



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: October 10, 2007

REPORT NO. 07-157

ATTENTION: Land Use and Housing Committee
Meeting of October 17, 2007

SUBJECT: Options Relating to Assistance for Property Owners in the La Jolla Mesa
Vista Undergrounding Assessment District and Future Assessment Districts

REQUESTED ACTIONS:

Accept the report, and consider the options described in the report relating to Assessment Districts.

STAFF RECOMMENDATION:

Accept the report, and consider the options described in the report relating to Assessment Districts.

SUMMARY:

I. BACKGROUND:

La Jolla Mesa Vista Undergrounding District

In connection with the City Council's July 23, 2007 action to form the La Jolla Mesa Vista Undergrounding Assessment District (the "LJMV District"), the City Council requested that City staff explore options to assist property owners, including those in the LJMV District, facing a financial hardship due to the creation of an assessment district and levy of assessment. This topic was specifically referred by the City Council to the Land Use and Housing Committee ("LU&H"). In addition, during Non-Agenda Public Comment on July 31, 2007, public comments relating to the LJMV District were also referred to LU&H.

The formation of the LJMV District was initiated by certain property owners within the La Jolla Mesa Vista neighborhood who filed a petition requesting that the City begin the process to form the district under the Municipal Improvement Act of 1913 ("1913 Act") to fund the undergrounding of utilities in their neighborhood. These property owners wanted to accelerate the project in advance of the time-frame provided in the City's Master Plan for undergrounding utilities by forming a 1913 Act District wherein property owners would pay for costs to underground their utilities. The petition was signed by 46 of the 56 property owners within the proposed district, representing 77% of the land area proposed to be assessed, which exceeds the

75% level required pursuant to Council Policy 800-03 and the 60% threshold required under the 1913 Act.

After the property owners filed their petition with the City, the City Attorney's Office hired outside counsel, Best, Best and Krieger, LLP, with specialized knowledge of the applicable Assessment District laws, and Debt Management hired a registered professional engineer certified by the State of California, Bureau Veritas North America, Inc., to prepare the Engineer's Report as required by the 1913 Act, Article XIID of the California Constitution and Proposition 218. The Engineer's Report, among other things, includes: a boundary map of the district; a description of the project and the estimated total project costs; a description of the assessment methodology; and the assessment roll. A copy of the Engineer's Report is included as Attachment 1.

On June 5, 2007, the City Council passed resolutions accepting the property owner petition, declaring its intention to form the district, and establishing the date of the public hearing on the Assessment District as July 23, 2007. At the July 23, 2007 City Council meeting, property owner ballots were tabulated and the results reflected that 39 assessment ballots were in favor of forming the district, which represented 76% of the weighted assessment ballots cast. The City Council also considered public testimony on the district, and, using its discretion in terms of whether to approve formation of the district, passed a resolution to form the district and levy the assessments. Accordingly, the assessments were enrolled with the County by its August 10, 2007 deadline and will be included on the County issued property tax bills due in two installments payable December 10, 2007 and April 10, 2008. The average total assessment per parcel is approximately \$12,300. Under the project time-line, construction would commence in May 2008 and would be completed in April 2009.

Other Community Initiated Assessment Districts

The 1913 Act provides for a local agency to begin the process to form an Assessment District to finance certain infrastructure, including the undergrounding of overhead utility lines, upon a successful petition signed by owners of property who want the improvement. If an Assessment District is formed, the City may levy assessments that can be utilized to directly finance the public improvements, or to repay bonds issued to finance the improvements under the Improvement Bond Act of 1915 (the "1915 Act").

The City's Assessment Districts have been typically formed to finance public infrastructure in connection with new development, wherein a developer has sought a public financing mechanism to fund public infrastructure required in connection with its development. Prior to the formation of the LJMV District, the last time the City formed a 1913 Act Assessment District initiated by an existing community was 1999; this district was in the Del Mar Terrace neighborhood. Similar to the LJMV District, the Del Mar Terrace district was formed to underground utilities and involved a one-time levy of the assessment on each parcel (i.e., no bonds were issued, and the assessment was payable in not more than two installments and included on the property tax bill).

