

FILED
DEC 31 2019

CLERK OF THE SUPERIOR COURT
COUNTY OF STANISLAUS

BY *[Signature]*
CITY

SUPERIOR COURT OF THE STATE OF CALIFORNIA
COUNTY OF STANISLAUS

Andrew Hobbs and David Thomas,)
on behalf of themselves and all others)
similarly situated,)

Petitioners and Plaintiffs,)

vs.)

Modesto Irrigation District, et al.)

Respondent and Defendant)

Case No. 2019186

DECISION
on
Petitioners'
Petition For
Writ of Mandate

oOo

This matter came on calendar for oral argument on December 5, 2019.
Upon conclusion of the hearing, the Court took the matter under submission on
December 5, 2019.

After due consideration, the Court renders its Decision.

I
The Lawsuit

This case is somewhat of a repetition of the case on which, in part, the
parties essentially rely upon for their respective position. That case is Citizens For
Fair REV Rates, v. City of Redding, et al., (2018) 6 Cal 5th 1. The factual scenario
of the cases at bar is however somewhat different.

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III

Summary of the Parties' Contentions

[A] Petitioners' (Gleaned from their brief)

–MID imposes electric rates that exceed cost of service by millions of dollars each year. Thus, MID cannot meet its burden to prove its electric rates are not taxes as defined by Proposition 26.

–MID operates its electric utility solely for the benefit of its electric customers, and it may not use “gross” other income to subsidize irrigation farmers on the backs of electric ratepayers.

–MID cannot subsidize irrigation farmers with electric rate revenue because to do so constitutes an illegal gift of public funds.

–Petitioners also contend they have reason to suspect MID excluded important documents and information from the administrative record. Therefore, Petitioners suggest “the court take a particularly skeptical view when considering whether MID has met its burden of proof in this case under the circumstances.” (RB, p. 12-13, lines 27-28 and 1-2 respectively.)

–Recently, about 75% of irrigation costs are paid by electric retail customers.

–The alleged subsidy which MID has used from the electric utility revenues to fund irrigation assets is well known.

–MID comprises three utilities: electric, domestic water, and irrigation enterprises and by “allegedly commingling” its expenses for all three of its utilities, it is able to covertly shift electric utility profits to the benefit of irrigation farmers.

- 1 –The electric utility generates millions in profits, whereas the irrigation
2 utility operates at a multi-million dollar yearly loss.
- 3 –MID designed electric rates to fund the irrigation subsidy.
- 4 –MID carries the burden to prove its electric utility fees are not taxes.
5 Proposition 26 shifts the burden of proof to the agency that imposed
6 the fees.
- 7 –MID claims an internal transfer between one of its funds to another is
8 an “expense” paid by MID to operate its electric utility.
- 9 –MID overcharges its electric utility customers to generate profits; it
10 then transfers the profits from its electric utility to its irrigation utility
11 to provide nearly free services to irrigation farmers.

12
13 [B] Respondent/Defendant (Gleaned from their brief)

- 14 –MID does not dispute that its irrigation rates are below service cost, in
15 part, because Proposition 26 is not offended by rates below cost, only
16 by those which exceed it.
- 17 –The rates Petitioners challenge are supported by a detailed budget
18 analysis of electric service costs and expenses and a thorough cost-of-
19 service analysis.
- 20 –Petitioners’ challenge also fails for two procedural reasons. First, the
21 inter-utility transfer is a long-standing practice that pre-dates
22 Proposition 26, and because Proposition 26 is prospective only, the
23 inter-utility transfer is grandfathered.
- 24 –The challenge to MID’s rates set in 2015 is now moot because MID
25 re-adopted those rates in 2018.
- 26 –MID has substantial non-retail-rate revenues to cover the amount
27 transferred to its water utility in excess of what is necessary to pay for
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1 costs the electric utility should reasonably bear, such as for its use of
2 irrigation rights-of-way to deliver power.

3 –If Petitioners make out a prima facie case, MID bears the burden to
4 demonstrate by a preponderance of the evidence that the amount of
5 the challenged fee “is no more than necessary to cover the reasonable
6 costs of the government activity, and that the manner in which those
7 costs are allowed to MID customers bear a fair or reasonable
8 relationship to the [customer’s] burdens on, or benefits received from,
9 the governmental activity. California Building Industry Assn v. State
10 Water Resources Control Bd. (2018) 4 Cal. 5th 1032.

11 –MID has over 122,000 electric accounts and generates hydroelectric
12 power to Don Pedro Dam using water rights acquired by its irrigation
13 utility years before it entered the power business.

14 –MID also provides irrigation water to approximately 3,100
15 agricultural customers who irrigate approximately 58,000 acres.

