

**City of Modesto
Grand Jury Case # 06-20
2005-2006**

SUMMARY

The Stanislaus County Civil Grand Jury (CGJ) received a complaint from a resident living in the North Beyer Park District, which became known as Community Facilities District 1997-1 (CFD 1997-1.) The resident previously presented a complaint, containing five issues, to City of Modesto staff and the Modesto City Council. The resident has not been satisfied with the City's response to his complaint.

The CGJ investigation found that the City of Modesto had corrected four of the five issues referenced in the resident's complaint. The remaining claim, "reserve funds are being eroded by an ever escalating stream of administrative and consulting fees," the CGJ found to be true.

The CGJ, after reading the appropriate government code sections, the Modesto Policies and Procedures Manual, and the language of the CFD, recommends that all monies from CFD 1997-1, used for administrative, consulting, and/or audit purposes, shall be returned to the fund. The CGJ also recommends that all future CFD 1997-1 funds be used only for the purposes specified in the CFD language.

INTRODUCTION

The Community Facilities District Act of 1982 allows local governments, with the approval of those living within the identified subdivision - or the property owners before there is a subdivision - to create a special taxing plan to pay for the installation and maintenance of improvements that primarily benefit those living in that subdivision. When a new subdivision is proposed within the City of Modesto Master Plan, the city may designate the new subdivision as a Community Facilities District (CFD) for the installation and maintenance of storm drains, parks, medians, off-sight improvements, etc. The North Beyer Park subdivision was designated as Community Facilities District 1997-1.

The complaint submitted to the CGJ was specific to CFD 1997-1. CFD 1997-1 was one of the earliest CFDs created by the City of Modesto, and as such is different in its design than subsequent CFDs. Current CFDs have a portion of the taxes collected designated for the administrative costs of maintaining the CFD. CFD 1997-1 does not have an administrative cost component.

According to a City of Modesto Audit Committee Report, November 17, 2004, "CFD 1997-1 was formed to provide funding for the installation of landscape medians and planter strips along Oakdale Road and Coffee Road, as well as, funding for ongoing maintenance of landscape medians along Oakdale Road, Coffee Road, and the future Pelandale Expressway (now Pelandale/Claratina.)"

CFD 1997-1 consists of 464 single-family residence parcels and two mixed-use parcels. Although all of the residential parcels are fully developed, the mixed-use parcels are not. The installation of the medians on Coffee and Oakdale Roads cannot take place until development of the mixed-use parcels takes place. The land needed to fully widen the roadway and to install the medians and planting strips will need to be dedicated by whoever develops these properties.

Under CFD 1997-1, the installation of the Pelandale medians will not take place until the roadway is built out to the planned six-lane expressway. The installation of the medians will be accomplished as part of the roadway construction, but the maintenance cost of those medians will be provided by CFD 1997-1.

As of the June 30, 2004, CFD Status report, a sum of \$128,710.18 in total maintenance special tax revenues for CFD 1997-1 had been collected (between 1997 to 2003). Interest payments on this fund totaled \$186.00, for a total amount of \$128,896.18. Administration costs of \$37,792.00 have been spent, leaving \$91,104.00. Collection of the CFD 1997-1 tax was temporarily discontinued in 2003 by action of the Modesto City Council.

The citizen complaint asked the CGJ to investigate the following:

- 1) The City of Modesto has no idea how much money they have collected for the North Beyer Park Community Facilities District (CFD 1997-1) or what they spent the money on.
- 2) The reserve funds are being eroded by an ever-escalating stream of administrative and consulting fees.
- 3) The City of Modesto will not allow an election to change the Community Facilities District (CFD.)
- 4) The City of Modesto needs to maintain better oversight on their special districts. The administrative and consulting costs must be controlled.
- 5) The consultant's charges should be subject to review.

The CGJ integrated those issues into the following:

- 1) Does the City of Modesto have accurate records to show the amount of money collected and expended for CFD 1997-1?
- 2) How has CFD 1997-1 been administered; what amount of funds are being spent on administration, auditing, and consulting fees; and what level of management does the City of Modesto exercise in the administration of Community Facilities District funds?
- 3) Is there a provision in law for an election to change an existing Community Facilities District and under what circumstances?

METHOD OF INVESTIGATION

The CGJ interviewed the following:

- Complainant, Case #06-20.
- Representative of the Attorney's office, City of Modesto.
- Representative of the Engineering Staff, City of Modesto.
- Representative of the Planning Department, City of Modesto.
- Current and previous administration officials of the City of Modesto.

