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IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

SUPREME COURT
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CALIFORNIA FARM BUREAU FEDERATION, ET AL.

Plaintiffs and Appellants,

v.

CALIFORNIA STATE WATER RESOURCES CONTROL BOARD, ET AL.,

Defendants and Respondents.

S 150518

Court of Appeal, Third Appellate District, Case No. C050289
Sacramento County Superior Court Case Nos. 03CS01776, 04CS00473
The Honorable Raymond Cadei, Judge

STATE'S ANSWER BRIEF ON THE MERITS TO BRIEF OF CALIFORNIA FARM BUREAU FEDERATION

EDMUND G. BROWN JR.
Attorney General of the State of California
PAUL GIFFORD
Senior Assistant Attorney General
GORDON BURNS
Deputy Solicitor General
WILLIAM L. CARTER
Supervising Deputy Attorney General
MATTHEW J. GOLDMAN
MOLLY K. MOSLEY, SBN 185483
Deputy Attorneys General
1300 I Street
P.O. Box 944255
Sacramento, California 94244-2550
Telephone: (916) 445-5367
Facsimile: (916) 327-2247

Attorneys for the California State Water Resources Control Board, the California State Board of Equalization, et al.

TABLE OF CONTENTS

	Page
ISSUES PRESENTED	1
STATEMENT	1
A. The fee legislation.	1
B. The SWRCB's extensive regulation of permits and licenses, and its limited regulation of other water rights.	2
C. The SWRCB's regulations implementing the fees.	4
D. Trial court proceedings.	10
E. Court of Appeal proceedings.	11
ARGUMENT	12
I. Water Code section 1525 is constitutional.	12
A. The *Sinclair Paint* test is met because most of the agency's costs are attributable to the regulation of permittees and licensees, not other water right holders.	12
1. The Farm Bureau mischaracterizes the water right program.	13
2. The Legislature's annual budget for the regulatory activities does not invalidate the fee.	15
3. Section 1525's imposition of annual permit and license fees to support most of the water right fee program, when most of the program is directed to the regulation of permits and licenses, does not cause this case to differ "materially" from cases upholding the fee structure.	16
4. The "polluter pays" rationale applies.	17
5. Neither the legislative history nor the SWRCB's comments on the the proposed legislation support the Farm Bureau's contentions.	19

TABLE OF CONTENTS (continued)

Page

C. Asserting that water rights are a type of real property does not make the ad valorem taxes on real property in violation of Proposition 13. 20

II. The regulations validly allocate the fees. 21

A. The regulations do not impose the "costs" of others on annual fee payers. 21

B. The flat, minimum fee of $100 is reasonable and does not disproportionately allocate costs among the fee payers. 23

C. Neither the statute nor the regulations are made invalid by the fact that the SWRCB collected fees in an amount greater than set in the Budget Act. 26

D. The risk of non-collection is an administrative cost that must be taken into consideration in setting fees that provide most of a regulatory program's support. 30

III. Courts do not have the power to fashion a refund remedy when the Legislature has provided one. 32

A. The issue of whether administrative exhaustion is required even if the agency cannot grant the relief requested is not presented. 33

B. Exhaustion of administrative remedies is a jurisdictional pre-requisite where mandated by statute. 35

C. The provisions of Revenue and Taxation Code section 55221 are not applicable. 38

D. The Takings Clause is not implicated by the requirement of the exhaustion of administrative remedies. 40

CONCLUSION 41

CERTIFICATION OF WORD COUNT 42

TABLE OF AUTHORITIES

Page

Cases

Abelleira v. District Court of Appeal
(1941) 17 Cal.2d 280 ... 34, 35

California Assn. of Professional Scientists v. Department of Fish and Game
(2000) 79 Cal.App.4th 935 ... passim

California Trout, Inc. v. State Water Resources Control Bd.
(1989) 207 Cal.App.3d 585 ... 18

City of Pasadena v. City of Alhambra
(1949) 33 Cal.2d 908 ... 3

In re Attorney Discipline System
(1998) 19 Cal.4th 582 ... 15

Joerger v. Pacific Gas & Elec. Co.
(1929) 207 Cal. 8 ... 4

Jordan v. Department of Motor Vehicles
(1999) 75 Cal.App.4th 449 ... 37

Marquez v. Gourley
(2003) 102 Cal.App.4th 710 ... 35

Metcalf v. Los Angeles
(1944) 24 Cal.2d 267 ... 40

Mills v. County of Trinity
(1980) 108 Cal.App.3d 656 ... 15

Modern Barber Colleges, Inc. v. California Employment Stabilization Comm.
(1948) 31 Cal.2d 720 ... 34

National Audubon Society v. Superior Court
(1983) 33 Cal.3d 419 ... 4, 14

	Page
Pacific Motor Transport Co. v. State Bd. of Equalization (1972) 28 Cal.App.3d 230	39
Patane v. Kiddoo (1985) 167 Cal.App.3d 1207	34, 36
Pennell v. City of San Jose (1986) 42 Cal.3d 365	25
People v. Shirokow (1980) 26 Cal.3d 301	3
San Diego Gas & Electric Co. v. San Diego County Air Pollution Control Dist. (1988) 203 Cal.App.3d 1132	12, 25
Sinclair Paint Co. v. State Bd. of Equalization (1997) 15 Cal.4th 866	passim
Walker v. Birmingham (1967) 388 U.S. 307	40
White v. Davis (2003) 30 Cal.4th 528	28
Yakus v. United States (1944) 321 U.S. 414, 64 S.Ct. 660	40
United States Constitution	
art. VI, § 2 (Supremacy Clause)	10, 12
California Constitution	
art. III, § 3.5(a)	36
art. III, § 5	32
art. X, § 2	4
art. XIII A, § 3 (Proposition 13)	passim

Page

California Statutes

Government Code

§ 11254 27
§ 11350 (a) 39

Revenue & Taxation Code

§ 55221 38, 39
§ 55221 (a) 39

Water Code

§ 100 4
§ 102 3, 23
§ 174 3, 23
§ 275 4
§ 1120 34, 38
§ 1126 33, 34, 38
§ 1126 (b) 35
§ 1126 (d) 33
§ 1126 (e) 34
§ 1201 3, 23
§ 1202 3, 23
§ 1525 passim
§ 1525 (a) 1, 9
§ 1525 (c) 2, 3, 13
§ 1525 (d) 27
§ 1525 (d)(1) 2
§ 1525 (d)(3) passim
§ 1525 (e) 26
§ 1528 19
§ 1530 (a) 7, 27
§ 1535 (b) 30
§ 1537 (b) 32, 33
§ 1537 (b)(1) 38
§ 1537 (b)(2)-(3) passim
§ 1537 (b)(4) 33, 34, 39

TABLE OF AUTHORITIES (continued)

	Page
§ 1540	8, 22
§ 1550	2
§ 1552	2
§ 1560	8, 22
§ 1675	4
§ 2850 et seq.	19

California Rules of Court

Rule 8.520	1

California Code of Regulations

tit. 23, § 769	36
tit. 23, § 1066	5, 7, 9, 11
tit. 23, § 1066 (a)	8
tit. 23, § 1071	8
tit. 23, § 1073	8, 9, 12, 22
tit. 23, § 1077	36, 38
tit. 23, § 1077 (c)	39

ANSWER BRIEF ON THE MERITS

Under California Rules of Court, Rule 8.520, the California State Board of Equalization (BOE) and the California State Water Resources Control Board (SWRCB) (SWRCB and BOE, collectively, the State) submit the following Answer to the California Farm Bureau Federation's (Farm Bureau's) Opening Brief on the Merits.

ISSUES PRESENTED

The Farm Bureau briefs the following issues:

1. Does Water Code section 1525, which was amended by the Legislature by majority vote in 2003 to impose annual fees on the persons and entities holding permits and licenses issued by the [SWRCB], impose an invalid tax or a lawful regulatory fee?

2. If the statutory scheme is valid, but the regulations implementing it are invalid, did the Court of Appeal err in limiting refunds to only those persons and entities filing petitions for reconsideration before the [SWRCB]?

STATEMENT

A. The fee legislation.

The SWRCB and its Division of Water Rights (Division) are responsible for the regulation of water rights in California. New legislation that took effect in fiscal year 2003-2004 aimed to shift most of the burden of water right regulation from the General Fund to the regulated community of state water right permit and license holders by enacting new, annual permit and license fees and increasing the existing filing fees. (Wat. Code, § 1525, subd. (a) [establishing the annual permit and license fees]; Slip op., pp. 2, 13.) The fees cover essentially all of the activities that comprise the

SWRCB's water right program. (Wat. Code, § 1525, subd. (c).) The fees are deposited in the Water Rights Fund. (*Id.*, § 1525, subd. (d)(1); *id.*, § 1550.) Monies in the Water Rights Fund are "available for expenditure, upon appropriation by the Legislature" to carry out the statutory purposes of the SWRCB's water right program. (*Id.*, § 1552.)

