

**Office of  
The City Attorney  
City of San Diego**

**MEMORANDUM  
MS 59**

**(619) 236-6220**

**DATE:** April 1, 2011  
**TO:** Councilmember Kevin Faulconer & Todd Gloria  
**FROM:** City Attorney  
**SUBJECT:** Establishment of a New Policy for Allocating Maintenance Assessment District Assessment Funds to the Non-profit Corporations that Administer the Districts

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**INTRODUCTION**

The current process for allocating Maintenance Assessment District (MAD) revenues to the non-profits corporations (non-profits) that administer certain MADs is done via reimbursement. As part of the reimbursement process, the City requires the non-profits to show proof of eligible expenditures through submission of receipts and invoices prior to reimbursement. Due to perceived delays in the reimbursement process, it has been suggested that a new process for allocating MAD assessment revenues be adopted. This new process would involve the City advancing such revenues to the non-profits prior to the non-profits actually incurring expenses. As part of the discussions on the feasibility and legality of the proposed new process, the issue of whether San Diego Charter section 93 prohibited such advancement of revenues was raised.

**QUESTION PRESENTED**

Does Charter section 93 prohibit advancing money to the non-profits that administer contracts for goods and services on behalf of certain Maintenance Assessment Districts?

**SHORT ANSWER**

No. Charter section 93 does not prohibit any expenditure that serves a valid public purpose or that is made in performance of a bona fide contract. In the matter at hand, the expenditure would meet both requirements.

## BACKGROUND

A MAD is a mechanism by which property owners can elect to assess themselves in order to pay for and receive services beyond what the City normally provides. MADs are governed by California Streets and Highways Code sections 22500 - 22679 (Landscaping and Lighting Act of 1972) and Chapter 6, Article 5, Division 2, sections 65.0201 - 65.0234 of the San Diego Municipal Code. The statutes contain legislative declarations that their purpose and intent is to establish a procedure for making and maintaining certain improvements, as that term is defined in State law, and to provide a method for the City Council to authorize a non-profit to assume responsibility for the administration of certain contracts within a MAD. Cal. Sts. & High. Code § 22502; SDMC §§ 65.0201(a), (e).

California Streets and Highways Code section 22525, defines the type of improvements eligible for funding with MAD assessment revenues. Section 22525 states:

“Improvement” means one or any combination of the following:

- (a) The installation or planting of landscaping.
- (b) The installation or construction of statuary, fountains, and other ornamental structures and facilities.
- (c) The installation or construction of public lighting facilities, including, but not limited to, traffic signals.
- (d) The installation or construction of any facilities which are appurtenant to any of the foregoing or which are necessary or convenient for the maintenance or servicing thereof, including, but not limited to, grading, clearing, removal of debris, the installation or construction of curbs, gutters, walls, sidewalks, or paving, or water, irrigation, drainage, or electrical facilities.
- (e) The installation of park or recreational improvements, including, but not limited to, all of the following:
  - (1) Land preparation, such as grading, leveling, cutting and filling, sod, landscaping, irrigation systems, sidewalks, and drainage.

(2) Lights, playground equipment, play courts, and public restrooms.

(f) The maintenance or servicing, or both, of any of the foregoing.

(g) The acquisition of land for park, recreational, or open-space purposes.

(h) The acquisition of any existing improvement otherwise authorized pursuant to this section.

(i) The acquisition or construction of any community center, municipal auditorium or hall, or similar public facility for the indoor presentation of performances, shows, stage productions, fairs, conventions, exhibitions, pageants, meetings, parties, or other group events, activities, or functions, whether those events, activities, or functions are public or private.

Cal. Sts. & High. Code § 22525.

Under the San Diego Municipal Code, if a non-profit wishes to establish the right to administer contracts for goods and services on behalf of a MAD, that non-profit must provide written documentation verifying that property owners representing “at least a majority of the parcel area” of the MAD support the non-profit assuming responsibility for administration. SDMC § 65.0212(a). Upon submission of such documentation, the Mayor will docket for City Council review a resolution authorizing the Mayor to enter into an agreement with the non-profit for administration of the MAD. SDMC § 65.0212(c). MADs in which a non-profit administers the contracts for goods and services are referred to in the City as “self-managed” MADs or “self-administered” MADs.