The following documents were reviewed:

- Financial report for CFD 1997-1, June 4, 2004.
- Report of Fiscal Year 2003/04 expenditures for CFD 1997-1, April 25, 2005.
- Notice to Homeowners regarding the suspension of special tax levies between 2003 and 2006 for CFD 1997-1.
- Performance Audit of CFDs 1996-1, 1997-1, 1998-1, 1998-2, 2000-2, 2001-1 for the year 2003.
- CFD Act of 1982.
- City of Modesto CFD Status Report for CFD 1997-1 dated 2002, 2003, and 2004 by Goodwin Consulting.
- City of Modesto Policies and Procedures for the formation and administration of CFDs, Adopted September 1996, amended 10/96, 3/98, 4/98, 6/98, 9/98, 8/99, 10/99, 1/02, 4/04, and 6/04.
- California Government Code Sections 53332, 53312.7, 53343.

FINDINGS

1. Accuracy of records for revenues and expenditures of CFD 1997-1 funds.

The City of Modesto presented the CGJ with several financial audits and account reviews for the North Beyer Park CFD 1997-1. The spreadsheets show the revenue and expenses for CFD1997-1. The Consultant's Performance Audit of CFD 1997-1, as reviewed by the City of Modesto's Audit Committee at their November 22, 2004 meeting, verified the accuracy of the spreadsheets.

These records, and the responses from City Staff during sworn testimony before the CGJ, indicate that the City of Modesto has maintained an accurate and responsible record of the taxes collected and the expenditures paid from the CFD 1997-1 account. The Capital Investment Plan indicates the anticipated future expenditures for CFD 1997-1.

2. Level of management the City of Modesto exercises in the administration of Community Facilities District funds; the amount of funds being spent for administrative and consulting fees, and the control of consultant charges.

Management of CFDs

Administrative direction to local agencies desiring to create a Community Facilities District is provided in Government Code Section 53312.7(a), "On or after January 1, 1994, a local agency may initiate proceedings to establish a district pursuant to this chapter only if it has considered and adopted local goals and policies concerning the use of this chapter." ("Goals and Policies to be Adopted Before Initiation of Proceedings to Establish District.")

The City of Modesto has met this requirement by adopting "*Policies And Procedures for the Formation, Annexation and Administration of Community Facilities Districts Created Pursuant to the Provisions of The Mello-Roos Community Facilities Act Of 1982.*" (adopted September 3, 1996 Policy Manual.)

The Policy Manual specifies the City's intent to use the Mello-Roos Act to provide for the financing of City owned and operated infrastructure and services. The Policy Manual, p. 26, further establishes the staff/administrative infrastructure to oversee CFDs and defines the duties of the District Administrator post formation/post annexation.

Currently, a division within the City Manager's office oversees the CFDs for the City of Modesto. The City Manager, one Senior Structural Engineer, one Administrative Office Assistant, and two CFD Administrative Officers (who share one position) comprise the CFD Administration division.

Services paid from the CFD 1997-1 account

The City of Modesto, as the legislative body, has established administrative and financial services for the management of the nine (9) CFDs within the City's jurisdiction. CFD administration employees bill the CFD for working time spent on CFD services, including responding to questions from citizens, providing reports and documents, and an annual audit/ financial reporting program for CFD 1997-1. The City has been utilizing consultants to perform some of these services. During sworn testimony before the CGJ several City staff members contended that this section of Policy Manual indicates that these are necessary administrative/ financial services and the "CFD must pay its own way."

Government Code Sections 6250 through 6276.48, The California Public Records Act, includes inquiries regarding CFDs. Under this Code, public agencies must give access to view the records of the CFD at no cost, and if a citizen requests a copy of that report, he can only be charged the direct cost of duplication, usually \$.10 to \$.25 per page. Charges for search, review and deletion are not allowed.

The Policy Manual does not define "services." The CGJ reviewed the definition of services applicable to a CFD, as stated in Government Code Section 53313, "Services Which May Be Provided." The definition of services eligible under this government code section does not support the City's practice of charging administrative fees for answering questions, committee work, or other administrative functions.

Government Code section 53343, "Use of Charges," states, "A Community Facilities District may be established under this chapter to finance any one or more of the following types of services within an area ..." Administrative, audit, and consulting fees are not included as authorized "services."

Government Code Section 53343.1 "Annual Report" only requires this report if requested by a person who resides in or owns property in the district. The district may charge a fee for the report not exceeding the cost of preparing the report.

There is no provision for an administrative services component. The Policy Manual (page 7) states: "all City administrative and consultant costs, including those of the District Administrator, related to administration of a CFD and incurred after formation shall be included within the *special tax formula* (emphasis added) in accordance with applicable provisions of law."

