

# FUNDAMENTALS OF LAND-SECURED FINANCING



**NOVEMBER 2, 2022 | POMONA, CALIFORNIA**



FUNDAMENTALS OF LAND-SECURED FINANCING

# PRESENTERS



**Ed Espinoza**  
*Principal*  
Francisco and  
Associates



**James V. Fabian**  
*Principal*  
Fieldman Rolapp &  
Associates Inc.



**Susan Goodwin**  
*Managing Principal*  
Goodwin Consulting  
Group



**Bradley R. Neal**  
*Shareholder*  
Stradling Yocca Carlson &  
Rauth, P.C.



# Session I

## **Basic Structures of Assessment and Community Facilities Districts**



# History of Each in a Nutshell

## Special Assessment Districts

- Municipal Improvement Act of 1913
- Used with the Improvement Bond Act of 1915
- Other Acts normally used for maintenance

## Mello-Roos Community Facilities Districts

- In 1978, Proposition 13 was approved by California voters
- In response to Prop. 13 revenue constraints, the Mello-Roos Community Facilities Act of 1982 was adopted

# California Statutes & Constitution

## Assessment District (AD)

- Primarily 1913 & 1915 Acts for capital projects
- Primarily 1972 & 1982 Acts for maintenance and public services
- Article XIID of California Constitution
- Section 53753 of the Government Code

## Community Facilities District (CFD)

- Mello-Roos Community Facilities Act of 1982
- Articles XIII A & XIII C of CA Constitution
- Charter cities can use legislative powers



# Eligible Capital Facilities to Finance

## Assessment District

- Authorized public improvements
- Must provide local, special benefits to property

## Community Facilities District

- Public improvements with useful life of 5 years or longer
- Can finance facilities:
  - Owned/controlled by issuer and/or
  - Owned, operated and maintained by other public entities
    - JCFA's with other public agencies



# AD vs. CFD

## Assessment District

- Sets a fixed lien for every parcel
- Annual payment reduces lien
- Term of payments = term of bonds

## Community Facilities District

- Sets a maximum annual special tax rate
- Maximum tax rate may escalate
- Term of tax may outlive term of bonds



# Special Benefits vs. Reasonableness

## Special Benefits - ADs

- Assessment based on the direct and special benefit each property receives from improvements

## Reasonableness - CFDs

- Special tax is not a special assessment
- May be allocated on any “reasonable” basis, as determined by the legislative body
- Cannot be an ad valorem tax





# Usual Sequence of Events - ADs

1. Local agency/property owner petition initiated
2. Legislative body commences assessment proceedings
3. Notices of hearing and assessment ballots mailed
4. Public hearing
5. Ballot tabulation and “majority protest”
6. Final actions taken by legislative body
7. End of cash collection / statute of limitations
8. Bonds issued
9. Project costs funded / reimbursed
10. Annual assessment installments levied



# Usual Sequence of Events - CFDs

1. Local agency/property owner petition initiated
2. Local goals & policies adopted
3. Legislative body commences CFD proceedings
4. Public hearing
5. Election
6. Final actions taken by legislative body
7. Bonds issued
8. Project costs funded / reimbursed
9. Annual special taxes levied
10. Annual continuing disclosure reports prepared

# AD vs. CFD Comparison - Similarities

Issue	ADs	CFDs
Pay-as-you-go finance	1913 Act - Not common but possible 1972 Act – Permitted and fairly common	Permitted and fairly common
Pay-off or Prepayment of Lien	Automatically allowed by State statute	Allowed if included in RMA
Debt Service Structure	Almost universally level debt service	Usually level or escalating debt service
Maximum Residential Property Tax Burden as % of Sales Price	No State statutory limit. Standard is not to exceed 2%	No State statutory limit. Standard is not to exceed 2%

# AD vs. CFD Comparison - Differences

Issue	ADs	CFDs
District Boundaries	1913 Act - Boundaries are generally fixed once assessment confirmed  1972 Act – Annexation permitted	May be expanded through future annexations
Land Use Changes	1913 Act - Lien apportionments cannot easily be modified  1972 Act – Annual assessment can adapt	Special taxes generally adapt to changes in land use
Assessment of Undeveloped Property	1913 Act - Assessments on undeveloped land is based on potential development  1972 Act – Annual assessments generally differ between undeveloped and developed parcels	Special taxes between undeveloped and developed land can differ



