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BULLETIN

Update on Public Law

A Proposition 218 Victory for Municipal Tiered Water Rates and Enforcement of the “Pay Under Protest” Rule

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The latest legal development on tiered water rates came on December 8, 2025, when we prevailed at the Second District of the California Court of Appeal in a published decision in *Dreher v. City of Los Angeles*, a putative class action challenge to the City of Los Angeles’ residential water rates. In *Dreher*, the court addressed two pivotal issues: Whether Health & Safety Code Section 5472’s payment under protest requirement applies to municipal water rates, and whether the City of Los Angeles’s four-tiered residential water rates comply with Proposition 218’s proportionality requirements. In a welcome win for municipal water providers, the Court of Appeal ruled in the City’s favor on both points.

The City’s Tiered Water Rates Comply with Proposition 218

The City has four primary sources of water supply and in 2016 developed a rate study to support four usage tiers, with Tier 1 allotted 8 HCF per month for basic, indoor water needs, and increasing allotments for Tiers 2, 3 and 4. The City’s rate formula allocates the cheapest source of water to Tier 1’s forecast demand until the supply is exhausted, and then allocates the next lowest cost water until Tier 1’s remaining demand is satisfied, before allocating that source to Tier 2’s forecast demand, supplementing that tier’s forecast demand with the third lowest source, and so on until each tier’s forecast demand is satisfied. Plaintiffs argued

this rate structure could not meet Proposition 218’s proportionality without tracking which parcels actually used which sources of supply.

The Court of Appeal rejected Plaintiffs’ argument, holding that “The Constitution does not require the City to trace the flow of water from each source of supply to each parcel, molecule by molecule.” Citing *Capistrano*, the Court found Proposition 218 does not require an exact measure of the cost of service for each individual parcel. Departing from the conclusion in the recent *Patz v. City of San Diego* case, the Second District ruled “We read nothing in section 6(b)(3) that would require a water agency to trace drops of water from source of supply to parcel. . . .”

It further departed from *Patz* by finding that using water budgets to establish the tier breakpoints is not, in and of itself, unconstitutional provided the agency calculates the proportional costs of service within each tier. The Court also held the City could consider conservation goals and parcel characteristics in setting water budgets, so long as rates remain proportional.

Finally, the Court determined the City’s allocation of peak pumping and storage costs across the tiers complied with Proposition 218. The City’s formula allocated to all four tiers the base pumping and storage costs that did not vary based on demand. The incremental costs of pumping and storage linked to peak demand were allocated to Tiers 3

and 4. Again citing *Capistrano*, the Court noted that Proposition 218 protects lower water users from paying rates higher than the cost to serve them because those rates cover capital costs their consumption levels do not make necessary. That rationale supports the trial court's ruling, which the Court of Appeal left undisturbed.

In short, the Court found the City had met its burden under Proposition 218 by calculating the unit cost of each water source, forecasting demand within each tier, and using formulas to allocate costs proportionally as customers move into higher tiers of usage. The record supported the City's methodology, including its allocation of portions of peak pumping and storage costs to higher tiers.

Health & Safety Code section 5472 Applies to Municipal Water Rate Refund Claims

At trial, Plaintiffs also challenged the City's low-income subsidy adjustment (LISA), which covered the City's cost to provide rate assistance to low-income customers. The trial court found the LISA violated Proposition 218, but ruled that Health & Safety Code section 5472's payment under protest requirement barred Plaintiffs from recovering any refunds attributable to the LISA individually or even on behalf of all customers. Plaintiffs challenged that ruling on appeal, arguing section 5472 applied to sanitation and sewer charges but not to municipal water service charges.

On an issue of first impression as applied to municipal water charges, the Court of Appeal applied the plain statutory language in section 5472 to reject Plaintiffs' claim. Section 5472 applies by its plain terms to water service, those water service charges were approved by the required two-thirds vote of the City Council and the City is a "covered entity" within the statutory scheme. Following a comprehensive analysis of the legislative history, the Court determined nothing in that history demonstrated a contrary purpose to that indicated in the statute's plain language.

The Court also rejected Plaintiffs' arguments that section 5472 provides an inadequate remedy for Proposition 218 violations and that the Government Claims Act applies instead. The Court found no support for either claim, instead it found section 5472 provides an adequate remedy but Plaintiffs failed to comply with the payment under protest provisions before challenging the rates. Ratepayers must give written notice of protest at the time of payment to preserve their right to seek a refund in court and such refund requests are limited to the individual ratepayer, who may not seek refunds on behalf of a class.

Conclusion

Dreher helpfully clarifies that municipal ratepayers seeking refunds must comply with Section 5472's payment under protest requirement, and that cities may use tiered rate structures that allocate costs, including peak pumping and storage costs, based on usage and parcel characteristics, provided they are supported by data and formulas demonstrating proportionality. The ruling affirms the City's compliance with Proposition 218 and provides meaningful guidance for other agencies designing tiered rates in California.

Plaintiffs will likely seek Supreme Court review so stay tuned for further updates!

For more information on this topic, please contact Holly at HWhatley@chwlaw.us or 213.542.5700.

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