Final Report

The Economics of Land Use

Fiscal Analysis and Implementation Strategy for Duarte Town Center Specific Plan

Prepared for:

The City of Duarte

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SECTION 1: INTRODUCTION AND SUMMARY OF FINDINGS

This Report addresses key fiscal, public financing, and related implementation issues associated with the Duarte Town Center Specific Plan. It has been prepared by Economic & Planning Systems, Inc. (EPS) on behalf of the City of Duarte as part of the Specific Plan effort. The proposed Duarte Town Center is a Mixed-Use Activity Center intended to serve as Duarte's Civic and cultural hub and be an active, dynamic, social gathering place for the entire city.

This report is designed to address two inter-related issues: (1) determine how build-out of the Specific Plan is likely to impact the General Fund of the City of Duarte; and (2) identify potential financing and implementation tools to fund the necessary infrastructure and public facilities needed to achieve the Specific Plan vision.

The report builds on a number of prior documents, including the *Town Center Specific Plan Existing Conditions Report,* prepared by MIG in July 2015, the *Market Assessment Study: Duarte Town Center Specific Plan,* prepared by EPS, November 23, 2015, and a number of draft land use program documents, prepared by MIG in March 2016.

The report is organized into three sections, consisting of Summary Findings, Fiscal Impact Analysis, and Infrastructure Financing and Implementation Strategy.

Key Findings

Key findings are described below and shown on **Exhibit 1**. All results are in constant 2015 dollars.

1. ***The Duarte Town Center program proposes approximately 217,000 square feet of net new commercial area, 1,036 net new residential units, and 331 net new hotel rooms.*** Net new area is calculated by subtracting the area of total existing uses, which include 107 residential units, 119 hotel rooms, and 516,000 commercial square feet, from the area of the proposed new land use mix of 1,143 units, 450 hotel rooms, and 733,000 commercial square feet. When fully stabilized, the new development will provide capacity for 792 new jobs and 3,051 new residents. Overall, this substantial increase in the level of economic activity will present a variety of fiscal benefits to the City and opportunities for financing critical infrastructure and public facilities over time.

2. ***The Project will generate a fiscal surplus over and above the revenues required to cover the costs to the City of providing public services.*** The fiscal impact of the Project on the City's General Fund at Project buildout will be positive, with the revenues generated by the Project estimated to be greater than the costs of providing additional public services. By buildout, the Project is expected to generate annual revenues of approximately $2.6 million. General Fund costs will sum to approximately $1.3 million annually. The resulting net impact on the General Fund will be an annual positive surplus of approximately $1.3 million, equivalent to 9 percent of the Fiscal Year 2014-2015 City Budget. This analysis demonstrates that the Project should be able to cover its service costs and provide surplus revenues to support infrastructure development and to increase levels of service in other parts of the City.

3. ***Duarte real estate market weakness limits short-term financing capacity, which means an opportunistic approach to financing infrastructure development is recommended.*** Steps may include finalizing the Specific Plan to ensure development readiness; evaluating financing opportunities when new development increases financing capacity; and expanding the plan area geography to increase financing capacity. Pooling the Town Center, Duarte Station, and City of Hope Plan areas would allow for greater scale economies, access to TOD-oriented financing resources, and possibly also help establish tax-increment-secured tool such as an EIFD or a CRIA.

Exhibit 1 Summary of Net Fiscal Benefits

Category	Outputs
<u>**City General Fund Revenues**</u>	
Property Taxes	$525,042
Sales and Use Tax	$395,497
Franchise Taxes	$117,012
Business License Tax	$23,422
Transient Occupancy Tax	$1,515,020
Real Property Transfer Tax	$8,897
Total Annual General Fund Revenues (rounded)	**$2,585,000**
<u>**City General Fund Expenses**</u>	
City Council	$715
City Council/City Clerk	$5,560
Legal Services	$4,146
Public Safety	$513,603
Community Development	$220,876
Field Services	$86,313
Parks and Recreation	$225,802
Facilities Maintenance	$83,628
Administrative Services	$149,000
Total Annual General Fund Expenditures (rounded)	**$1,290,000**
Net Fiscal Impact	**$1,295,000**
% of FY 2014-15 General Fund Budget	*9%*

Sources: City of Duarte 2014-15 Operating Budget; Economic & Planning Systems, Inc.

SECTION 2: FISCAL IMPACT ANALYSIS

This section evaluates the fiscal impact of the proposed Duarte Town Center Specific Plan on the City's General Fund costs and revenues. The analysis is focused on the net new development at full build-out (the net new commercial square feet, hotel rooms, and residential units) based on typical factors and activities of residents, on-site employees, and visitors. The analysis compares the potential additional costs incurred by the City from providing public services to the Project with the additional tax revenues generated by the Project and indicates whether the Project can be expected to have a positive or negative overall effect on the City's General Fund at buildout.