## Major Factors Favoring an AD

- ADs are appropriate for:
  - Small, local infrastructure projects with little “General Benefit”
  - Projects with multiple property owners
  - Large variable rate financing programs that anticipate multiple conversion of bonds to a fixed rate of interest over several years
  - Some maintenance programs and services



# Major Factors Favoring a CFD

- CFDs are appropriate for:
  - General benefit “community facilities”
  - Projects with few property owners, or broad support
  - Projects requiring flexibility
    - Phased land development projects
    - Uncertainties about eventual land use
  - Projects needing targeted economic burden
    - Exempting publicly-owned parcels
    - Reducing burden on select categories of parcels/uses
  - Projects requiring funding for eligible services and maintenance & operation activities



# Session II

# Pre-Formation Considerations



## Local Goals and Policies

- Legal requirement for CFDs
- Good idea for ADs
- Important to provide guidance, consistency and assurances
- Not the place to cover all deal points





# Key Issues to Cover in Policies

- Priority & Eligibility of Facilities and Services
- Disclosure to:
  - Homebuyers
  - Bond Investors
  - Financial Markets
- Appraisal Criteria
- Application Process
- Credit Quality Requirements



# Acquisition vs. Construction

- ACQUISITION:
  - Developer funds and builds improvements, and public agency “acquires” them
- CONSTRUCTION:
  - Public agency builds
- COMBINATION



## Selecting the Team

- Public agency should choose team
- Municipal Advisor can assist
- RFP Process / Consultant Pool
- Mello-Roos or Assessment District experience is key



# Consultant Roles

## Bond Counsel

- Legal guidance and opinion; formation documents

## Municipal Advisor

- Guidance & market knowledge
- Fiduciary obligation to public agency

## Special Tax Consultant

- Cash flow analysis, tax formula, boundary map, CFD report

## Assessment Engineer

- Benefit finding & Engineer's Report

## Underwriter

- Although not needed until bond issuance, usually part of formation team



# Consultant Roles (cont.)

## Market Consultant

- Price point analysis
- Absorption study
- Mortgage study/report

## Appraiser

- Determines value of properties to be assessed/taxed

## Developer and its Counsel and Consultants

- Provide the required information about the developer, the project, and the financing proposal



# Important Considerations in Assembling Team

- Good communication among team members
- How to best facilitate meetings and calls
- Involve legal counsel to protect agency
- Understand structure and associated workload



## Other Agencies/Utilities Coordination

- Jurisdictional overlap
- Who will own and operate facilities?
- Joint Community Facilities Agreements required for CFDs
- Consent of legislative body required for CFDs and ADs



# 15-MINUTE BREAK





# Session III

## District Formation Process



# Formation Process

- LET'S GET STARTED
  - *Petition*
- MULL IT OVER
  - *Resolution of Intention*
  - *CFD: Rate & Method of Apportionment and Boundary Map*
  - *AD: Engineer's Report and Assessment Diagram*
- HASH IT OUT
  - *Public Hearing*
  - *AD ballot tabulation & CFD written protests*
- SEAL THE DEAL
  - *Resolution of Formation (CFD and AD)*
  - *CFD election*



# CFD Special Election Process

- Conducted after Resolution of Formation
- This is an election under the Elections Code
- Requires 2/3 approval of “qualified electors”
  - If 12 or more registered voters in CFD, registered voter election
  - If less than 12 registered voters, landowner election (one vote per acre or portion of acre)
- Record Notice of Special Tax Lien within 15 days of election



# Assessment Ballot Process

- Required by Proposition 218
- Mailed with Notice of Public Hearing
- This is **not** an election, **not** a secret ballot
- Ballots opened and tallied after hearing
- Weighted by assessment amount
- More “no” than “yes”, then no assessment can be levied



# Assessment Process After Formation

- Recordation of Notice of Assessment
- 30-Day Cash Collection Period
  - Mailed Notice to Pay Assessment
  - Cash payment discount
  - Paid / Unpaid List