For fiscal year 2003-2004, the Legislature directed that the new fees would provide only about half of the water right program's funding (although the fees may be used to pay for virtually all of the water right program's activities). (Appellants' Appendix (Appendix) 2473.) The total cost of the program for fiscal year 2003-2004 was about $9 million. (Slip op., p. 21, fn. 16.) To implement the fee-based funding in fiscal year 2003-2004, the law required SWRCB to adopt emergency regulations immediately (slip op., p. 21) to collect a budget "target" for the Water Rights Fund of about $4.4 million. (Appendix 2341-2342; 2473 [Budget Act specifies $4.4 million in fee revenues].) Amounts payable from other funds, including the General Fund, covered the difference between the $9 million budget for the water right program (Appendix 2341 [schedule item 2] and the $4.4 million in regulatory fees to be collected and deposited into the Water Rights Fund (Appendix 2342 [schedule item 21.5]).

B. The SWRCB's extensive regulation of permits and licenses, and its limited regulation of other water rights.

The annual fees at issue in this lawsuit are imposed on the group of water right users -- users of water held under state permits and licenses -- that account for about 95

percent of the SWRCB's regulatory efforts. (Appendix 2298; Water Code, §§ 102, 174, 1201-1202.) The lower court recognized, and plaintiffs concede, that the agency has limited authority over various types of water rights that, under California law, exist independently of the permit and license scheme–including riparian,[1] pueblo, and appropriative rights acquired prior to 1914. (See slip op., p. 7 [SWRCB's "core regulatory program, the administration of water right permits and licenses, does not apply" to holders of other types of water rights]; see also Appendix 1200:9-10 [plaintiff's brief claiming SWRCB has *no* authority over pre-1914 water rights] and 3289:13-25 [transcript of trial court hearing discussing plaintiff's claim that SWRCB lacks jurisdiction over non-permitted and licensed water rights].) Indeed, the SWRCB estimates that it spends only a de minimis amount (about five percent) of its time regulating the water rights that are not subject to the annual fees at issue in this lawsuit. (Appendix 2298; see Wat. Code, § 1525, subd. (c).)

The SWRCB regulates the complex system of water rights in California to bring order and certainty to the system as well as to protect the public interest. (See Appendix 2679-2686.) The SWRCB must act to ensure that each permittee and licensee is obeying the terms and conditions of the permits or licenses under which they hold their water rights. The SWRCB may periodically reevaluate those terms and

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[1] A riparian water right "confers upon the owner of land contiguous to a water course the right to the reasonable and beneficial use of water on his land." (*People v. Shirokow* (1980) 26 Cal.3d 301 quoting *City of Pasadena v. City of Alhambra* (1949) 33 Cal.2d 908, 925.) The riparian right does not include a right to use water on parcels that are not adjacent to and in the watershed of the stream.

conditions because what constitutes both a reasonable and beneficial use can change over time. (Appendix 2100 [permit describing SWRCB's continuing authority over "all rights and privileges under this permit and under any license issued pursuant thereto"].) Even after the permittee has obtained a license, the SWRCB may revoke the license if it finds that the licensee has not put or has ceased to put the water to a useful and beneficial purpose or has not complied with any of the terms and conditions of the license. (Wat. Code, § 1675.)

The SWRCB also has authority to ensure that the waters of the State are put to full beneficial use and to prevent waste, unreasonable use, unreasonable method of use or unreasonable method of diversion (Cal. Const., art. X, § 2; Wat. Code, §§ 100, 275; *Joerger v. Pacific Gas & Elec. Co.* (1929) 207 Cal. 8, 22); protect the public trust (*National Audubon Society v. Superior Court* (1983) 33 Cal.3d 419); and avoid or minimize any harm to natural and public trust resources where feasible. (See, e.g., Appendix 2847-2854 [SWRCB Decision directing action to avoid adverse impact of water project on wildlife habitat and irreplaceable oak trees]; Appendix 2090-2101 [permit for diversion and use of water containing terms to protect recreational uses of various lakes involved and requiring mitigation plan to prevent wastewater discharges from the project from unreasonably affecting wildlife or aquatic habitat].)

C. The SWRCB's regulations implementing the fees.

After considerable review and two public workshops, the SWRCB decided to impose annual fees that are calculated based on the "face value" of the permits or licenses (i.e., the total amount of water that theoretically could be diverted in any year

under a permit or license). (Cal.Code Regs., tit. 23, § 1066.) In so doing, the SWRCB rejected several other options.

The agency decided against basing the fees on *actual* water usage, as opposed to the face value of the permit or license: "Staff also does not recommend basing the fee on the amount of water actually diverted or used, as this information is not submitted to the SWRCB on an annual basis, and the SWRCB cannot annually calculate or adjust fee revenues accurately using this approach." (Appendix 2305; *id.*, 2305-2306 [explaining the difficulties]; 2507-2520 [issue paper studying whether SWRCB could assess fees based on actual water usage].)

The SWRCB also rejected a "fee-for-service" approach, under which each water right holder or applicant is charged based on the time spent reviewing that person's proposals or activities, as infeasible because the program is a regulatory program and is not based on requested "services." (Appendix 2304-2305; 2473-2474 [Notice of Public Workshops].) Funding for the program must be stable because continuing regulatory oversight requires constant SWRCB administration. Sporadic, one-time filing fees are insufficient to support an ongoing regulatory program.

Furthermore, water right regulation is necessarily complex because of the interlocking nature of water rights. (E.g., Slip op., pp. 4-12 [describing complex system of water rights]; Appendix 2508 [describing irrigation district claiming to hold 47 water rights including riparian, prescriptive, pre-1914 and appropriative rights, many of which combine water, making it impossible to segregate water use and determine annual use of a particular right].) Because of this complexity, the calculation of precise

actual costs would be difficult, if not impossible, and may unjustifiably increase the administrative costs of the fee. (Appendix 2249:11 - 2250:24.)

Moreover, collecting precise actual costs would entail much higher filing fees (e.g., $23,000 per application), increasing the likelihood of unauthorized diversions and a greater enforcement burden. (Appendix 2423.) Annual fees are less expensive to administer and provide certainty to the regulated community regarding the amount of fees to be assessed.

The SWRCB determined that protecting other water right holders represents a substantial portion of the cost of processing water right applications and petitions, including the consideration of protests from permit and license holders. (Appendix 2304.) More broadly, a substantial portion of the SWRCB's costs are related to actions that are for the primary purpose of managing existing permitted and licensed water rights.

For these reasons, the SWRCB determined that the annual fees would most reasonably apportion the costs of regulation and should provide most of the fee funding. (Appendix 2304-2305; see *id.,* 2354-2377 [presentation at workshops explaining fee regulations].) It adopted fee regulations that, while substantially increasing the one-time filing fees related to the permit and license system (e.g., application and petition fees), kept these filing fees relatively low to encourage voluntary filings and to reduce enforcement problems associated with unauthorized diversions. (Appendix 2423.)

To meet the Legislature's target amount for fiscal year 2003-2004, $4.4 million, the SWRCB set the annual fees at the greater of $100 or $0.03 per acre-foot based on the "face value" of the permit or license, not the amount that was actually used or delivered. (Appendix 2438; *id.,* 2453 [former Cal. Code Regs., tit. 23, § 1066, subd. (a) (2004)];[2] see Wat. Code, § 1530, subd. (a) [permitting fee schedules to be "graduated in accordance with the number of diversions or the amount of water involved"]; Appendix 2429-2430.) It is important to note that the "face value" almost always exceeds the actual amount of water that can be used or diverted–sometimes vastly so–for a variety of reasons, including, for example, regulatory restrictions that require a permittee to provide a minimum flow downstream and limits on the availability of water. (Appendix 2121-2122; *id.*, 2306 [explaining "face value"]; see e.g., *id.*, 2093-2095 [permit items 8-11] and 2099 [item 31].)

The SWRCB used the face value of the permit or license to set the annual fee, reasoning that, in general, the more water held under the permit or license, the greater the regulatory burden. In general, larger projects have greater environmental impacts, involve more controversial issues, and affect a greater number of people, correspondingly increasing the costs of regulation. (Appendix 2243:17 - 2244:15; Cal.

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[2] In 2004, section 1066 was amended to change the way the fees were calculated: "A person who holds a water right permit or license shall pay a minimum annual fee of $100. If the total annual amount of diversion authorized by the permit or license is greater than 10 acre-feet, then the permittee or licensee shall pay an additional $0.025 for each acre-foot in excess of 10 acre-feet." The rate per acre-foot can change on a yearly basis to reflect the adjustment required under section 1525, subdivision (d)(3) of the Water Code.

Code Regs., tit. 23, § 1066, subd. (a).)

