had reached agreements with four of its seven unions.

Ultimately, the City met its burden of declaration of fiscal emergency and is therefore eligible to be a Chapter 9 debtor. Now, it must find a way to formulate a plan of adjustment that will allow it to operate in an uncertain future.

THE CITY OF STOCKTON'S PATH TO ELIGIBILITY

Stockton preceded the City of San Bernardino, but gained eligibility through an entirely different route—the neutral evaluation contemplated in Government Code § 53760.3(b). The order for relief was entered on April 1, 2013. In conjunction with the Order for Relief, the Honorable Christopher Klein rendered his fifth formal written opinion in that case.[25]

In about 2008, the City of Stockton engaged in a concerted effort to right its fiscal ship. In 2010, Stockton adopted a Plan of Action and hired a new city manager to implement that plan. The plan included unilateral actions to reduce costs as well as consensual agreements with labor for reduction of wages and benefits. These reductions, which accounted for about 71% of Stockton's annual budget, were not enough. In February 2012 the City initiated the neutral evaluation process.

The process lasted the maximum 90 days authorized by agreement of the City and a majority of the parties. Through that process, the City reached agreements with all

of its unions and made substantial progress with other creditors.[26] Over 40 mediation sessions were held.[27] Notably, the representatives of the capital market and bond creditors refused to continue to participate in the negotiations after receiving the initial offer from the City.[28]

These bond creditors raised numerous legal issues during the neutral evaluation process. For example, the creditors maintained that they were not required to pay one half of the costs of the neutral evaluation process as required by Government Code §53760.3(s). Their rationale was couched in the language of that section which excused payment by a party "unless otherwise agreed to by the parties." They argued that the bond indenture agreements provided that any costs related to litigation would be borne by the City. Judge Klein found that the specificity of the language of the Government Code "trumped the indenture contractual language."[29]

The requirement of good faith negotiations was another point of contention between the bond creditors and the City. The bond creditors contended that they were not bound by the requirements of Government Code §53760.3(o) to negotiate in good faith. They took the position that the City's "ask" was a "take it or leave it proposition" and therefore they were justified in walking away from the negotiations. Judge Klein disagreed, noting a myriad of factors, including the fact that the City had reached agreement with all of its collective bargaining units.[30]

The bond creditors also challenged the City's good faith during the eligibility proceedings, arguing that the City's proposal was not in good faith because it omitted any proposal to impair CalPERS.[31] The Court, however, found this to be irrelevant to eligibility, noting that the issue more properly related to the plan confirmation.[32] The Court reserved some of its harshest language in the opinion for the bond creditors and their negotiation posture when it stated:

> The mentality of the macho manager that authorizes uneconomic litigation activity on the premise that the opponent will pay the bills, which is the dysfunctional contractual corollary of the so-called "American Rule" regarding fees that escalates the legal expense, has been rejected as a matter of California law in the difficult arena of municipal insolvency.
>
> In other words, the decision makers for the capital markets creditors need to check their testosterone at the door, stop assuming that they are spending their opponent's money when they direct their counsel to pursue wasteful legal tasks, and make their litigation business decision on the premise that they will be responsible for every dollar of legal effort that they order.[33]

In Stockton's eligibility proceedings, the Court adopted the notion of "service delivery insolvency" as an indicator of financial insolvency. In other words, the Court found that the level of services the City was able or, more importantly, not able to provide, especially in police and fire protection, was probative of true fiscal insolvency under the Government and Bankruptcy Codes.[34]

The bankruptcy cases of both San Bernardino and Stockton are the first to be governed by Assembly Bill 506. The opinions written by Judge Klein in the Stockton case will provide useful guidance for other municipalities as they contemplate their own fiscal difficulties, particularly as to the strategies municipalities should utilize to resolve issues before attempting Chapter 9, as well as how to successfully navigate the neutral evaluation process. The San Bernardino case will also provide useful guidance on the use of declarations of fiscal emergency as the path to Chapter 9 eligibility.

Both cases have a long way to go to successful completion. These initial battles over eligibility give an extremely useful look as to what lies ahead in the confirmation battles to come. Judge Klein may be prophetic in this last opinion when he previewed the conflicting interests of two of the most influential and moneyed combatants—bond creditors (objectors) and CalPERS —when he said:

> It has long been evident that the objectors are itching for a fight over pensions, to answer interesting questions whether the City has an executory contract with CalPERS and whether liabilities to CalPERS might be dischargeable debts. And CalPERS itself has been bellowing and pawing the sidelines during the eligibility phase waiting for the main event that will come only after relief is ordered. . . .
>
> An appropriate method for achieving their goal of spreading the pain to CalPERS would be to challenge CalPERS head-on

in battle over the actual plan filed after relief is ordered, in which battle the City could watch from the sidelines.[35]

(Note: After preparation of this article and prior to publication it appears that Stockton has reached agreement with its bond creditors on approximately $150 million in bond debt.[36])

Franklin C. Adams is a partner at Best Best & Krieger, Riverside, California and is the practice group leader for the Bankruptcy and Insolvency Department of the Firm. Mr. Adams has practiced in this field for 34 years.

Endnotes

1 This is usually termed a "Statement of Qualifications"

2 California Government Code §§53760 et. seq. These sections were added as the result of passage of AB 506 which became effective January 1, 2012.

3 California Government Code §53760.3.

4 Interested Parties is defined at Government Code §53760.1(c) and includes among others, trustees, committees of creditors, affected creditors, pension funds, unions with certain qualifications and others.

5 California Government Code §53760.1

6 California Government Code §53760.3(r)

7 California Government Code §53760.3(d).

8 California Government Code §53760.3(s).

9 California Government Code §53760.3(t).

10 California Government Code §53760.5.

11 All references to the Bankruptcy Code shall mean the United States Bankruptcy Code at 11 U.S.C. §§ 101 et. seq.

12 11 U.S.C. §109(c)(5).

13 Executory contracts are subject to rejection under bankruptcy law at 11 U.S.C. §365. Collective bargaining agreements are a type of executory contract that is subject to rejection under 11 U.S.C§ 1113 which was added to the Bankruptcy Code in 1984 as part of the Bankruptcy Amendments and Federal Judgeship Act of 1984 and became effective on July 10, 1984 in response to the Supreme Court Decision in *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 104. S. Ct. 1188 (1984). (*See* Collier's Pamphlet Edition of Bankruptcy Code(2013) at page 867, 1984 Amendments.)

14 *See* Endnote 9 above.

15 *See* 11 U.S.C. §901.

16 *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 104. S. Ct. 1188 (1984).

17 11 U.S.C.§109(c)(2)

18 United States Bankruptcy Court for the Central District of California, case no. 6:12:-bk-28006MJ.

19 An order for relief is entered by the bankruptcy court once it determines that the debtor has met all of the requirements for eligibility. *See* 11 U.S.C. §921(d).

20 *See* docket item #798 for case no. 6:12:-bk-28006MJ, United States Bankruptcy Court for the Central District of California, Riverside Division.

21 *See* docket item #843 of City of Stockton, United States Bankruptcy Court for the Eastern District of California, case no. 12-32118.

22 *See* objection of Public Employees to petition at docket item no. 203, for case no. 6:12:-bk-28006MJ, United States Bankruptcy Court for the Central District of California, Riverside Division..

23 A Chapter 11 plan of reorganization is called a plan of adjustment in the Chapter 9 setting.

24 *See* Court's Statement of Uncontroverted Facts and Conclusions of Law, docket item no. 796, case no. 6:12:-bk-28006MJ, United States Bankruptcy Court for the Central District of California, Riverside Division..

25 *In Re Stockton*, 493 B.R. 772 (E.D. Cal. June 12, 2013). This opinion in Case No. 12-32118, Docket Number 950, is for publication and is hereinafter referred to as the Opinion.

26 Opinion at page 14 lines 19 to 22.

27 Opinion at page 17, line 4.

28 Opinion at page 13, line 4 and page 14, lines 5 to 11.

29 Opinion at page page 23, lines 7 to 13.

30 Opinion at page 19, lines 17 to 26.

31 Opinion at page 17, lines 24 to 26.

32 Opinion at page 21, lines 26 to 28 and page 22 at line 1.

33 Opinion at page 23, lines 14 to 25.

34 Opinion at page 29, lines 18 to 28 and page 30, lines 2 to 12.

35 Opinion at page 46, lines 7 to 21.

36 Rueters, U.S. Edition, October 3, 2013. http://www.reuters.com/article/2013/10/04/us-stockton-bankruptcy-assured-guaranty-idUSBRE99301620131004

When Uniform Taxes Aren't Uniform Enough: How An Appellate Decision Striking One School District's Special Tax May Inhibit The Use Of Special Taxes By Many Local Agencies

*By William B. Tunick**

With Sacramento frequently raiding local agency funding to address State budget woes, the ability to levy local taxes has become an important part of many local agencies' budgets. Multiple types of agencies, from healthcare districts to counties have been authorized by the Legislature to levy special taxes with the consent of a supermajority of their voters. While skirmishes over the voter-approval requirement for taxes, fees and charges are common, there has been much less litigation surrounding the way special taxes can be calculated and levied.

This was evident in the question raised for the first time in *Borikas v. Alameda Unif. Sch. Dist.* (2013) 214 Cal.App.4th 135: Does statutory authorization to levy "uniform" special taxes limit those taxes to single-rate formulas, or does it simply require that all like parcels be treated alike? For over 25 years, school districts, believing the latter, levied special taxes with a variety of structures and formulas without challenge. Yet *Borikas* found fault with this practice, ultimately holding the "uniformity" requirement imposed a limitation on school district special taxes, prohibiting any taxes that classified and taxed parcels differently based on that classification–even if parcels within each classification were treated similarly.

While the decision is particularly important for school districts throughout the State, it has the potential to affect a large number of local agencies well beyond school districts because the statutory authority interpreted by *Borikas* arguably has served as a template for multiple statutes providing authority for many other types of local agencies to levy special taxes. Moreover, while *Borikas* answers the question presented in the case, its holding raises many new questions about the type of tax formulas that meet the definition of "uniformity." For example, it does not address whether local agencies may levy special taxes based on the size of parcels.

It appears that these and other fundamental questions left unanswered by *Borikas* will need to be resolved by further litigation. While at least one bill has been introduced in the Legislature to clarify the law in light of *Borikas*, it met staunch opposition from anti-tax groups and has yet to gain any traction. In light of this holding and the uncertainty it brings, local agencies that depend on statutory authorization to levy special taxes may be wise to take a more conservative approach in structuring future special taxes until either the courts or the Legislature can resolve the issues raised by *Borikas*. Ultimately, this may mean *Borikas*'s most significant impact may be dissuading some local agencies from even seeking tax authorization at all.

ORIGIN OF SPECIAL TAXING AUTHORITY

Among other restrictions, Proposition 13 prohibited local agencies from levying "special taxes" without approval of two-thirds of the electorate.[1] It also prevented the levy of special taxes without express authorization from the Legislature.[2] Responding to this requirement, in 1979 the Legislature enacted general legislation in the form of Government Code section 50075[3] which: "provide[d] all cities, counties, and districts with the

authority to impose special taxes, pursuant to the provisions of Article XIII A ...."[4]

Apparently dissatisfied with application of Proposition 13, voters adopted Proposition 62 in 1986. Significant to *Borikas*, Proposition 62 declared that the article of the Government Code containing section 50075 should not "be construed to authorize any local government or district to impose any general or special tax which it is not otherwise authorized to impose."[5] Although apparently an unintended consequence, this amendment had the effect of removing the statutory authority for local agencies to seek voter approval for special taxes.[6]

As a result, the status of this taxing power in the wake of Proposition 62 became unclear.[7] Specifically, many school districts contended that section 4 of article XIII A was self-executing and could be relied upon, absent any specific statutory authorization, to allow school districts to levy special taxes.[8] This position was later rejected by a Court of Appeal.[9] This confusion and concern—especially from school districts which had adopted special taxes following Proposition 62—led to a flurry of legislative activity to provide a wide variety of local agencies with specific power to levy special taxes.

