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WHAT ARE THE DIFFERENCES BETWEEN ASSESSMENTS, FEES, AND TAXES?

Local governments use a variety of means besides taxation to generate revenue, including fees and assessments. Since the passage of the 1978 property tax limitation initiative known as Proposition 13, local governments have increasingly turned to alternative methods of raising money to pay for specific services. Revenue from benefit assessments levied by cities more than quadrupled between 1981 and 1994, although it continues to account for a very small portion (1.3 percent) of total city revenue. Assessments also account for a small portion of revenue for counties (.02 percent in 1993-94) and special districts (3 percent of non-enterprise special district revenue in 1992-93).¹

Between 1975-76 and 1993-94, the portion of city revenue accounted for by fees and service charges increased from 32 percent to 41 percent.² Counties' share of revenue from service charges remained constant at nine percent. Service charges have accounted for more than 70 percent of special district budgets during the past 20 years, mostly due to user fees charged for enterprise activities such as water and sewer.³

California laws authorizing local benefit assessments date back to the early years of this century, when local governments used assessments primarily to pay for physical improvements adjacent to the assessed land. Use of assessments as a local revenue source actually peaked during the early decades of the century. More recently, the state has authorized the use of assessments for a broad array of facilities and services ranging from fire suppression to pedestrian malls to the control of pests in the wine industry.⁴ In recent years, local governments' use of fees and assessments has come under increasing criticism from taxpayers'-rights groups, who allege that local jurisdictions disguise tax increases as fees or assessments to circumvent voter approval requirements for new taxes. Local governments respond that they merely follow a long-established practice of charging property owners for services or improvements that benefit the owners' land.

The debate about fees and assessments will attract more attention in the months to come. The November ballot will include an initiative that would amend the state constitution to make it more difficult for local governments to raise revenue through fees and assessments. To promote an informed debate, this

¹ Data is from the State Controller's series of reports on financial transactions of cities, counties, and special districts. The Controller's publications rely on self-reporting by local governments.

² *State and Local Government Finance in California: A Primer* (California Budget Project, 1996).

³ *Ibid.*

⁴ *Assessing the Benefits of Benefit Assessments* (Senate Local Government Committee, May 1995).

Budget Brief describes the differences between taxes, fees, and assessments and the purposes for which they are used. These three revenue tools -- and their uses -- are legally distinct from one another. In practice, however, there is considerable overlap among them. An activity financed by taxes in one jurisdiction might be financed through fees or assessments in another jurisdiction.

WHAT CONSTITUTES "LOCAL GOVERNMENT?"

There is more to local government than cities and counties. Two other major forms of local government are school and community college districts and special districts. The categories of local government differ in terms of the kinds of power they possess and the range of services they provide.

Cities and counties are general purpose governments that provide a wide range of services to local residents. The authority of counties and general law cities is limited to that expressly provided by the state constitution or by statute. Charter cities' powers are defined by their individual charters, by the constitution, and, with respect to matters of statewide concern, by the Legislature.⁵

Special districts are limited-purpose governments that differ from cities and counties in important ways. Special districts are usually formed to provide a specific service, such as fire protection, water service, or street lighting, to a defined geographic area. Some special districts, such as county service areas, provide multiple services. State laws set out the types of special districts that can be formed as well as the rules for forming them.

Cities and counties can make and enforce rules governing behavior and activities (police power), whereas special districts' powers are generally restricted to raising money and providing a service. Special districts may be independent, with their own separately elected governing boards, or they may be dependent, meaning the city council or county board of supervisors serves as the governing board. Roughly two-thirds of California's approximately 4,900 special districts are independent.

Enterprise special districts, which provide services such as water, electricity, or transit that are used by individual customers, are funded primarily through user fees. *Non-enterprise districts*, which provide services such as parks or fire protection that benefit the entire community, rely more heavily on taxes.

School and community college districts exist to provide one service: education. Unlike cities, counties, and special districts, school districts are guaranteed a minimum level of funding by the State Constitution. In addition to their property tax allotment, school districts can raise revenues locally through voter-approved special taxes, assessments for some purposes, and developer fees.

WHAT IS A TAX?

A tax is a charge against an individual or landowner, which pays for public services and facilities that provide general benefits. There need not be a direct relation between an individual taxpayer's relative benefit from services or facilities and the tax he or she pays.

