

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

MEMORANDUM

DATE: January 30, 2015

TO: Honorable Mayor and City Council Members

FROM: Adam R. Wander, Deputy City Attorney

SUBJECT: Potential Changes to City's Administration of
Maintenance Assessment District Funds

INTRODUCTION

On December 19, 2014, Councilmember Gloria sent a memorandum to this Office with the subject "Maximizing the effectiveness of assessment district revenue and enhanced neighborhood services" (December 19 Memo). Based on the December 19 Memo and conversations with Anthony Bernal in Councilmember Gloria's office, this Office understands that the Councilmember is interested in the City's ability to: (1) modify the amount of contingency reserve required in Maintenance Assessment District (MAD) budgets; and (2) regularly advance MAD assessment revenue to the nonprofit corporations (nonprofits) that administer the City's self-managed MADs¹ rather than maintain the current process of reimbursement-based distribution.

QUESTIONS PRESENTED

1. May the City modify the amount of contingency reserve required in MAD budgets?
2. May the City regularly advance MAD assessment funds to the nonprofits that administer the City's self-managed MADs?
3. What safeguards must be put in place to ensure accountability of the MAD assessment revenues?

SHORT ANSWERS

1. The laws governing the City's MADs do not require a contingency reserve of any amount. Establishing and maintaining a contingency reserve, however, is a prudent measure that protects the City and property owners from loss of services due to potential revenue shortfalls.

¹ The term "self-managed MADs" is a colloquialism used to describe those MADs in which the City Council has authorized a nonprofit entity to administer MAD contracts and activities on behalf of the City.

2. The San Diego Municipal Code (SDMC or Municipal Code) currently requires that the self-managed MADs operate on a reimbursement basis. This Office is currently working with City staff to overhaul the MAD Ordinance, including allowing for regular advances of assessment revenues to the nonprofits.

3. The City must retain enough control over the administration of the MAD assessment revenues to adequately protect the property owners and safeguard against improper use of the assessment revenues.

BACKGROUND

A MAD is a mechanism by which property owners can elect to assess their properties in order to pay for and receive improvements and services beyond what the City normally provides. MADs are formed pursuant to 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 Municipal Code (MAD Ordinance). 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 nonprofit to assume responsibility for the administration of certain contracts within a MAD. Cal. Sts. & High. Code § 22502; SDMC §§ 65.0201(a), (e).

ANALYSIS

I. THE CITY IS NOT LEGALLY REQUIRED TO BUDGET A CONTINGENCY RESERVE FOR THE MAINTENANCE ASSESSMENT DISTRICTS

The current operating agreement between the City and the nonprofit administrators of self-managed MADs requires the nonprofit to submit to the City no later than February 1 of each year a line item budget for the upcoming fiscal year. Pursuant to section I.B.6 of the operating agreement, the nonprofits are required to budget a minimum of 10 percent as a contingency reserve.

No law governing the City's MADs obligates the City to establish a contingency reserve of any amount. A simple amendment to the current MAD operating agreement could modify the level of contingency reserve the City requires in the MAD budgets. However, Economic Development Department staff has informed this Office that the current contingency reserve of 10 percent is based on best practices. From this Office's standpoint, the current contingency reserve appears to be a prudent measure under the circumstances. The budget for any given MAD is created and approved based on the estimated amount of assessment revenue to be collected and the proposed expenditures within the MAD during the upcoming fiscal year. The purpose of a contingency reserve is to protect the City and property owners from loss of services due to potential revenue shortfalls. Such shortfalls may be created by service cost overruns, overestimation of assessment revenues, or delinquent payment of assessments. Therefore, this Office urges the City Council to carefully consider the potential negative ramifications of any policy decision that would reduce the amount of contingency reserve in the MAD budgets.

