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**Sent:** Tuesday, July 28, 2020 4:28 PM

**To:** Mayor <Mayor@longbeach.gov>; Council District 1 <District1@longbeach.gov>; Council District 2 <District2@longbeach.gov>; Council District 3 <District3@longbeach.gov>; Council District 4 <District4@longbeach.gov>; Council District 5 <District5@longbeach.gov>; Council District 6 <District6@longbeach.gov>; Council District 7 <District7@longbeach.gov>; Council District 8 <District8@longbeach.gov>; Council District 9 <District9@longbeach.gov>

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**Subject:** Agenda Item R-1 - File # 20-0687 Oil Barrel Production Tax

**-EXTERNAL-**

Good afternoon,

On behalf of Chief Counsel Seth Blackmon, please find attached a comment letter regarding Agenda Item R-1 – File # 20-0687 Oil Barrel Production Tax. If you have any questions concerning the attached document, please contact Seth Blackmon at [Seth.Blackmon@slc.ca.gov](mailto:Seth.Blackmon@slc.ca.gov).

Regards,



**Micaela L. Wiemer**, Attorney

**CALIFORNIA STATE LANDS COMMISSION**

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July 28, 2020

File Ref: G05-03

Honorable Mayor Robert Garcia  
411 W. Ocean Blvd.  
Long Beach, CA 90802  
[mayor@longbeach.gov](mailto:mayor@longbeach.gov)

Long Beach City Council  
411 W. Ocean Blvd.  
Long Beach, CA 90802

RE: Agenda Item R-1 – File # 20-0687 Oil Barrel Production Tax

Dear Mayor Garcia and Members of the City Council:

On July 7, 2020, the Long Beach City Council adopted Agenda Item NB-23 that, in part, directed the City Manager to engage the California State Lands Commission and other stakeholders regarding potential modifications to the City's Oil Barrel Production Tax and directed the City Attorney to prepare necessary documents to place a potential increase of the tax on the November 2020 ballot. Last week Commission staff was informed that City staff is scheduled to report to the Council at a special meeting on July 29 on the results of its engagement with the Commission, and the numerous other stakeholders affected by the proposed ballot measure, and that despite the concerns raised during these engagements, the City intends to proceed as originally planned by placing the tax increase on the November 2020 ballot.

While Commission staff appreciates the Council's direction to engage with all stakeholders regarding the proposed increase to the Oil Barrel Production Tax, the time allotted to develop approaches that jointly address Commission staff and City concerns has been inadequate. Since July 7, Commission staff communicated repeated concerns to City staff that the existing and proposed tax, as applied to the Long Beach Tidelands, run afoul of the State constitution, legislative grants, and the City's obligations as trustee to the People of California.

The Oil Barrel Production Tax, as the City applies it to State interests, unilaterally and unlawfully diverts revenue due the State's General Fund to the City without the consent of the Legislature, the Governor, or the statewide public. The tax improperly seeks to

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convert Public Trust assets for expressly municipal purposes<sup>1</sup>, notwithstanding explicit prohibitions by the Legislature and California Supreme Court against doing so. Finally, the tax violates the City's fiduciary duty to the State as trustee.

The City has not substantively responded to the legal issues raised by Commission staff and provided no analysis or law supporting its position that it has the authority to tax the State and Long Beach Tidelands operations in the way contemplated by the Oil Barrel Production Tax. The Oil Barrel Production Tax thus fails both substantively and procedurally. Substantively, the tax is illegal as applied to State interests for the reasons noted above and discussed in more detail below.

Commission staff desire to work with the City to address these legal defects and find alternatives that can sustainably fund necessary and timely racial and social equity programs, which the City initially stated to be the purpose of the tax increase (although this is not reflected in the ballot measure itself or the City's staff report for the July 29 meeting). But doing so will require longer than the August 4 deadline for the City to act on the tax increase ballot measure. As such, Commission staff respectfully request that the City table the proposed tax increase to allow for a meaningful, robust discussion between the City and Commission, and to avoid litigation which may otherwise become necessary.

#### I. Background – The Long Beach Tidelands

The State granted the Long Beach Tidelands to the City of Long Beach to manage and to hold in trust for the benefit of all Californians. The land itself, the oil, gas, and other hydrocarbons produced therefrom, and the revenue generated thereby, are subject to the Public Trust. The State is the trustor, the City is trustee, and all Californians are beneficiaries. As a grantee and trustee, the City has a fiduciary duty to manage the Long Beach Tidelands assets in a manner consistent with the statutory trust grant, the Public Trust Doctrine, the California Constitution, and case law. The City has the primary responsibility for administering the trust within the parameters of the granting statutes. This requires in part that revenue the City receives from Long Beach Tidelands operations be used for Public Trust, rather than municipal, purposes.