The first of these statutes was Assembly Bill No. 1440 (1987-1988 Reg. Session) ("AB 1440"), which re-authorized school districts to levy what it defined as "qualified special taxes." As enacted in 1987, section 50075 read:

> (a) Subject to Section 4 of Article XIII A of the California Constitution, any school district may impose qualified special taxes within the district pursuant to the procedure established in Article 3.5 (commencing with Section 50075) and any other applicable procedures provided by law.
>
> (b) As used in this section, "qualified special taxes" means special taxes that apply uniformly to all taxpayers or all real property within the school district, except that "qualified special taxes" may include taxes that provide for an exemption from those taxes for taxpayers 65 years of age or older.
>
> "Qualified special taxes" do not include special taxes imposed on a particular class of property or taxpayers.[10]

The legislative history behind AB 1440 makes clear that its purpose was to "clarify that school districts can continue to impose special taxes"[11] and that the bill "merely authorizes school districts to continue to impose special taxes ...."[12]

With this authority, over 200 school districts have asked voters to approve qualified special taxes, with voters in over 100 school districts agreeing to do so.[13] The number of school districts seeking voter approval of special taxes is rapidly increasing.[14] And the total amount of revenue raised by these measures is substantial, nearly $350 million in 2011-12 alone.[15] In some school districts, special tax funding has accounted for as much as 31% of the school district's budget.[16]

While the majority of school districts opted to seek authorization of "single-rate taxes" (e.g., $100 per parcel, regardless of size or type of parcel), others sought voter approval of taxing formulas dependent on the size and/or use of certain parcels ("classification-based taxes").[17] Some school districts believed this to be a fairer form of tax than a single-rate tax, which is inherently regressive.[18] Prior to *Borikas* no appellate court had ruled on whether such taxes complied with the "uniformity" language of section 50079.

"While the majority of school districts opted to seek authorization of "single-rate taxes," others sought voter approval of taxing formulas dependent on the size and/or use of certain parcels. Some school districts believed this to be a fairer form of tax than a single-rate tax, which is inherently regressive."

BORIKAS LIMITS SPECIAL TAXING AUTHORITY

Several school districts levied classification-based taxes both prior and after passage of AB 1440.[19] One such district was the Alameda Unified School District ("District"), whose voters passed Measure H in 2008 and Measure A in 2011.

Specifically, as authorized by voters, Measure H imposed a tax of $120 on all residential parcels, as well as a tax of $0.15 per square foot on all other parcels, with a minimum tax of $120 and maximum tax of $9,500 for those parcels.

Borikas's challenge to Measure H, filed in late 2008, argued that it was outside the "uniformity" requirement of section 50079 and therefore beyond the power of the District to levy.[20] Essentially, the challenge argued that "uniformity" required one rate of tax be applied to all parcels. The District responded that "uniformity" should be read to require that all like parcels be treated similarly, allowing for reasonable classifications, as is the case where taxes are otherwise required to be applied uniformly for equal protection purposes. The trial court agreed with the District reasoning that the Legislature had not explicitly indicated a different meaning for "uniform" and Measure H was "uniform" as that term was understood in the taxing context.[21] Challengers appealed, raising essentially the same arguments on appeal as they had at trial.[22]

Two years later, the First District Court of Appeal partially reversed the trial court, holding that to the extent the tax created classifications and then assigned rates based on those classifications it violated the authority granted by the Legislature through section 50079.[23] Ultimately, the Court allowed part of the tax to stand—reasoning that the Measure's severance clause allowed the single rate of $120 to be applied to all parcels.[24]

The Court of Appeal based its conclusion on three grounds: (1) portions of the statute would become unnecessary surplusage otherwise; (2) actions and interpretations surrounding the enactment of section 50079 evidenced the Legislature's intent to limit school districts' taxing authority; and, (3) language in somewhat similar statutes allowing other local agencies to levy special taxes informed the meaning of section 50079 as a limit on taxing powers.[25]

I. RULES OF STATUTORY INTERPRETATION

The Court of Appeal began by reasoning that if the broader authority the District claimed was intended by the Legislature, a large portion of the statute would be meaningless. It posited, "if section 50079 did not include the language in question, there would be no question that school districts could create rational tax classifications and impose differential tax rates."[26] Thus:

> if the Legislature had intended to delegate to school districts the broadest taxing authority allowed by law ... it needed only to have authorized school districts to impose special taxes,.... This would mean, however, that the *entirety* of subdivision (b) is meaningless surplusage, a result that cannot be reasonably ascribed to the Legislature ....[27]

The Court of Appeal also explained that there was no reason for the Legislature to include specific language allowing exemptions for certain taxpayers if the language at issue "allowed school districts ... to impose different tax burdens on different taxpayers."[28]

In support of this point, the Court of Appeal pointed to section 50079.1, enacted many years after section 50079 to authorize community college districts to levy special taxes. It noted that section 50079.1 also required special taxes to "be applied uniformly," but went on to provide, "except that unimproved property may be taxed at a lower rate than improved property."[29] It concluded that this provision would not have been necessary in section 50079.1 if "uniformity" as used in section 50079, allowed for classifications. Based on its determination that the Legislature intended the words of both statutes to be read similarly, it concluded that "uniformity" in section 50079 must prohibit such classifications.

II. SUPPORT IN LEGISLATIVE HISTORY

The Court of Appeal also examined the legislative history of AB 1440. Specifically, it focused on correspondence from school districts regarding their understanding of section 50079 at the time it was being considered. It seized on a letter to one of the school districts involved with the drafting of AB 1440—which was ultimately transmitted to legislative staff—which gave the preliminary opinion that AB 1440 would not "'provide the necessary authority for the districts to impose their special taxes.'"[30] The Court of Appeal further pointed out that the letter stated, "'the bifurcated rate ... special tax also appears inconsistent with [AB 1440], since the tax is apparently not applied uniformly to residential and non-residential properties.'"[31] The Court of Appeal found this revealing, particularly because one of school districts involved

in drafting AB 1440 had a classification-based tax. Based on this record, it concluded that the Legislature had the same understanding of AB 1440 as the author of the cited letter.[32]

III. DIRECTION FROM SUBSEQUENT STATUTES

Finally, the Court of Appeal looked to statutes enacted after section 50079, which gave taxing authority to other local agencies. It focused on section 53730.1 (authorizing local healthcare districts to impose special taxes), Public Resources Code section 5789.1 (authorizing recreation and park districts to impose special taxes), and Senate Bill No. 158 (1991 Reg. Sess.) (enacting several statutes authorizing local agencies to levy special taxes including section 50079.1 noted above).[33] The Court of Appeal viewed "[t]his string of enabling legislation [as] further demonstrat[ing] that the definitional language at issue ... is language of limitation ...."[34] Summarizing the legislative history and statutory language of these statutes led the Court of Appeal to conclude that in enacting AB 1440, the Legislature understood that without express authorization, school districts could not "classify and differentially tax property within the district."[35]

The Court of Appeal partially struck Measure H, finding the District was only authorized to levy a single rate tax of $120 per parcel on all parcels. The California Supreme Court denied review and rejected multiple requests for depublications in July 2013.[36]

BORIKAS'S FULL IMPACT MAY NOT BECOME APPARENT FOR YEARS

On the surface, the impact of *Borikas* on school districts is fairly clear—school districts may not seek authorization from voters to levy classification-based taxes under section 50079. However, the direct impact of this ruling is actually relatively limited.

That is not to say there has not been a direct and immediate impact on some school districts. In January, counsel for the Plaintiffs in *Borikas* filed suit against four additional education parcel taxes seeking to invalidate them based on *Borikas*.[37] For these entities, *Borikas*'s impact is all too immediate and severe.

However, this direct impact has been muted by the fact that school district special taxes are protected by validation statutes.[38] These statutes require challenge to any special tax within 60 days;[39] if a challenge is not brought, the tax is immune from later challenge whether the tax is "valid or not."[40] Thus, many previously existing classification-based taxes may continue to be levied by school districts despite *Borikas*.

Equally as important as the immediate impacts of *Borikas* may be the harder to predict impacts of the opinion on future special taxes.

I. *BORIKAS* MAY PREVENT VOTER RENEWAL OF CURRENT TAXES & LIMIT FLEXIBILITY FOR NEW TAXES

While validation statutes may protect current special taxes, when current taxes expire—most are imposed for a period of several years—any voter authorized renewal of those taxes will need to comply with *Borikas* or face potential challenge. Ultimately, this means that many school districts will not be able to offer their voters the option to simply renew a special tax already in place, but will likely be forced to ask them to adopt taxes structured in ways which may result in a larger share of the tax

"Instead, it appears that the true impact of *Borikas* may not be felt until local agencies are required to squarely address questions left open by the opinion."

burden being borne by residential property owners.

Beyond inhibiting the ability of school districts to simply seek voter renewal of existing special taxes upon their expiration, *Borikas*'s interpretation of section 50079 means that school districts may have much less flexibility in crafting special taxes in the future. This may result in less equitable taxes and could make it more difficult to persuade voters to adopt such taxes.

II. *BORIKAS*'S HOLDING MAY LIMIT MANY LOCAL AGENCIES WHOSE STATUTORY TAXING AUTHORIZATION IS SIMILAR TO SCHOOL DISTRICTS

As the Court of Appeal noted in its opinion, AB 1440 was just the first of many bills which provided local agencies with statutory authorization to levy special taxes.[41] In the years that followed AB 1440, the legislature passed a number of bills providing similar authority to counties,[42] community college districts,[43] cities, counties and library districts for library services,[44] healthcare districts,[45] community service districts,[46] harbor districts,[47] port districts,[48] cemetery districts,[49] veterans memorial districts,[50] park and recreation districts,[51] resource conservations districts,[52] resort improvement districts,[53] public utility districts,[54] public utility districts,[55] airport districts,[56] transit districts,[57] irrigation districts,[58] county water districts,[59] and municipal water districts.[60] While not all of these statutes contain language identical to section 50079, all contain the basic "uniformity" requirement which served as the basis for the decision in *Borikas*.

While the Court of Appeal did not address the application of its holding to these statutes or local agencies beyond school districts, it is not difficult to imagine that an opponent could seize on the arguments and reasoning of *Borikas* to attack non-school district special taxes where the local agency's statutory authorization is at least similar to section 50079. Thus, in the same way that *Borikas* limits the taxing authority of school districts, it is possible it could also impact the flexibility otherwise provided to other local agencies in crafting special tax measures.

III. UNCERTAINTY CREATED BY *BORIKAS* MAY BE AS PROBLEMATIC AS ITS HOLDING

Beyond the explicit implications of *Borikas*—that classification-based taxes cannot be levied by school districts—the questions *Borikas* raises and does not answer may be equally problematic for local agencies. The most poignant example of this ambiguity is the extent to which *Borikas* prohibits any tax structures other than a single fixed dollar amount per parcel.

For example, many school districts and other local agencies apply special taxes based on square footage of lot. While *Borikas* did not necessarily prohibit such tax structures, its reasoning may call such taxes into question. Such taxes do not necessarily classify parcels in that the same rate is applied to all parcels, but they result in different amounts of tax being levied depending on the characteristics of various parcels.

Many of these questions could be addressed—or the result of *Borikas* could be counteracted—by the Legislature, but attempts to do so have been unsuccessful to date. Assemblymember Bonta introduced Assembly Bill No. 59 (2013-14 Reg. Session) shortly after *Borikas* was released. It proposed to revise section 50079 to clarify that the Legislature did not intend to prohibit classification-based taxes. However, the bill has yet to make it out of legislative committee, suggesting that the more likely source for clarification of the questions raised by *Borikas* is future litigation.

