

*Office of the  
City Manager*

*1010 Tenth Street  
Suite 6100  
P.O. Box 642  
Modesto, CA 95353  
209/577-5223  
209/571-5128 Fax*

*Hearing and Speech  
Impaired Only  
TDD 209/526-9211*

August 9, 2006

Superior Court – Stanislaus County  
The Honorable Presiding Judge Marie Sovey Silveira  
P.O. Box 3488  
Modesto, California 95353

Re: **2005-2006 Stanislaus County Civil Grand Jury Report  
City of Modesto CFD No. 1997-1 (North Beyer Park)**

Dear Judge Silveira:

Enclosed please find an original and three copies of the *City of Modesto's Response to the Findings and Recommendations of the Stanislaus County 2005-2006 Civil Grand Jury Final Report Relating to City of Modesto Community Facilities District No. 1997-1 (North Beyer Park)*. By copy of this letter to the Stanislaus County Clerk-Record and the Modesto City Clerk/Auditor I am requesting that a copy of this report be placed on file in their respective offices.

Sincerely,

George W. Britton  
City Manager

GWB:pdl  
Enclosure as noted

cc: Lee Lundrigan, Stanislaus County Clerk-Recorder  
Jean Morris, City Clerk/Auditor  
Susana Alacala Wood, City Attorney  
Tina Rocha, IFP Administrative Officer

**City of Modesto**  
**Response to the Findings and Recommendations of the**  
**Stanislaus County 2005-2006 Civil Grand Jury ("CGJ") Final Report Relating to**  
**City of Modesto Community Facilities District No. 1997-1 (North Beyer Park)**

**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 CFD 1997-1. 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. **Agree.**

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.* (emphasis added) The Capital Investment Plan indicates the anticipated future expenditures for CFD 1997-1. **Agree.**

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**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.") **Agree.**

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.) **Agree.**

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. **Agree.**

Currently, a division with 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. **A Senior Civil Engineer, not a Senior Structural Engineer, assists with the administration of the CFDs. Otherwise, agree.**

- 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 question 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." **Agree.**

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 be charged the direct cost of duplication, usually \$.10 to \$.25 per page. Charges for research, review and deletion are not allowed. **We agree that records pertaining to a CFD are subject to the California Public Records Act and that an individual can only be charged for the direct cost of duplication.**

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. **We agree that Government Code Section 53313 defines "Services" that are eligible to be funded through a CFD. However, the City is not relying on this code section for its authority to charge administrative expenses. The City's authority is found in Government Code Section 53340(d). See below.**

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." **Disagree.** Government Code section 53343 states "[a]ny charges collected pursuant to this chapter may only be used for facilities and services authorized by this chapter. Government Code section 53340(d) further provides that any special tax may be used to pay for the "cost of providing public facilities, services, and incidental expenses." Government Code section 53317(e)(2) specifically defines "incidental expenses" to include, among other things, "The costs associated with the creation of the district, issuance of bonds, determination of the amount of taxes, collection of taxes, payment of taxes, or costs otherwise incurred in order to carry out the authorized purposes of the district." (emphasis added). In addition, Government Code Section 53343.1(d)(5) specifically requires a District to include "Other administrative and overhead costs" in an Annual Report, demonstrating that such costs are both authorized and anticipated. These Government Code sections and others clearly allow the CFD to pay for administrative expenses. Reasonable administrative expenses include but are not limited to the costs and staff time associated with oversight and management of a CFD, costs and staff time related to property owner inquiries, and consultant time and costs associated with levy of annual taxes and preparation of reports.

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. **While we agree that this code section provides for preparation of an Annual Report if requested to do so by a person who resides in or owns**

property in the district, we disagree with the CGJ's interpretation. While it only requires a report under specified circumstances, this section does not preclude a local agency from preparing an Annual report should a legislative body choose to do so.