In setting the $100 minimum annual fee, the SWRCB took into consideration the cost of billing the fees as well as an estimate of the minimum amount of time spent regulating smaller water rights. (Appendix 2307, 2382-2427 [worksheets for fee system development]; Appendix 2242:20-24 [explanatory testimony]; Administrative Record 2.)

To ensure that it collected no less than the amount set by the Budget Act, the SWRCB estimated the risk of non-collection, an administrative cost. For the first year of fee collection, the SWRCB conservatively assumed a 60 percent rate of collection based on staff's experience with return rates on required filings, initial resistance to the fees, and the accuracy of the billings. (10 Appendix 2304.)

About 20 percent of the face value of all state permitted and licensed water rights are held by the United States Bureau of Reclamation ("Bureau") for the Central Valley Project ("CVP"). The Legislature addressed the likelihood that the Bureau would claim sovereign immunity and refuse to pay the fees by enacting statutes to allow for these fees to be imposed on the federal water contractors instead of the Bureau. (Slip op., p. 11; Wat Code, §§ 1540, 1560; slip op., p. 19, fn. 15.)

Accordingly, the SWRCB imposed the annual fees for permits and licenses held by the Bureau for the purpose of water delivery on the CVP contractors who hold the contractual right to the water developed under the Bureau's CVP permits and licenses. (Cal. Code Regs., tit. 23, §§ 1071, 1073; Appendix 2332 [main purpose of CVP is to supply water]; see Appendix 2322 et seq. [examples of contracts]; slip op.,

pp. 24-25 [describing the regulatory allocation to the CVP contractors].) The regulations also provide a fifty percent discount for all of the Bureau's hydropower permits and licenses (for diverting the water) not subject to licensing by the Federal Energy Regulatory Commission (FERC), effectively further reducing the face value of the Bureau's permits and licenses. (Appendix 2307-2308; *id.*, 2294 [errata to discussion].) The federal contractors pay only the annual fees for the permits and licenses associated with their projects; they do not pay any other fees, such as any application and petition filing fees associated with CVP water rights.

Together, sections 1066 (annual fees) and 1073 (imposition of annual fees on federal contractors) of the California Code of Regulations, title 23, impose annual fees on all water rights subject to permit and license. (Wat. Code, § 1525, subd. (a).) Regulation of appropriations subject to permit and license constitutes the core of the SWRCB water right program –accounting for about 95 percent of all expenditures -- and appropriations under permit and license amount to about 60 percent of all water diverted under all water rights. (Appendix 2298; see slip op., p. 55 [Appendix to Opinion].) The regulations impose annual permit and license fees on all permits and licenses, either directly (section 1066) or indirectly (section 1073). As it does for many other fee programs, BOE acts as the SWRCB's collector for the annual fees, but it does not have any authority to review SWRCB's fee determinations. (Wat. Code, § 1537, subd. (b)(2)-(3); slip op. p. 51.)

D. Trial court proceedings.

After the SWRCB denied their petitions for reconsideration challenging the fees, persons subject to the annual permit and license fees filed lawsuits against SWRCB and BOE to challenge the constitutionality of the statutes and the validity of the regulations. The consolidated action (brought as writs of administrative mandate and complaints for declaratory relief) alleges that the fee statutes and regulations are unconstitutional because they fail to meet the test for a valid regulatory fee. Plaintiffs contend: (1) the fees collected exceed the regulatory program costs they are designed to support; and (2) there are insufficient facts to support the basis for determining the manner in which the costs are apportioned, so that charges allocated have not been shown to bear a fair or reasonable relationship to the payer's burdens on or benefits from the regulatory activity. (Slip op., p. 26.) Plaintiffs allege, among other things, that requiring state permit and license holders to pay for most of the program, when 40 percent of all water rights in the state are held under other types of rights, is not reasonably related to the burdens imposed or the benefits received. They also allege that the SWRCB's fee schedule is invalid because it is not based on actual costs. Finally, they allege that the imposition of fees associated with the CVP on the water supply contractors violates the Supremacy Clause of the United States Constitution. (U.S. Const., art. VI, § 2.)

Plaintiffs seek declarations of the invalidity of the statutes and regulations imposing the annual water right fees, injunctive relief against their enforcement, and on that basis, refunds of all fees paid. (Appendix 25-26 [NCWA's Verified Complaint,

Prayer for Relief]; Appendix 154 [NCWA's First Amended Verified Complaint, Prayer for Relief]; Clerk's Augmented Transcript on Appeal 37-40 [Farm Bureau's Verified Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandate, Prayer for Relief].) The statutes require a writ of administrative mandamus to obtain the requested refunds. (Wat. Code, § 1537, subd. (b)(2)-(3).)

In 2005, the trial court entered its judgment denying the consolidated petitions for writ of mandate and complaints for declaratory and injunctive relief. The trial court held that all of the activities funded by section 1525 fees bear a "sufficiently close relation to the regulation of water rights that they may be legitimately considered to be part of the water rights regulatory program." (Appendix 3363:1-2.) Giving deference to the agency's factual findings and considerations in allocating the fees, the trial court found that the SWRCB satisfied the requirements of law in developing its fee structure: "[T]he fee structure . . . was not adopted on a merely arbitrary basis, but was developed after careful consideration of factors specific to the regulatory program of the Division of Water Rights." (Appendix 3364:7-10.)

E. Court of Appeal proceedings.

In January 2007, the Court of Appeal issued its opinion upholding the fee statutes but striking down the regulations based on its conclusion that the fee allocation made by the regulations failed to meet the test for a valid regulatory fee. (Slip op., pp. 30, 43, and 44.) Although the Court of Appeal held that the statutes imposed valid regulatory fees (slip op., p. 29), it invalidated the water right fee regulations because the court found (1) section 1066 violates Proposition 13 by failing to show the basis for

apportioning costs as between fee payers subject to annual permit and license fees and other types of water right holders who are not, but who "benefit" from the regulatory program (slip op., pp. 40-43); and (2) the allocation of most of the Bureau's fees to the federal water contractors under section 1073 violates the Supremacy Clause because the Court of Appeal found that the SWRCB did not determine what share of the costs of regulating the CVP should be allocated to the contractors (slip op., pp. 44-45).

ARGUMENT

I.

Water Code section 1525 is constitutional.

A. The *Sinclair Paint* test is met because most of the agency's costs are attributable to the regulation of permittees and licensees, not other water right holders.

Most of the Farm Bureau's arguments founder on one key fact that the Farm Bureau fails to grapple with: the fee covers the cost of regulating those who pay the fee -- the permittees and licensees -- not other water right holders or the general public. Under *Sinclair Paint*, therefore, the fee bears a "reasonable relationship" to the payor's "burdens on . . . the regulated activity" because the payors (the permittees and licensees) are paying the cost of regulating *their* activities. (*Sinclair Paint Co. v. State Bd. of Equalization* (1997) 15 Cal.4th 866, 878, quoting *San Diego Gas & Electric Co. v. San Diego County Air Pollution Control Dist.* (1988) 203 Cal.App.3d 1132, 1146 *(SDG&E)*.)

Regulatory fees are not imposed on those who are not the subject of the regulatory program, even if they may also affect the resource. The Legislature does not

have to charge a fee on all manufacturers of heavy metals to mitigate their effects on children for the Childhood Lead Poisoning Prevention fee to be valid.

1. The Farm Bureau mischaracterizes the water right program.

The Farm Bureau's argument rests primarily on the notion that Water Code section 1525 imposes a fee on one small class of water right holders -- permittees and licensees -- for regulatory costs that are somehow attributable to others. Like the court below, the Farm Bureau is mistaken.

The Farm Bureau implies that the plain language of Water Code section 1525 requires licensees and permittees to pay for the agency's regulation of other water right holders. (E.g., Farm Bureau, p. 18.) The claim cannot withstand scrutiny. NCWA claimed the agency has no significant regulatory authority over these water rights (Appendix 1200:9-10) and the Farm Bureau points only to the benefits received by other water right holders and the general public. The SWRCB estimates that it spends only a de minimis amount (about five percent) of its time regulating these other water rights. (Appendix 2298 [about five percent of time spent regulating other water rights besides post-1914 appropriative].)

The Farm Bureau accepts that the activities for which the fees may be used to pay amount to virtually all of the water rights program. (Farm Bureau, p. 31.) These activities, by their express terms, all involve the regulation of the fee payers, i.e., the "issuance . . . monitoring, and enforcement of permits, licenses . . . ." (Wat. Code, § 1525, subd. (c).) Nevertheless, the Farm Bureau also maintains that a significant portion of the program involves activities not listed in subdivision (c) of Water Code section

1525. (Farm Bureau, p. 33.) If -- as in fact is the case -- the activities for which costs may be recovered describe *virtually* all of the water right program activities (see Farm Bureau, p. 31), then the law reasonably apportions water right program costs between permit and license holders and holders of other types of water rights because the former account for virtually all of the burden on the regulatory program.