ULTIMATELY, *BORIKAS* MAY PUT SPECIAL TAXES OUT OF REACH FOR SOME LOCAL AGENCIES

While *Borikas* limits special taxes, it does not prevent them. However, the limitation it imposes will make it more difficult for school districts and local agencies to authorize such taxes. Notwithstanding *Borikas*, obtaining a two-thirds majority to authorize a special tax is no small feat. Now school districts and local agencies may lose the ability to eliminate the inequalities that can result from oversimplified tax structures or to craft those taxes in the ways voters desire. Moreover, *Borikas* creates uncertainty and the specter of litigation over special taxes. This in and of itself may be reason enough for some local agencies to decide to avoid special taxes or at least avoid the most advantageous structure for those taxes.

Until another court or the Legislature act to remove the impediments and uncertainty created by *Borikas*, these limitations are likely to hamstring attempts to seek voter authorization to renew and adopt new special taxes, impairing the ability of local agencies to fund important programs and services in the future.

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Endnotes

1 Cal. Const., art. XIII A, § 4.

2 *California Bldg. Industry Assn. v. Governing Bd. of the Newhall Sch. Dist. of Los Angeles Cnty.* (1988) 206 Cal.App.3d 212, 222-23 ("CBIA").

3 Unless otherwise noted, all statutory references are to the Government Code.

4 Stats. 1979, ch. 903; see *Beaumont Investors v. Beaumont-Cherry Valley Water Dist.* (1985) 165 Cal. App.3d 227, 234 (section 50075 enacted to "implement the authorization grated by section 4"). As originally enacted, it was unclear if section 50075 applied to school districts. However, the Legislature sought to include school districts under this authority through amendment in 1980. Stats. 1980, ch. 672; see *CBIA, supra, 206* Cal.App.3d at p. 223.

5 § 53727, subd. (a).

6 *CBIA, supra*, 206 Cal.App.3d at p. 224 (holding the authority provided by section 50075 was withdrawn by Proposition 62).

7 After Proposition 62, Assemblymember Hannigan sought the opinion of the Legislative Counsel which concluded that the ballot measure had removed the special taxing authority from school districts. (Ops. Cal. Legis. Counsel, No. 3061 (April 17, 1987) Voter Approval of Special Taxes Levied by School Districts.)

8 Although such taxes are termed "special taxes" or "qualified special taxes," most special taxes are referred to as "parcel taxes," as they are levied on parcels of real priority.

9 *CBIA, supra, 206* Cal.App.3d at p. 224 (noting Proposition 62 confirmed that article XIII A, section 4 require implementing language).

10 Stats. 1987, ch. 100. Section 50079 was amended in 2006 (stats. 2006, ch. 41) and in 2012 (stats. 2012, ch. 791) to allow exemptions for those "receiving Supplemental Security Income for a disability, regardless of age" and those "receiving Social Security Disability Insurance benefits, regardless of age, whose yearly income does not exceed 250 percent of the 2012 federal poverty guidelines issued by the United States Department of Health and Human Services."

11 Cal. Dept. of Finance, Enrolled Bill Rep. on Assem. Bill No. 1440 (1987-88 Reg. Sess.) July 1, 1987, p. 1.

12 *Id.* at p. 2.

13 EdSource, *Raising Revenue Locally, Parcel Taxes in California School Districts 1983-2012*, p. 8 ("*Raising Revenue*"), available at http://www.edsource.org/pub13-parcel-tax-local.html. Although AB 1440 clarified the ability of school districts to levy parcel taxes, some school districts had levied voter-approved special taxes as early as 1983.

14 *Id.* at p. 7. Noting the number of current special taxes is nearly double that of 2003-04.

15 *Id.* at p. 9.

16 *Id.* at p. 25.

17 Voters in about a dozen school districts in the last decade have adopted classification-based parcel taxes including the Alameda Unified School District, the school district involved in *Borikas*. (*Raising Revenue, supra*, p. 6.)

18 See *Heckendorn v. City of San Marino* (1986) 42 Cal.3d 481, 488 (suggesting that flat rate of tax per parcel on all parcels may create an "unjust result" which is constitutionally suspect).

19 Albany Unified School District, one of several school districts intimately involved with the drafting of AB 1440 had adopted a classification-based tax prior to AB 1440 and renewed the tax within one year of section 50079's enactment.

20 The challenge also took issue with the requirements Measure H placed on the exemptions otherwise authorized by section 50079. The Court of Appeal ultimately upheld these conditions. (*Borikas, supra*, 214 Cal.App. 4th at p. 169.)

21 *Borikas, supra*, 214 Cal.App.4th at p. 142.

22 While *Borikas* was pending on appeal, another challenge was filed against the District's Measure A, another classification-based tax proposed by the District and approved by voters in part to replace Measure H before it would otherwise expire. (*Nelco, Inc. v. Alameda Unif. Sch. Dist.*, Alameda Cnty. Super. Ct., Case No. RG08405984.) Like Measure H, Measure A was upheld by the trial court; however, the challengers in that case did not choose to appeal the ruling as to Measure A.

23 *Borikas, supra*, 214 Cal.App.4th at pp. 139-40. The Court of Appeal originally released its opinion on appeal in December 2012 (*Borikas v. Alameda Unif. Sch. Dist.* (2012) 211 Cal.App.4th 833, rehg. granted Jan. 7, 2013); however, in January 2013, it accepted the District's Petition for Rehearing. It issued its final opinion in March 2013. The original and final opinions came to identical conclusions based on essentially the same reasoning.

24 *Borikas, supra*, 214 Cal.App.4th at pp. 165-68.

25 The final opinion issued on rehearing also included a concurring opinion from Presiding Justice Marchiano stressing the plain language of the statute and questioning the need to rely on legislative history to reach the court's conclusion. (*Borikas, supra*, 214 Cal.App.4th at pp. 170-72 (conc. opn. of Marchiano, P.J.).

26 *Id.* at p. 151.

27 *Ibid.*

28 *Id.* at pp.151-52.

29 *CBIA, supra*, 214 Cal.App.4th at p. 152.

30 *Borikas, supra*, 214 Cal.App.4th at p. 154, quoting Thomas Steele, letter to Robert Caine, Superintendent of the Kentfield School Dist., June 9, 1987, p. 3.

31 *Ibid.*

32 *Id.* at p. 157.

33 *Borikas, supra*, 214 Cal.App.4th at pp. 159-164.

34 *Id.* at p. 163.

35 *Id.* at p. 164.

36 The District's Petition for Review and Request for Depublication were supported by the California School Boards Association, the California Coalition for Adequate School Housing, the California Teachers Association, several individual school districts, and the California Library Association. The California Special Districts Association and Association of California Healthcare Districts also supported the Petition for Review while submitting separate Requests for Depublication.

37 *Bypass 93 Properties v. West Contra Costa Unif. Sch. Dist.*, Contra Costa Cnty. Super. Ct., Case No. MSC13-00024; *Granda v. Davis Jt. Unif. Sch. Dist.*, Yolo Cnty. Super. Ct., Case No. CV13-18; *Suarez v. Centinela Valley Union High Sch. Dist.*, Los Angeles Cnty. Super. Ct., Case No. BC498402; and, *Williams Properties v. San Leandro Unif. Sch. Dist.*, Alameda Cnty. Super. Ct., Case No. RG13662223.

38 See § 50077.5 (making the validation procedures of Code of Civ. Proc., § 860 et. seq. applicable to special taxes); see also *Katz v. Campbell Union High School Dist.* (2006) 144 Cal. App.4th 1024, 1027 (applying validation procedure in challenge to school district parcel tax).

39 Code Civ. Proc., §§ 860, 863.

40 *City of Ontario v. Super. Ct.* (1970) 2 Cal.3d 335, 341-42.

41 *Borikas, supra*, 214 Cal.App.4th at pp. 158-168.

42 § 23027.

43 § 50079.1.

44 § 53717.

45 § 53730.01.

46 § 61121.

47 Harb. & Nav. Code, § 6092.5.

48 *Id.* at § 6364.

49 Health & Saf. Code, § 9081.

50 Mil. & Vet. Code, § 1192.5.

51 Pub. Resources Code, § 5789.1.

52 *Id.* at § 9513.

53 *Id.* at § 13161.6.

54 Pub. Util. Code, § 12891.

55 *Id.* at § 16641.5.

56 *Id.* at § 22909.

57 *Id.* at § 25892.

58 Wat. Code, § 22078.5.

59 *Id.* at § 31653.

60 *Id.* at § 72090.5.

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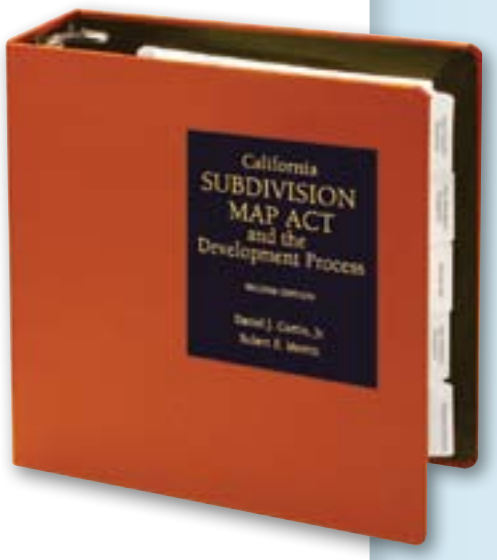

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USC Law Student Wins Public Law Student Writing Competition

This year, the Public Law Executive Committee honored Jennifer Lai as the winner of its student writing competition. Ms. Lai, a third year law student at University of Southern California Gould School of Law, receives the $2,000 cash prize for winning the award.

Ms. Lai's article, "California Environmental Quality Act ("CEQA") Reform: Standing as a Tool to Limit Cases Unrelated to CEQA's Purposes," examines using traditional standing principles as a means to accomplish the Legislatures stated goal of streamlining development in California by reducing the number of projects challenged in court using CEQA. The article is published in this edition of the Journal at page 32.

Ms. Lai earned her undergraduate degree magna cum laude in Political Science from Loyola Marymount University. Prior to law school, she interned at the San Francisco City Planning Department working on the Western South of Market Community Plan's EIR process. While in law school, she interned at the Sierra Club, NBC Universal's Government Affairs Department, Wood Smith Henning & Berman, and externed full-time at the U.S. District Court for the Central District of California.

Ms. Lai received her award at the Public Lawyer of the Year award ceremony at the Annual State Bar meeting in San Jose on October 11, 2013. She looks forward to a career practicing land use and environmental law.

The Public Law section sponsors its Student Writing Competition each year. The competition is open to students at all California-accredited law schools, and the winner receives a $2,000 cash prize and their article is published in the Section's Public Law Journal.

Jennifer Lai with her mother, Susan Wong

Student Writing Competition winner Jennifer Lai with Student Writing Competition's Co-Chairs Rachel Sommovilla (left) and Caroline Fowler, with Chief Justice Cantil-Sakauye

CALIFORNIA ENVIRONMENTAL QUALITY ACT ("CEQA") REFORM: THE DOCTRINE OF STANDING AS A TOOL FOR CEQA REFORM

*By Jennifer Lai**

I. INTRODUCTION

The principles and mechanisms of the California Environmental Quality Act, ("CEQA"), contained at California Public Resources Code section 21000, et. seq., are under substantial criticism for being abused and for impeding economic growth and good planning. CEQA reform is shaping up to be a big legislative battle in the 2013 session.[1] Pitted on one side are organized labor and environmental groups who hold CEQA as a landmark regulation that should remain unchanged; on the other side is the business community who holds that CEQA has delayed development and been used to raise costs for competitors or extract payments from project proponents and, thus, needs to be reformed.[2] California Governor Jerry Brown has been very vocal about his intent to ensure CEQA reform happens, calling it "the Lord's work."[3] Recently, in the 2011-2012 legislative sessions, legislators responded to CEQA reform demands by establishing litigation streamlining provisions and exempting projects completely from CEQA review.[4] However, these legislative responses do not solve the abuses of CEQA; rather, they make special accommodations for projects where developers have resources to lobby for specialized legislation. Instead, legislators need to look at where the abuses are happening within CEQA and find ways to limit them, without defeating the main principles of CEQA, which are accountability and transparency.

