

FEES VERSUS TAXES

ISSUE

Because of the loss of revenue from sales taxes; the statutory cap on the utility (franchise) taxes; and the local politician's reasonable fear of raising property tax, Utah cities and towns are experiencing a revenue crisis. One solution is the increase use of fees as a means of raising revenue. Fees are being proposed, and in some cases already used, to provide revenue for services that have been traditionally financed through the general fund from tax revenue. A prime example of this is the Salt Lake County police fee which incidentally is very similar to a fee that Herriman City has had for some time without much notoriety or controversy. (A copy of the Herriman fee material is attached for the curious) Other fees being considered, or at least talked about by some municipalities, include transportation utility fees, fire service fees, and a general recreation (park use) fee.

STATUTORY AUTHORITY FOR FEES and TAXES

Most fees traditionally charged by Utah municipalities have direct enabling legislation. For example water and sewer rates and fees are specifically enabled by Utah Code 10-8-22 and 10-8-38. Where there is no direct enabling legislation Utah municipalities have relied on the grant of general welfare power found in Utah Code 10-8-84 which the Utah Supreme Court has interpreted in *State v. Hutchinson*, 624 P.2d 1116, to give both cities and counties general powers to enact all necessary measures to promote the general health, safety, morals, and welfare of their citizens, even where there is no specific grant of enabling authority.

In addition many cities and towns have relied on their power to create service areas and districts under the laws governing limited purpose entities—local districts and its predecessor statutes. These enable municipalities to create local districts or service areas and provide municipal type services to part, or all, of the municipality. Local Districts have specific enabling legislation to charge rates and fees and also have specific legislation that can give some advantages in the collection of fees.

Tax authority is normally specifically provided in statute. Examples are of course the local property tax; municipal sales and use tax; the telecommunications tax; the local transient room tax; and the energy sales and use tax. However there is a general grant of authority to cities and towns to “divide the city into districts for the purpose of local taxation as occasion may require” and to “consistent with general law, provide the manner and form in which special taxes are levied and collected.” (U.C.A. 10-8-3, 4) These sections seem to imply that municipalities may have authority to create tax schemes other than those specifically provided by the legislature.

IS IT A TAX OR IS IT A FEE?

One of the clearest statement by the courts on the differences between taxes and fees is found in *V-I Oil Co. v. Utah State Tax Com'n*, 942 P.2d 906 (Utah 1996). The relevant distinction (with citations omitted) between the two was set out as follows:

- No bright line test for distinguishing a tax from a fee. How such exactions should be classified depends upon their purpose.
- Generally a tax raises revenue for general governmental purposes, while a fee raises revenue either to compensate the government for the provision of a specific service or benefit to the one paying the fee or to defray the government's costs of regulating and policing a business or activity engaged in by the one paying the fee.
- There are two broad types of fees: (i) a fee for service, i.e., a specific charge in return for a specific benefit to the one paying the fee, and (ii) a regulatory fee, i.e., a specific charge which defrays the government's cost of regulating and monitoring the class of entities paying the fee.
- To be a legitimate fee for service, the amount charged must bear a reasonable relationship to the services provided, the benefits received, or a need created by those who must actually pay the fee. More specifically, for a fee for service to be reasonable, the total cost of the service so financed must fall equitably upon those who are similarly situated and in a just proportion to the benefits conferred.
- The court does not insist on exact mathematical precision, however, in holding that a certain charge is a legitimate fee instead of a tax. The revenues raised by the fee may exceed the precise cost of providing the service to those paying the fee, yet the fee may be reasonable as long as its reasonableness can be determined in some other manner.
- The nature of the service or benefit provided may also make it difficult or impossible to distribute the services or benefits equally to all who pay the fee. For such a fee to be reasonable, the court has directed that it should be fixed so as to be equitable in light of the relative benefits conferred as well as the relative burdens imposed. If the fee bears no reasonable relationship to some need created by the one paying the fee, or if the services provided through the fee are not of "demonstrable benefit" to the one paying the fee, then the fee is likely to be unreasonable and, hence, illegitimate.
- Like all fees, a regulatory fee must bear some reasonable relationship to the cost of the thing said to justify its imposition.