The Farm Bureau suggests that permittees and licensees "are forced to shoulder the burdens . . . attributable to more than two thirds of all water right holders." (Farm Bureau, p. 18, emphasis omitted.) It is unclear what "burdens" the Farm Bureau means. The relevant burden is the cost of the regulatory activities for which the fee is charged, and, again, 95% of that cost is attributable to permittees and licensees.[3] Because other water right holders are not subject to the state's permit and license system, they account for only about five percent of the state's regulatory effort. (Appendix 2298.) Accordingly, most of the SWRCB's regulatory costs arise from the regulation of those who use water subject to permit and license.

Finally, the Farm Bureau suggests that it is illegal to impose a fee for regulatory activities that benefit the general public. (E.g., Farm Bureau, pp. 18-20.) Of course, when the SWRCB regulates permittees and licensees, it frequently enforces the public trust, environmental laws, or similar requirements that benefit the general public. (See *National Audubon Society v. Superior Court* (1983) 33 Cal.3d 419 [SWRCB has a duty

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[3] In any case, permittees and licensees account for about sixty percent of the appropriated water in the state, not one third. (AA567 [post-1914 appropriative rights, i.e., permitted and licensed water rights, approximate 60 percent of all surface water rights].)

to enforce public trust against permit holders].) But a regulatory fee is not invalid because the regulation benefits the general public. (Cf., *In re Attorney Discipline System* (1998) 19 Cal.4th 582 [imposing regulatory fee on licensed attorneys to cover cost of attorney disciplinary system that protects the public].) Regulatory fees, enacted pursuant to the state's police power, inherently benefit the public by protecting its health, safety, and welfare. (*Mills v. County of Trinity* (1980) 108 Cal.App.3d 656, 661.) The whole point of the fee – like most regulatory fees – is to shift the cost of regulating permittees and licensees *from* the general public to the regulated community. (*Sinclair Paint, supra,* 15 Cal.4th at p. 879 [reasonable way to achieve Proposition 13's goal of tax relief is to shift the costs of regulation off the back of the tax-paying public and to the regulated entities themselves].)

2. The Legislature's annual budget for the regulatory activities does not invalidate the fee.

The Farm Bureau observes that because the amount of the fees depends upon the Legislature's annual budget for the SWRCB's regulatory activities, and on that basis, argues that the legislation necessarily fails the "reasonable relationship" test of *Sinclair Paint* because the fees "correlate" to a potentially-variable budget figure, rather than to the burdens created by the permittees and licensees. (Farm Bureau, p. 32.)

This is incorrect. The fees correspond to a burden created by the permittees and licensees because the fee covers the agency's cost of regulating them. The Legislature, by its grace, may increase or decrease the scope of the program through the budget process, and it may choose to subsidize the program with General Funds. (See Wat.

Code, § 1525, subd. (d)(3).) But whether and to what extent the Legislature and the General Fund should support the regulation of permittees and licensees in California are policy decisions for the Legislature. (Cf., *Sinclair Paint, supra,* 15 Cal.4th at p. 879 [reasonable way to achieve Proposition 13's goal of tax relief is to shift the costs of regulation off the back of the tax-paying public and to the regulated entities themselves].) For purposes of *Sinclair Paint*, the requisite burden is met because the fees pay the cost (whatever its precise amount) of regulating the fee payers.

3. Section 1525's imposition of annual permit and license fees to support most of the water right fee program, when most of the program is directed to the regulation of permits and licenses, does not cause this case to differ "materially" from cases upholding the fee structure.

The Farm Bureau states that "no case has upheld a regulatory fee where the costs of essentially an entire regulatory program are allocated to only one of the several classes imposing burdens on or benefiting from that program." (Farm Bureau, p. 38.)

Having chosen to obfuscate the nature of the regulatory program, however, the Farm Bureau misperceives the issue. As explain in Section IA, above, 95% of the agency's regulatory costs are attributable to the fee-payers – the permittees and licensees. The remaining five percent (costs attributable to regulating other water right holders) is the sort of *de minimis* exception necessarily inherent in any fee schedule recognized by this Court and approved of in *California Assn. of Professional Scientists v. Department of Fish and Game* (2000) 79 Cal.App.4th 935 (*CAPS*). (*Sea & Sage Audubon Society, Inc. v. Planning Com.* (1983) 34 Cal.3d 412, 422, fn. 5 ["practical considerations dictate that a fee schedule be based on reasonable generalizations"];

CAPS, supra, 79 Cal.App.4th at p. 943 [upholding exemption of sixty-eight percent of all projects from payment of fees because they may be *presumed to be* less of a burden to the state].)

The Farm Bureau's real complaint is that the Legislature should have allocated a portion of the fee to the general public and to other classes of water right holders because they benefit from the regulatory program. No cases suggest that the Legislature is required to do so. The Legislature has discretion to regulate, and impose a fee on, one group to the exclusion of others, so long as the requisite nexus in *Sinclair Paint* is met.

4. The "polluter pays" rationale applies.

The Farm Bureau argues that the "polluter pays" rationale of regulatory fee cases does not apply here because the fee payers serve a public purpose and should be encouraged, not discouraged, from using water to the fullest extent of which they are capable. (Farm Bureau, pp. 41-45.) The Farm Bureau misses the point entirely.

The constitutional mandate to ensure that water is put to its fullest beneficial use requires the SWRCB's oversight to ensure that water is not wasted or monopolized. The need to conserve water in California is essential: it allows the fullest possible beneficial use by all diverters and preserves water for instream beneficial use.

Who decides what is the most beneficial use? Local public water agencies who hold permits and licenses, no less than other permittees and licensees, are subject to – and require – ongoing SWRCB regulation. (E.g., Appendix 2728-2735 [cease and desist order against Mendocino County Russian River Flood Control and Water Conservation Improvement District to prevent illegal diversion of water]; Appendix

2737-2742 [settlement after issuance of Administrative Civil Liability Complaint against the Metropolitan Water District of Southern California for violation of Water Code].) The concerns of local public water agencies are necessarily provincial. The SWRCB is the state-wide agency charged with efficiently allocating the state's scarce water resources among all permittees and licensees.

By keeping the application and petition fees low, the SWRCB seeks to encourage voluntary filings and to reduce enforcement problems associated with unauthorized diversions. (Appendix 2423.) Likewise, charging higher fees for higher face value may reasonably be assumed to provide incentives to seek voluntary revocation of permits that are not being used, and to conserve water. The Farm Bureau assumes no public policy in favor of any of these incentives. (See *California Trout, Inc. v. State Water Resources Control Bd.* (1989) 207 Cal.App.3d 585, 618-619 [strong public policy against holding water in "cold storage" by holding permits and licenses for excessive amounts].)

Finally, the "polluter pays" rationale does not require the fee structure itself to incorporate incentives that "regulate" the fee payer; it simply means that the regulated entities (the polluter) can be made to pay for the cost of regulating their activities. *Sinclair Paint* was *unusual* in that the fees did not pay for the cost of a program to regulate the feepayers. (*Sinclair Paint, supra,* 15 Cal.4th at p. 877 [usual police power measures impose fees to defray the actual or anticipated adverse effects of various business operations].) In *Sinclair Paint*, the fees paid to mitigate harm caused by *past* actions that were not illegal at the time; it was enough that the heavy fees might encourage the entities to try to be more careful in the future. (*Ibid.*)

5. Neither the legislative history nor the SWRCB's comments on the proposed legislation support the Farm Bureau's contentions.

Finally, the Farm Bureau points to various statements made by the SWRCB during the early stages of the legislation to support its argument that the statute covers activities unrelated to the permittees and licensees.

Whether the SWRCB preferred to maintain the funding status quo is of no legal consequence. No authority supports the proposition that the arguments of a bill's opponents establish either the intent of the Legislature or the facts upon which the validity of the bill is to be judged. A better assumption is that the Legislature rejected the arguments.

The SWRCB's comments on the Legislative Analyst's recommendations – *not the ultimate legislation* – made assumptions about the proposed fee system that did not come to fruition. For example, the SWRCB assumed that the fees attributable to the CVP would be reallocated to other permit and license holders, instead of allocated to the CVP contractors. The SWRCB also assumed that permit and license fees would be used to help cover the cost of adjudicating the rights of riparian and pre-1914 water right holders. (See Farm Bureau, p. 13.) However, the fee legislation revised the statutes related to statutory adjudications and court references (which carry fees and expenses that apply to riparians and pre-1914s to the same extent as they apply to permit and license holders), to ensure recovery of the full cost of these proceedings. (See Wat. Code, §§ 1528, 2850 et seq.)