A large controversy over the existing CEQA process is how easy it is to bring a suit. The ability for the public to challenge projects that do not meet existing environmental standards is a pivotal portion of the law. However, there is no denying that the pervasive threat of being sued under CEQA can complicate and further burden a project. Examples of abusive CEQA litigation are anti-competitive litigation brought by businesses, citizens suits by groups pursuing social and economic agendas unrelated to environmental protection, and suits by "NIMBY" (Not in my backyard) neighbors seeking to delay or derail unwanted projects.[5]

This paper attempts to address whether anything can be done to prevent abusive CEQA lawsuits that are motivated purely by economic desires rather than genuine environmental concerns. This paper will argue that a way to reduce this type of abusive CEQA free-ranging litigation activity is using the legal doctrine of standing to reduce cases that are not concerned with environmental protection, without barring other meritorious CEQA actions. A meaningful CEQA reform legislation will limit the broad standing rules to exclude parties who are not motivated by environmental concerns.

II. CEQA—A LEGAL FRAMEWORK

On January 1, 1970, President Richard Nixon signed into law the National Environmental Policy Act ("NEPA").[6] Shortly thereafter, modeling itself after its federal counterpart, the California Legislature passed the California Environmental Quality Act ("CEQA").[7] CEQA establishes a process that requires public agencies to analyze environmental impacts of significant proposed projects, both private and public.[8] Forty-three years later, CEQA's expansive character makes it an extremely controversial statute as it governs the review and approval process of all developments in California.

A CEQA process is triggered whenever a project requires discretionary approval by a government agency.[9] Once the agency deems an activity a "project" subject to CEQA, the lead agency must prepare an Initial Study ("IS") to determine whether the project may have a significant effect on the environment.[10] An Environmental Impact Report ("EIR") shall be prepared if the IS indicates that the project may have a significant effect on the environment.[11] The

EIR is not meant to just identify and acknowledge adverse impacts to the environment. It must also describe any mitigation measures or project alternatives to lessen the negative effects on the environment.[12] The EIR is the "heart of CEQA."[13]

A large component of CEQA is its ability to provide individuals with the opportunity to participate effectively in all steps of the environmental review process. The public's right to participate in CEQA's process is mandated in the statute itself[14] and vigilantly protected by the California courts, emphasizing the public holds a "privileged position" in the CEQA process.[15] A member of the public may legally challenge an agency's decision during the CEQA process only if "all available administrative appeals and remedies" have been pursued during the CEQA process.[16] The courts' recognition of public participation in administrative policies, reinforced by legal tools, gives the public a substantial role in land use planning in California.

III. DOCTRINE OF STANDING UNDER CEQA

Standing is the legal right to bring a lawsuit to court.[17] Standing is a threshold jurisdictional issue to ensure that the proper parties bring a matter to the court for adjudication, and can be raised at any time during the proceedings. It plays an important role in ensuring that courts only adjudicate disputes between parties with a real stake in the outcome and prevents the courts from issuing advisory opinions. Therefore, the ability to dismiss a lawsuit based on a standing challenge makes it a powerful procedural strategy in litigation.

A. Beneficial Interest under Code of Civil Procedure § 1086

To have standing to compel a government action under a traditional writ of mandamus, the party must be "beneficially interested" pursuant to California Code of Civil Procedure ("CCP") § 1086. Beneficial interest is generally defined as having "some special interest to be served or some particular right to be preserved or protected over and above the interest held in common with the public at large."[18] This means that the party must show that it will obtain some direct and substantial benefit from the issuance of the writ or suffer a detriment from its denial.[19]

B. Public Interest Standing or Citizen Standing

An exception to the "beneficially interested" requirement for standing is "public interest standing" or "citizen standing."[20] The courts have held that in the absence of a beneficial interest, if the question is one of public right and the object of the action is to enforce a public duty, the party will have public interest standing. The policy underlying public interest standing is that citizens should be guaranteed the opportunity to ensure that "no governmental body impairs or defeats the purpose of legislation establishing a public right."[21] The court has held that the propriety of a citizen suit requires judicial balancing of interests and can be found appropriate "when the public duty is sharp and the public need weighty."[22]

C. No Standing for Commercial and Competitive Interests

In *Waste Management v. County of Alameda*, a private landfill operator sued the County of Alameda after it approved a competitor's waste disposal permit without an EIR.[23] Previously, Waste Management was required to go through a permit revision under CEQA and had to prepare an EIR. Therefore, when their competitor, Browning-Ferris, was given a permit without undergoing CEQA review, Waste Management appealed the permit arguing CEQA review was required.

First, the court in Waste Management held that to have standing under CCP §1086 as a beneficially interested party, the interest the party is seeking to advance must be within the "zone of interests" to be protected or regulated by the legal duty asserted.[24] The zone of interests test, first articulated in the 1970 federal case *Association Data Processing Service Organization v. Camp*[25] and used in NEPA standing analysis, stated the zone of interest test as: "The interest [the plaintiff] asserts must be 'arguably within the zone of interests to be protected or regulated by the statute' that he says was violated."[26] The Court of Appeal held that Waste Management was not a beneficially interested party because its interest in imposing greater regulatory costs upon a competitor was not within the zone of interests CEQA was meant to protect.[27] "CEQA is not a fair competition statutory scheme… None of [the goals] suggests a purpose of fostering, protecting, or otherwise affecting economic competition among commercial enterprises."[28]

Second, the court analyzed whether Waste Management can obtain public interest standing. The court reasoned that because Waste Management was a corporate entity, to establish public interest standing, the corporate entity had to demonstrate the "attributes of a citizen litigant" through several factors.[29] After analyzing the factors, the court held that Waste Management could not establish public interest standing because "it is pursuing its own economic and competitive interests, rather than any demonstrable interest in the environmental concerns which are the essence of CEQA."[30]

Waste Management served as guidance for cases thereafter.[31] It set out a workable standard that a litigant's interest had to fall within the "zone of interest" that the applicable law was meant to protect – in this instance, environmental concerns. The standard articulated in *Waste Management* would limit lawsuits brought by those who are not motivated by environmental concerns, but mainly use CEQA as an abusive anti-competitive tactic.

D. Lowering the Bar for Standing

The recent California Supreme Court case, *Save the Plastic Bag Coalition v. City of Manhattan Beach*,[32] dealt with the issue of corporate standing under CEQA. The City of Manhattan Beach circulated a report containing a proposed ordinance that would ban the use of plastic bags at licensed retail establishments.[33] Save the Plastic Bag Coalition, formed by private businesses and manufactures within the plastic bag industry, petitioned for a writ of mandamus to force the City to prepare an EIR.[34] The City of Manhattan Beach argued that Save the Plastic Bag Coalition had no standing to bring a CEQA suit under the holding of *Waste Management*, because it was seeking to advance its commercial and economic interests, not actual environmental concerns.[35]

First, the court held that Save the Plastic Bag Coalition had standing to sue as a beneficially interested party under CCP § 1086. The court held that they did not need to resort to the public interest exception, but instead "plainly possess the direct, substantial sort of beneficial interest required" under CEQA.[36] The court reasoned that because the ordinance's ban on plastic bags would have an effect on their business that this was a "particular right to be preserved and protected over and above the interest held in common with the public at large."[37] The court essentially rejected *Waste Management*'s zone of interest test that a plaintiff needed to be impacted by an adverse environmental effect to sue under CEQA; rather, economic interest permitted beneficial interest standing under CEQA.

Second, the court analyzed Save the Plastic Bag Coalition's ability to sue under "public interest" standing. Rejecting the *Waste Management* factors, the court looked to the Coalition's argument and held that they offered some environmental arguments and thus had standing. Under the facts of *Save the Plastic Bag Coalition*, it seems that merely a nominal showing of environmental concern is sufficient to show standing.[38]

With such liberal standing rules established by the California Supreme Court in *Save the Plastic Bag Coalition*, lead agencies and project proponents will now be exposed to expend millions each year defending or settling suits that do not advance the environmental purposes of CEQA. Moreover, these sums do not account for the enormous expenses arising from the delays that can ensue once a project is challenged in court. Liberal standing rules now open the gates for parties to use the threat of lawsuits and lawsuits as tools to thwart their competitors and extract payments or favorable terms for a project.

IV. LIMITING STANDING TO CASES THAT ARE RELATED TO CEQA'S PURPOSES

An effective CEQA reform legislation will limit CEQA standing only to parties that can demonstrate a direct potential environmental harm that would result from the project. First, the legislation should require that the lawsuit is within the "zone of interest" CEQA seeks to protect. The federal courts have set out such a standing doctrine for NEPA, which requires court to look at whether the harm the party is alleging is within the zone of interests of the statute. This will not bar meritorious CEQA actions, because just like under NEPA, if the economic consideration bears a substantial relationship to a real environmental interest, the interest would be in CEQA's zone of interest. In cases where plaintiffs attempt to bring economic injuries within CEQA by alleging remote environmental effects, standing would be denied. This would help eliminate some of the most egregious examples of CEQA abuses.

Second, a legislative reform should limit the "public interest" exception to only non-profit groups or individuals with a demonstrated

history of actual public interest commitment through environmental advocacy or litigation. The courts have stated that the public interest suit is an exception to the beneficial interest writ standing requirement. If parties cannot demonstrate a direct and substantial interest in the lawsuit and proceed persuant to the public interest exception, the parties should be subjected to meaningful scrutiny. Corporate organizations or individuals with a history of vexatious CEQA litigation trying to assert standing under the public interest exception should be required to plead with specificity their past litigation and environmental advocacy history. Such standing hurdles for corporations, associations, or individuals who abuse CEQA lawsuits will limit the amount of delay and harassment on project proponents.

V. CONCLUSION

Courts must balance the competing policies of preventing unwarranted lawsuits by inappropriate parties whose interests are not protected within the statute against the danger of preventing parties who suffer injury from "getting their day in court." CEQA litigation is a powerful and frequently used tool that can delay or stop projects and should thus be relegated to the purposes for which the CEQA statute was intended.

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Endnotes

1 John Howard, "The Battle for CEQA" CAPITOL WEEKLY (Jan. 24, 2013) available at http://www.capitolweekly.net/article.php?xid=116395uhwgjhsts ("California's core environmental protection law, a 43-year-old statute frequently denounced by developers and business interests as a tangle of red tape, is on a Capitol hit list once again.")

2 Steven Harmon, "Reform of California's landmark environmental law is on life support." MERCURY NEWS (April 07, 2013) available at *http://www.mercurynews.com/california-budget/ci_22974449/reform-californias-landmark-environmental-law-is-life-support.*

3 Joe Garofoli, "CEQA Future Tied to Oakland's Experience," SF GATE (Feb. 26, 2013) available at *http://www.sfgate.com/politics/joegarofoli/article/CEQA-future-tied-to-Oakland-s-experience-4308007.php.*

4 *See* Senate Bill 292 (expediting judicial review progress for the development of a stadium, Convention Center Modernization and Farmers Field Project, in the City of Los Angeles); Assembly Bill 900 (expediting review procedures for any project that the Governor certifies as "environmental leadership development projects"); Assembly Bill 226 (statutorily exempting Solar PV projects on commercial and industrial roof tops and exisiting parking lots from CEQA review); Assembly Bill 381 (exempting City of Industry's stadium project from CEQA review).

5 *See* Tina A. Thomas, "CEQA Turns Twenty-One: In Defense of CEQA," *Land Use Forum*, Vol. 2, No. 2 (Spring 1993) (formulating three categories of abusive CEQA litigation).

6 National Environmental Policy Act (NEPA) of 1969, 42 U.S.C. §§ 4321–47 (Westlaw 2012).

7 Several other states, such as Connecticut, Hawaii, Indiana, Maryland, Massachusetts, Minnesota, Montana, New York, North Carolina, South Dakota, Virginia, Washington and Wisconsin, have also passed mini-NEPAs at the state level.