However, CFD 1997-1, as one of the first Community Facilities Districts enacted by the City of Modesto and unlike current CFD programs, does not have the "*special tax formula*" (an administrative account.)

The City Attorney's office informed the CGJ that, "There are two special tax components in the North Beyer Community Facilities District: a one-time Facilities Special Tax and an annual Maintenance Special Tax. Administrative expenses are included within the Maintenance Special Tax component."

Based on the time of issuance of the administrative component section of the Policy Manual (July 18, 2000), the lack of the special tax formula, the cited Government Code sections, and the opinion from the City Attorney's office, the administrative fees policy does not apply to CFD 1997-1.

To date, the CFD has been unable to construct the medians, because (1) insufficient tax monies have been collected for the construction projects and (2) the medians cannot be installed until property owners/developers on both Oakdale Road and Coffee Road dedicate the necessary right-of-way to construct the full roadway width.

Additionally, while CFD 1997-1 have been sitting for nine years without being used for the purposes for which they were intended, the city has continued to deduct CFD funds to pay for services not authorized by CFD 1997-1 language or account design. The City's practice of charging for annual audits and reports is not supported by Government Code Sections 53343, 53343.1, or the Policy Manual. Therefore, the CGJ finds that the City is performing unnecessary financial functions and charging in a manner not provided for in the language or design of CFD1997-1. The City may not charge administrative, auditing, or consulting fees against CFD 1997-1 until CFD 1997-1 enters its landscape maintenance phase.

3. The provision in law for an election to change an existing Community Facilities District is found in the following sections of the Government code.

Government Code Section 53332(a). "Petition For Changes In Facilities, Services, Or Taxes":

If a petition signed by 25 percent or more of the registered voters residing in the district, or by the owners of 25 percent or more of the territory within the district, is filed with the legislative body requesting that proceedings be commenced to change the types of public facilities or services financed by the district or that the rate or method of apportionment of an existing special tax be changed, or that a new special tax be levied, the legislative body shall within 40 days thereafter adopt a resolution of consideration in the form specified in Section 53334 to make those changes within the community facilities district ...

The following exchange took place between the CGJ and a representative of the City Attorney's Office:

CGJ: "If a proposal to dissolve a community facilities district is submitted to the qualified electors of the district and two-thirds (2/3) of the qualified electors are in favor of the dissolution, is the vote binding on the City?"

Interviewee: "Government Code Section 53338(b) provides that if two thirds of the votes cast on a proposition are in favor of the proposed change, then the legislative body is required to adopt a resolution determining that the proposed change is lawfully authorized."

The law clearly provides a method for altering a CFD by election. The outcome of that election is binding on the City of Modesto as the legislative body. However, according to Government Code Section 53332(b), "Any petition filed by the landowners shall be accompanied by the payment of the fee which the legislative body determines. That fee may be imposed in an amount sufficient to compensate the legislative body for all costs incurred in conducting proceedings to change the district pursuant to this article."

RECOMMENDATIONS

1) Accuracy of records for revenues and expenditures of CFD 1997-1 funds.

- The records provided to the CGJ established that the City of Modesto has maintained an accurate and responsible record of the taxes collected and the expenditures paid for the CFD 1997-1 account.

No recommendation.

2) Level of management the City of Modesto exercises in the administration of Community Facilities District funds; the amount of funds being spent for administrative and consulting fees, and the control of consultant charges.

- The Mello-Roos Community Facilities Act Of 1982 allows the agency to charge for the formation, annexation, and administration of a new CFD. The agency can charge for bond development and sales, but the agency **cannot** charge citizens for inquires, questions, request for copies, etcetera.

The records indicate that:

- a. The City of Modesto Resolution 2000-376, adopted July 18, 2000, permitting a special tax formula for administrative fees, but Resolution 2000-376 was adopted after the formation of CFD 1997-1, and therefore does not apply to CFD 1997-1.
 - b. Neither the Government Codes nor the Policy Manual support the current program of annual financial audits and reports. Therefore, Government Code 53343.1, which allows charges for specified facilities and services only, does not support the City's current practice of charging CFD 1997-1 for administrative and financial "services" and is not allowed.
- The CGJ recommends that fees deducted from CFD 1997-1 accounts for administrative and/or financial services shall be reimbursed to CFD 1997-1 account by the City of Modesto within 180 days. The CGJ further recommends that this account be frozen against any further charges unless specified as approved expenditures by the language of the CFD 1997-1.

3) California law provides for an election to change an existing Community Facilities District and specifies under what circumstances.

- Government Code 53332, petition for changes in facilities, services, or taxes, establishes that there is provision for altering a CFD and the decision of the electors is binding on the City of Modesto as the legislative body.

No recommendation.