In making its policy arguments before the law's enactment, the SWRCB did not state any facts that would support a legal finding of the fees' invalidity. (See e.g., Farm Bureau's Opening Brief, pp. 12-13.) To the contrary, imposing fees on persons whose activities the SWRCB spends most of its time regulating -- while exempting others who may benefit from the regulation but *"are not routinely supervised"* (3 AA 597, 599) and are "outside the [SWRCB's permitting and licensing] jurisdiction" (4 AA843) -- meets the test for a valid fee established by this Court in *Sinclair Paint*.

The Farm Bureau also cites from the "Arguments . . . Pro and Con" section of the Enrolled Bill Report the statement that other water right holders "will get a 'free ride' because they will not be subject to the annual fees. . . ." (Farm Bureau, p. 18, citing 4 AA891 [SB 1049 Enrolled Bill Report]; *id.*, pp. 35-36 and fn. 12.) An enrolled bill report includes both a pro (sign the bill) and a con (do not sign the bill) argument. This statement is taken from the arguments against signing the bill, and cannot reasonably be represented as the position of either the Legislature that passed the bill or the Governor who signed it.

C. Asserting that water rights are a type of real property does not make the fees ad valorem taxes on real property in violation of Proposition 13.

Section 1525 does not impose new ad valorem taxes. (Farm Bureau, p. 29; see Cal. Const., art. XIII A, § 3 [barring all new ad valorem taxes on real property].) The Farm Bureau does not contend that the fees are ad valorem; i.e., imposed based on an assessment or appraisal of the value of the water right. The water right fees are imposed based on the cost of the regulation. Arguing about the nature of property right involved

does not answer the issue presented.

II.

The regulations validly allocate the fees.

Under the guise of attacking the statute "as applied," (meaning "as applied" through the regulations), the Farm Bureau also attacks the SWRCB's regulations implementing Water Code section 1525. (Farm Bureau, pp. 45-52.) The Farm Bureau does not challenge the statute "as applied," it challenges the SWRCB's quasi-legislative rulemaking.

A. The regulations do not impose the "costs" of others on annual fee payers.

The State has already explained that the statute – not the regulation – reasonably allocates most of the cost of the regulatory program to those users of water under permit and license. The SWRCB and the Farm Bureau both interpret the statute to allocate most of the cost of the regulatory program to such persons. Notwithstanding the flood of misstatements made by the Farm Bureau, the simple fact is that virtually all of the cost of the regulatory activity is attributable to regulation of permitted and licensed water rights. Thus, having those who use water under permit and license pay for most of the cost of this regulatory activity meets the "reasonable relationship" requirement for a valid fee as between "classes" of water right holders.

In support of its argument that the regulations impose costs attributable to others on the annual feepayers, the Farm Bureau disingenuously represents that the fees were inflated by 40 percent because the federal government refused to pay the fees. (Farm Bureau, p. 46.) The statement completely ignores the effect of Water Code sections

1540, 1560, and the California Code of Regulations, title 23, section 1073, which impose the fees associated with the CVP on the federal contractors. It also ignores the actual reasons stated for SWRCB's estimate of the risk of noncollection factor used to calculate the fees. (See 10 Appendix 2304; 2495-2496, fn. 10 and accompanying text [SWRCB order denying Farm Bureau's Petition for Reconsideration].) Finally, it makes no sense mathematically: exactly how is the quoted 30 percent related to the 40 percent?

The Farm Bureau also points to the use of the annual fees to pay for a portion of the cost of processing applications and petitions, thus reducing the one-time filing fees related to the permit and license system (e.g., application and petition fees), to support its position that the fee regulations disproportionately allocate the "costs caused by others" to the annual fee payers. (Farm Bureau, pp. 46-47.) The argument ignores the fact that the permit and license holders are filing the petitions and paying the petition fees and the persons paying application fees are seeking to become permit holders. Petitioners already pay, and applicants are seeking to pay, the annual fees. The Farm Bureau is arguing that permit and license holders are subsidizing other permit and license holders.

The state has explained the reasons for the distribution of the program costs between the annual fees and the filing fees. They include the determination that higher filing fees would increase the likelihood of unauthorized diversions and a greater enforcement burden. (Appendix 2423.) The majority of annual fee payers, as the Farm Bureau has noted, paid the minimum annual fee of $100. (Appendix 2242:4-12

[seventy percent of current permits and licenses have a "face value" of less than 100 af, while 45 percent have a "face value" of less than 10 af].) Thus, the majority of annual fee payers may pay for 200 years or more before meeting the cost of processing the application for the permit they received. (Appendix 2423.) Having much of the cost of application and petition processing covered through annual fees is no different than charging all licensed attorneys an annual fee to pay for the attorney disciplinary system.

By using the annual fees to apportion most of the costs of the regulation, the State places most of the burden on the existing permittees and licensees. This makes sense because most of the cost of processing water right applications and petitions are for the primary purpose of managing existing permitted and licensed water rights. (Appendix 2298 [95 percent of the SWRCB's effort is devoted to regulating users of water held under state permits and licenses]; see Wat. Code, §§ 102, 174, 1201-1202; Appendix 2304-2305 [explaining in detail the reasons for the apportionment between filing fees and annual fees].)

B. The flat, minimum fee of $100 is reasonable and does not disproportionately allocate costs among the fee payers.

The Farm Bureau claims no evidence supports the minimum fee and that the evidence does not support the conclusion that the fee is reasonable. (Farm Bureau, pp. 48-50.) In making this argument, the Farm Bureau makes several factual misrepresentations.

The $100 fee was based on the minimum estimated yearly cost, on average, of overseeing small water rights. (Appendix, pp. 526.01:3-25, 526.02:7-25, 2137-2138,

2307, 2382-2427 [worksheets for fee system development].) The SWRCB determined: "the minimum fee of $100 is adequate to cover the cost of processing the fee, the water use reports that water right holders are required to submit and any notices that the Division is required to provide to the water right holder." (Administrative Record, p. 2.)[4]

The $100 fee was not based on an estimate of how much revenue is necessary to meet the budget target. The SWRCB took the Budget Act target, subtracted estimated fee revenues from other sources, and set the $0.03 per acre foot amount based on what was estimated to raise the additional amount to bring fee collections up to the target amount:

> To initially estimate the necessary revenue that must be generated this fiscal year from water right permit and license fees, staff estimated the revenues that will result from the imposition of the one-time fees that will be assessed (see Table 2). Staff subtracted the estimated one-time fee revenues from the required revenues of $4.4 million, then divided the difference by 60 percent to account for non-collectable billings. The resulting quotient of $7 million was then divided by the total amount of water allowed to be appropriated according to the adjusted face value of the existing 13,000 permits and licenses. This resulted in an estimated fee rate of $0.03 per acre-foot (af). However, approximately half of water right permits and licenses authorize the diversion of 10 af of water or less. If these water right holders were billed based on the per acre-foot charge of $0.03, the cost of billing would exceed the amount of the bill. Therefore, staff determined that a minimum fee was needed to make the fee program cost-effective. *Staff determined that a minimum charge of $100 is necessary to recover the cost of providing services to these water right holders.*

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[4] The Court of Appeal's statement that the annual fee was based on an estimate of the cost of merely billing the fees, as opposed to an estimate of the *minimum cost of the regulation*, conflicts with the SWRCB's own determination. (Compare slip op., pp. 21 and 43 with Admin. Record 2.)

(Appendix pp. 2306-2307 [italics added].)

The Farm Bureau relies on, and misrepresents, the testimony of the Division Chief (Appendix 526.04) for its statement (directly contrary to the SWRCB's determination), "the $100 minimum fee was not the result of any determination of the costs associated with burdens imposed or benefits received by annual 'fee' payors holding permits or licenses. . . ." (Farm Bureau, p. 48.) Her testimony "admits" only that the SWRCB did not conduct any formal study in making this determination. As a matter of law, no formal study is required. (*CAPS, supra,* 79 Cal.App.4th at p. 950 [upholding flat fee against claims more precise accounting was required]; see *Pennell v. City of San Jose* (1986) 42 Cal.3d 365, 375, fn. 10 [city council set fees each year to recover costs of hearing process based on recommendations of city officials].)

Only a reasonable allocation of the fees, not a precise one, is required. (*Sinclair Paint, supra,* 15 Cal.4th at p. 878 quoting *SDG&E, supra,* 203 Cal.App.3d at pp. 1145-1149.) The state need not provide an expert's cost analysis or "document how a forest was saved or how many spotted owls were saved" as a result of its actions to justify the fees. (*CAPS, supra,* 79 Cal.App.4th at pp. 951-952.)

The Farm Bureau alleges that the "end result" is that "individuals who have rights to a few acre-feet of water pay substantially more per acre-foot than persons with rights to many thousands of acre-feet." (Farm Bureau, p. 49.) But a permit or license holder imposes a burden on the regulatory program to provide notices, process reports, and updates records, no matter how small the authorized diversion, and these costs are greater for several separate permits and licenses than for a single, larger diversion

amounting to the same total amount of water. Also, as noted above, those fee payers who pay only the minimum annual fee of $100 may pay for 200 years or more before meeting the cost of processing the application for the permit they received. (Appendix 2423.)