After a MAD is successfully formed, City staff prepares the annual enrollment and delivers it to the County Assessor to be included on property tax statements to property owners within the MAD boundaries. MAD assessment revenues are collected by the County Tax Collector at the same time and in the same manner as property tax revenues. The County receives the majority of MAD assessment revenues in December and April. The County then transfers the MAD revenues to the City approximately one month after the County receives it. Each MAD is separately accounted for in its own City fund. The cash balances of substantially all City funds, including the MAD funds, are pooled and invested by the City Treasurer for the purpose of increasing interest earnings through investment activities.

As the non-profits administer their respective MADs, they submit monthly reimbursement requests to the City. Those requests are reviewed by City Planning and Community Investment Department (CP&CI) staff to ensure that the expenditures are eligible for reimbursement. Once CP&CI staff determines that the expenditure is eligible for reimbursement, staff forwards the request to the Comptroller's office for payment from the appropriate MAD fund. Recently, there have been delays in this process due to, among other things, the City's recent transition to a new accounting system. These delays have led to discussions on advancing assessment revenues to the non-profits in order to streamline the process.

## ANALYSIS

### **I. THE CITY CHARTER GOVERNS THE MANNER IN WHICH THE CITY MAY APPROPRIATE AND EXPEND FUNDS**

San Diego is a charter city. *Mira Development Corp. v. City of San Diego*, 205 Cal. App. 3d 1201, 1214 (1988). City charters, adopted pursuant to the authority of article XI, section 5 of the California Constitution (Constitution), are not grants of power but act as limitations, and a charter city may exercise all powers in regards to municipal affairs unless specifically and explicitly limited by its charter. *See Taylor v. Crane*, 24 Cal. 3d 442, 450 (1979); *City of Grass Valley v. Walkinshaw*, 34 Cal. 2d 595, 598-99 (1949). The determination of fiscal policies and procedures is a municipal affair. *Cramer v. City of San Diego*, 164 Cal. App. 2d 168, 171 (1958). The exercise of power by a charter city is favored against any limitation or restriction on that exercise "which is not expressly stated in the charter. . . . So guided, reason dictates that the full exercise of the power is permitted except as clearly and explicitly curtailed. Thus, in construing the city's charter, a restriction on the exercise of municipal power may not be implied." *City of Grass Valley*, 34 Cal. 2d at 599. Accordingly, the Charter provides the authority for, and limitations upon, the manner in which the City may appropriate and expend funds.

### **II. THE CITY MAY MAKE AN EXPENDITURE FOR A VALID PUBLIC PURPOSE OR IN PERFORMANCE OF A BONA FIDE CONTRACT**

Several limitations exist in the Charter regarding the City's ability to expend funds. For example, the City may not incur indebtedness beyond its fiscal year without a vote of the electorate nor enter into contracts for more than five years without a two-thirds vote of the City Council. San Diego Charter § 99. These limitations are not applicable to the question presented here. Charter section 93, however, sets forth the relevant limitation that may apply. It provides, in pertinent part: "The credit of the City shall not be given or loaned to or in aid of any individual, association or corporation; except that suitable provision may be made for the aid and support of the poor." The City Attorney has previously opined that this provision is similar to article XVI, section 6 of the Constitution, and the cases interpreting that constitutional provision

are relevant in interpreting the Charter provision.<sup>1</sup> See 1979 Op. City Att’y 8 (79-2; Mar. 2, 1979); 1979 City Att’y MOL 168 (Sept. 4, 1979); 1952 Op. City Att’y 23 (Feb 27, 1952).

Article XVI, section 6, is generally referred to as prohibiting a “gift of public funds.” See, e.g., *California Housing Finance Agency v. Elliott*, 17 Cal. 3d 575, 582-83 (1976); *County of Alameda v. Carleson*, 5 Cal. 3d 730, 745 (1971). An exception to this prohibition exists if a “public purpose” is served by the expenditure. “Money spent for public purposes is not a gift. . . .” *Community Memorial Hospital v. County of Ventura*, 50 Cal. App. 4th 199, 207 (1996). See also *White v. State of California*, 88 Cal. App. 4th 298, 311 (2001).

In *Carleson*, one of the leading cases concerning the prohibition against the making of gifts or the lending of credit, the court explained the meaning of the proscription:

It is generally held that in determining whether an appropriation of public funds is to be considered a gift, the primary question is whether the funds are to be used for a ‘public’ or ‘private’ purpose; the benefit to the state from an expenditure for a public purpose is in the nature of consideration and the funds expended are therefore not a gift even though private persons are benefited therefrom. The determination of what constitutes a public purpose is primarily a matter for the Legislature, and its discretion will not be disturbed by the courts so long as that determination has a reasonable basis.