II. DISCUSSION:

At the July 23, 2007 public hearing on the LJMVDistrict and during Non-Agenda Public Comment on July 31, 2007, certain property owners in the LJMVDistrict neighborhood voiced concerns that a financial hardship would be imposed as a result of the formation of the district. In response to the discussion on this topic at the two meetings, staff explored potential options to address this issue for property owners in the LJMVDistrict neighborhood as well as for property owners in any future, proposed districts. Following, is a summary of these options:

Discussion of Options for LJMVDistrict:

1. Property Owner Financing/Home Equity Loans

An avenue that could be available to many property owners is the option of property owner financing, through a home equity loan or some other type of private financing, which would enable the property owner to finance the assessment over an extended period of time. For property owners within a small district, such as the LJMVDistrict, home equity financing, if available, may actually be less expensive over the life of the financing and in terms of the amount borrowed than a City issued 1915 Act bond financing due to costs of issuance, the establishment of a debt service reserve fund, and on-going administrative costs of the district (see below for description of 1915 Act bonds). For illustration purposes, Attachment 2 provides a chart comparing estimated private financing and 1915 Act financing costs.

2. Assistance Programs Offered by State of California

As outlined in the Reports to City Council pertaining to the LJMVDistrict item, it is staff's understanding that certain programs (the Homeowner and Renter Assistance Program and the Property Tax Postponement for Senior Citizens, Blind or Disabled Citizens) offered by the State of California for assistance of up to \$472 or postponement of the assessment may be available to property owners if specific eligibility criteria, including financial hardship and age, blindness or disability are met. The Notice of Public Hearing to the LJMVDistrict property owners advised property owners that they could contact the California State Controller's Office and the State Franchise Tax Board to obtain information and eligibility requirements for such programs.

3. Assistance from other Property Owners within the District

Through staff's research of this topic, it found at least a few examples involving other agencies whereby property owners made voluntary contributions to other property owners, or donations or irrevocable pledges toward a fund to assist those with hardship situations in paying their assessments. If the LJMVDistrict neighborhood chooses, it can establish and administer a fund or some other type of program to independently aid property owners in need of assistance.

4. **Amendment to Municipal Code – Chapter 6 – Public Works and Property, Article 1 – Public Improvement and Assessment Proceedings, Division 19 – Assessment Deferrals for Low-Income Property Owners**

As explained during City Council discussion of the LJMV District item on July 23, 2007, the City has an existing Assessment Deferral Program, as set forth in Chapter 6, Article 1, Division 19 of the Municipal Code and entitled “Assessment Deferrals for Low-Income Property Owners.” In addition, Council Policy 800-09, Assessment Deferral Program, more generally describes the program set forth in the Municipal Code. Essentially, the program enables a qualified applicant to defer the payment of his/her assessment until the property is sold, otherwise transferred, or re-financed. The applicant must show proof of financial hardship through an extensive review of the applicant’s financial records, and must execute and deliver a note or mortgage bearing interest to the City securing the unpaid assessment. However, the City Attorney’s Office has advised that the program only applies in connection with a district involving the issuance of bonds. Thus, the program as it currently exists is not available to property owners within the LJMV District.

If LU&H desires, the changes described below could be made and forwarded to the City Council for consideration to address this situation as well as to update the eligibility criteria. The anticipated time-frame to update the code, including seeking City Council approval, is six to eight months, and the changes would consist of the following:

- a. Modify the program so that 1913 Act districts, formed without the issuance of bonds, are eligible for the Assessment Deferral Program.
- b. Adjust the criteria related to an owner’s net assets as set forth in the Municipal Code, by the rate of inflation since the criteria was established.

Currently, the qualifications for eligibility established in Municipal Code Section 61.1907 - Qualifications for Low-Income Owners are expressly stated as follows: (i) Owner’s income must be within the guidelines for low-income citizens and families set by the United States Department of Housing and Urban Development, Economic Marketing Analysis Division, as adjusted annually for the San Diego Metropolitan Statistical Area; (ii) The value of owner’s net assets cannot exceed \$10,000¹; (iii) The real property for which assessment deferral is sought must be owner-occupied unless otherwise excepted and approved by the City Council.