## CFD Public Hearing Report

- Description and estimated costs of facilities and services being funded
- Usually includes copy of Rate and Method of Apportionment of Special Tax
- Must be filed with the Clerk prior to public hearing



## Rate and Method of Apportionment

- Approved by public agency at ROF and by 2/3 vote of qualified electors
- Describes methodology used to calculate the annual special tax levy
- Must generate amount needed each year to pay bond debt service and admin expenses, to replenish reserve fund, and to pay directly for facilities and/or services



# CFD Special Tax Formulas: Developed Property Special Tax

- Bond market expects 110% debt service coverage at buildout
- “Developed” trigger can be final map, building permit, certificate of occupancy, or other defined event as of a specified date
- Categories can be based on land use, home size, lot size, density, or other “reasonable” criteria
- Public agency policy limits maximum tax rate
- Avoid variability in special taxes levied on Developed Property





# CFD Special Tax Formulas: Undeveloped Property Special Tax

- Applies to parcels that do not yet meet definition of “Developed Property”
- Typically charged on a per-acre basis
- Provides coverage prior to buildout
- Should absorb variability in special tax levy prior to buildout



# CFD Special Tax Formulas: Additional Items to Consider

- Rate of Escalation (facilities vs. services)
- Steps of Taxation
- Backup Special Tax
- Transition Event
- “PayGo” Special Tax Revenues
- Prepayment Formula



# Engineer's Report

## S&H Code §10204 (1913 Act)

- Plans & Specifications
- Estimate of Costs
- Assessment Diagram
- Assessment Methodology
- Assessment Roll
- Annual Administration Costs



# Engineer's Report

## S&H Code §2960 (1931 Debt Limitation Act)

- Total principal amount of Unpaid Assessments on parcels
- Total true value of parcels
- Total Lien / Value  
(must be less than 50%, by Code)



## Engineer's Report

- Key information document in a dispute
- Prepared by a Registered Prof. Engineer
- Proposition 218 requirements
  - General Benefit should be identified, quantified and discussed
  - Special Benefit should be clearly defined
  - Assessment spread clearly detailed
  - Special treatment of public parcels should be discussed



# LUNCH

Lunch will be held upstairs in Dining Room A/B



# Session IV

# Project Implementation



# Construction or Acquisition?

## Construction Project

- Issuer constructs project
- Bond proceeds pay costs as needed

## Acquisition Project

- Developer/Owner constructs improvements (must front the costs)
- Issuer to “acquire” with bond proceeds





# Developer Constructs Improvements

- Acquisition Agreement specifies purchase processes and eligible improvements
- Review and payment timelines
- Completed Facility vs. Discrete Portions
- Other considerations and requirements
  - Bidding procedures
  - Inspection
  - Insurance
  - Change Orders
  - Soft costs



# Developer Constructs Improvements

## Requirements for Developer to get paid:

- Contracts, invoices, & proof of payment
- Prevailing wages
- Confirmation of construction quantities
- Evidence of transfer of title
- Evidence of acceptance of improvements or deemed capable of serviceable use
- Lien releases from contractor and subs



## Delta Shores CFD No. 2019-1

- Payment request submitted by Developer included roadway, sewer, storm drain, and water improvements
- Documentation included contracts, change orders, invoices, canceled checks, improvement plans, agency approvals, and lien releases covering \$17.6 million
- The final recommended payment was \$13.5 million



# Issuer Constructs Improvements

Expand working group to include:

- Public Works staff
- Representatives from other local agencies
- Design engineer / environmental consultant
- Contract administrator / inspectors
- Real property appraiser



# Issuer Constructs Improvements

- Project Design
- Property Acquisition
- Environmental Clearance
- Review and Approval of Plans & Specs
- Solicitation of Sealed Bids



# Session V

# Bond Issuance



# Bond or Debt Issuance

- Financing Team
- Overview of Process
- Upfront Considerations/Timing
- Disclosure



# Expansion of Financing Team

## Existing Financing Team & Staff, plus...

- Appraiser
  - Estimates value of liened property
- Underwriter
  - Structures and markets the bonds
    - (if negotiated sale)
- Disclosure / Underwriter's Counsel
  - Prepares bond sale financing documents  
(Official Statement, bond purchase agreement, etc.)