*Carleson*, 5 Cal. 3d at 745-46 (citations omitted).

*Carleson* has been followed by numerous court decisions (See, e.g., *Elliot*, 17 Cal.3d 575; *Winkelman v. City of Tiburon*, 32 Cal.App.3d 834 (1973)) and courts have been liberal in deciding what constitutes a public purpose for which expenditures may be made. In *Elliot*, the California Supreme Court held that the Housing and Home Finance Act and resolutions promulgated thereunder, which authorizes, among other things, a public agency to make loans to private housing sponsors and mortgage lenders at below-market rates, do not amount to a gift of public funds. Citing *Carleson*, the Court gave great weight to the public purposes found by the Legislature regarding the shortage of housing for low and moderate income families. *Elliot*, 17

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<sup>1</sup>Article XVI, section 6 provides: “The Legislature shall have no power to give or to lend, or to authorize the giving or lending, of the credit of the State, or of any county, city and county, city, township or other political corporation or subdivision of the State now existing, or that may be hereafter established, in aid of or to any person, association, or corporation, whether municipal or otherwise, or to pledge the credit thereof, in any manner whatever, for the payment of the liabilities of any individual, association, municipal or other corporation whatever; nor shall it have power to make any gift or authorize the making of any gift, of any public money or thing of value to any individual, municipal or other corporation whatever; . . . .” However, because of a charter city’s control over its fiscal affairs, which, as discussed above, are considered solely “municipal affairs,” the courts have held that Article XVI, section 6 is not applicable to charter cities. *Tevis v. City & County of San Francisco*, 43 Cal. 2d 190, 196-97 (1954); *Mullins v. Henderson*, 75 Cal. App. 2d 117, 132-33 (1946); *Los Angeles Gas & Electric v. City of Los Angeles*, 188 Cal. 307, 317 (1922).

Cal.3d 575 at 583. The Court also found that other public purposes were served such as increasing safe and decent housing and the avoidance of ethnic, economic, and racial isolation. *Id.* at 583-85. “Given the broad public purposes supporting the program and the close relationship between the elements of the program and these purposes, we conclude that the Act, and the Agency’s resolutions thereunder, do not violate the constitutional prohibition against the gift of public funds and extension of public credit.” *Id.* at 586

In *Winkelman*, the City of Tiburon proposed to construct an affordable housing project on land it owned and offered to sell the property well below the market-rate to a private non-profit which would build the project. Adjacent property owners challenged that decision on the grounds that the sale of the property to the non-profit corporation constituted an illegal gift of public funds. The trial court rejected that challenge and the appellate court affirmed, stating that so long as the consideration for the sale was plainly substantial and not nominal, there was no gift of public funds. *Winkelman*, 32 Cal.App.3d at 844-45.

Under *Winkelman*, there is no unconstitutional gift if the transfer promotes a public purpose, therefore providing a benefit to the state “in the nature of consideration,” or if the consideration given in exchange is “adequate,” so as to evidence a bona fide contract.” *Winkelman*, 32 Cal.App.3d at 844-46. The notion that performance of a “bona fide contract” does not amount to a gift of public funds is consistent with past cases such as *People v. City of Long Beach*, 51 Cal.2d 875 (1959), in which the Supreme Court stated, “[i]t is clear, however, that the performance of a bona fide contract by a public body is not the making of a gift. . . .” *City of Long Beach*, 51 Cal.2d 875 at 881.

Therefore, it appears there are at least two tests to determine whether a particular expenditure is a gift of public funds. The first is whether the expenditure promotes a public purpose. If a public purpose is promoted by the expenditure, the public benefit received amounts to consideration in return for that expenditure, and thus, it is not a gift. The second test is whether the expenditure is performance under a bona fide contract. To be considered a bona fide contract, the public agency must receive adequate consideration in return for the expenditure. When determining whether adequate consideration is received or not, it is not necessary to weigh the expenditure against the benefit on a scale. Instead, the public agency need only receive a benefit that is not nominal and plainly substantial. “The law, however, does not require a weighing of the quantum of benefit received by a promisor or of the detriment suffered by a promisee where the consideration is plainly substantial.” *Winkelman*, 32 Cal.App.3d at 845.