16 –Petitioners challenge the electric rates MID adopted on November 17,
17 2015 (Resolution No. 2015-110) which took effect January 1, 2016.
18 The 2016 rates were MID’s first change in electric rates since January
19 2012 and embody a revenue-neutral change that increased the Fixed
20 Charge to \$20 per month to more closely align the rates to MID’s cost
21 structure and decreased the Energy Charge proportionally.
22

23 –There has been a perception for many years that MID’s electric
24 customers have subsidized irrigation rates. The dispute has focused
25 on the annual transfer of revenues from the electric division to the
26 irrigation division. From approximately 1995 to 2013, MID justified
27 this transfer as so-called “falling water” charge. This was a credit
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1 towards the irrigation division's revenues to account for the value of
2 the irrigation utility's surface water to generate electricity at Don
3 Pedro Dam. The falling water charge was blended into the electric
4 rate and was not separately reflected on customers' electric bills.
5 Upon passage of Proposition 26 in 2010, however, there were
6 questions about the methodology used to calculate the falling water
7 charge and whether it reflected the reasonable cost of providing
8 electric service, as Proposition 26 required prospectively.

9 Accordingly, MID suspended use of the falling water charge in 2013.
10 (40 AR 16025; 41 AR 16066)

11
12 –After this lawsuit was filed, MID retained new independent
13 consultants to prepare a comprehensive cost-of-service analysis of
14 both the electric and irrigation rates, to further analyze the allocation
15 of revenues and expenses between its irrigation and electric division.
16 The resulting studies led MID to adopt Resolution No. 2018-74 on
17 December 4, 2018 to repeal the 2016 rates and to adopt electric rates
18 in the same amounts and to reallocate costs and discretionary revenues
19 between MID's utilities and among its customer classes. The electric
20 rate consultant concluded that MID's electric rates are reasonable and
21 that the rate revenue collected by the electric division is less than
22 MID's cost of electric service.

23
24 –MID contends Petitioners' challenge to the 2016 Electric Rates is
25 MOOT because the 2016 rates have been repealed and the rate
26 structure adopted in Resolution No. 2018-74 is based on an entirely
27 new rate study.

28 –The Inter-Utility Fund Transfer is not a tax because MID has
sufficient non-rate revenues to cover the transfer.

1 –Petitioners concede that MID may use non-rate revenues for the inter-
2 utility fund transfer, but argue wholesale revenues so used must be
3 limited to net revenues – not gross.

4 –The Inter-Utility Transfer is not a gift of Public Funds. Respondent
5 contends, based on the following case that, “It is the general rule in
6 California that an expenditure of public funds for a public purpose,
7 notwithstanding incidental benefits to private persons, does not violate
8 the constitutional prohibition against gifts of public funds.” (San
9 Bernardino County Flood Control Dist. V. Grabowski (1988) 205 Cal.
10 App. 3d 885, 903)

11 IV

12 Discussion

13
14 In many respects, this Court finds the contentions of both sides to be
15 compelling. However, ultimately it is Respondent/Defendant’s burden of proving
16 by a preponderance of the evidence that a levy, charge, or other exaction is not a
17 tax. This definition of “tax” was defined by Proposition 218.

18 Article XIII C, §1, subd. (e) then lists seven exceptions to its definition. A
19 computer copy of the California Constitution provision in issue is printed as
20 Attachment A.

21 As described in briefing, MID is a non-regulated special District located in
22 the City of Modesto, California which was formed in 1887 pursuant to the
23 California Irrigation District Law (29 AR 11380; 40 AR 15883; Cal. Water Code
24 §20500. It was originally formed only to provide irrigation services. (emphasis
25 added) In 1923, MID expanded into electricity generation and distribution. In
26 1995, MID added domestic water services.

27
28 Petitioners allege MID electric utility subsidizes irrigation farmers. This is
the gravamen of the lawsuit.

1 Respondent/Defendant avers that the second exception to subsection (e) of
2 Article XIII C, §1 is applicable. It reads:

3 “(2) A charge imposed for a specific government service
4 or product provided directly to the payor that is not
5 provided to those not charged, and which does not exceed
6 the reasonable costs to the local government of providing
7 the service or product.”

8 As MID counsel notes, Petitioners do not dispute the applicability of the
9 exception just quoted. What Petitioners dispute regarding the quoted exception is
10 that the costs to the local government (MID) of providing the service (or product)
11 are not reasonable as required and the precise issue for the Court to decide. There
12 are many factors which come into the mix to determine what constitutes
13 reasonableness.
14

15 The Reasonableness Issues

16 [1] Inter-Utility Fund Transfers

17 Respondent/Defendant contends Petitioners must prove more than a
18 transfer from power to water or that water rates do not cover the cost of
19 water service; they must show that power rates generate more revenue
20 than MID reasonably requires to provide electric service, and they must
21 show that power rates generate more revenue that MID reasonably
22 requires to provide electric service.

