California Supreme Court Allows Challenge to Oakland's Franchise Fee

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On August 11, 2022, the California Supreme Court issued its opinion in *Zolly v. City of Oakland*, holding that a group of property owners had pleaded sufficient facts to maintain a challenge to the City's solid-waste franchise fee, under Article XIII C of the California Constitution, commonly called "Proposition 26."

The case arises from two contracts the City approved and adopted by local ordinance, awarding franchises to two private companies for waste collection services for City residents and businesses. In exchange for that franchise, the agreements require the companies to pay negotiated franchise fees to the City. The plaintiffs—owners of property in the City—sued, claiming that the franchise fees did not bear a reasonable relationship to the franchises' values and so were illegal taxes adopted without voter approval under Proposition 26.

The City filed a demurrer, arguing that the franchise fee could not be challenged by the plaintiffs under Proposition 26, and the Alameda County Superior Court agreed, dismissing the case. The Court of Appeal reversed in part, finding that plaintiffs adequately stated a constitutional claim. The California Supreme Court then granted review and affirmed the Court of Appeal, holding that the City failed to demonstrate as a matter of law that its franchise fees were exempt from plaintiffs' challenge. The Court remanded the case to the trial court for proceedings consistent with its opinion.

The Court's decision rests on three pillars:

1. **Alleged economic injury is sufficient to confer standing for purposes of demurrer.** The City argued that the plaintiffs lack standing to challenge the franchise fee because the plaintiffs do not pay the franchise fee. Plaintiffs only claim that their garbage rates are higher than they would be if the City charged the waste haulers a lower franchise fee. The Court found that plaintiffs' alleged economic injury—even if indirect—is sufficient to confer standing on them to challenge the franchise fee to overcome demurrer.
2. **A franchise fee may be considered "imposed by local government," and therefore may be limited by**

Proposition 26, if it is "established" by the agency, even if by contract. One of the touchstones of Proposition 26's definition of "taxes" is that they are "imposed" by local government. The City argued that a charge is only imposed if it reflects a unilateral exercise of government power. The Court rejected that view, holding that "imposed" is synonymous with "established." Even though the franchise fee was a negotiated price term in a contract between the City and the waste haulers, the Court found that the franchise fee was "imposed" within the meaning of Proposition 26 when the City established that fee as part of an ordinance approving the contract.

3. **The City did not demonstrate that the franchise fee fit any of Proposition 26's exceptions.** Proposition 26 defines local "taxes" that are subject to voter-approval requirements as any charge, fee, or levy imposed by local government, except those that fit a list of seven, enumerated exceptions. The Court held that, on demurrer, the City had not demonstrated as a matter of law that the franchise fees fit any of Proposition 26's exceptions. The majority opinion considered that a franchise fee might fit either the exception for government-conferred privileges and benefits or the exception for purchase or use of government property, but it did not resolve which exception governed, concluding that the City had not demonstrated the franchise fee met either standard.

Public agencies that receive franchise fees should review the case closely and consult with their legal counsel regarding the implications of the case.

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