As stated above, MADs are formed for the purpose of installing, constructing, and maintaining public improvements, parks, open space, and public facilities beyond what the City normally provides. A strong argument can be made that installing, constructing, and maintaining public improvements, parks, open space, and public facilities at no cost to the taxpayer in this challenging economic environment is a public purpose. Given the deference accorded to legislative bodies, it is unlikely that a court would invalidate a City Council determination that

advancing funds to the non-profits for such improvements constitutes a public purpose. No court has addressed whether the law requires the City to make a formal finding of public purpose. However, this Office advises that City staff include the facts relied upon to determine the public purpose in the staff report, should the City Council decide to adopt a process of advancing revenues to the non-profits. Furthermore, any funds that may potentially be advanced to the non-profits would be in exchange for the non-profits fulfilling their contractual duties to undertake the improvements. Such an undertaking on the part of the non-profits is substantial and more than nominal consideration. Therefore, both tests are met and the advance of funds to the non-profits administering the MADs would not be a violation of Charter section 93.

### **III. THE CITY RETAINS CONTROL OVER THE ASSESSMENT REVENUES, AND THUS, HAS RESPONSIBILITY FOR THE PROPER EXPENDITURE OF THOSE REVENUES**

As a word of caution, it is important to note that no matter what method of allocating MAD assessment revenues to the non-profits is used, those revenues are public funds, and as such, the City is responsible for ensuring that the funds are spent properly. There are only a few court cases which touch upon the issue of assessment district funds being public funds. One such case is *Epstein v. Hollywood Entertainment District II Business Improvement District*, 87 Cal. App. 4th 862 (2001). In *Epstein*, a non-profit corporation administered the funds that the city raised through assessments on businesses in a special assessment district. A property owner within this district brought an action seeking declaratory and injunctive relief to establish that the non-profit was required to comply with the Ralph M. Brown Act and the City's competitive bidding requirements for contracts. The trial court denied plaintiff's motion for a preliminary injunction. The Court of Appeal reversed and remanded, directing the trial court to enter a preliminary injunction in plaintiff's favor. The court held that the non-profit was subject to the Brown Act and stated, in dicta, that the funds involved were public funds. "Very simply, the Brown Act contains no exemptions for decisions about expenditures of *public funds* for 'supplemental services.'" *Epstein*, 87 Cal. App. 4th at 875 (emphasis in original).

The City, as the elected legislative body, retains plenary decision-making authority over the MADs' council activities, in that the City Council may modify any particular contained in the MADs' engineers' reports and budgets. Cal. Sts. & High. Code §§ 22586; 22591; 22623; 22630. This retention of power is not only provided for by California Streets and Highways Code, but it is required by well-established law. The City may only delegate the performance of administrative functions, such as administration of the MADs, to a non-profit if it "retains ultimate control over administration so that it may safeguard the public interest." *Chamber of Commerce v. Stephens* 212 Cal. 607, 610 (1931); *County of Los Angeles v. Nesvig* 231 Cal. App. 2d 603, 616-617 (1965). Advancing funds to the non-profits that administer MADs obviously exposes the City to additional risk by virtue of the fact that the City would have less control to

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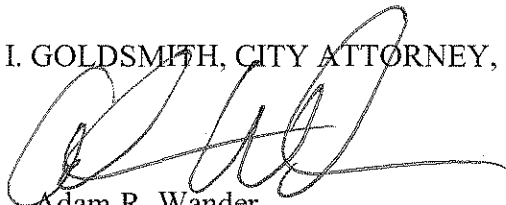
ensure the proper expenditure of assessment revenues and would restrict its ability to safeguard the public interest.

### CONCLUSION

Charter section 93 does not prohibit advancing funds to the non-profits that administer MADs if the City Council finds that a valid public purpose is served by such an advance and a reasonable basis exists to support the finding. A strong argument can be made that the improvements provided by the MADs at no cost to the taxpayer in this challenging economic environment is a public purpose. Given the deference accorded to legislative bodies, it is extremely unlikely that a court would invalidate a City Council determination that advancing funds to the non-profits for such improvements constitutes a public purpose. Furthermore, the advancing of funds would be in performance of a bona fide contract, in that the non-profits' undertaking of those improvements in exchange for the advanced funds is substantial and more than nominal consideration. Therefore, the advance of funds to the non-profits administering the MADs would not be a violation of Charter section 93. However, this Office cautions the City Council that further advancing funds to the non-profits exposes the City to additional risk by virtue of the fact that the City would have less control to ensure the proper expenditure of assessment revenues which could restrict its ability to safeguard the public interest.

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