The Commission is vested with oversight authority to protect the statewide public interest in the granted Long Beach Tidelands. In that role, Commission staff has an obligation to assist the City in complying with the terms of the statutory grants and the Public Trust Doctrine. Commission staff prefers to work cooperatively and proactively with local government grantees to ensure the requirements of legislative grants and the Public Trust Doctrine are met. Commission staff and City staff have worked cooperatively over the years to resolve issues as they arise with respect to the Long Beach Tidelands. However, where an abuse of the Public Trust or a violation of a

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<sup>1</sup> Long Beach Mun. Code § 3.80.110, "This Chapter is enacted solely for the purpose of raising revenue for *general municipal purposes* . . ." (emphasis added).

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legislative grant occurs, Commission staff has the responsibility committed to it by the Legislature to address and correct the abuse or violation.

In addition to serving as trustee, the City is the unit operator for the Long Beach Tidelands oil production operations and exercises overall supervision and control of all matters pertaining to the rate of production, repressuring operations, and development and operation of the Long Beach Tidelands. The contractor, presently California Resources Corporation (CRC), is charged with day-to-day responsibilities, under the direction and control of the City. The City is party to several agreements that outline its responsibilities with respect to the Long Beach Tidelands operations, including Unit Agreements, Unit Operating Agreements, and Contractors Agreements for the Long Beach Unit and West Wilmington. The State is a party or third-party beneficiary to these agreements.

## II. Background – The Oil Barrel Production Tax

It is staff's understanding that the existing Oil Barrel Production Tax consists of a \$0.15 per barrel tax imposed on oil production, including on State granted lands in the Long Beach Tidelands, first imposed in 1990, and an additional \$0.25 per barrel Police and Fire Public Safety Oil Production Tax (Proposition H) approved by Long Beach voters in 2007, the total of which has increased to \$0.48 per barrel after Consumer Price Index adjustments. The ballot measure proposed for November 2020 amends Chapter 3.80 of the municipal code to increase the per barrel tax, which is earmarked for general fund programs, from \$0.15 to \$0.30, which will bring the total tax up to at least \$0.63 per barrel.

## III. The Oil Barrel Production Tax, as the City applies it to State interests, unilaterally and unlawfully diverts revenue, due the State's General Fund, to the City

The Oil Barrel Production Tax violates and is preempted by the Long Beach granting statutes.<sup>2</sup> The Legislature established a comprehensive statutory framework for classification, allocation, and expenditure of revenue generated by oil production in the Long Beach Tidelands.<sup>3</sup> These statutes were, by their own terms, intended to forever settle any disputes between the City and State regarding the division of such revenue. The legislative grants allow oil revenue to fund subsidence control, oil production operations, and Public Trust-consistent activities and purposes on and adjacent to the waterfront. But the statutory scheme expressly caps the revenue derived from Tidelands oil production that is received by the City and expressly sets forth the specific Public Trust purposes for which such revenue may be used. Any deviation from this defined

<sup>2</sup> Charter cities may not make or enforce ordinances in conflict with State law. Cal. Const., art. XI §§ 5, subd. (a); 7; see *California Fed. Savings & Loan Assn. v. City of Los Angeles* (1991) 54 Cal.3d 1, 17. The California Constitution also exempts property owned by the State and local agencies from taxation. Cal. Const., art. XIII, § 3, subd. (a).

<sup>3</sup> See Ch. 29, Stats. 1956, 1 Ex. Sess.; Ch. 138, Stats. 1964, 1 Ex. Sess.; Ch. 941, Stats. 1991; Ch. 446, Stats. 2008; Cal. Pub. Resources Code, § 6217, "the [C]ommission shall deposit all revenue . . . under Chapter 138 of the Statutes of 1964 . . . in the General Fund."

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revenue allocation requires amending the statutory grants through an act of the Legislature.

Yet the Oil Barrel Production Tax circumvents these granting statutes. By the City's own analysis, 36 cents of every dollar generated by the tax is money that would otherwise go to the State General Fund but is instead diverted to the City's General Purpose Fund. This exceeds the express statutory allocations and directs revenue beyond what the Legislature authorized the City to receive, violating the statutory framework that defines permissible uses of the State's Public Trust assets.

IV. The tax improperly seeks to convert Public Trust assets for expressly municipal purposes

California case law confirms that the revenue generated on Public Trust lands are Public Trust assets; that the Public Trust is lifted only from the revenue paid to the State; and that it is inappropriate to use Public Trust assets and revenues for municipal affairs.<sup>4</sup>

In *City of Long Beach v. Morse* (1947) 31 Cal.2d 254, the California Supreme Court examined the Long Beach granting statute and found that general trust principles apply to the Long Beach Tidelands, which were "transferred in trust for certain uses and purposes."<sup>5</sup> There the City argued that the proceeds of oil and gas production constituted income from the land and were not subject to the Public Trust.<sup>6</sup> The Court rejected this argument, holding that "[w]hether the fund should be regarded as part of the corpus of the trust or merely as a part of the rents and profits of the land, the city as trustee has no right to devote the proceeds to general municipal improvements unconnected with trust purposes."<sup>7</sup> "If the proceeds from the sale of oil and gas are regarded as corpus...they must be used for the purposes set forth in the legislative grants in trust, for the city, as trustee, clearly has no authority to appropriate the corpus to its own uses contrary to the terms of the trust. If the proceeds are regarded as income from trust property, the trustee, in the absence of a legislative provision to the contrary, has no more right to them than it has to the corpus."<sup>8</sup>