23 MID avers it has substantial non-retail-rate revenues to cover the
24 amount transferred to its water utility in excess of what is necessary to
25 pay for costs the electric utility should reasonably bear, such as for its
26 use of irrigation rights of way to deliver power.
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1 MID also argues the issue, in part, as to reasonableness is whether the
2 rate charged exceeds the reasonable cost of service under Article XIII C,
3 §1, subd. (c)(2).

4 Citing Redding at pp. 15-19, supra, MID notes that if the inter-utility
5 transfer is offset by non-rate revenues that transfer is appropriate and has
6 no bearing on the validity of the rates being challenged. Furthermore,
7 “If the agency has resources of revenue other than the rates it imposes,
8 then the total rates charged may actually be lower than the reasonable
9 costs of providing the service.”

10 However, in Reply to the above arguments, Petitioners persuasively
11 rebut them on several grounds:

12 --They show that MID’s 2015 electricity cost of service study included
13 an “explicit” \$2.65 million profit and a \$7.6 million transfer to
14 irrigation.

15 --They point to MID’s Municipal Securities Rule Making Board
16 (“MSRB”) filings which show its actual costs are consistently tens of
17 millions of dollars less than its projected costs used to set rates.

18 Petitioners thereafter conclude that MID’s multi-million dollar annual
19 deficit in its irrigation division is strong evidence of a massive subsidy
20 from its electric ratepayers and to that point MID has no answer.

21 Furthermore, the 2015 MID electricity division cost of service study
22 referred to, supra, failed to identify any evidence of actual costs
23 associated with the transfer (emphasis added). MID proffers that it
24 needs to project the potential revenue for its entities and such
25 projections cannot be precise. However, if the projections are in
26 millions beyond what revenue from electric ratepayers is received,
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1 there is a palpable disconnect in being cognizant of continuous
2 millions of anticipated need.

3 [2] Mootness

4 MID argues Petitioners' Petition for Writ of Mandate, including the
5 refund claim, is moot based upon MID's "re-adoption" of electric rates
6 in December 2018.

7 Petitioners agree their equitable claims, such as their request to
8 invalidate the 2016 rates are likely foreclosed by the new rates.
9 However, Petitioners contend their claim for class-wide refunds remains.

10 Petitioners also note the above mootness arguments are properly
11 addressed in the remedy stage of this case since the current stage only
12 comprises Defendant's/Respondent's liability.

13 The Court disagrees with Petitioners that the mootness arguments are
14 to be addressed only in the remedy state. Since mootness could
15 comprise an affirmative defense for the liability phase, it can be
16 addressed at this point. However, only if this Court finds for
17 Respondent/Defendant as to liability would the liability phase be moot.

18 [3] Burden of Proof

19 As discussed, supra, Respondent/Defendant initially contended
20 Petitioners must present a prima facie case that its rates are taxes and
21 thus the burden shifts to MID only after Petitioners make out a prima
22 facie case. Such is no longer the law and the burden must be carried by
23 MID by a preponderance of the evidence. (Article XIII A, §3, subd. (d))

24 Whether or not a prima facie case must be the precursor to the burden
25 to be carried, the Court has concluded that Petitioners have presented a
26 prima facie case, nevertheless.

27 [4] Petitioners' Retorts to MID's Primary Contentions

1
2 (a) MID failed to prove its 2016 Electric Rates are not taxes.

3 Petitioners aver in 2016 MID reported that its irrigation utility
4 would operate at a loss of \$17,380,000 (emphasis added).

5 (b) MID's irrigation loss in 2016 was consistent with years past.

6 (c) Petitioners argue the irrigation loss must be recouped from
7 electric revenue because MID's electric utility is the only division
8 with a commensurate profit.

9 (d) MID concedes its irrigation division loses millions (of dollars)
10 annually. Instead of explaining how it makes up the loss, it
11 responds, in part, that Proposition 26 is not offended by rates
12 below cost.

13 (e) While MID claims it separately "analyzed costs and revenues for
14 its irrigation and electric services," it fails to identify such
15 analyses in the record.

16 (f) Sinclair Paint Company v. State Board of Equalization (1997) 15
17 Cal. 4th 866 established a test to examine taxes under Proposition
18 26. Thereafter, in 2018, California Building Industry Association
19 v. State Water Resources Control Board, supra, further continued
20 to refine Sinclair's three-prong test regarding the tax issue. The
21 prongs now are:
22

23 First: Whether the approved fees would exceed the
24 reasonable, estimated costs of administering the permit
25 program.

26 Petitioners contend MID admits its retail electric rates exceeded
27 costs by \$2.6 million.
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1 Second: Is the fee used to general excess revenue, i.e., to
2 generate more revenue than necessary to pay for the
3 regulatory program?

