

300 S. Grand Avenue, Suite 2700
Los Angeles, CA 90071-3137
Voice (213) 542-5700
Fax (213) 542-5710

COLANTUONO
HIGHSMITH
WHATLEY, PC

Michael G. Colantuono
(530) 432-7357
MColantuono@chwlaw.us

MEMORANDUM

TO: Gary Geuss, City Attorney
City of Riverside
FILE NO: 11082.0003

FROM: Michael G. Colantuono, Esq. *mgc/al*
Amy C. Sparrow, Esq. DATE: March 16, 2016

RE: Northside Property Transactions

Introduction

As you asked, we write to express our opinion regarding the application of Proposition 26, Proposition 218 and Riverside Charter section 1204 to recent transfers of four properties among the Water Fund, the Electric Fund, and the General Fund ("Northside Property Transactions").

As discussed below, we conclude these transfers comply with law.

Factual Background

The facts on which our opinion turns follow. If these facts are incorrect or materially incomplete, please let us know, as different facts might require us to change our advice to you.

The Northside Property Transactions consist of the following transfers among the Water Fund, the Electric Fund, and the General Fund:

- Transfer of the AB Brown Sports Complex from the Water Fund to the Electric Fund on January 4, 2011, where the \$11,600,000 purchase price was based on an independent appraisal;
- Transfer of Reid Park property from the Water Fund to the General Fund on January 25, 2011, where the \$720,000 purchase price was based on an independent appraisal;
- Transfer of former Riverside Golf Course property from the Water Fund to the General Fund on January 25, 2011, where the \$4,837,500 purchase price was based on comparable sales; and

- Transfer of Pellisier Ranch property from the General Fund to the Water Fund on June 16, 2009, where the \$9,258,818.19 purchase price was based on an independent appraisal.

Analysis

The Northside Property Transactions are subject to Propositions 26 and 218, in addition to Riverside Charter section 1204, which governs the use of all revenues of the City's utilities. Proposition 218 governs the use of proceeds of water rates and Proposition 26 governs the use of proceeds of power rates.

A. APPLICATION OF PROPOSITIONS 26 AND 218

Proposition 26, which added subdivision (e) to article XIII C, section 1 of the California Constitution, provides that all local government charges are taxes subject to voter approval, with seven exceptions. Charges subject to Proposition 218 (like water rates) are exempt under the seventh exception. (Cal. Const., art. XIII C, § 1, subd. (e)(7).) Proposition 218, in turn, limits such charges to the cost of service. (Cal. Const., art. XIII D, § 6, subd. (b)(1) & (3).) Other utility charges that do not exceed the cost of service fall within the second exception for:

A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.

(Cal Const., art. XIII C, § 1, subd. (e)(2).) Thus, both water and electric utility charges are limited by the cost of service, which means that revenue transferred out of either fund must accomplish utility purposes or be exchanged for fair consideration. Otherwise, rate revenue would be siphoned away from the utility, thus indicating that rates exceed the cost of service because only a portion of rate proceeds are used to fund service. (E.g., *Howard Jarvis Taxpayers Ass'n v. City of Fresno* (2005) 127 Cal.App.4th 914 [general fund transfer from water utility violated Prop. 218].)

Similarly, Proposition 218 requires that water rate revenue "shall not be used for any purpose other than that for which the fee or charge was imposed." (Cal. Const., art. XIII D, § 6, subd. (b)(2).) Like Proposition 26, this language prohibits use of the proceeds of water rates for non-utility purposes in the absence of fair consideration to the utility for its expenditures.

The Northside Property Transactions all involve water utility transfers, and the AB Brown Sports Complex transfer involves both the water and electric utilities. Thus each of these transactions must reflect fair consideration to the utilities involved. This can be expected to mean that it obtains or pays market value for an asset sold or acquired. As fairness is a range, rather than a point, it is determined by the City's reasonable business judgment in light of record evidence. (E.g., *California Sch. Employees Assn. v. Sunnyvale Elementary Sch. Dist.* (1973) 36 Cal.App.3d 46, 58 [no gift of public funds in violation of Cal. Const., art. XVI, § 6 if adequate consideration for expenditure received in reasoned judgment of school board].)

The purchase price for the AB Brown Sports Complex, which was transferred from the Water Fund to the Electric Fund, was based on an independent appraisal, as were the Reid Park and Pellisier Ranch transfers. It is therefore likely that a court would uphold these transactions as an exercise of the City's reasonable business judgment. Similarly, the transfer of Riverside Golf Course property, where the purchase price was based on comparable market transactions, should be upheld if challenged.

Moreover, neither Proposition 26 nor Proposition 218 prohibit investment in real estate for purposes of diversifying assets. (Cf. *Griffith v. Pajaro Valley Water Management Agency* (2013) 220 Cal.App.4th 586, 600 [Prop. 218 permits water rate to recover all costs of service, including stranded debt and reserves for future services].)

B. CHARTER SECTION 1204.

Charter section 1204 provides in relevant part:

The revenue of each public utility for each fiscal year shall be kept separate and apart from all other moneys of the City by deposit in the appropriate revenue fund and shall be used for the purposes and in the order as follows:

....

(e) For capital expenditures of such utility.

The purchase of land, which is a capital asset, is therefore a permissible use of rate revenue under section 1204. Moreover, we see nothing in this section to prevent the utility from building reserves and investing those reserves in appropriate investments. Whether the land involved here is such an investment

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is a business judgment reserved to the City Council acting on the advice of its Board of Public Utilities and its professional staff.

Conclusion

As discussed above, we conclude these transfers comply with law. Thank you for the opportunity to assist. If we can provide any further assistance, please contact Michael at (530) 432-7357 or MColantuono@chwlaw.us or Amy at (213) 542-5700 or ASparrow@chwlaw.us.