8 California Public Resources Code §§ 21000, et. seq.

9 California Public Resources Code § 21080.

10 California Code of Regulations §§15060, 15063, 15102, 15365. The IS determines whether the lead agency needs to proceed and prepare a Negative Declaration, a Mitigated Negative Declaration, or a full EIR. Negative Declaration ("ND") is prepared if the project will not have a significant environmental impact. Another option is if the IS shows potentially significant effects on the environment, but can be easily revised to avoid or mitigate the effects, a Mitigated Negative Declaration ("MND") can be prepared in lieu of an EIR

11 *Id.* at §§15065, 15081. The lead agency can decide to do the EIR in house or hire a consultant to prepare it. The Applicant bears the cost of preparing an EIR. The legal standard for determining significance of impacts is whether a "fair argument" can be made on the basis of "substantial evidence" that a potential environmental effect could be significant. Public Resources Code § 21168 specifies that "the court shall not exercise its independent judgment on the evidence but shall only determine whether the act or decision is supported by substantial evidence in light of the whole record." The purposes of an EIR are to examine the potential adverse effects on the environment, disclose them to decision-makers and the public, and specify feasible mitigation measures and project alternatives.

12 Mitigation of environmental impacts might include avoiding a particular action altogether, limiting the degree of a proposed action, rectifying the impact of the action, or compensating for the impact of the action. (14 C.C.R § 15370). *See also* Douglas P. Carstens and Arthur Pugsley, "The Recent Re-emergence of CEQA's Substantive Mandate" *Environmental Law Reporter*, v. 2 (March 2008) for further analysis of CEQA's substantive mandate.

13 *County of Inyo v. Yorty*, 32 Cal. App. 3d 795, 810 (1973). The lead agency can prepare a statement of overriding consideration, if they can present with evidence, that the project's benefits outweigh the unavoidable significant effects on the environment. Public Resources Code § 21081 provides: "[N]o public agency shall approve or carry out a project for which an environmental impact report has been certified which identifies one or more significant effects on the environment that would occur if the project is approved or carried out unless both of the following occur:

(a) The public agency makes one or more of the following findings with respect to each significant effect:

(1) Changes or alterations have been required in, or incorporated into, the project which mitigate or avoid the significant effects on the environment.

(2) Those changes or alterations are within the responsibility and jurisdiction of another public agency and have been, or can and should be, adopted by that other agency.

(3) Specific economic, legal, social, technological, or other considerations, including considerations for the provision of employment opportunities for highly trained workers, make infeasible the mitigation measures or alternatives identified in the environmental impact report.

(b) With respect to significant effects which were subject to a finding under paragraph (3) of subdivision (a), the public agency finds that specific overriding economic, legal, social, technological, or other benefits of the project outweigh the significant effects on the environment.)."

Note that the overriding considerations were not in the original CEQA statute.

14 Public Resources Code §21083.

15 *Concerned Citizens v. Costa Mesa, Inc. v. 32nd District Agricultural Ass'n.* 42 Cal. 3d 929 (1986).

16 Public Resources Code §21167

17 *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 559, 112 S.Ct. 2130, 119 L.Ed.2d 351 (1992).

18 *Carsten v. Psychology Examining Committee of the Board of Medical Quality Assurance*, 614 P.2d 276, 278 (1980).

19 *See Waste Mgmt. v. County of Alameda*, 79 Cal. App. 4th, 1223, 1233 (2000).

20 *See, e.g., Dix v. Superior Court*, 53 Cal.3d 442 (1991).

21 *Green v. Obledo*, 29 Cal. 3d 126, 144 (1981).

22 22 *Waste Mgmt v. County of Alameda,* 79 Cal.App.4th 1223, 1237 (2000).

23 *Id.* at 1233.

24 *Id.*

25 *Ass'n of Data Processing Serv. Orgs. v. Camp*, 397 U.S. 150 (1970).

26 *Id.* at 153.

27 *Id.* at 1235.

28 *Id.*

29 *Id.* at 1238. Among the factors that may be considered are whether the corporation has demonstrated a continuing interest in or commitment to the subject matter of the public right being asserted; whether the entity is comprised of or represents individuals who would be beneficially interested in the action; whether individual persons who are beneficially interested in the action would find it difficult or impossible to seek vindication of their own rights; and whether prosecution of the action as a citizen's suit by a corporation would conflict with other competing legislative policies.

30 *Id.* at 1239.

31 *See Regency Outdoor Ad. Inc., v. City of West Hollywood*, 152 Cal. App. 4th 825 (2007) (holding because Regency pursued the litigation "to promote its commercial or competitive interests," it had no standing to sue under CEQA).

32 *Save the Plastic Bag Coal. v. City of Manhattan Beach*, 254 P.3d 1005 (Cal. 2011).

33 *See* Jennie Romer & Shanna Foley, "Wolf in Sheep's Clothing: The Plastic Industry's Public Interest Role in Legislation and Litigation of Plastic Bag Laws in California," 5 *Golden Gate U. Envtl. L. J.* 377 (2012).

34 *Save the Plastic Bag Coal.*, at 1010-11.

35 *Id. See also* Jessica Diaz, "Save the Plastic Bag Coalition v. City of Manhattan Beach: California Supreme Court Answers More than 'Paper or Plastic?' in Major Decision on Corporate Standing under CEQA," *Ecology Law Quarterly* v.39, 627-634 (2012), for the procedural history of case.

36 *Save the Plastic Bag Coal.*, at 1014.

37 *Id.* (quoting *Carsten v. Psychology Examining Comm. of Bd. of Med. Quality Assurance*, 614 P.2d 276, 278 (1980)).

38 *Id.* at 1009.

PUBLIC-PRIVATE PARTNERSHIPS IN CALIFORNIA

*By B. Scott Douglass and Jeffrey A. Sykes**

Public-private partnerships ("P3s") cannot completely meet our increasing infrastructure needs, but they should be part of the mix. P3s have been successfully used for decades in Europe, Canada and Australia to develop public infrastructure projects.[1] They have also been available for use in California for nearly twenty years, but they have not been widely embraced by California public agencies despite their benefits. This is the second installment of a two-part article on P3s and "best practices" for addressing California's infrastructure needs through private funding. In Part I, which appeared in the Public Law Journal's Summer 2013 edition, the definition of P3s and various forms of P3s were initially examined. The legal framework and enabling legislation for the use of P3s by California's local government agencies was also covered. In this Part II, we drill down further on P3s, examining the pros and cons of developing infrastructure projects on a P3 basis, and then relay a recent P3 success story and "best practices" for establishing and implementing P3 programs.

PROS AND CONS OF P3S

At its core, P3 projects involve private financing and the sharing of a project's risks and rewards beyond the construction phase between private and public partners. Projects built under a P3 approach can have far-reaching benefits that go beyond the mere completion of infrastructure projects that would be infeasible under a traditional public-funding model. Building projects on a P3 basis generally means that such projects get built quicker, better and at less cost than would be the case if the project were built under a traditional design-bid-build basis with solely public funds. The reason for this is several-fold. Initially, P3 projects get built quicker because they are usually developed on a design-build basis where the design phase and construction phase occur simultaneously, with design just a step ahead of construction (called "fast-tracking" in the construction industry), such that the overall duration of the project from design through construction is reduced.

Additionally, the private partner is incentivized to complete the project as quickly as possible, even if the project requires acceleration through additional workforce or overtime, because the private partner is usually not paid until after the project has been satisfactorily constructed and is operating to pre-determined performance requirements. This delayed-payment component also has a cash-flow benefit to the public partner. Instead of incurring significant costs for design and construction at the front-end of a project, as would be the case under a traditional delivery method, the public partner's costs (or the cost to the users of the public facility) are postponed until construction is completed and then the costs tend to gradually increase for the duration of the P3 agreement. This, in turn, allows the public partner to leverage whatever funds it has "saved" on the front-end, thereby stretching tax dollars for other purposes or to develop other projects that would not be appropriate for pursuit on a P3 basis.

Another significant cash-flow benefit to public partners arising from P3s is that P3 agreements frequently include an upfront cash payment from the private partner. This cash infusion can be used by the public partner to retire existing debt or can be used for other public purposes. Retiring public debt removes liability from the public sector's balance sheet, which positively impacts the public partner's credit rating and reduces financing costs for future barrowing and bond sales. Similarly, the cost to build or upgrade a P3 facility is not on the public entity's balance sheet, which

also positively impacts the public partner's credit rating.

Further, in terms of lower costs generally for a P3 project, because P3 projects are typically fast-tracked, labor and materials to construct the project are purchased sooner. This means the escalation costs that normally accompany later-purchased labor and materials due to inflation or other market conditions are avoided.

In addition, P3 projects can be done under a design-build-finance-operate-maintain ("DBFOM") approach by which the obligations to do such tasks are packaged together and transferred to the government agency's private sector partner. Under a DBFOM approach, the full lifecycle costs for the infrastructure facility are generally less than what they otherwise would be under a traditional project delivery method, or even under a design-build delivery method.[2] This is because the DBFOM project benefits from multiple efficiencies. The private partner is incentivized to design and construct the project to the highest standards with best practices for operation and maintenance of the completed facility in mind. If the private partner were to not design and construct to such standards (or tried to cut corners in other ways), the cost to operate and maintain the facility for the duration of the P3 agreement would be higher and would erode the private partner's rate of return on its investment. Some liken this to an extended warranty for the public partner that can last as long as the term of the P3 agreement.

Aside from time, cost and quality benefits, the P3 approach is also advantageous to public partners from a liability perspective. Specifically, the risks stemming from design and construction of the public facility are shifted from the public partner to the private partner under P3 agreements. Therefore, the private partner is the single point of contact for the public partner, responsible for any shortcomings in a P3 project's design, construction, operations, and maintenance in the case of a DBFOM project. This avoids the "liability gap" that public entities frequently find themselves in, and the inevitable finger pointing that arises between the public entity's designer and contractor, when a facility's performance is deficient and the project was delivered under a traditional design-bid-build method.[3]

There are other, less tangible but equally important benefits that P3 projects can offer public partners. For instance, where a P3 project includes post-construction operation and maintenance by the private partner, the public partner can remove itself from the day-to-day operations and maintenance of the facility (while maintaining appropriate oversight) and focus on its core strengths. So, in the case of a wastewater or water treatment facility, for example, which requires expertise to operate and maintain correctly, the public partner can use the private partner to operate and maintain the facility consistent with the latest innovations, efficiencies and best practices that the private sector has to offer. (These private partner contributions, which would be difficult for many public entities to match, include asset management and preventive-and-predictive maintenance programs that drive cost-efficient capital investments to assure best lifecycles costs for delivered services.) Thus, the shifting of operation-and-maintenance functions to a private partner allows the public partner to focus on other community services and priorities.

Additionally, in terms of some of the wider-ranging benefits that P3s offer, construction projects generate jobs and increase government tax revenues. According to the Associated General Contractors of America, for each $1 billion invested in construction, 28,500 jobs are created or sustained, adding about $1.1 billion to personal earnings and about $3.4 billion to the nation's GDP.[4] The growth in jobs, personal earnings and revenue for local businesses, in turn, generate additional revenue for public entities in the form of taxes.

Although P3s can offer many direct and indirect benefits, P3s do not come without their challenges. Chief among them is the increased complexity of P3 deals. Despite some common characteristics that P3 projects share, each P3 agreement is unique and there is no "form" P3 agreement used in the United States. The delivery of projects on a P3 basis requires significant legal and technical input to both the public partner and the private partner.[5] Additionally, because P3 projects are relatively rare in California, there is a general lack of familiarity with the P3 delivery model. Therefore, P3 deals currently tend to take a long

time to come together, and involve high transactional costs, making the delivery of a project on a P3 basis inappropriate unless the project is of adequate size and cost. However, as P3 programs become more common and standardized in California, P3 deals should become more streamlined, meaning that the project-cost threshold should decrease for P3 projects.