4 Petitioners at bar contend MID's electric rates are designed to
5 generate a \$2.6 million (dollar) profit thus comprising excess
6 revenue.

7 Third: Is there a fair allocation of what is referred to as the
8 pie?

9 As to this prong, Petitioners argue that MID admits its electric
10 utility revenue pie was too big in the first place. Furthermore,
11 Petitioners contend MID does not dispute that its electric rates
12 were designed to generate a \$2,652,235 profit.

13
14 (g) Petitioners argue that MID strains to cite any evidence to
15 support its Inter-Utility transfer to actual costs. Its Cost of
16 Service Study it is contended is entirely deficient, merely
17 identifying it as an Inter-Utility Transfer without further
18 explanation. For example, it (MID) asserts that "the irrigation
19 division provides raw water used by the electric enterprise to
20 create hydro-generation" – also known as a "falling water
21 share" which MID suspended due to concerns it violates
22 Proposition 26. Respondent/Defendant cites Moore v. City of
23 Lemon Grove (2015) 237 Cal. App. 4th 363 for the proposition
24 that a transfer of raw water/falling water is a legitimate
25 transfer. However, the Lemon Grove case noted that the city
26 identified "other employees" who provided support for the
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1 sanitation district and the amount of such costs (emphasis
2 added).

3 V

4 Disposition

5 Based upon consideration of the evidence and the exhaustive briefing, the
6 Court finds in favor of the Petitioners and concludes MID's electric rates are taxes
7 and therefore liable. Furthermore, MID failed to meet their burden of proof by a
8 preponderance of the evidence.

9 The primary basis for the Court's decision is the ubiquitous absence of
10 actual costs throughout MID's arguments. Although the Court understands MID's
11 argument regarding the projection issue used to set rates, there is little to no
12 foundation to explain what specific costs were attributable primarily to the utility
13 transfers.

14 To quote a decade's old and often used question by Clara Peller in a
15 television commercial, the ultimate failing by MID is/was to answer the question,
16 "Where's the beef?"
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18 For example, Petitioners proffer in their Reply Conclusion, in part, as
19 follows and with which the Court agrees:

20 "The record in this case reveals a massive multimillion
21 dollar hole in MID's irrigation budget, with a
22 corresponding electric utility profit It (MID) utterly
23 failed to justify its \$2.6 million profit and \$7.6 million
24 Inter-Utility Transfer, instead hastily pointing to its
25 policies and procedures, but never tying these explicit
26 subsidies to any actual costs."
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1 -Lastly, counsel have already been notified of this Judge's retirement
2 as of December 31,2019. Therefore, Judge Sandhu will be assigned to
3 Dept. 24 and will likely be the Judge assigned to oversee the
4 subsequent proceedings in this case. However, the Presiding Judge is
5 ultimately the assigning judge.
6

7 Counsel for Petitioners shall submit an Interlocutory Judgment or other
8 appropriate order as deemed applicable with opposing counsel's input.
9

10 IT IS SO ORDERED
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12
13 Dated: December 30, 2019 Roger M. Beauchesne
14 Roger M. Beauchesne
15 Judge of the Superior Court
16 Stanislaus County

17 cc: Mr. Vincent Slavens, Esq.
18 Mr. Michael Colantuono, Esq.
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Text of Section 1:

Definitions. As used in this article:

(a) "General tax" means any tax imposed for general governmental purposes.


(b) "Local government" means any county, city, city and county, including a charter city or county, any special district, or any other local or regional governmental entity.

(c) "Special district" means an agency of the State, formed pursuant to general law or a special act, for the local performance of governmental or proprietary functions with limited geographic boundaries including, but not limited to, school districts and redevelopment agencies.

(d) "Special tax" means any tax imposed for specific purposes, including a tax imposed for specific purposes, which is placed into a general fund.

(e) As used in this article, "tax" means any levy, charge, or exaction of any kind imposed by a local government, except the following:

(1) A charge imposed for a specific benefit conferred or privilege granted 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 conferring the benefit or granting the privilege.

 (2) 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.

(3) A charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof.

(4) A charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property.

(5) A fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law.

(6) A charge imposed as a condition of property development.

(7) Assessments and property-related fees imposed in accordance with the provisions of Article XIII D.

The local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor's burdens on, or benefits received from, the governmental activity.^[1]

CLERK'S CERTIFICATE OF MAILING

I certify that I am not a party to this cause and that a copy of the foregoing DECISION on Petitioners' Petition for Writ of Mandate was mailed first class, postage prepaid in a sealed envelope at Modesto, California, on December 31, 2019 to the parties whose name(s)/address(es) are given below.

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I declare under penalty of perjury that the foregoing is true and correct. This certification is executed on December 31, 2019 at Modesto, California.

By 
Nicole Nelson, Deputy