In *Mallon*,<sup>9</sup> the California Supreme Court again held the City's use of Public Trust assets for "municipal affairs" or "strictly local improvements" to be a violation of the constitutional prohibition on gifts of public funds.<sup>10</sup> The Court specifically held that

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<sup>4</sup> Ch. 29, Stats. 1956, 1 Ex. Sess.; Ch. 138, Stats. 1964, 1 Ex. Sess.; *City of Long Beach v. Morse* (1947) 31 Cal.2d 254; *Mallon v. City of Long Beach* (1955) 44 Cal.2d 199.

<sup>5</sup> *Morse, supra*, 31 Cal.2d at 257.

<sup>6</sup> *Ibid.*

<sup>7</sup> *Ibid.*

<sup>8</sup> *Id.* at 257-258.

<sup>9</sup> *Mallon, supra*.

<sup>10</sup> *Id.* at 205.

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construction and establishment by the City of storm drains, a city incinerator, a public library, public hospitals, public parks, a fire alarm system, off-street parking facilities, city streets and highways, and other expenditures authorized by city charter to be made from the public improvement fund are not of such general statewide interest that Public Trust funds can be expended thereon. Instead these are “municipal affairs” within the meaning of article XI, section 6, of the California Constitution, and thus applying Public Trust funds to these uses would be a violation of article IV, section 31.<sup>11</sup>

In any respect, as *Morse* indicated, there must be a direct link between the expenditure of Public Trust assets and a discrete and readily quantifiable benefit to Public Trust resources.<sup>12</sup> Staff is unaware of any nexus study developed for the programs proposed for funding by the tax and the express references to generating revenue for “Municipal Purposes” suggest that the tax, on its face, uses Public Trust assets for non-Public Trust uses in violation of well-established California Supreme Court precedent.

#### V. The tax violates the City’s fiduciary duty to the State as trustee

As trustee to the People of the State of California, the City is held to the highest standard of care and has fiduciary duties to administer the trust according to the terms of the trust instrument,<sup>13</sup> of loyalty,<sup>14</sup> of impartiality,<sup>15</sup> and a duty against self-dealing.<sup>16</sup> This last element includes an obligation on the trustee not to profit from trust income due the beneficiary. But the proposed tax does exactly this. The tax placed on the trust assets by the City, as trustee, has the direct effect of causing the City, as operator of Tidelands oil production, to directly charge those taxes to the State’s oil revenue and redeposit them into the City’s General Purpose Fund. The City then profits from trust revenue due the State, violating the City’s basic duties as trustee. The misappropriation of Public Trust funds or assets to municipal uses violates fiduciary duties the City, as grantee, owes the State and the public.<sup>17</sup>

#### VI. Next Steps

Exploring a viable solution will require longer than the Council’s August 4, 2020 deadline for approving ballot measures. As a result of these concerns, and to promote cooperation in pursuing alternatives that may meet the City’s goals, staff reiterates its requests that the City postpone consideration of this item until a later election cycle, so that the City, the State, and various stakeholders are not rushed in their analysis and

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<sup>11</sup> *Ibid.*

<sup>12</sup> *Morse, supra*, 31 Cal.2d at 261.

<sup>13</sup> Cal. Prob. Code § 16000 (i.e. the granting statutes)

<sup>14</sup> *Id.* at 16002.

<sup>15</sup> *Id.* at 16003.

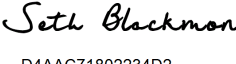
<sup>16</sup> *Id.* at 16004.

<sup>17</sup> *Mallon, supra*, 44 Cal.2d at 207; Pub. Resources Code, § 6009.1 [Tidelands grantee bears duties “to not use or deal with trust property for the trustee’s own profit or for any other purpose unconnected with the trust,” “to keep the trust property separate from other property not subject to the trust,” “to administer the trust solely in the interest of the beneficiaries,” etc.].

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discussions of these complex and important issues. To the extent consideration of the ballot measure is not postponed, and the City refuses to engage in further conversations to address the significant issues, the Commission will be forced to consider, fully, its legal options. To that end, the Commission has engaged the Attorney General's Office to explore what options are available to protect the State's interests and the Public Trust and to ensure that the City complies with its obligations as trustee.

Sincerely,

DocuSigned by:  
  
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Seth Blackmon  
Chief Counsel  
California State Lands Commission

cc: Charles Parkin, Long Beach City Attorney  
Dan Olivas, Senior Assistant Attorney General  
Andrew Vogel, Supervising Deputy Attorney General  
Dan Bromberg, Deputy Legal Affairs Secretary, Office of Governor Newsom