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 the applicable provisions of law." **Agree as to the policy language. Disagree that the special tax formula for CFD 1997-1 does not provide for administrative expenses. A special tax formula is also known as the Rate and Method of Apportionment ("RMA"). An RMA was adopted for CFD 1997-1 and can be found in Appendix A of the CFD Report adopted for CFD 1997-1 (a copy of which is provided as Attachment 1.) Page 2 of the RMA defines the "Maintenance Special Tax Requirement" to be "the amount necessary ... to (i) pay for authorized maintenance expenses [and] (ii) pay *administrative expenses* (emphasis added) of CFD No. 1997-1."**

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.) **Disagree, see response above.**

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." **Agree.**

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. **Disagree. As discussed above, Government Code Sections 53317(e)(2), 53340(d) and 53343.1(d)(5), as well as others, allow a CFD to pay for administrative expenses. In addition, an RMA was adopted for CFD 1997-1 that includes a provision for administrative expenses to be collected and charged against the maintenance special taxes collected for CFD 1997-1. There is no legal requirement that administrative expenses be collected as a separate "component" of the special tax. The City Attorney's office and the City's outside bond counsel have reviewed the relevant Government Code sections, the Rate and Method of**

**Apportionment for CFD No. 1997-1 and this response and concur that the City is legally authorized to charge administrative expenses to CFD No. 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. **Agree.**

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 support by Government Code Section 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 CFD 1997-1. The City may not charge administrative, auditing, or consulting fees against CFD 1997-1 until CFD 1997-1 enters its landscape maintenance phase. **Disagree. As discussed above, Government Code Section 53340(d) provides that any special tax may be used to pay for the "cost of providing public facilities, services, and incidental expenses." Administrative expenses are considered incidental expenses and are authorized charges against the Maintenance Special Taxes.**

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**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 ... **Agree.**

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." **Agree.**

### **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.

**We concur.**

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#### **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.

**The recommendation will not be implemented because it is unwarranted or unreasonable. Additionally, the recommendation does not recognize that the Government Code as well as the RMA adopted for CFD 1997-1 allows special tax monies to be used for administrative expenses. However, on June 6, 2006, the City reviewed its current policies with respect to preparation of annual financial audits and will be making changes as set forth below.**

**City of Modesto Resolution 2000-376 pertains to the responsibilities of the City Council Audit Committee and is not relevant to CFD 1997-1, RMAs or administrative fees.**

**Pursuant to Government Code Section 53312.7, the City Council adopted local goals and policies concerning CFDs ("Policies & Procedures"). These Policies & Procedures were first adopted on September 3, 1996 and have been amended from time to time, most recently on June 22, 2004. While the Policies &**



Procedures are guidelines in developing and administering RMAs, the RMA actually adopted for a CFD dictates how the special taxes will be levied and what those taxes may be used for.

As discussed above, Government Code section 53340(d) provides that any special tax may be used to pay for the "cost of providing public facilities, services, and incidental expenses." Page 2 of the RMA adopted for CFD 1997-1 defines the "Maintenance Special Tax Requirement" to be "the amount necessary ... to (i) pay for authorized maintenance expenses [and] (ii) pay administrative expenses (emphasis added) of CFD No. 1997-1." Accordingly, administrative expenses are authorized by both the Government Code and the RMA adopted for CFD 1997-1.

The recommendation incorrectly implies that "citizens" have been charged for inquires, questions, requests for copies, etc. No "citizen" has been charged for inquires, questions, copies, etc. other than as provided by the RMA. Rather, administrative expenses for such things as oversight and management of the CFD, responses to resident inquiries, etc., considered incidental expenses, have been correctly charged against the Special Maintenance taxes collected within CFD 1997-1.

In 2003 staff began preparing annual status reports for all of the City's CFDs for the benefit of all residents within the CFDs. With this approach, the cost of the Annual Reports is borne by the entire CFD and is paid by the annual special taxes. On June 6, 2006, the City Council provided policy direction to staff with respect to the preparation of annual financial audits, Annual Reports and allocation of administrative expenses, as they relate to CFD 1997-1. (A copy of the staff report is provided as Attachment 2.) The City is reviewing and revising its cost allocation policy to proportionately distribute the cost of the CFD audits based on the size of a CFD and its volume of activity within the fiscal year rather than charging all CFDs equally for audit expenses. The City is also discontinuing preparation of the CFD No. 1997-1 Annual Report until CFD-funded improvements are installed.

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**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**

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

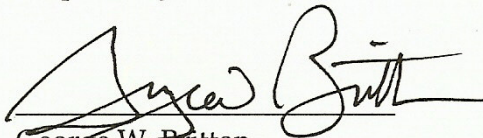
Government Code 53332, petition for changes in facilities, services, or taxes, establishes that there is provision for altering a CFD and the decision of the electors is binding on the City of Modesto as the legislative body.

No recommendation.

**We concur.**

August 9, 2006

Respectfully Submitted:

A handwritten signature in black ink, appearing to read "George W. Britton", written over a horizontal line.

George W. Britton  
City Manager