

Top Ten Matters Every First Time (or Second or Third...) Mello-Roos Issuer Must Know

Effective January 1, 1983, the Community Facilities District (CFD) Act (the Act) was developed in response to Proposition 13's impact on the ability of local government in California to finance public facilities and services needed to accommodate growth. The legislative sponsors of the Act were Senator Henry Mello and Assemblyman Michael Roos. As California's population continues to increase and as development patterns and locations shift the use of CFD's to fund infrastructure will most likely increase.

The following list is provided to give local agencies that are requested to form CFD's some insights into the CFD formation process and points to consider.

1

Adopt Policies

Per an amendment to the Act after January 1, 1994, a local agency may only initiate proceedings to establish a CFD if it has first considered and adopted local policies concerning CFDs. The code section (Government Code Section 53312.7 (a)) also provides for minimum requirements of the local goals and policies. There are two general viewpoints related to the content and scope of local CFD policies. The first is a minimalist approach is with the local goals and policies providing only what is required to comply with the Government Code. This approach provides for flexibility in later interpretation of the policies and is the more open approach. The second approach is a more comprehensive approach where the local goals and policies exceed the minimum requirements of the Government Code. This broader approach is more restrictive than the minimalist approach and provides jurisdictions the ability to proactively set limits on CFDs. Depending upon local factors and circumstances either approach may be useful. Typically adopted local goals and policies contain provisions for a waiver based upon a finding of need and majority vote of the governing body.

2

Require A Developer Application And Deposit

Formation of CFDs may be initiated by landowners through a petition initiated CFD or by a local agency's legislative body. Most CFDs are formed to finance infrastructure in newly developing areas and at the request of landowners. When approached by landowners requesting formation of a CFD a local agency should provide the proponents a CFD Formation application. This application, which the agency can develop at the same time as the CFD policies, requests information on physical attributes, ownership, entitlements, tax payment history and other information on property within the proposed CFD. When returned, the application should be accompanied by a cash deposit. The deposit is provided to fund staff and consultant efforts to determine CFD feasibility and to initiate the CFD formation process.

3

The Issuer Selects The CFD Consulting Team

Formation of a CFD and a subsequent issuance of bonds typically involves a diverse specialized financing team. Members of this typically ad hoc team include a Financial Advisor, Special Tax Consultant, Bond Counsel, Appraiser, Real Estate Market Consultant and Underwriter. Sometimes a Disclosure Counsel also joins the Issuer's finance team to prepare disclosure documents. As the issuer of bonds, the jurisdiction should control selection and management of the finance team. As a rule of thumb, an agency should avoid accepting a slate of finance team members proposed by project proponents.

4

Land Use Decisions Prevail

CFD bonds are typically issued to finance public facilities required by new development. As such they can be viewed as a mechanism to implement a jurisdiction's already determined land use policies. CFDs should not be formed too early in the land use decision process. If formed too early a CFD could compromise the land use decision process. Additionally, if a CFD is formed prior to the time certain land use decisions are made the information required to complete the Rate and Method of Apportionment may be insufficient for an effective tax formula.

5

Fund On-Going Administration

When forming a CFD make sure to address long term administrative processes and costs. Keep in mind certain activities may need to continue throughout the term of bonds (up to approximately 30 years) and require funding. On-going activities include Fiscal Agent fees, special tax administration, continuing disclosure, arbitrage/rebate and foreclosure activities. Make sure administrative items are well-funded, subject to adjustment for inflation and not a burden on the general fund.

6

Patience Is A Virtue

The formation of a CFD and subsequent issuance of bonds can be a long, complex process. During CFD formation, multiple decisions with far reaching implications need to be made. Decisions regarding special tax levels, duration and allocation need to be discussed, negotiated and finalized. There are few short cuts to a prudent CFD formation and bond issuance. Proper planning and due diligence are required. Being in a hurry is generally not the best approach.

7

Negotiate From Strength

An Issuer should negotiate from a place of strength regarding a developer requested CFD. Access to a CFD to finance required infrastructure can greatly enhance the viability of a development project. Use of a CFD provides a developer with a low interest rate, non-recourse, off-balance sheet financing alternative. Agencies should remember the benefits a project's financial picture receives from a CFD financing, and negotiate from a position of strength to achieve its goals.

8

Regional Improvement Should Be Emphasized

When originally enacted the intent of the CFD Act was to assist in the financing of improvements providing more regional than local benefit. Besides matching the original intent of the Act the provision of regional improvements tends to more positively impact land value than provision of local improvements and is potentially more politically defensible. In tract improvements have been traditionally funded via bank loans or owner equity and not financed via CFD's.

9

Consider All Regional Infrastructure; (Or Don't Be A Tax Hog)

It is quite likely that a number of municipal entities will need to provide infrastructure for a growing community. New development requires new schools, water, sewer, streets, freeway interchanges and other infrastructure typically provided by different jurisdictions. An entity forming a CFD should be aware of and consider the needs of other governmental entities when determining what it will finance through a CFD. There is a limit to overall tax rates, only so much infrastructure can be financed. Therefore, it is best when a regional approach is used and a single jurisdiction does not use up all the taxing capacity.

10

Ask Questions; Read The Documents Then Repeat Several Times

Ultimately the responsibility for forming CFD's and selling bonds lies with the issuing entity. No matter how many consultants or lawyers for bonds there are, the issuing entity has responsibility. It is imperative that both staff and governing board members ask questions regarding CFD formation, bond issuance and to read documents slate of finance team members proposed by project proponents.