⁵ The California Supreme Court has held that where a city charter and a state statute are in conflict, for the statute to prevail, the state must have good reasons, grounded in statewide interest, to override a charter city's authority. *Johnson v. Bradley* (1992), 14 Cal.Rptr. 2d 470, 4 Cal.4th 389, 841 P.2d 990.

Counties, school districts, and special districts can only impose taxes specifically authorized by the Legislature. Cities may impose any tax not otherwise prohibited by state law.⁶ The state has “reserved” a number of taxes for its own purposes, prohibiting local governments’ use of these revenue sources. For example, the state reserves the right to tax cigarettes and alcoholic beverages.

There are two basic categories of taxes, general and special:

General taxes are defined as those that generate revenue for the general operation of government. In other words, revenues from a general tax may be used for any purpose the governing board chooses to spend it on.

State statutes lay out requirements for local governments planning a new or increased general tax. Generally speaking, the board considering the tax must notify the public of the proposal and hold a public meeting on the tax before adopting it. In 1986, California voters approved Proposition 62, a statutory initiative that required local governments to get majority voter approval before levying a general tax. California appellate courts ruled the vote requirement unconstitutional, but in 1995 the State Supreme Court upheld it.⁷ As a result, California’s general law cities and counties must now gain majority voter approval for all new or increased general taxes. Legal experts disagree as to whether this requirement also applies to the state’s 89 charter cities, since the State Constitution allows charter cities to control their own “municipal affairs.”

A **special tax** is one whose proceeds can only be used for a specified purpose. For example, a city might levy a parcel tax on property to pay for library services, or a county could vote to levy a sales tax for jails. The State Constitution requires that local special taxes be approved by two-thirds of voters. “Special” taxes have been defined through a long series of often conflicting court decisions.⁸

WHAT IS A BENEFIT ASSESSMENT?

A benefit assessment is an involuntary charge levied on property to pay for public improvements, such as roads or street lights, that benefit property. The philosophy behind benefit assessments (also known as special assessments) is to link the cost of public improvements to those landowners who specifically benefit from those improvements. The amount of an assessment on a particular property is related to the amount of benefit that property receives. An assessment may be a flat amount per parcel or based on a measure such as square footage. Assessments cannot be based on the value of property, because Proposition 13 limits the property value-based tax rate to one percent plus additions for certain types of voter-approved debt service. Assessments usually appear on property tax bills.

Charter cities can levy any benefit assessment not otherwise prohibited by state law. General law cities, counties, special districts, and school districts can levy benefit assessments under specific authority granted by state law. California currently has 34 benefit assessment acts on the books, ranging from the Improvement Act of 1911 (for street paving, grading, sewers, and “other necessary improvements”) to

⁶ Charter cities have this power under the home rule provision of the state constitution. The legislature granted the same autonomy to general law cities in 1982 (Government Code Section 37100.5).

⁷ City of Westminster v. County of Orange (1988) 251 Cal.Rptr. 511, 204 Cal.App.3d 623; City of Woodlake v. Logan (1991) 282 Cal.Rptr. 27, 230 Cal.App.3d 1058. In Santa Clara County Local Transportation Authority v. Guardino (1995), the California Supreme Court ruled that a half-cent sales tax imposed by a local transportation authority was a special tax requiring two-thirds voter approval under the terms of Proposition 62.

⁸ See City and County of San Francisco v. Farrell (1982) 184 Cal.Rptr. 713, 32 Cal.3d 47, 648 P.2d 935; Los Angeles County Transportation Commission v. Richmond (1982) 182 Cal.Rptr. 506, 31 Cal.3d 318, 644 P.2d 192; Rider v. County of San Diego (1991) 2 Cal.Rptr.2d 490, 1 Cal.4th 1, 820 P.2d 1000; Santa Clara County Local Transportation Authority v. Guardino (1995) 45 Cal.Rptr.2d 207, 11 Cal.4th 220, 902 P.2d 225.

the Property and Business Improvement District Law of 1994 (for tourism promotion, parking lots, fountains, and other facilities and services to improve commercial areas). The authorization acts vary in terms of which types of local governments can use them, whether voter approval is required, how to spread the costs among landowners, and whether an assessment can be nullified based on property owner protest. Some assessment acts require landowners to petition local officials in order to form a benefit assessment district. Most assessment acts do not require local agencies to get voter approval for a new or increased assessment. However, most do contain provisions nullifying the assessment if a majority of property owners protest, and all require due process.