WHY IT MAKES A DIFFERENCE IF IT IS A TAX RATHER THAN A FEE

- First and foremost it is a question of who has to pay the fee/tax. One of the advantages of a fee is that tax exempt organizations still have to pay them. They do not have to pay taxes or assessments.
- Tax revenue can be used for anything. Fee revenue is restricted to the purpose of the fee –cost of service or cost of regulation.

- While the imposition of both taxes and fees will have a presumption of constitutionality, the amount of a fee will be subject to review for reasonableness of amount and appropriateness of use of the moneys received. This may necessitate the use of professional fee and rate studies to justify the amount of the fee.
- There is some language in cases that seems to indicate that a municipality's authority to enact a new tax without a specific legislative authorization is questionable. Most of these cases, however, predate *Hutchinson*.
- There is a different statute of limitations for challenges to fees and to tax challenges. A challenge to most fees is probably subject to the four year statute of limitations while a tax challenge normally requires payment under protest and claim for refund within six months.

PROBLEMS WITH FEES

Collection is a problem. Common method is withdrawal of service for failure to pay fee. This doesn't practically work for issues like police and fire services. There is specific enabling legislation allowing municipalities to cut off of sewer for failure to pay water. What about cut off of water for failure to pay street lights, garbage? Local Districts have specific enabling legislation allowing them to cut off any service or commodity for failure to pay for another service or commodity. Local Districts also have lien rights not apparently provided to municipalities. (See attached U.C.A. 17B-1-901 et. seq)

Fees are subject to challenges for reasonableness of amount and appropriateness of use. These are fact issues that do not lend itself easily to summary judgment. This may mandate the need for fee studies to justify amount and more diligent oversight of the budgeting and accounting in the less sophisticated municipalities.

SPECIAL FEE ISSUES

Development, building permit and plan check fees are subject to the limitations contained in Utah Code 10-9a-510. This limits amount of fee and provides for itemization and justification of amount. The North Salt Lake current litigation with Woodside Homes is illustrative of the potential problem. Woodside Homes is suing for more than \$500,000 in reimbursement of plan check fees for reviewing what are claimed as identical plans. (See attached amended complaint).

Impact fee limitations and problems are well known and I will leave the discussion of these to others.

Fees that are tied to business licenses are now limited to licensing for regulation purposes only unless the business causes a disproportionate cost of municipal services or the municipality provides an enhanced level of municipal services (with limited exceptions). These fees require specific studies and findings. (See U.C.A. 10-1-203)

LESSONS TO BE LEARNED FROM RECENT HISTORY

While it seems apparent that municipalities have a broad grant of authority under the Utah Municipal Code and court decisions to enact new fees and possibly new taxes to solve the current revenue problems lessons learned from the recent history of business license fees and taxes and impact fees should be educational.

In Utah, before the recent past, it was fairly common for Utah cities and towns to raise general fund revenue from a fee or tax associated with the right to do business in the municipality. This was commonly expressed by things like a gross receipts business license fee. These types of fees/taxes were routinely upheld by Utah courts. However, these types of revenue raising licensing schemes raised the ire of a few legislators when a few new cities adopted new ordinances. The result is the hodgepodge of laws restricting our business licensing authority. A similar history exists for fees and taxes from the licensing of apartments, utilities, telecommunications, and to some extent impact fees. A fair summation of this history is that one or two cities pioneer the concept; the courts uphold the general authority of the city to act as it does and when more municipalities jump onto the bandwagon the legislature moves to restrict municipal authority. We then fight a rear guard action to preserve some of what we have.

This will probably be the story of police service, fire service, transportation utility fees and any other fee we can think of. If they become common place in Utah municipalities, and appear to the legislature to be tax masquerading as a fee, the legislature will either restrict or prevent the use of these fees.