II. THE MUNICIPAL CODE CURRENTLY REQUIRES THAT THE SELF-MANAGED MAINTENANCE ASSESSMENT DISTRICTS OPERATE ON A REIMBURSEMENT BASIS

The MAD Ordinance requires that, before the City pays a nonprofit for work done or goods received in a self-managed MAD, the nonprofit must first submit to the City a report indicating that the nonprofit has completed on-site inspections of the work, or submit any bill or invoice for goods or services received. The City is not authorized to pay until such report, bill, or invoice “for work done” or “for the goods received” has been submitted. SDMC §65.0212(c)(4). However, this Office is currently working with Economic Development Department and Park and Recreation Department staff to overhaul the MAD Ordinance. One of the modifications to the MAD Ordinance being considered is to allow for regular advances of assessment revenues to the nonprofits. Any modifications will be presented to a City Council committee at least once and the full City Council at least twice. The goal is to have the modifications to the MAD Ordinance in place prior to July 1, 2015.

III. THE DELEGATION OF ADMINISTRATIVE AUTHORITY MUST BE ACCOMPANIED BY SAFEGUARDS ADEQUATE TO PREVENT ABUSE

Every year the City Council approves an annual budget for each MAD, which outlines the activities and improvements for which the assessment revenues will be spent in the given fiscal year. The City Council, duly exercising its legislative discretion, contracts with the nonprofits to perform the administrative function of expending assessment revenues in furtherance of the objectives for which they were collected.

The City may only delegate the performance of administrative functions, such as administration of the MADs, to a nonprofit if the City retains ultimate control over administration so that it may safeguard the public interest. “[A] public body may only delegate the performance of its administrative functions to a private entity if it retains ultimate control over administration so that it may safeguard the public interest.” *Epstein v. Hollywood Entm’t Dist. II Bus. Improvement Dist.*, 87 Cal. App. 4th 862, 873 (2001). A public body must retain enough power to make fundamental policy decisions and must ensure that the procedure established for the exercise of the delegated power adequately safeguards those affected. *Groch v. City of Berkeley*, 118 Cal. App. 3d 518, 522 (1981). “[T]he Legislature’s power to delegate its authority is not unlimited. To survive constitutional scrutiny, a delegation of legislative power must be accompanied by safeguards adequate to prevent an abuse of that power.” *Indep. Roofing Contractors of Cal., Inc. v. Dep’t of Indus. Relations*, 23 Cal. App. 4th 345, 354 (1994). Accordingly, any changes to the reimbursement procedure for the nonprofits would have to be structured in a manner ensuring that the assessment revenues are properly expended.

Adherence to the district annual budget is one way to gauge whether the revenues are being properly expended. However, it may be prudent to establish further measures which can be used to ensure adherence to the district budget and adequately safeguard against misuse of the assessment revenues if funds are advanced prior to authentication of the propriety of certain

expenditures. Advance, direct payment of MAD assessment revenues to the nonprofits that administer MADs would restrict the City's ability to ensure the proper expenditure of assessment revenues or recoup the funds. Restricting the City's ability to safeguard against improper expenditure could leave the City open to risk of a lawsuit and could also expose the General Fund to liability for repayment of improperly expended funds. Accordingly, any new procedure would have to continue to ensure the proper expenditure of assessment revenues and, if needed, allow the City to quickly and efficiently recoup any funds which were not properly expended.

CONCLUSION

The law governing the City's MADs do not obligate the City to establish a contingency reserve of any amount. A simple amendment to the current MAD operating agreement could modify the level of contingency reserve the City requires in the MAD budgets. However, the purpose of a contingency reserve is to protect the City and property owners from loss of services due to potential revenue shortfalls and, therefore, this Office urges the City Council to carefully consider any policy decision that would reduce the amount of contingency reserve in the MAD budgets below the current level of 10 percent. The Municipal Code requires that the self-managed MADs operate on a reimbursement basis, but this Office is currently working with City staff to overhaul the MAD Ordinance to, among other things, provide for regular advances of assessment revenues to the nonprofits. The City must be cautious when establishing such a policy because the City must ensure that it retains enough control over the administration of the MAD assessment revenues to adequately protect the property owners and safeguard against the improper use of the MAD assessment revenues.

JAN I. GOLDSMITH, City Attorney

By /s/ Adam R. Wander
Adam R. Wander
Deputy City Attorney

ARW:mcm
Doc. No.: 940478
MS No. 2015-3