Since Section 61.1907 of the Code was added in 1977, it is recommended that, if the Code is modified to facilitate the use of the Assessment Deferral Program for 1913 Act districts, the \$10,000 net assets amount be adjusted by the rate of inflation for San Diego County since 1977 (and that a provision be added that such amount would be adjusted annually thereafter). It is

¹ Pursuant to Section 61.1903 (m) – Definitions of the Municipal Code, Net Assets “means all real and personal property of any character which a low-income owner owns or has an interest in, including stocks, bonds, and savings accounts but excluding the real property subject to assessment deferral.”

estimated, based on U.S. Department of Labor - Bureau of Labor Statistics Consumer Price Index data for the San Diego area, that such an adjustment would increase the \$10,000 threshold to approximately \$43,000, as of 2007.

Please note that it is unknown whether the changes described above would enable any property owners in the LJMV District to receive assistance under the program. However, the program, as it currently exists, is expressly intended "*for the aid and support of the poor*" (61.1900). Staff does not recommend at this time expanding the program through changes to the Municipal Code beyond those for whom it was originally intended. Following are factors considered in forming this recommendation:

- a. Funding Source for Program – Approximately \$105,000 is currently set aside for this program in Fund 10005 (Assessment Deferral Program). However, if the program is to be expanded, a revenue source would need to be identified to augment the fund.
- b. Costs to Administer an Expanded Program – Currently, no property owners are utilizing the program, and the last time the City administered an active deferral through the program was in Fiscal Year 2004. In the past, the program was most often utilized in connection with community initiated districts; as described earlier in the report, prior to the LJMV District, the last such district formed was in 1999. However, when the program was more active, significant staff time was spent in the administration of the program. Pursuant to the Municipal Code, for each applicant, a stringent review of financial records is required upon application, and going forward on an annual basis. If the program is expanded, additional City staff resources would need to be allocated to run the program.
- c. Establishment of Precedence – The City currently administers approximately 9,000 parcels within numerous Assessment Districts and Community Facilities Districts ("CFDs"). If the program is expanded, it could result in applications from property owners in existing districts who do not meet the current criteria as established in the Municipal Code, and could result in requests to expand the program to include CFDs and non-owner occupied parcels. It could also lead to requests for financial relief with respect to other City programs.

5. Revolving Surcharge Funds Loan Option

A revolving loan program utilizing a portion of the SDG&E Underground Surcharge Funds has been considered by staff of the Engineering and Capital Projects department (E&CP), and is not recommended by E&CP for the following reasons:

- a. Costs of creating and administering a loan program are beyond the core function of the Utilities Undergrounding Program.
- b. It would be difficult to develop meaningful criteria that would assist those who truly need assistance without creating a program that results in assistance to an

overly large number of customers, which would place a significant burden on the Surcharge Fund.

- c. Most property owners have access to other private financing options.
- d. Surcharge funds intended for the Undergrounding Program would be diverted away from the City's Master Plan for undergrounding towards community driven assessment projects.
- e. Council Policy 600-08 already provides a mechanism for Council Districts to allocate a portion of their underground allocations toward privately funded underground projects such as those involving assessment districts. On the LJMVB project, Council District 2 allocated \$380,000 of its share of Underground Surcharge Funds in order to reduce the amount of the LJMVB District assessments. This represented approximately 36% of the total cost of the LJMVB project.

6. Multi-Year Installment Plan

Debt Management staff also explored the feasibility of a multi-year installment payment plan with the outside counsel, Best, Best, & Krieger, and the City Attorney's Office. Municipal Code Section 61.2361 – Collection by County Treasurer of Special Assessments provides for the collection of a special assessment to occur in the manner utilized for the LJMVB District (a one time enrollment of the assessment on the property tax bill, payable in two installments) or through an annual levy of the assessment in connection with the issuance of bonds. For the LJMVB assessments to be repaid through some type of multi-year payment or installment plan, including accrued interest, the City Council would need to take action to modify Municipal Code Section 61.2361 to facilitate the payment of the assessments in this manner. In addition, a funding source would need to be identified to provide interim, or advanced, funding to the LJMVB Project to meet the construction time-line, otherwise there would be insufficient funds available to construct the project under its current budget and schedule.