C. Neither the statute nor the regulations are made invalid by the fact that the SWRCB collected fees in an amount greater than the amount set in the Budget Act.

The Farm Bureau alleges that simply because the SWRCB's regulations resulted in the collection of annual fees in fiscal year 2003-2004 exceeding the amount set forth in the Budget Act for this activity (about $4.4 million), the fees collected exceeded the cost of the regulatory program as a whole. (Farm Bureau, p. 50.) Not so.

The annual fees are "assessed for the entire 2003-2004 fiscal year." (Wat. Code, § 1525, subd. (e).) The entire cost of the water right program for fiscal year 2003-2004 was about $9 million. (10 Appendix 2341.) Because of its overly conservative estimation of the risk of noncollection, the SWRCB collected about $7.4 million in fees. (3 Appendix 519.) Obviously, $7.4 million is less than $9 million.

The Farm Bureau falsely alleges that the SWRCB "admits" that "the new 'fees' could not be implemented in time to fund operations for the first half of the Fiscal Year" and that the fees were intended to fund "*all of the costs* of the [water right program] in the *remaining portion* of that year." (Farm Bureau, p. 10, fn. 6 [italics original].) These allegations are also false as a matter of law. The *annual* fees are *annual* fees. (Wat. Code, § 1525, subd. (e).)

The Farm Bureau assumes that expenditures could not be made from the Water Right Fund until the fees were implemented and collected. But the Budget Act authorizes transfers between funds, making it possible to spend money appropriated from the Fund before the first fee revenues are collected: "Notwithstanding any other provision of law, upon approval and order of the Director of Finance, the [SWRCB] may borrow sufficient funds, from special funds that otherwise provide support for the board, for cash purposes." (Stats. 2003, ch. 157, §2.00 Item 3940-001-0001, Provision 1; see Gov. Code, § 11254 [authorizing procedures for transfers between funds and appropriations to a state agency]; *id.*, § 13302 [state accounting system provides for accrual of expenditures and revenues at the end of the fiscal year].)

The SWRCB must adjust the amount of the annual fees each year to compensate for any over- or under-collection. (Wat. Code, § 1525, subd. (d)(3).) Accordingly, the SWRCB must adjust the fees *each year*, *as necessary, by regulation* with the goal of collecting the amount of the revenue level set forth in the Budget, minus any carryover or plus any shortfall from the previous year. (Wat. Code, § 1525, subd. (d); *id.*, § 1530, subd. (a).)

If, as the Farm Bureau suggests, expenditures cannot be made from the Water Right Fund until the fees are implemented, the problem the Farm Bureau assumes occurred in the first fiscal year of the fees must occur every year. If the SWRCB could not spend its estimated revenue until: 1) the Budget Act is signed; 2) the SWRCB revises its fee schedule by regulation to meet the Water Right Fund appropriation, and 3) BOE sends out the fee bills (*and* deposits the collected fees in the Fund); then the

SWRCB's water right program would be closed down for at least some period after the start of every fiscal year. "In recent years, the timely adoption of the budget bill in California has proven to be the exception rather than the rule." (*White v. Davis* (2003) 30 Cal.4th 528, 533.)

The Farm Bureau also claims that the "annual adjustment" provision of Water Code section 1525, subd. (d)(3) does not save the fee schedule "because it does not compensate the vast majority of 'fee' payors for their over-payment in FY 2003-2004." (Farm Bureau, p. 52.) True, the adjustment affects only those feepayers who paid an amount in addition to the minimum fee, and most feepayers pay only the minimum $100 fee. But the assumption that those who paid the minimum fee are the ones who "overpaid" is baseless.

As explained above, the SWRCB did not based the $100 fee on an estimate of how much is needed to be charged to meet the budget target. The SWRCB based the $100 fee on the minimum estimated yearly cost, on average, of overseeing small water rights. (Appendix, pp. 526.01:3-25, 526.02:7-25, 2137-2138, 2307, 2382-2427 [worksheets for fee system development]; Administrative Record 2.) The additional $0.03 per acre foot (for larger water rights) was calibrated to meet the Budget Act target, not the flat, minimum fee.

When, a year later, the SWRCB adjusted the fee, it did not find any evidence that the $100 basic cost of overseeing a small water right (on average) was wrong. Rather, some of the estimates that went into calculating the $0.03 per acre foot turned out to be conservative (i.e., the SWRCB underestimated the revenues the 2003-04 fees would

generate). (Compare SWRCB Order WR 2004-0011 at Appendix, pp. 2114-2115 [discussing assumption used to estimate fee collections, based on experience in analogous non-fee situations, in the context of setting fees for fiscal year 2003-04] with SWRCB Order WR 2005-0007 at Appendix, pp. 2797-2798 [recalibrating that assumption, for purposes of setting fiscal year 2004-05 fees, based on actual experience with respect to fee collections in fiscal year 2003-04].)

The Farm Bureau also alleges the fees set for 2004-2005 fiscal year did not fix the "overpayment" problem because most fee payers "were obliged to continue to overpay at the same or a *higher* rate." (Farm Bureau, p. 24.) But in 2004-2005, a larger percentage of the program was paid for by fee revenue from the Water Right Fund. (Request for Judicial Notice, Ex. 3, p. EP, line 2; see Farm Bureau, p. 10 fn. 6 [claiming "[i]n subsequent years, such as FY 2004-2005, the 'fees' are intended to fund the entire Water Rights Program with essentially nothing from the General Fund"].) The Budget Act's appropriation of a larger portion of the program's revenue from the Water Right fund for the 2004-2005 fiscal year led to the rate increase, not the SWRCB's purported failure to make the annual adjustment (as the Farm Bureau implies).

Given that its conservative estimates resulted in the $0.03 per acre foot fee being set somewhat higher than turned out to be necessary, it was reasonable for the SWRCB to apply the "credit" to the calculation of the per acre foot fee, and not the $100 fee. Those who "overpaid" because their fees were calculated to meet the budget target received the credit for the surplus, while those who did not "overpay," because their fees were set based on considerations other than estimated revenues, received none. The

"annual adjustment" required by Water Code section 1525, subdivision (d)(3) is not intended to compensate individual fee payers for an "overpayment." It is a cumulative adjustment, not a refund remedy for an "overpayment."

D. The risk of non-collection is an administrative cost that must be taken into consideration in setting fees that provide most of a regulatory program's support.

The Farm Bureau also suggests that the "annual adjustment" in Water Code section 1525, subdivision (d)(3) does nothing to save the overpayment made by the annual feepayers resulting from the SWRCB's consideration of the noncollection risk in setting the amount of the fee. In its "Statement of the Facts," the Farm Bureau argues that by taking this risk into consideration, the SWRCB shifted costs that should have been attributed to persons who refused to pay onto the backs of "the remaining class of water right holders subject to the fees." (Farm Bureau, p. 16.) The "class of water right holders subject to the fees," however, is not drawn based on whether they paid the fee. *All* permits and licenses are subject to the annual fee.

The Farm Bureau's argument would make invalid any regulatory fee system that took into account the possibility of nonpayment, rendering all fee-supported regulatory programs chronically underfunded. It also ignores the ability of the State to pursue collection action seeking penalties and interest. (Wat. Code, § 1535, subd. (b).) When the revenues are collected, any overcollection is credited to later fees. (Wat. Code, § 1525, subd. (d)(3).)

The point of the *Sinclair Paint* test is to ensure that the funds are being used to support the regulatory program, and not for some unrelated purpose. The statutorily-

mandated "annual adjustment" ensures that the fees are used solely for the costs of the regulatory program for which they are collected.

Feepayers can assure themselves that the SWRCB is adjusting the fees annually, so that fee revenues carried over from previous years are credited against future fees and not allowed to build up in the Water Rights Fund indefinitely. The California Department of Finance maintains a public web site that includes the Governor's budget and reports on fund conditions and previous years' expenditures. No more detailed accounting is required.

The Farm Bureau assumes the fees must be set with a precision not required by the case law. But a fee system that reasonably apportions fees overall is not invalid, either in general or as applied to a particular fee payer, because facts specific to that particular fee payer indicate that the fee may have been high as applied to that fee payer. (*CAPS, supra,* 79 Cal.App.4th at pp. 954-955.)

In sum, the Farm Bureau's case rests on its disagreement with the Legislature's decision to shift the cost of regulating water rights from the backs of general taxpayers to permitted and licensed water right users. Because the fee structure, as set up by the statutes and implemented through the regulations, meets the test for a valid fee, the Farm Bureau must seek legislative, not judicial, intervention to achieve its goals.