Further, there seems to be a public perception problem with respect to P3 projects. Some concerns include fears that: P3s cause the total privatization of public infrastructure assets and the loss of public control over such assets; [6] P3 projects cost more than those paid for by public funds;[7] P3s hold the public responsible for the private sector's mistakes;[8] and P3s make the private sector rich.[9] These concerns are unfounded and are prevented by the terms of most P3 agreements. Nevertheless, these concerns exist and can make it difficult for a public entity (and especially its elected officials) to pursue projects on a P3 basis.

A RECENT P3 SUCCESS STORY

Although California's P3 enabling statutes for local government agencies have been in existence for nearly twenty years, there is only one significant project known to the authors that was pursued under these statutes. That P3 project was recently undertaken by the City of Rialto, a city 60 miles east of Los Angeles, on a DBFOM basis. The private partner on that project closed its debt and equity financing for $176 million in late-November 2012.

Rialto, like many other California cities, has aging water and wastewater systems and treatment facilities. It had deferred rate increases and capital maintenance investments for a decade. It needed to upgrade and expand its systems and facilities, but it neither had the funds nor the public debt financing ability to pay for this work. Instead, it decided to pursue the project on a P3 basis, so that it could finance the project with private funds and avoid significant upfront costs, benefit from the technical, commercial and financial skills and expertise of the private sector, and focus on its core city management competencies, which did not include operating and maintaining water and wastewater systems and treatment facilities. It should be noted that Rialto put the concession's substantial rate increases to a Proposition 218 vote before entering into a P3 agreement. The residents of Rialto passed the measure, even though the rate increases were set to be twenty-five percent per year for the first four years of the P3's term, and Rialto then finalized the P3 concession procurement.

After three years of negotiation, Rialto and its special purpose joint powers agency, the Public Utility Authority, entered into a P3 agreement with a private entity partner to design, build and finance upgrades and expansions to Rialto's water and wastewater facilities. The P3 agreement required the private partner to construct such facilities and upgrades within the first five years of agreement and required the private partner to operate and maintain the systems and facilities for the agreement's entire 30-year term. [10] A capital improvements plan was established by Rialto, its private partner and various technical experts for the initial upgrades under a collaborative approach with objectives of rectifying deferred capital investments, implementing robust maintenance programs over the concession term and beyond, and optimizing life-cycle costs. It is estimated that the work to upgrade and expand the facilities in the short term will generate 445 construction jobs.[11]

Additionally, under the P3 agreement for Rialto's water and wastewater systems and treatment facilities, the Public Utility Authority's existing debt of $27.4 million was extinguished and Rialto received an upfront payment of $30 million from the private partner.[12] Various reserve funds for operations, capital maintenance, and financial security were also established. The private partner financed the P3 deal through debt and equity. Specifically, it issued $146 million in 30-year notes to pension plans and insurance companies, and raised $26 million in private equity.[13] Further, the private partner retained a reputable operator to operate and maintain Rialto's water and wastewater systems and facilities, and the operator committed to retain Rialto's government personnel who had previously worked at the facilities. [14] The private partner is paid by Rialto through a combination of monthly capital charges and operating payments. Rialto finances these payments through water and wastewater user fees and various non-rate revenues.

"BEST PRACTICES" FOR P3S

A P3 program should strive to achieve as many of the potential benefits that P3 projects can offer.[15] The overall premise supporting the development of projects under a P3 approach is that public infrastructure projects can benefit from the private sector's involvement in terms innovations, efficiencies and best practices for design, construction, operation and maintenance of such projects. Accordingly, as part of a P3 program, strong incentives should be established for the private sector to efficiently and cost-effectively deliver needed public infrastructure.

Initially, however, a P3 program should focus on whether a particular project should proceed on a P3 basis or a traditional, solely publicly-funded basis. After conducting a feasibility study and making the business case for developing a particular project, the determination of whether to proceed on a P3 basis should focus on a rigorous value for money ("VfM") analysis for the project's entire lifecycle.[16] The VfM for delivery under a P3 method then needs to be compared to the VfM for delivery under a traditional method. If the VfM analysis does not support a P3 approach, it should not be used for the project.

Additionally, a P3 program should establish criteria to evaluate whether a particular project is appropriate to pursue on a P3 basis. Such criteria could include an evaluation of the project's public benefits. For instance, if the project is needed to deliver immediate benefits, the project is a good candidate to proceed as a P3 given that P3 projects generally get built quicker due to the fast-track nature of their design and construction. Another criterion could include an evaluation of the project's technical complexity. If the project is technically complex, where the benefit of the private sector's expertise in design, construction, operation and maintenance would be better realized, the better suited it is to a P3 approach.

Equally important, a P3 program should emphasize fairness, consistency and transparency. Given that some of the public has a negative perception of P3s, it is critically important that P3 programs consistently adhere to clear evaluation criteria and apply them fairly. Further, the P3 evaluation should be open to public review to ward off concerns of cronyism and the like, and to generate public support for P3s.

A P3 program should also include objectives to be achieved in any P3 agreement prepared for a project that meets all the selection criteria. The overall goal of P3 agreements is to craft them to the strengths of the public and private sectors while respecting the fiduciary duties owed by public officials to their ratepayers and respecting the return on investment that drives the deals for private partners. This overall goal is accomplished through specific objectives. First and foremost is the clear definition of the technical aspects and the performance requirements for the project in the P3 agreement. It is best to state these as performance specifications that allow the private partner to determine how best to achieve those requirements given that the private partner is in a better position analyze various design and construction options that are able to create post-construction synergies with operation and maintenance of the completed facility.

Other objectives to be achieved in P3 agreements include allocating risks to the party best able to manage them. If certain risks are allocated to a private partner that is not able to control them, the government entity will pay a higher price for the P3 deal than it otherwise would if the risk were retained by the public entity. This is frequently called a "risk premium." For instance, the risk of environmental approvals and permits is best retained by the local government agency, whereas the risks associated with the design, construction, operation and maintenance of a P3 project are appropriately shifted to the private partner.

Another important objective is establishing incentives for the private partner in P3 agreements. A premise supporting the development of projects on a P3 basis is that such projects get built more efficiently than traditionally-delivered projects. The efficiencies that P3s can deliver take the form of lower costs, faster completion, and higher quality design and construction. The private partner should be incentivized in P3 agreements to achieve these efficiencies, and if done correctly, a project's overall lifecycle costs will be reduced while not sacrificing the facility's performance. A further objective is to enhance the local public agency's cash-flow through P3 agreements, by requiring, for

example, an upfront cash infusion, so that the agency's existing debt can be retired, or requiring that higher user fees not become effective until after the constructed facility becomes operational.

P3 agreements also need to avoid private-sector windfalls by capping the private partner's return on investment. This is frequently done by establishing a rate-setting formula to ensure that the cap is not exceeded, to ensure that rate increases to ratepayers are fixed and predictable, and to ensure that there is a known revenue stream to the private partner. Absent predictability for ratepayers, there is a risk of ratepayer revolt.

P3 agreements should further establish a governmental oversight mechanism that will regularly evaluate the private partner's performance under the P3 agreement. This is needed to maintain transparency for the public's benefit and to satisfy the government entity's fiduciary duties to its ratepayers.

Finally, for P3 programs to be successful, they must have the internal political support of local government agencies and broad-based public support, which can be achieved through education and outreach programs. Local government agencies supporting P3 programs must also be perceived as being stable and committed to P3s. Private partners rightly shy away from the risk of negotiating P3 transactions with state governments, cities, counties or special districts that have a history of electoral instability or bureaucratic impasse. Therefore, local government agencies need to establish themselves as "can do" agencies, where there is minimal political risk that projects will be derailed after time and money have been invested to put together a P3 deal.

CONCLUSION

Local government agencies have a powerful tool to address their infrastructure needs. That little-used tool is the P3 project delivery method that can be used to develop projects through private funding. P3s can help bridge the gap between the State's public infrastructure demands with the supply of private capital available to invest in P3 projects. Not every infrastructure project is appropriately pursued on a P3 basis, but many larger, technically-complex projects could benefit from the private sector's involvement. The benefits P3s offer extend beyond the particular P3 project to be built and can be wide ranging.

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Endnotes

1 In the United Kingdom, 700 projects have been pursued on a P3 basis since 1992, and over £ 55 billion in private funds has been invested in the UK's P3s. HM Treasury, *A New Approach to Public Private Partnerships* (Dec. 2012). These projects have included schools, hospitals, roads, prisons, housing, and waste facilities. *Id.* In Canada, over 100 P3 projects have been built under a P3 approach since the early-1990s. The Conference Board of Canada, *Dispelling the Myths: A Pan-Canada Assessment of Public-Private Partnerships for Infrastructure Investments* (Jan. 2010). Additionally, over the past eight years, Canada has used P3s to deliver 34 operational hospitals and 20 currently under construction. Consequently, the nation has fast-tracked the delivery of hospital facilities, improved health care to patients, and significantly reduced costs. Canadian Council for Public-Private Partnerships Database, available at http://projects.pppcouncil.ca/ccppp/src/public/search-project?pageid=3d067bedfe2f4677470dd6ccf64d05ed. By using P3s to design, build, finance and maintain eighteen schools in Calgary and Edmonton, the Alberta government saved $97 million over thirty-two years compared to a traditional approach ($634 million instead of $731 million, a 13% savings). *Id.* The use of P3s also delivered the schools two years earlier than they would have been delivered under traditional delivery methods. *Id.*

2 A Reason Foundation study found that if California used P3s for correctional facilities, it would save state taxpayers nearly $2 billion in inmate housing costs over the next five years. L. Gilroy, A. Summers et al., *Public-Private Partnerships for Corrections in California: Bridging the Gap Between Crisis and Reform*, Reason Foundation, April 2011. Similarly, an Australian study that focused on 54 social, transportation, water, and information technology projects comprised of 21 P3 projects and 33 traditionally-delivered projects found that the P3 projects were more efficient in terms of cost and time. Infrastructure Partnerships Australia, *Performance of PPPs and Traditional Procurement in Australia* (Nov. 2007). Specifically, the Australian study found that cost overruns on the P3 projects averaged about 1% (i.e., $58 million in overruns on $4.9 billion of P3 projects), whereas the cost overruns on the traditional projects averaged about 15% (i.e., $673 million in overruns on $4.5 billion of conventional projects). *Id.* Additionally, the study found that on a value-weighted basis, the P3 projects were completed about 3% ahead of schedule, whereas the traditional projects were completed about 23.5% behind schedule. *Id.* Finally, a recent study conducted by Arizona State University that focused on 12 US highway projects valued at over $90 million each compared P3 projects to those delivered under a design-bid-build approach and a design-build approach. A. Chasey, W. Maddex et al., *A Comparison of Public-Private Partnerships and Traditional Procurement Methods in North American Highway Construction* (March 2012). That study concluded that cost overruns on P3 projects averaged less than 1% and that the P3 projects were completed slightly ahead of schedule. *Id.* In contrast, cost overruns and schedule overruns on design-bid-build projects averaged about 13% and 4%, respectively, and cost overruns and schedule overruns on design-build projects averaged about 1% and 11%, respectively. *Id.*

3 Under a traditional design-bid-build delivery method, the public project owner initially retains a designer to fully design the facility and then awards a construction contract to the lowest responsive and responsible bidder. In such situations, the public owner impliedly warrants to the contractor the adequacy and completeness of the design it provides under what is commonly called the Spearin Doctrine. However, the design the public owner receives from its designer is not similarly warranted by the designer. Instead, the designer warrants that its design is only as good as that produced by a reasonably prudent designer under similar circumstances. This can create a "liability gap" for the public owner where there are errors and omissions in the design that do not fall below the designer's applicable standard of care but nevertheless cause the contractor to incur damages for which the public owner is liable.

4 Association of General Contractors, available at http://www.agc.org/cs/2012_election (citing Dr. Stephen Fuller of George Mason University).