Discussion of Options for Future Districts:

7. 1915 Act Bond Financing

The bond act associated with the 1913 Act is the Improvement Bond Act of 1915, which, like the 1913 Act, is contained within the California Streets and Highway Code. Although bonds could be issued in connection with a district formed under the 1913 Act, such as the LJMVB District, the issuance of bonds is not generally recommended for smaller districts, as outlined in the proposed Special District Formation and Financing Policy recently reviewed by the Budget and Finance Committee and forwarded to the City Council for consideration. This is due, in part, to the fact that costs of issuance would be significant relative to the size of the project being funded (in the case of the LJMVB District, the district includes 56 parcels and a \$690,000 total assessment).

It is important to note that small issuances have all of the attendant risks for the issuer, bond and disclosure counsel, and underwriter that a large issue has, and that the same due-diligence must be applied to a small bond financing as would be to a larger bond financing. Attachment 2 includes information on the estimated additional costs that would need to be financed if bonds had been issued in connection with the LJMVDistrict. As shown in this attachment, it is estimated that the total costs would increase from \$690,000 to \$905,000, a 31% increase. (The petition that was filed by property owners within the LJMVD neighborhood requesting that district formation proceedings under the 1913 Act be initiated on their behalf did not contemplate the issuance of bonds, but instead provided for assessments to be paid in not more than two installments to be included on the property tax bill.)

In addition to the increased costs to finance the project, the on-going costs to administer the district would be significant due to the small size of the district, and could potentially add several hundred dollars a year or more to each of the property owner's annual parcel assessment for the term of the bonds. On-going post-bond issuance activities include continuing disclosure report preparation and dissemination, annual levy preparation and enrollment, arbitrage calculations, and delinquency management as well as other post-bond issuance activities. If some property owners elect to pre-pay the full assessment lien on their property as permitted under the Streets and Highway Code, the on-going fixed costs would be spread over even fewer parcels and would increase the costs for the remaining parcels.

In lieu of pursuing bond financing for smaller districts, the City's goals in the debt management area can be better achieved by focusing on financings that have a broader, City-wide impact (e.g., Water, Wastewater, and General Fund bond financings, such as those issued for public safety and larger streets projects), than by diluting resources to form, finance, and administer projects that benefit only a small number of property owners. As outlined in the proposed Special District Formation and Financing Policy, it is recommended that if a bond financing is executed, a minimum threshold of \$3 million to \$5 million for financed project costs be established. This threshold could be achieved by identifying more than one group (i.e., more than one area or neighborhood) of property owners who are interested in forming a district in connection with a bond financing. The applicable City department (e.g., Engineering & Capital Projects and General Services) and City Council Offices will be in the best position to identify or have awareness of interested neighborhoods based on their interactions with members of the community. However, as established in the proposed Special District Formation and Financing Policy, it is recommended that these types of financings be prioritized after needed City General Fund and Utility financings.

8. California Statewide Communities Development Authority (CSCDA)

The Debt Management Department reviewed with the California Statewide Communities Development Authority ("CSCDA") the option of referring interested property owners to that entity to execute the process to form an assessment district and issue bonds. CSCDA is a state authority that provides local governments and certain private entities access to tax-exempt financing for projects that provide a public benefit. CSCDA is able to offer lower-cost financing through pooled financing programs (e.g., pooling together multiple

districts/projects into one financing). While CSCDA is an option, it requires 100%, or unanimous, voter approval to form an Assessment District. This level of approval is not typical for community initiated Assessment Districts.