III.

Courts do not have the power to fashion a refund remedy when the Legislature has provided one.

In striking down the SWRCB's regulations, the Court of Appeal stated that only persons or entities who paid annual fees and filed timely petitions for reconsideration [which together, the court noted, constituted a "claim for refund"] (slip op., p. 52) were entitled to receive a refund. The Farm Bureau claims that the "procedural hoops the Court of Appeal imposed" will result in windfall to the SWRCB in illegal taxes. (Farm Bureau, p. 6.) The Court of Appeal, however, did not impose these "procedural hoops" (Farm Bureau, p. 6). The Legislature did. (Wat. Code, § 1537, subd. (b); see Cal. Const. art. III, § 5 [suits may be brought against the state in such manner and in such courts as shall be directed by law].) The Farm Bureau makes the novel argument that, if a person fails to proceed in the manner required by law to obtain a refund from the State, a court may remedy that failure. No inequity exists to require such a novel result. The remedy is clear, and hundreds of persons, including eight individual members of the Farm Bureau, followed the law's direction.[5]

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[5] The Farm Bureau did not raise the issue of the validity of its petition for reconsideration in its opening brief or its reply brief to the Court of Appeal. Consequently, the Court of Appeal did not rule on this issue.

The SWRCB determined that the state and county farm bureaus and their *unnamed*, individual members did *not* file petitions for reconsideration. (Clerk's Augmented Transcript on Appeal (CATA), pp. 173-175; [SWRCB Order WRO 2004-0010 - EXEC, pp. 5-7].) The SWRCB refused to accept the Farm Bureau petition to the extent it purported to seek review of any fee determinations other than those of the eight specifically named fee payers. (CATA, p. 174.) Persons who did not file valid petitions for reconsideration are not entitled to a refund. (cont. next page)

A. **The issue of whether administrative exhaustion is required even if the agency cannot grant the relief requested is not presented.**

The Farm Bureau argues that administrative exhaustion is not required here because the SWRCB does not have the power to grant the relief sought: i.e., to receive a refund based on the statute's unconstitutionality, because it has no authority to rule a statute unconstitutional. (Farm Bureau, p. 54.) That issue is not presented by this case. The Court of Appeal upheld the statute; it struck down the *regulations*.

While a petition for reconsideration cannot be filed to challenge the mere adoption of fee regulations, the SWRCB has the authority to declare the regulations unconstitutional when the SWRCB has made a determination based on the regulations imposing the fee and the fee payer files a petition for reconsideration challenging that fee determination. (See Wat. Code, § 1537, subd. (b)(2).) Water Code section 1537, subdivision (b)(4), specifies that the provisions of section 1537, subdivision (b) shall not be construed to make the adoption of regulations subject to the statutory reconsideration procedures. But this language simply avoids expanding the circumstances under which a petition for reconsideration may be filed. By its terms, it does not exclude from consideration any issues that would otherwise be subject to review in a properly filed petition for reconsideration. It avoids any implication that the SWRCB's action in

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Similarly, persons who filed a timely petition for reconsideration but did not timely seek judicial review of the SWRCB's denial of the petition are not entitled to any refund because the decision has become final and, by statute, is not subject to judicial review: "If no aggrieved party petitions for a writ of mandate within the time provided by this section, the decision or order of the board is not subject to review by any court." (Wat. Code, § 1126, subd. (d).)

adopting regulations, a quasi-legislative action, is subject to the procedures for petitions for reconsideration, which apply to adjudicative decisions and orders. (Wat. Code, § 1120.) This prevents petitions for reconsideration from being filed at the time regulations are adopted, before they are applied in a fee determination. It does not immunize the regulations from review as part of a petition for reconsideration or subsequent petition for writ of administrative mandate challenging a fee determination applying the regulations to the fee payer.

Water Code section 1537, subdivision (b)(4) serves both to avoid delays before the fee regulations take effect, and to avoid making fee payers file petitions for reconsideration at the time the regulations are adopted. (See Wat. Code, §§ 1122, 1126, subd. (e).) The SWRCB has the authority to recognize that its own regulations are unconstitutional (or otherwise flawed). (See generally *Woods v. Superior Court* (1981) 28 Cal.3d 668, 680 [an invalid regulation is subject to attack in administrative proceedings].) Thus, the Court of Appeal properly limited the refund to parties who exhausted their administrative remedies, in accordance with settled law. (*Abelleira v. District Court of Appeal* (1941) 17 Cal.2d 280, 292-293; *Patane v. Kiddoo* (1985) 167 Cal.App.3d 1207, 1214; see *Modern Barber Colleges, Inc. v. California Employment Stabilization Comm.* (1948) 31 Cal.2d 720, 725-726 [due process clause does not guarantee the right to judicial review of tax liability before payment].)

B. Exhaustion of administrative remedies is a jurisdictional prerequisite where mandated by statute.

Regardless of whether a challenge is to the constitutionality of the statutes or the validity of the regulations, however, the Farm Bureau identifies no conflict of law on the issue of whether a feepayer can bypass an administrative process mandated by statute. "[I]t has long been the law in this state that where an administrative remedy is provided by statute, relief must be sought from the administrative body and this remedy exhausted before the courts will act." (*Marquez v. Gourley* (2003) 102 Cal.App.4th 710, 713 [citing *Abelleira v. District Court of Appeal, supra,* 17 Cal.2d at p. 292 and other cases].) The exhaustion of administrative remedies "is not a matter of judicial discretion, but is a fundamental rule of procedure laid down by courts of last resort, followed under the doctrine of *stare decisis*, and binding upon all courts. . . . [E]xhaustion of the administrative remedy is a jurisdictional prerequisite to resort to the courts." (*Abelleira v. District Court of Appeal, supra,* 17 Cal.2d 280, 293 [italics in the original].)

Here, most notably, the requirement to exhaust administrative remedies is *mandated by the statute*. (Wat. Code, § 1537, subd. (b)(2)-(3).) No refund may be issued by BOE unless "the determination has been set aside by [the SWRCB] or a court *reviewing the determination* of [the SWRCB]." (*Id.*, § 1537, subd. (b)(3).) A petition for reconsideration is *required* to exhaust administrative remedies in cases where, as here, the decision is issued under authority delegated to an officer or employee of the SWRCB. (*Id.*, § 1126, subd. (b).) The actual fee bill sent out by BOE is the "Notice of

Decision" by the Division of Water Rights setting that person's fee based on the regulations and the SWRCB's database. (CATA, p. 172 and fn. 5.) Consequently, the judicially developed rule of exhaustion of administrative remedies (and the exceptions thereto) have no application here, where the Legislature has provided the manner of proceeding. (*Patane v. Kiddoo, supra,* 167 Cal.App.3d at p. 1214.)

There are other reasons for requiring the exhaustion of administrative remedies. An exception that allowed litigants to avoid the requirement to exhaust administrative remedies by stating a constitutional cause of action would swallow the general rule. Under such reasoning, a litigant challenging the constitutionality of a statute enforced by the agency should skip the superior court and go directly to the appellate court, since the agency must continue to enforce a statute until an *appellate* court – not the superior court – has declared the statute unconstitutional. (Cal. Const., art. III, § 3.5(a).)

Moreover, a petition for reconsideration must contain certain information, including the specific order or decision for which it seeks review. (Cal. Code Regs., tit. 23, §§ 769, 1077.) This specificity is required "to enable the SWRCB to know exactly which fee determinations are before it, for purposes of its own review, for purposes of notifying BOE which bills to adjust. . . and for purposes of judicial review." (CATA, p. 173.)[6] To allow a fee payer to bypass the specific administrative refund procedures required would deprive the agency of stability and certainty regarding its funding and

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[6] Parties to the consolidated actions who are petitioners for reconsideration are set forth in the attachments to the SWRCB's orders on the petitions for reconsideration. (See Appendix, p. 297 et seq. and fn. 1; Admin. Record, pp. 3106-3114, 3170-3172, 3143.)

financial planning.

In addition, to allow a fee payer to bypass the administrative process deprives an agency of an opportunity to remedy any factual errors at the administrative level. An agency might make relevant factual findings regarding the fee as applied to that particular fee payer, as it did here. (E.g., CATA, p. 191.) The SWRCB can check the fee calculations and the facts, and in response to meritorious claims, direct BOE to refund or cancel fees, as appropriate.

It can also show the petitioner the agency's legal arguments in support of the fee. The SWRCB did not "summarily deny" the Farm Bureau's petition. (See Farm Bureau, p. 56.) The order denying reconsideration of the Farm Bureau's petition devoted over 15 pages to the constitutional issues raised. (Appendix 2488-2503.)