## Expansion of Financing Team (cont.)

- **Trustee / Fiscal Agent**
  - Holds, invests and disburses funds at direction of issuer
  - Has trust obligation to bond owners
- **District Administrator**
  - Assists Issuer in administering AD/CFD  
(good practice to retain earlier in process)
- **Developer/Developer's Counsel/Developer's Consultant**
  - Provides the required information about the Project, the Developer, and the financing for the Project



# Bond or Debt Issuance Process

## Overview: How is it done?

1. Financing team drafts legal and financing documents
2. Bond Counsel prepares bond resolution
3. Issuer approves financing documents
4. Issuer sells bonds to underwriter
5. Underwriter sells bonds to investors

# Bond or Debt Issuance Process (Cont.)

## Overview: How is it done?

6. Issuer receives \$s in exchange for bonds
7. Issuer disburses net proceeds used for:
  - a. Capital projects
  - b. Interest
  - c. Bond reserve, cost of issuance, other
8. Annual special taxes / assessment installments levied and collected
9. Bond owners paid (typically semiannually)



## Bond or Debt Issuance Process (Cont.)

### Issuer approves Resolution of Issuance

- Parameters
- Approval of Documents
- Authorized Officers

### Typical final legal documents

- Official Statement (preliminary)
- Continuing Disclosure Agreement(s)
- Bond Purchase Agreement or Notice of Sale
- Bond Indenture or Fiscal Agent Agreement



# Upfront Considerations / Timing

## Bond Sizing / Financial Feasibility

- How much is needed now?
- How many bonds can be supported?
  - Special tax revenue coverage
  - Impact on undeveloped property owners
  - Value-to-lien ratios



## Upfront Considerations / Timing (cont.)

- Status and progress of development
- Placing annual levy on Property Tax Bills
  - Capitalized interest for initial period (“stub period”) or longer
- Status of infrastructure funded by CFD/AD
  - Need for funds to pay for or reimburse for facility costs – 3-year window
- Market Conditions – can the bonds be sold?
  - Credit Quality
  - Investor suitability



# Upfront Considerations / Timing (cont.)

## Credit Quality / Market Issues

- Market's perception of credit quality of CFD/AD
- Developer's financial strength & ability to perform
- Diversification of ownership / amount already developed
- Land use type(s)
- Value-to-lien ratios
- Prevailing overall market conditions and market interest rates
- Demand for land-secured debt
- Overall perception of the real estate market



# Initial Bond Disclosure

## Preliminary Official Statement

- No misstatement of a material fact
- No omission of a material fact
- Material = important to investor when making an informed investment decision



# Disclosing Information to Investors

## Official Statement includes:

- Description of the Bonds
  - Authority for issuance
  - Redemption provisions
  - Debt service schedule
  - Sources and uses, etc.
- Project Information (what is being financed)
- Security for the Bonds
  - Special taxes / assessments
  - Reserve fund
  - Land value estimates
  - ability to issue additional debt
  - Foreclosure provisions, etc.
- The CFD/AD Development Plan and Status
  - Project pro-forma
  - Developer information

(Typically, a Developer Questionnaire is sent from Disclosure Counsel to the Developer to get a complete package of information about the Project)



## Disclosing Info to Investors (cont.)

Official Statement also includes:

- Bondholder Risks
- Special Tax Formula (RMA) /  
Assessment Spread (portions of Engineer's Report)
- Appraisal
- Market Absorption Report
- Summary of key legal documents
- Continuing disclosure agreements



# Securities Law Considerations

- SEC Rule 10b5 “anti-fraud” rule requiring all material information to be disclosed applies to all public municipal bond issues, continuing disclosure statements to the marketplace, and any other circumstance where the bond issuer is “speaking to the market”
- Negligence standard applies (facts known or should have known)
- Disclosures made through the Municipal Securities Rulemaking Board’s Electronic Municipal Market Access (EMMA) website at <https://emma.msrb.org/>