9. City Council Discretion to Approve Formation

As stated in the Reports to City Council and the PowerPoint presentation on the LJMVB item, even if the ballot process is successful in terms of forming a district, the City Council has the ultimate discretion as to whether to form the district or not. For the LJMVB item, alternative resolutions were presented for City Council consideration in the event the ballot process was successful, and the staff recommendation was to consider the public testimony in addition to the ballot results in making a decision on whether to form the district.

10. Petition Threshold

Due to the burden that could be placed on property owners who do not want a district formed and vote against a proposed district, Council Policy 800-03 (and the City's proposed Special District Formation and Financing Policy) requires a 75% petition threshold, which exceeds the 60% threshold required under the 1913 Act. In light of the City's experience with the LJMVB District, City Council may wish to increase the 75% threshold to an even higher level. If LU&H desires, the proposed Special District Formation and Financing Policy could be amended to reflect a higher threshold and the City Council could be advised of such change when it considers the proposed policy.

Survey of Other Local Agencies

In an informal survey of 10 other municipalities throughout the State, Debt Management staff found that two other entities offered some type of formal assessment assistance or deferral program (one other entity that does not have a formal program will work with individual property owners on a case by case basis) and that the programs included stringent eligibility criteria in terms of financial hardship or income levels. In addition, some of those surveyed refer property owners to the State for information on its programs, or do not offer the option of forming an Assessment District to interested property owners due to the financial hardship that could be imposed on those who do not want the district formed.

City's Cost Sharing Program

As described above, the City offers a cost-sharing program pursuant to Council Policy 600-08, under which City surcharge funds can be allocated to an assessment district. The policy permits City Council to make allocations of up to 75% for formation costs and there is no limit on contributions to construction costs. For the LJMVB District project, \$380,000 of City surcharge funds were allocated by the City Council to offset the project costs assessed to the homeowners. This offset constitutes 36% of the overall project cost, including the costs of district formation.

Summary

As described above, there are some options for addressing the topic of financial hardship for property owners in future, proposed assessment districts. These range from not forming the district if there is compelling public testimony of hardship that would result from formation of a district, bond financing through CSCDA in the case of districts with 100% approval through the petition and ballot processes, as well as City 1915 Act bond financing if a district is large enough, or if more than one project area seeks district formation and financing and can be pooled into a larger issuance, ranging from \$3 million to \$5 million in project size.

On July 23, 2007, the City Council passed a resolution forming the LJMVDistrict. Pursuant to the passage of the resolution and formation of the district, liens have been recorded against the parcels in the district and the assessments were enrolled by the County's August 10, 2007 deadline for inclusion in the Fiscal Year 2008 property tax bills. Existing options for the LJMVDistrict are limited to private property owner financing/home equity loans, and the assistance programs offered by the State. If LU&H and City Council desire, City staff, including staff of the City Attorney's Office, could prepare the changes to the Municipal Code described above to modify the City's existing Assessment Deferral Program so that property owners within 1913 Act districts are eligible, and to adjust the net assets eligibility criteria by the rate of inflation.

III. ASSESSEMENT METHODOLOGY FOR LJMVDISTRICT:

During the July 23, 2007 Public Hearing on the LJMVDistrict and Non-Agenda Public Comment on July 31, 2007, public comments were made in which the fairness of the assessment methodology utilized for the LJMVDistrict was questioned. These comments were also referred to LU&H. The following paragraphs provide information in response to such comments.

Pursuant to California State Law, Article 13D, Section 4(b), all assessments shall be supported by a detailed engineer's report prepared by a registered professional engineer certified by the State of California. The City hired the firm of Bureau Veritas North America, Inc., a firm which has extensive experience in the development of assessment methodologies as required under the 1913 Act. The firm was selected from an as-needed list of special tax consultants and assessment engineers generated by a request for proposals process.

Mr. Dennis Klingelhofer is a Senior Vice President with Bureau Veritas North America, Inc. and a registered professional engineer; he developed the assessment methodology which was used to apportion the costs to each parcel within the LJMVDistrict. Pages five and six of the Engineers Report for the LJMVDistrict, which was attached to the Reports to City Council on the district, outline the assessment methodology used, including a discussion of the special benefits related to improved safety and reliability and aesthetic enhancement of the neighborhood area which the parcels would receive.