5 P3 agreements for existing infrastructure facilities can be more technically and legally complex than P3 agreements for new facilities. Existing public infrastructure facilities have an "as-is" risk that new, to-be-constructed facilities do not have. With existing facilities that are to be upgraded and expanded, one major challenge of a P3 deal is balancing the public partner's goal of shifting all operation-and-maintenance cost risks to the private partner and the private partner's interest in not taking on open-ended or undefined cost risks associated with a facility that was built many years ago. To overcome these as-is risk transfer issues, P3 deals are often structured around a defined approach for preventative, predictive and corrective maintenance management. This results in a shared responsibility for the as-is risk that is transferred to the private partner over the first several years of the P3 agreement's term.

6 P3s do not amount to privatization. Although the P3 enabling statutes for local government agencies permit the lease or transfer of ownership of a public infrastructure facility to a private partner, the public facility must be returned to the public partner at the end of the P3 agreement. Gov't Code § 5956.6(a). Additionally, the public maintains control over public infrastructure assets through P3 agreements, which establish performance standards and rate-setting mechanisms to which the private partner must adhere.

7 P3 projects are not more costly than non-P3 projects if the project is appropriately evaluated. As discussed *infra*, a rigorous money-for-value analysis of a particular project's lifecycle costs is required to determine whether the cost to develop the project on a P3 basis is less than the cost to develop it with public funds. As a part of that analysis, the risks involved in developing the project needs to be considered and monetarily quantified. If the analysis supports proceeding with the project on a P3 basis, it means that the cost for the project over its lifecycle (in terms of the net present value) is estimated to be less than it would cost through a non-P3 approach. Importantly, not all projects are appropriately pursued under a P3 approach.

8 P3s do not make the public responsible for the private partner's mistakes. A private partner is held to certain performance standards under a properly structured P3 agreement. If the private partner fails to meet those performance requirements, the private partner's revenue is reduced or the P3 agreement may be terminated by the public partner for the private partner's default.

9 P3s do not make private partners rich. A properly structured P3 agreement has a fee-setting mechanism with caps that are designed to prevent the private partner from receiving a windfall. If user fees generated by a P3 project exceed projections, the P3 agreement should call for the sharing of the reward between the public and private partners.

10 R. Jensen, *Southern California City Enters into P3 for Its Water and Sewer Systems*, The Bond Buyer, Feb. 20, 2013, available at www.bondbuyer.com/121_234/rialto-california-water-sewer-utilities-pubioc-private-partnership/.

11 The 20/20 Network, *Saving Cities Through Public-Private Partnerships*, available at www.the2020network.com/2012/12/saving-cities-through-public-private-partnerships/.

12 R. Jensen, *Southern California City Enters into P3 for Its Water and Sewer Systems*, The Bond Buyer, Feb. 20, 2013, *supra*.

13 *Id.*

14 *Id.*

15 Local government agencies have not previously pursued P3 projects because they generally seem to have been ill-equipped to develop P3 programs that fully protect the public interest. To overcome this and to advance the goal of developing public infrastructure projects, local government agencies should develop the expertise to establish a P3 program. Many such agencies, however, simply do not have the staff or resources to develop this expertise internally, so they will have to either join forces to develop in-house expertise collectively or rely on outside legal, technical and financial advisers to pursue P3 opportunities. Ideally, however, a specialized, state-wide P3 department or taskforce could be established to assist local government agencies in expanding P3 opportunities by providing technical input, quality control, policy coordination and other assistance. Specialized P3 departments like this have been established in 31 countries to promote P3s. R. Puentes and E. Istrate, *A Path to Public/Private Partnerships for Infrastructure*, The New Republic, Dec. 9, 2011.

16 The importance of a rigorous value for money analysis was highlighted in a controversial report issued by California's Legislative Analyst's Office ("LAO") on November 8, 2012, entitled *Maximizing State Benefits from Public-Private Partnerships*. In that report, the LAO criticized the VfM analyses used to support the development of the Long Beach Courthouse and the Presidio Parkway Project on a P3 basis, concluding that the projects could have been developed for $160 million and $140 million less, respectively, if they had been delivered under a traditional, public-financed approach.

Legislative Update

*By Kenneth J. Price**

The first half of the 2012-2014 legislative calendar has come to a close. It was productive.

Over the last several issues, I have been updating you on the relative good times in Sacramento as compared to the last several years. Declining unemployment, significant increases in tax revenues, a pay down of debt, and a projected operating surplus for the state have brightened up the Legislature's mood. As a result, legislators are doing what legislators are prone to do (except in Washington D.C.): drafting bills, and getting many of them passed and signed into law.

By the October 13 deadline, Governor Brown signed nearly 9 out of 10 every bills passed by the Legislature—signing approximately 800 regular session bills this year and vetoing only 96. These bills cover just about every topic one could imagine. The bills generating the most press coverage were the sweeping gun control legislation, cracking down on assault weapons, high-capacity magazines and lead ammunition, and the measure allowing undocumented residents to obtain drivers licenses. Despite vetoing so few bills, the Governor seemed frustrated by the exercise. "[T]hese damn bills . . . [They] are all big issues," Brown said, "and then on top of that you have the endless desire of the Legislature for more and more activities or interventions or spending or law." The Governor noted the Legislature's "pent-up desire" to legislate and said, "Going forward, there could be more 'No's.'"

One prominent political analyst pointed out that in addition to labor, the one traditional constituency that normally benefits from a Democratic-controlled Legislature and a Democratic Governor, the California Chamber of Commerce, also was influential, with only one (raising the minimum wage) of the 38 bills that it pegged as "job-killers" being signed into law.

The editors of the Public Law Journal would not be pleased if I were to include a short summary of each of the 800 regular session bills passed and signed into law (even those that interest our members). However, I have received several requests to discuss California Environmental Quality Act (CEQA) reform proposals signed into law by the Governor, which is where I will focus my attention. Additionally, there were three very important changes to the Political Reform Act of which our readers should be aware.

CEQA

According to pundits, this was supposed to be the year for comprehensive CEQA reform. While landmark legislation never materialized, there were some incremental changes signed into law.

On February 22, 2013, Senate President pro Tempore Darrel Steinberg introduced two pieces of legislation concerning CEQA—SB 731 and SB 743.

SB 731 was aimed at achieving comprehensive CEQA reform. As introduced, key elements of SB 731 included:

- Updating CEQA to encourage and expand infill developments to reduce urban sprawl. This change was designed to help jump start the state's housing market while promoting development consistent with state climate and planning laws like SB 375.
- Expedite the CEQA process, without compromising underlying public disclosure or environmental protection, for new investments in clean energy, bike lanes and transportation projects that help California meet its renewable energy, clean air, jobs, and transit goals.
- Modernize CEQA and its implementing regulations to

set clear minimum thresholds for impacts like parking, traffic, noise and aesthetics to allow local agencies to standardize mitigation of those impacts. This change was designed to preserve local control to set more stringent thresholds where communities choose to do so.

- Reduce duplication in Environmental Impact Report filings by expanding the use of "tiering." This streamlines and limits further paperwork whereby local land use plans that have sufficient detail and recently completed EIRs can be used by people building projects within those plans.
- Where EIRs have been successfully challenged, allow the courts to send back for repair only the portion of the EIR that is found to be incomplete or lacking required specificity. This would eliminate the need for the entire EIR to be recirculated for public comment which can create additional delays.
- In those cases where project developers and agencies haven't made any substantive change to a project and the public has already had time to comment on it, limit or prohibit so-called "late hits" and "document dumps," designed solely to delay projects late in the environmental review process.
- Appropriate $30 million in new funding to local governments to update their general, area, and specific plans so that they can be better used to "tier" and streamline environmental review of projects built pursuant to those plans.

After meeting with Governor Brown, Senator Steinberg abandoned his statewide CEQA reform package (SB 731) one day before the final vote and shifted his focus to SB 743. Initially, SB 743 was aimed at increasing electricity rates. However, the bill was amended in early September to streamline the CEQA process for a new Sacramento Kings arena, which must be completed by 2017.

Senator Steinberg then further amended SB 743 to incorporate three significant reform provisions from SB 731. Both the Assembly (56-15) and the Senate (32-5) approved SB 743, a bill that will substantially change the way CEQA works, just not in the blockbuster way Steinberg originally contemplated.

As passed, SB 743 is good for the Sacramento Kings. Under a deadline set by the NBA, the Sacramento Kings have until 2017 to build a new arena. SB 743 gives the City of Sacramento the power to use eminent domain to claim property for the arena project, while also creating a new, compressed timeline for public review that will end disputes in non-binding mediation instead of in court. Whether this kind of CEQA reform will result in better defense and perimeter shooting for the Kings remains to be seen.

Furthermore, under SB 743, major green projects statewide, including the new Kings' arena, will have a new expedited 270-day period for judicial review. This new review period replaces a provision of existing law that allowed specially-certified, large green projects to move directly to a Court of Appeals when challenged by CEQA lawsuits, a provision that was declared unconstitutional in 2012.

The final bill included key provisions from SB 731. The bill provides that aesthetic (other than as related to historical or cultural resources) and parking impacts from residential, mixed-use residential, or employment center projects on infill sites within transit priority areas shall not be considered significant impacts on the environment under CEQA. In other words, opponents of such infill projects cannot use CEQA to slow down a project in court based on the look of the project or how it deals with parking. The bill also requires the Governor's Office of Planning and Research to establish "new methodologies" for determining the transportation impacts in transit priority areas. Specifically, OPR is required to look for alternative metrics to the state's current "levels of service" rules. Such rules require all projects to prove they will not impact local drive times.

POLITICAL REFORM ACT

Finally, moving away from CEQA, the Governor signed thee public-disclosure bills amending the Political Reform Act but vetoed one that updates California's antiquated campaign finance reporting website. These revisions to the Political Reform Act are significant.

AB 409 by Assembly Member Silva, which was signed by the Governor, establishes a state-wide, electronic public official disclosure system for the first time in state history. The bill, which was sponsored by the Fair Political Practices Committee (FPPC), authorizes the Commission to develop an electronic filing system for the disclosure of income and economic interests of public officials at all levels of State and local government, covering hundreds of thousands of public officials. "The current system of disclosure for public officials is scattershot and doesn't provide the public the information it deserves on the economic interests of public officials," said FPPC Chair Ann Ravel. "This landmark bill will revolutionize the ability to hold public officials accountable across the State."

The law currently requires all public officials involved in governmental decision making to file a Statement of Economic Interests (known as a Form 700) with either the FPPC, or a state or local agency. The forms detail an official's economic interests so the public can ensure that the official is not making or participating in any decision in which the official could be financially interested. The Form 700 also details any gifts over $50 given to the public official in a calendar year.

The Governor signed two other FPPC sponsored bills. In the summer edition of the Public Law Journal, I discussed those bills, AB 1090 and AB 552. AB 1090 gives the FPPC enforcement authority over violations of Government Code Section 1090 (prohibiting state and local officials from being financially interested in contracts that they approve). It increases penalties and authorizes the FPPC to pursue enforcement of these violations by bringing administrative or civil actions against a person who violates the law, if the local district attorney authorizes such actions. The bill also authorizes an official to request an opinion or advice from the FPPC with respect to the Government Code 1090 *et seq.* prohibitions.

AB 552 allows the FPPC to collect unpaid fines and penalties. It authorizes the FPPC to apply to the clerk of the superior court for a judgment enforcing a monetary penalty, fee, or civil penalty, and would require the clerk of the court to enter a judgment.

The second half of this two-year legislative calendar begins shortly. Stay tuned.

Please feel free to email me (kprice@bakermanock.com) about any bills you would like covered in future issues of Public Law Journal Legislative Report.

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Litigation & Case Law Update

*By Scott Dickey**

LAW ENFORCEMENT/TORT LIABILITY

Hayes v. County of San Diego (2013) 57 Cal.4th 622

Whether law enforcement officers are negligent in the use of deadly force depends upon an examination of the totality of the circumstances surrounding the shooting, including tactical conduct and decisions employed by law enforcement preceding the use of deadly force.