It should be noted that fiscal results (annual surpluses or deficits) are simply indicators of fiscal performance; they do not mean that the City will automatically have surplus revenues or deficits, because the City must have a balanced budget each year. Persistent shortfalls shown in a fiscal analysis may indicate the need to reduce service levels or obtain additional revenues; persistent surpluses will provide the City with resources to reduce liabilities such as deferred maintenance or improve service levels.

Land Use Program

The proposed Town Center land use program is shown in plain view in **Exhibit 2.** The program at full buildout would substantially change the existing mix of uses, which includes approximately 516,000 square feet of commercial area, 107 residential units, and 119 hotel rooms. At full buildout, the proposed land use program would increase commercial square footage to 733,000 square feet, residential to 1,173 units, and hotel rooms to 450.

In order to measure only new fiscal impacts to the general fund, the analysis considers only net new amounts of these uses. As shown on **Exhibit 3**, net new growth after subtracting new development from existing uses totals 217,000 commercial square feet, 1,036 residential units, and 331 hotel rooms.

Exhibit 2 Proposed Land Use Program

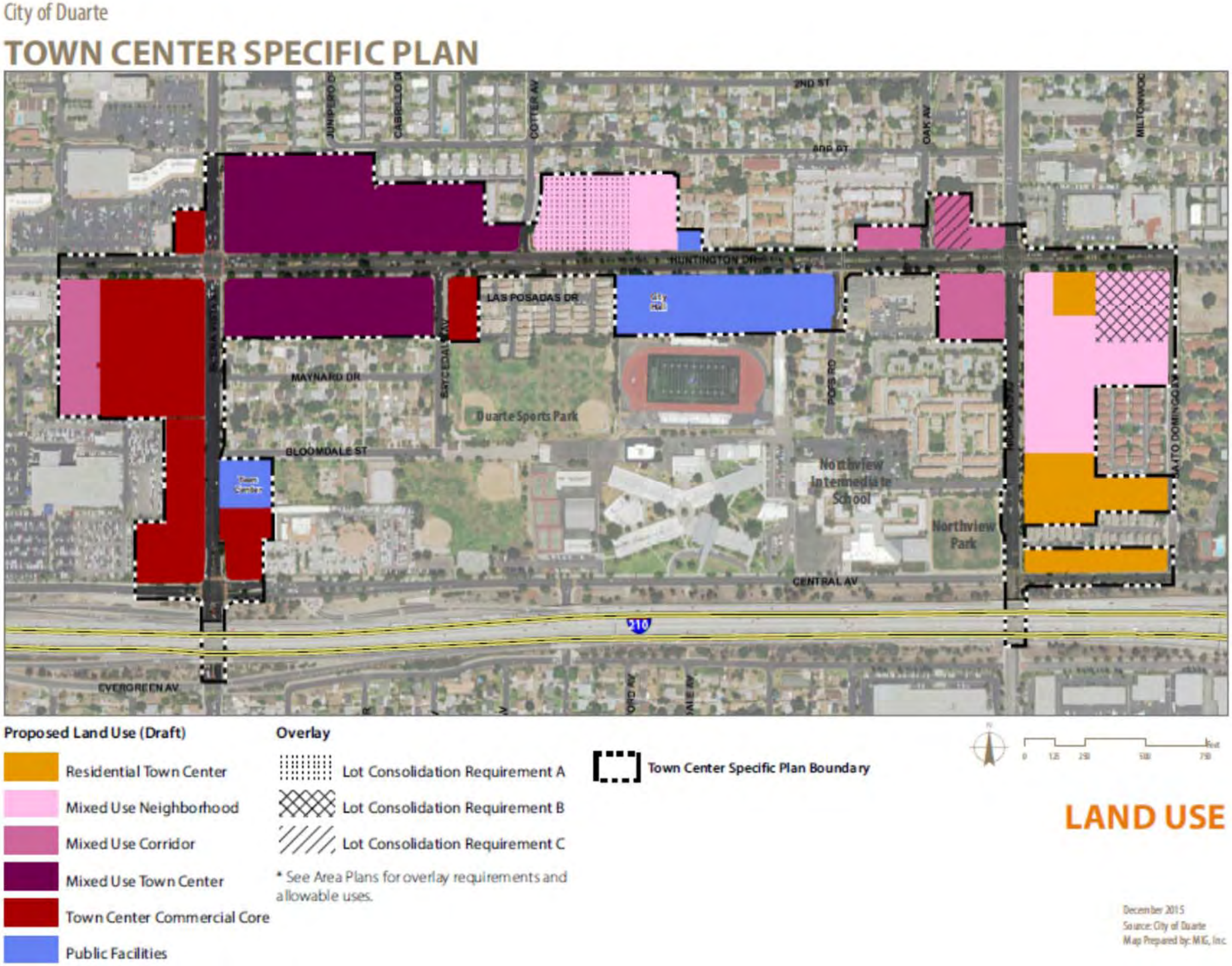

Exhibit 3 Existing, Proposed, and Net New Uses

	Residential Units	Hotel	Commercial Sq.Ft.
Existing Uses			
Commercial Retail	0	0	291,536
Office	0	0	91,043
Single-Family	46	0	0
Multi-Family	61	0	0
Hotel/Motel	0	119	0
Government	0	0	82,954
Institutional: Church	0	0	11,630
Insitutional: Nursing Homes	0	0	38,527
	107	**119**	**515,691**
Proposed Uses			
Commercial Retail	0	0	391,970
Office	0	0	222,271
Single-Family	46	0	0
Multi-Family	1,097	0	0
Hotel/Motel	0	450	0
Government	0	0	118,472
Institutional: Church	0	0	0
Insitutional: Nursing Homes	0	0	0
	1,143	**450**	**732,712**
Net New Development			
Commercial Retail	0	0	100,433
Office	0	0	131,227
Single-Family	0	0	0
Multi-Family	1,036	0	0
Hotel/Motel	0	331	0
Government	0	0	35,518
Institutional: Church	0	0	(11,630)
Insitutional: Nursing Homes	0	0	(38,527)
	1,036	**331**	**217,021**

Source: MIG, Economic & Planning Systems, Inc.

Key Assumptions

The impacts of the proposed land use plan are estimated assuming full buildout and stabilized occupancy of all uses. The assumptions that underlie the analysis come from a variety of sources including: prototype development pro formas from EPS; the City of Duarte 2014/2015 Adopted Operating Budget; U.S. Census Bureau (2013, 5-year estimates); CoStar; the Bureau of Labor Statistics; and other public real estate data. All results are expressed in constant 2015 dollars.

The analysis only considers net new development, which is computed by subtracting proposed total development from total existing development. This approach is conservative and likely underestimates the General Fund revenue impact. When an existing use is replaced by new construction on a one-to-one basis, fiscal benefits generally increase, because new construction typically has a higher land value and generates greater sales and/or hotel revenue per square foot. But because the analysis only considers net new development, existing development that has been replaced by fiscally positive new development is not counted towards total impact.