Among the informational letters sent by the Debt Management Department to all property owners of record within the LJMVDistrict was a letter dated May 25, 2007 which, among other things, specified how property owners could access materials related to the initial formal legislative action (taken on June 5, 2007), including the Preliminary Assessment Engineer's Report. In addition, following the City Council's adoption of resolutions relating to the

formation of the district on June 5, each property owner of record received a Notice of Public Hearing which also specified how property owners could access the report.

As outlined in the Engineer's Report (Attachment 1) under the section entitled "Improved Safety and Reliability," those properties (55) that received "a direct safety and reliability benefit (their overhead service will be converted to an underground utility system) [will] be assigned a safety and reliability benefit factor ("BF") of 1.00 BF. One parcel...[will receive] an indirect safety and reliability benefit since [it] will still have an overhead service adjacent to [the] property, although [it] will be served by the newly undergrounded system. This parcel will be assigned a safety and reliability benefit factor of one-half (.50 BF)." Also as outlined in the Engineer's Report under the "Aesthetic Enhancement Benefit" section, "[f]ifty five (55) parcels [will] receive a direct aesthetic enhancement benefit (obstructions removed directly adjacent to their property lines) and will be assigned an aesthetic benefit ("BF") factor of (1.00 BF). One (1) parcel...[will] receive an indirect aesthetic enhancement benefit (minor obstructions remaining adjacent to [the] property lines) and will be assigned an aesthetic benefit factor of one-half (.50BF)."

The following observations have also been made by Mr. Klingelhofer regarding the methodology used for the LJMVDistrict: (1) there are different methods used for Assessment Districts, but *that for projects involving the undergrounding of utilities the method used in the case of the LJMVDistrict is the more common methodology*; (2) another methodology, which is based on street footage, is more typical for districts created for curb and street improvements; (3) with underground utility assessment districts, the benefit is the improved system reliability resulting from the undergrounded electrical service, which is not a function of street frontage; and, (4) unless there are significant view differentials, the methodology needs to be applied as a system (i.e., the neighborhood will be undergrounded, or it will not be). In Mr. Klingelhofer's opinion, there is not a lot of view disparity in the subject area, and the aesthetics are similar.

One of the public speakers referred to the methodology used for an undergrounding Assessment District formed in the Town of Tiburon. Staff researched the project and found the following language from the subject Engineer's Report, prepared by Harris & Associates:

"The aesthetic benefit of removing poles and overhead lines adjacent to properties is deemed to be the same for all properties whether or not one property is thought to have a better view than another, because the increase in property value from the improvements is considered the same on a percentage basis. For properties where utility equipment must remain, the benefit is reduced and therefore the assessment is reduced."

The methodology employed for this district appears similar to that used for the LJMVDistrict.

Mr. Klingelhofer was present at each of the City Council Meetings relating to the formation of the district, and staff has also requested that he attend the LU&H Meeting to answer any questions of the committee related to the assessment methodology utilized for the LJMVDistrict.

IV. FISCAL CONSIDERATIONS:

None specific to this action.

V. PREVIOUS COUNCIL ACTION:


Actions related to the Assessment Deferral Program include the adoption of Council Policy 800-09 (Assessment Deferral Program) by Resolution R-217635 on February 2, 1977 and the addition of Section 61.1907 (Qualifications of Low-Income Owners) to the Municipal Code by Ordinance O-12196 on October 26, 1977.

VI. COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:

There were no community participation or outreach efforts specific to the subject of City options for addressing financial hardships in the case of Assessment Districts and the levy of assessments.

VII. KEY STAKEHOLDERS & PROJECTED IMPACTS (if applicable):

Key stakeholders include future applicants for Assessment District formation and/or financing. Other key stakeholders include owners of existing property subject to an assessment lien.



Lakshmi Kommi
Debt Management Director



Jay M. Goldstone
Chief Operating Officer

Attachments:

(1) LJMV District Engineers Report

(2) Comparison Chart