In September 2006, San Diego County sheriff's deputies responded to a call regarding screaming coming from a neighbor's house. When the deputies arrived they encountered Geri Neill, who told them that her boyfriend, Shane Hayes, had attempted suicide earlier in the evening by inhaling exhaust fumes from his car. She said there were no guns in the house. The deputies did not ask whether Hayes was under the influence of drugs or alcohol. They were unaware that Hayes had been drinking, and had four months earlier attempted suicide with a knife.

A few minutes later, the deputies entered the house to conduct a welfare check on Hayes, with their guns holstered. From the living room, they could see Hayes standing in the kitchen, and one deputy ordered him to show his hands. As Hayes did so, he walked towards them and revealed that he was holding a large kitchen knife in his raised right hand. Both deputies drew their weapons and fired simultaneously, killing Hayes.

Hayes's minor daughter, Chelsea filed a complaint against the County and the deputies in federal district court alleging federal claims under the Fourth Amendment, and two state-law claims against the County of San Diego for negligent hiring, training, retention, and supervision. The District Court found in favor of the County and the deputies on all counts. With respect to the California state law claims, the Court found that the deputies owed plaintiff no duty of care with regard to their preshooting conduct and decisions, relying on two California appellate decisions: *Adams v. City of Fremont* (1998) 68 Cal. App.4th 243, and *Munoz v. City of Union City* (2004) 120 Cal.App.4th 1077. Plaintiff appealed.

On appeal, the Ninth Circuit asked the California Supreme Court to determine as a matter of state law "[w]hether under California negligence law, sheriff's deputies owe a duty of care to a suicidal person when preparing, approaching, and performing a welfare check on him." The Supreme Court restated this issue as "[w]hether under California negligence law, liability can arise from tactical conduct and decisions employed by law enforcement preceding the use of deadly force."

In *Hayes v. County of San Diego* (2013) 57 Cal.4th 622, the California Supreme Court answered the restated question in the affirmative: "liability . . . can arise if the tactical conduct and decisions leading up to the use of deadly force show, as part of the totality of the circumstances,

that the use of deadly force is unreasonable." In reaching this conclusion, the Court noted a distinction between Fourth Amendment and California negligence law: under a Fourth Amendment analysis, a Court concerns itself only with the moment of the shooting, but under California negligence law, the shooting cannot be examined in isolation; "preshooting circumstances might show that an otherwise reasonable use of deadly force was in fact unreasonable." The Court went on to disapprove the *Munoz* decision to the extent it held that an officer owes no duty of care with respect to preshooting conduct that results in a use of deadly force.

LAW ENFORCEMENT/FIRST AMENDMENT RIGHTS

Dahlia v. Rodriguez (9th Cir., August 21, 2013) ___ F.3d ___, 2013 WL 4437594

Disclosure of alleged misconduct by fellow officers to officials from other agencies is an independent act—not a professional responsibility—and thus subject to First Amendment protection; placement of police officer on administrative leave can constitute adverse employment action.

In 2007, Angelo Dahlia was a detective in the Burbank Police Department ("BPD"), supervised by Lieutenant Jon Murphy. Dahlia was assigned, along with others, to investigate a robbery at a downtown café. The day after the robbery, Dahlia observed Lieutenant Omar Rodriguez grab a suspect by the throat with one hand, and use the other to place his gun under the suspect's eye. Rodriguez than asked the suspect, "How does it feel to have a gun in your face [expletive]?"

Later that same evening, Dahlia heard someone being hit and slapped inside a room where Sergeant Edgar Penaranda was interviewing another suspect. Dahlia was excluded from the interviews, and BPD officers were placed outside the interview and audio rooms to prevent anyone from walking past or listening in to the interviews. Although he did not witness specific attacks, booking photos confirmed that suspects had been abused in the field. The BPD Chief, upon learning at a briefing that not all of the robbery suspects were in custody comments "[w]ell then beat another one until they are all in custody."

Throughout the investigation, Dahlia, sometimes with others, complained of the misconduct and abuse to Murphy, his supervising officer. Murphy advised him to "stop his sniveling," told him that he "didn't want to hear about it," and that he was "tired of all the B.S." When the BPD's Internal Affairs Division began looking into allegations of abuse and other illegal procedures in the café investigation, Murphy and Penaranda began contacting Dahlia daily, threatening him to keep quiet. Following meetings with the Internal Affairs investigators, Murphy would either confront him immediately afterwards with threats and demands, or order Dahlia to report to a location in the field for intimidating questioning.

In late 2008, Murphy and Penaranda learned that the FBI intended to investigate abuse and illegal conduct in the café investigation. The threats and intimidation of Dahlia intensified, with Murphy and Penaranda ordering him not to say anything to anyone, and Rodriguez threatening to "put a case on [him] and put [him] in jail. I put all kinds of people in jail, especially anyone who [expletive] with me!" Dahlia reported this interaction—which began with Rodriguez closing the door and blinds in his office and unholstering his gun—to the Police Officers' Association.

In May 2009, the Los Angeles Sheriff's Department interviewed Dahlia about the café investigation. Dahlia disclosed the misconduct he had witnessed, as well as the threats, intimidation, and harassment. Four days later, the BPD placed Dahlia on administrative leave pending discipline.

In November 2009, Dahlia filed a complaint under 42 U.S.C. § 1983 alleging that he was subjected to adverse employment actions as a result of his protected speech activities, and that there was no legitimate for the adverse actions. Dahlia sued the City of Burbank, the Police Chief, Murphy, Rodriguez, Penaranda, a sergeant, and a detective. The individual defendants, with the exception of the Chief, moved to dismiss the case for failure to state a claim on the grounds that Dahlia's speech was not constitutionally protected because it was made in the course of his official duties, and placement on administrative leave was not an adverse employment act. A three-member panel of the Ninth Circuit

affirmed, relying on *Huppert v. City of Pittsburg* (9th Cir. 2009) 574 F.3d 696, in which the Court held that reports by fellow officers of police misconduct are not protected by the First Amendment because officers are professionally obligated to make such reports.

On a request for rehearing, the Ninth Circuit took the case up again en banc. In *Dahlia v. Rodriguez* (9th Cir., August 21, 2013) ___ F.3d ___, 2013 WL 4437594, the Court held that courts must make a "practical" inquiry when determining the scope of a government employee's professional duties for the purpose of First Amendment retaliation analysis, because "employers [cannot] restrict employees' rights by creating excessively broad job descriptions." The Court noted that the recipient of the speech matters: "[w]hen a public employee communicates with individuals or entities outside of his chain of command, it is unlikely that he is speaking pursuant to his duties, and that placement on administrative leave can constitute an adverse employment action. . . [If] a public employee takes his job concerns to persons outside the work place in addition to raising them up the chain of command at his workplace, then those external communications are ordinarily nor made as an employee, but as a citizen."

The Court also noted that the content of the speech matters. An internal report by a public employee is likely within the scope of his or her duties; allegations of broad corruption within a department are not likely within the employee's duties unless they are in Internal Affairs or some similar watchdog unit. And the Court noted that practical considerations can include whether the statements were made with the assent of the employer: "[w]hen a public employee speaks in direct contravention to his supervisor's orders, that speech may often fall outside of the speaker's professional duties."

Applying these principles to Dahlia, the Court concluded that his disclosures to the Los Angeles Sheriff's Department, which he alleges were why the BPD put him on administrative leave, were protected by the First Amendment, because they were outside his chain of command, beyond his usual job duties, and clearly made in contravention to orders. Accordingly, the Court concluded that Dahlia had stated a claim for violation of his First Amendment rights under section 1983. The Court declined, however, to definitively conclude that Dahlia's discussions with Internal Affairs were protected.

Finally, the Court considered the question whether placement on administrative leave was an adverse employment action, and if so, whether Dahlia had adequately pleaded an adverse employment action. The Court concluded that "under some circumstances, placement on administrative leave can constitute an adverse employment action." The Court found that to establish a valid claim for an adverse employment action in retaliation for First Amendment activity, [a plaintiff] must establish that the actions taken by the defendants were 'reasonably likely to deter [them] from engaging in protected activity." The Court concluded that Dahlia's allegations met this standard, and that he has stated a claim for adverse employment action.

ENVIRONMENTAL JUSTICE/LAND USE

Communidad en Accion v. Los Angeles City Council (September 20, 2013) ___ Cal.App.4th ___, 2013 WL 5306190

To be subject to the anti-discrimination provisions of Government Code section 11135, the challenged action must arise directly from a program or activity funded by the state; failure to meet the 90-day deadline for requesting a hearing in a CEQA matter is excusable neglect subject to relief under Code of Civil Procedure section 473 where Petitioner otherwise vigorously prosecutes action and Respondent is not harmed.

On May 11, 2010, the Los Angeles City Council certified an Environmental Impact Report and approved Waste Management Recycling and Disposal Services of California Inc.'s request to build a new 104,000-square-foot solid waste transfer station, an expanded materials recycling facility, and an expanded green waste processing center at a landfill site in Sun Valley. The City's Planning Department acted as the lead agency and also processed the applications and approvals. The City did not consider siting the facilities in another location.

Communidad en Accion challenged the City's siting of the facilities under the antidiscrimination statute in Government Code section 11135, which precludes discrimination in a "program or activity . . . funded directly by the state, or [that] receives any financial

assistance from the state." The lawsuit sought to prevent the construction of the challenged facilities in Sun Valley, where members of Communidad live, and where residents are predominately Latino. Communidad alleged that the approval of the facilities was discriminatory because it "has the intended and unintended effect of subjecting the residents of Sun Valley to substantially more air and groundwater pollution, and more truck traffic, odor, noise, trash, and vermin than most or all other parts of the City." Communidad alleged that "the City of Los Angeles receives funding from the State of California to operate and administer its waste disposal and management programs." Communidad also challenged the facilities under the California Environmental Quality Act (CEQA).

The trial court granted summary judgment on Communidad's section 11135 claim, concluding that the City's zoning and land use decisions were not a state funded program or activity. The trial court also dismissed Communidad's CEQA claims, on the grounds that Communidad's counsel failed to request a hearing within 90 days of the decision as required by Public Resources Code section 21167.4, and rejected Communidad Counsel's request for relief under Code of Civil Procedure section 473. Communidad appealed all three determinations.

In *Communidad en Accion v. Los Angeles City Council* (September 20, 2013) ___ Cal.App.4th ___, 2013 WL 5306190, the Second District Court of Appeal affirmed in part and reversed in part. The Court affirmed summary judgment against Communidad's section 11135 claim. The Court concluded that Communidad challenged the site approval by the City Council, and that that action did not involve state funding of a program or activity as required by the section. The Court rejected claims that the City's approvals were a program or activity funded by the state because the Local Enforcement Agency ("LEA") – which receives state funding for its operations – played an integral role in the City's waste disposal and management program. The Court found that the LEA was a separate legal entity controlled by the State, and that a reading of section 11135 that would permit payments to the LEA to support a claim would be far too broad.

The Court reversed the trial court's dismissal of Communidad's CEQA claim, finding that the court abused its discretion by not providing relief from the missed deadline under Code of Civil Procedure section 473. The Court noted that Communidad had filed its request for hearing one week after learning that it had missed the 90-day deadline. Citing the principle that matters should be heard on the merits, and concluding that the City was not harmed by the late notice, and noting that Communidad had been otherwise vigorous in its prosecution of the case, the Court concluded that the missed deadline was inadvertent and excusable error for which Communidad should have been relieved under section 473: "[t]he one-week delay in requesting a hearing was an isolated mistake in an otherwise vigorous and thorough presentation of Communidad's claims This isolated mistake is indistinguishable from ones that courts have regularly granted relief [from] and any doubt is to be resolved in favor of granting relief."

Scott Dickey is a Partner in the San Francisco law firm Renne Sloan Holtzman Sakai LLP. His practice includes government law and litigation, appellate advocacy, election law and tax allocation and assessment. He has represented numerous California cities and other public agencies in complex litigation and appeals.

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