Under the Farm Bureau's theory, an administrative agency would have to bear the burden of trying to identify exactly who is subject to a court's order and, in a factual vacuum, determine the proper refund and recipient. It is the agency that would be unreasonably burdened, not the court system. No court can fashion a remedy for the fee payers who are not properly before it. (*Jordan v. Department of Motor Vehicles* (1999) 75 Cal.App.4th 449, 466-468.) In sum, it is well-established that review of the SWRCB's determination regarding a refund may not be had absent exhaustion of administrative remedies.

C. The provisions of Revenue and Taxation Code section 55221 are not applicable.

The Farm Bureau argues that the "plain language" of the Revenue and Taxation Code section 55221 requires the refund of illegal fees to all who paid them. The Farm Bureau persists in its mistaken presumption that Revenue and Taxation Code section 55221 is applicable to claims for refund of the water right fees, which it is not. (Farm Bureau, pp. 56-59.)

The applicable statutes are in the Water Code. Water Code section 1537 provides that BOE "shall *collect* the fees pursuant to the Fee Collection Procedures Law [Rev. & Tax. Code, § 55001 et seq.]." (Wat. Code, § 1537, subd. (b)(1) [italics added].) "*Notwithstanding* the *appeal* provisions in the Fee Collection Procedures Law," however, a fee determination by the SWRCB is subject to review under Water Code section 1120 et seq. (*Id.*, § 1537, subd. (b)(2).) And finally, "[n]otwithstanding the *refund* provisions of the Fee Collection Procedures Law," BOE cannot accept any claim for refund unless that determination has been set aside by the SWRCB or a court *reviewing the SWRCB's determination.* (*Id.*, § 1537, subd. (b)(3) [italics added].)

Accordingly, the Court of Appeal correctly found that section 55221 is not applicable. (Slip op., p. 19 ["the BOE has no role in reviewing refund claims under section 1537 or the emergency regulations"].) It found that the governing statutes in the Water Code limited BOE's typical role under the Revenue and Taxation Code:

> As we explained, the SWRCB contracts with the BOE to collect and refund annual fees. Sections 1126 and 1537 and regulations 1074 and 1077 limit the BOE's typical role under the Fee Collection Procedures Law (Rev. & Tax. Code, § 55001 et seq.). Thus it is for the SWRCB, not

> the BOE, to determine whether "a person or entity is required to pay a fee" and whether the amount of the fee was incorrectly calculated. (Cal. Code Regs., tit. 23, § 1077, subd. (c)."

(Slip op., pp. 51-52 [footnote omitted].) Revenue and Taxation Code section 55221 refers to a determination by the BOE, not the SWRCB. (See Farm Bureau, p. 56 citing Rev. & Tax. Code, § 55221, subd. (a).)

Further, the Court of Appeal correctly found that review of a water right fee refund determination is "by writ of mandate in the superior court, not by petition for redetermination by the BOE." (Slip op., p. 52; Wat. Code, § 1537, subd. (b)(2).) It also recognized that BOE is "authorized to accept a refund claim only after the SWRCB or a reviewing court has set the fee determination aside." (Slip op., p. 52, citing Wat. Code, § 1537, subd. (b)(3).) Accordingly, the Court of Appeal correctly limited refunds to "persons and entities who paid annual fees and filed petitions for reconsideration" which together constitute a "claim for refund" under the regulations. (Slip op., p. 53.)

The Farm Bureau argues that a petition for reconsideration is not required to challenge the adoption of regulations. (Farm Bureau, p. 58.) Of course, any party may seek prospective, declaratory relief to have the statutes or regulations declared invalid without exhausting administrative remedies. (Govt. Code, § 11350, subd. (a); see *Pacific Motor Transport Co. v. State Bd. of Equalization* (1972) 28 Cal.App.3d 230 [allowing prepayment declaratory action to test the validity of a tax regulation subject to the rulemaking provisions of the California Administrative Procedure Act].) As discussed above, Water Code section 1537, subdivision (b)(4) provides that the reconsideration provisions of the Water Code shall not be construed to apply to the

adoption of the regulations, as opposed to their application to individual fee payers through determinations that they are subject to fees and the amount of the applicable fee. Declaratory relief may be sought when the fee regulations are adopted, but the remedy of declaratory relief is not the same as the remedy of a refund.

The Farm Bureau is well aware of the difference. Here, the Farm Bureau combined a writ of administrative mandate seeking a refund of the water right fees with an action for declaratory relief seeking to strike down the statutes and regulations as invalid. (See e.g., CATA, p. 1.) Only those named individuals who filed valid petitions for reconsideration and exhaust their administrative and judicial remedies through the statutory procedures for a refund claim may be entitled to the remedy of a refund.

D. The Takings Clause is not implicated by the requirement of the exhaustion of administrative remedies.

Some fee payers may not receive a refund under the Court of Appeal's decision because they failed to exhaust their administrative remedies. An exhaustion requirement is not a "taking." "[A] constitutional right may be forfeited in criminal as well as civil cases by the failure to make timely assertion of the right before a tribunal having jurisdiction to determine it." (*Yakus v. United States* (1944) 321 U.S. 414, 64 S.Ct. 660, 677; accord, *Walker v. Birmingham* (1967) 388 U.S. 307, 87 S.Ct. 1824; *Metcalf v. Los Angeles* (1944) 24 Cal.2d 267, 269.) The requirement of administrative exhaustion to obtain a water right fee refund does not violate the Takings Clause any more than the analogous requirement for a tax refund does.

The cases the Farm Bureau relies on in this regard have nothing to do with a

requirement to exhaust administrative remedies. (Farm Bureau, pp. 60-61.) No case law supports the argument that the Takings Clause requires payment of a blanket refund in the absence of the exhaustion of administrative remedies.

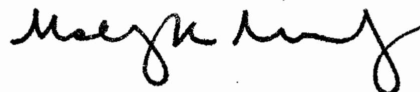
CONCLUSION

For all of the reasons stated, the Court should uphold the constitutionality of the statutes and regulations implementing the water right fees.

Dated: July 11, 2007

Respectfully submitted,

EDMUND G. BROWN JR.
Attorney General of the State of California
PAUL GIFFORD
Senior Assistant Attorney General
GORDON BURNS
Deputy State Solicitor General
WILLIAM L. CARTER
Supervising Deputy Attorney General
MATTHEW J. GOLDMAN



MOLLY K. MOSLEY, SBN 185483
Deputy Attorneys General

Attorneys for the California State Water Resources Control Board and the California State Board of Equalization, et al.

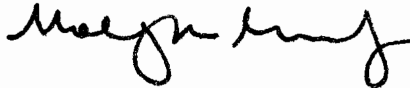
CERTIFICATION OF WORD COUNT

The text of the State's Answer to the California Farm Bureau's Opening Brief on the Merits consists of 11,623 words according to the word processing program used to prepare the brief.

Dated: July 11, 2007

Respectfully submitted,

EDMUND G. BROWN JR.
Attorney General of the State of California
PAUL GIFFORD
Senior Assistant Attorney General
GORDON BURNS
Deputy State Solicitor General
WILLIAM L. CARTER
Supervising Deputy Attorney General
MATTHEW J. GOLDMAN



MOLLY K. MOSLEY, SBN 185483
Deputy Attorneys General

Attorneys for the California State Water Resources Control Board and the California State Board of Equalization, et al.

DECLARATION OF SERVICE BY U.S. MAIL

Case Name: **California Farm Bureau Federation v. SWRCB**

No.: **S150518**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for mailing with the United States Postal Service. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the United States Postal Service that same day in the ordinary course of business.

On July 11, 2007, I served the attached **STATE'S ANSWER BRIEF ON THE MERITS TO BRIEF OF CALIFORNIA FARM BUREAU FEDERATION** by placing a true copy thereof enclosed in a sealed envelope with postage thereon fully prepaid, in the internal mail collection system at the Office of the Attorney General at 1300 I Street, Suite 125, P.O. Box 944255, Sacramento, CA 94244-2550, addressed as follows:

David A. Battaglia
Gibson Dunn & Crutcher
333 South Grand Avenue
Los Angeles, CA 90071

Attorneys for Plaintiffs and Appellants California Farm Bureau Federation, et al.

Nancy N. McDonough
California Farm Bureau Federation
2300 River Plaza Drive
Sacramento CA 95833

Attorneys for Plaintiffs and Appellants California Farm Bureau Federation, et al.

Stuart L. Somach
Somach Simmons & Dunn
813 Sixth Street, Third Floor
Sacramento CA 95814-2403

Attorneys for Plaintiffs and Appellants Northern California Water Assn. et al.

Clerk of the Court
Superior Court of California
County of Sacramento
720 9th Street, Appeals Unit
Sacramento, CA 95814

Clerk of the Court
The Court of Appeal of the State of
California
Third Appellate District
900 N Street, #400
Sacramento, CA 95814-4869

I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on July 11, 2007, at Sacramento, California.

D. Burgess	D. Burgess
Declarant	Signature

Brief #1 pos.wpd