Since 1992, state law has required that local agencies considering implementing any assessment notify affected landowners 45 days in advance and hold a public meeting and a public hearing on the proposal.⁹ The notice must include the estimated amount of assessment per parcel, the purpose of the assessment, the dates, times, and locations of the public meeting and public hearing, and instructions for protesting the assessment, if applicable. The notice must either be mailed to all affected landowners or advertised in local newspapers, depending on the number of affected parcels and the use of the proposed assessment.

Benefit assessments are usually defined geographically and levied on all properties within a designated benefit assessment district. Some assessment districts exclude certain types of properties from assessments. The boundaries of a benefit assessment district may coincide exactly with those of a city, county, or special district, or they may cover only part of those jurisdictions.

What is the difference between a benefit assessment district and a special district? A special district is a unit of government with a governing board and the authority to raise revenue and provide a limited number of services. A benefit assessment district is not a unit of government. Rather, it is a financing tool used by governments such as cities, counties, and special districts.

WHAT IS A MELLO-ROOS DISTRICT?

A Mello-Roos Community Facilities District is a financing tool that local governments can use to levy special taxes for designated community improvements, such as freeway interchanges, library services, or recreation programs. To levy a Mello-Roos tax, the area's voters (or affected landowners if fewer than 12 voters reside in the district) must consent to being taxed. A two-thirds approval vote is required, since a Mello-Roos tax is always a special tax. Most Mello-Roos districts are established prior to development and are used to finance basic infrastructure.

WHAT IS A FEE OR CHARGE FOR SERVICE?

A fee is a voluntary charge imposed on an individual for a service or facility provided directly to that individual. State law requires that a fee cannot exceed the estimated reasonable cost of providing a service or facility, or else it is considered a special tax. Many enterprise special districts, such as those that provide water or electricity, rely heavily on fees for their operating revenues. Fees usually show up on utility bills, although some fees show up on property tax bills. Community hospitals, operated by hospital districts, are another example of an enterprise activity.

⁹ Government Code, Section 54954.6.

Cities, counties, non-enterprise special districts, and school districts also charge fees for various services, such as sewer connection, user permits, and building code approvals. School districts typically utilize developer fees to partially offset the increased demand for school facilities brought about by new construction.

Local governments are not required to gain voter approval for a new or increased fee, but they must hold a public hearing on the proposed fee and notify the public of the hearing 10 days in advance. For some types of fees affecting property, construction, and development, the public notice must specify the estimated cost of providing the service for which the fee is proposed, and the local agency must hold an additional public meeting where citizens may present testimony.

Certain fees, known as “standby charges,” can be levied on a new development that is or can be connected to local water and sewer systems. Local agencies must notify the general public and affected property owners of the description and amount of the proposed charge, as well as the date, time, and location of a public hearing on the charge. Property owners have a chance to protest these charges. If the local agency receives protests from 40 percent or more of the affected parcels, it must abandon the proposed charge for one year.

Cities, counties, and school districts may impose fees on new developments without voter approval. The fees must bear a reasonable relationship to the need for additional public services and facilities generated by the new development. Developer fees are subject to public notice and hearing requirements similar to those for other types of fees.

CONCLUSION

Despite recent controversy over their use, benefit assessments are actually a long-standing source of local revenues. Assessments provide a relatively small share of local revenues for a broad range services. How assessments work, what they fund, who they are levied by, and how they are imposed is often confusing due to the large number of laws governing their use. Improved communication can help alleviate misconceptions and provide voters with the information needed to evaluate the use of the taxes and fees they pay. Future *Budget Briefs* will explore in greater detail how fees and assessments are used, their costs, and the services funded through the use of benefit assessments.

SOURCES FOR MORE INFORMATION:

The following publications provide additional details on the role of fees and assessments in local government finance:

League of Women Voters, *State and Local Finances: The Current Situation, Study Guide I*. (1994)

Paik, Helen C., *Local Government Finances Since Proposition 13: A Historical Primer*. Sacramento, CA: California Research Bureau, California State Library (1995).

Senate Committee on Local Government, *Assessing the Benefits of Benefit Assessments: A Citizen's Guide to Benefit Assessments in California*. Sacramento, CA: Senate Publications (1995).

Senate Committee on Local Government, *Public Revenues, Public Awareness*. Sacramento, CA: Senate Publications (1993).

Senate Committee on Local Government, *What's So Special About Special Districts? A Citizen's Guide*

to *Special Districts in California* Second Edition. Sacramento, CA: Senate Publications (1993).

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