## Securities Law Considerations (cont.)

- Official Statement is the Issuer's offering document to investors
- Policies and Procedures should be in place to ensure proper staff in all departments are empowered to gather all material information and ask the right questions and raise material issues
- Due diligence meeting/call before distribution of the Preliminary Official Statement
- Failure to adequately disclose all material facts has led to fines against bond issuers, charges against individual officials along with the issuer, fines against individuals and barring officials from involvement in municipal finance



# 15-MINUTE BREAK



# Session VI

# Ongoing Administration



# Administration - Basic Steps

## Community Facilities Districts

- Assign taxable parcels to appropriate tax category
- Calculate “Special Tax Requirement”
  - Debt Service
  - Administrative Expenses
  - Pay-as-you-go facilities costs
  - Services costs
- Apply RMA to determine special tax for each parcel
- Submit levy to county auditor’s office before deadline
- With most CFDs, one-time ordinance at formation allows for annual special tax levy without further action of legislative body

# Administration - Basic Steps

## Assessment Districts

- Confirm prepayment of assessment liens
- Perform reapportionments as needed
- Identify Debt Service (principal & interest) for each parcel
- Determine Administrative Cost and allocate to each parcel
- Debt service + Administrative Cost = Annual Payment
- Submit levy to county auditor's office before deadline
- Record release of assessment lien for prepayments
- With ADs, resolution at formation allows for annual assessment levy without further action of legislative body





# Additional Administrative Responsibilities

## Delinquency Management

- Accelerated judicial foreclosure
- Monitor delinquencies, even in Teeter Plan counties
  - Delinquency thresholds
  - Notice to delinquent owners
  - Strip delinquent levies from tax roll
  - Involve foreclosure counsel

## Arbitrage Rebate Calculations

- Positive arbitrage must be rebated every 5 years
- Annual calculation keeps track of what will be due



# Continuing Disclosure

- SEC Rule 15c2-12
- Obligated Persons - Issuer & Developer
- What to disclose
  - Material events
  - Items in Continuing Disclosure Certificate
- Information Repository – MSRB  
(Municipal Securities Rule-making Board)
- Reports must be filed on time

# Annual Disclosure Reports

## S.E.C. Rule 15c2-12 (Continuing Disclosure)

- Obligated persons: Issuer and Developer
- What to disclose: annual report and notice of listed events
- EMMA System of the Municipal Securities Rulemaking Board (MSRB)

## California Debt and Investment Advisory Commission (CDIAC)

- Yearly Fiscal Status Report: October 30 deadline
- Annual Debt Transparency Report: January 31 deadline
- 10-day significant event reporting

## State Controller's Office

- AB 2109 Parcel Tax Reporting in Financial Transactions Report

## Local Agency Special Tax & Bond Accountability Act (SB 165)

- Report filed with Clerk each year
- CFD Administration Report will suffice

## Assembly Bill 1666

- Requires public agencies to post on its website the CDIAC YFSR and the AB 2109 report
- Copy of report with CFD budgetary information if requested by a taxpayer

## Assembly Bill 1483 (new in 2020)

- Requires public agencies to post on its website a current schedule of fees, exactions, and affordability requirements imposed on housing developments
- Special taxes and assessments are exactions
- Information must be updated within 30 days of a change, including annual escalation of special taxes or assessments



## Other Administrative Items

- Reconcile bank statements
- Disbursing and investing bond proceeds (fiscal agent or trustee)
- Prepayment calculations and release of special tax or assessment lien
- Answer questions from homeowners, appraisers, realtors, and bond investors



## Consultants or Staff?

- Staff's experience
- Evaluation of workloads
- Number of districts
- Complexity of districts
- Combined approach

# FUNDAMENTALS OF LAND-SECURED FINANCING



**NOVEMBER 2, 2022 | POMONA, CALIFORNIA**





Complete the seminar evaluation  
and leave it on your table.



Return your name badge at the  
registration table on your way out.

## UPCOMING **CDIAC** EVENTS

### **2023 CDIAC & CMTA Public Funds Investment Essentials: The Workshop**

January 25-26, 2023 | Montebello, CA

### **Municipal Market Disclosure**

March 1-2, 2023 | Folsom, CA