Land use assumptions are based on the land-use plan discussed above in **Exhibit 2**. Assessed values for each program element are based on estimated total development costs (including land) of the prototypical uses, which are shown in **Exhibit 4.** For designated "commercial square feet," EPS allocated a portion to office and a portion to retail in accordance with existing and/or proposed nodes, with restaurant uses contributing 25 percent of total retail square feet. For multifamily, EPS assumed all for-rent uses consisting of a higher-density stacked-flat with structured parking product (90 percent of the total units), and attached townhomes (10 percent). A summary of program values is shown on **Exhibit 5** with resulting economic direct impacts shown on **Exhibit 6.**

Exhibit 4 Assumed New Development Prototypes

Use	Description
Multi-family for rent	1,750 square-foot attached townhome
Multi-family for rent	1,100 square-foot wrap with structured parking
Ground-Floor Retail	Ground-floor mixed use, surface parked
Restaurant Pad	Stand-alone pad
Office	1.0 FAR Podium, 75% surface-parked
Hotel	150-175 room limited-service hotel

Source: Economic & Planning Systems

Exhibit 5 Program Elements and Assessed Value Assumptions

Proposed Net New Uses	Net New Development		Value/Unit or /Sq.Ft. (1)	Estimated Value
Hotel	331	rooms	$210,000	$69,510,000
Office	131,227	sq.ft.	$425	$55,771,513
Retail	100,433	sq.ft.	$370	$37,160,284
Multi-Family Residential	1,036	units	$350,000	$362,600,000
Total				**$525,041,797**

(1) Values based on typical costs with land for prototypical uses, derived from conceptual proformas developed by EPS. Retail assumes a 10/15/75 mix of ground floor restaurant, standalone pad restaurant, and ground-floor retail sq.ft.; multi-family includes a 90/10 mix of for-rent texas-wrap-style and attached townhome typologies.

Source: Economic & Planning Systems, Inc.

Exhibit 6 Summary of Net New Direct Economic Impacts

Category	Outputs
Net New Full-Time Employees	792
Net New Taxable Sales	$39,549,704

Source: Economic & Planning Systems, Inc.

The analysis uses standard estimating procedures to estimate new General Fund revenues, which are summarized in **Exhibit 7** and discussed further in a separate section below. General Fund expenditures are estimated using a variable-cost-per-capita approach, which assumes that for each budget item, a portion of costs is fixed regardless of service demand, and a portion is variable with service demand. For example, because public safety expenses consist mainly of salaries and overtime hours, most costs in this item are assumed to be variable, as shown in **Exhibit 8**. City Council costs by comparison vary little with regard to changes in residential or service population and most City Council budgeted costs are thus assumed to be fixed.[1]

Existing and new daytime service population are key inputs for General Fund revenue and expense projections. The service population is not equivalent to the residential population, as the

[1] Fixed and variable assumptions are EPS estimates based on general rules-of-thumb regarding typical city fixed and variable operating costs

service population must also account for service demand by in-commuting workers and hotel visitors while also deducting demand from out-commuting residents. The service population estimate combined with a General Fund budget estimate provides the basis for calculating the per-capita cost of providing municipal services. See **Exhibit 9** for derivation of the existing service population.

Growth in the residential and service population resulting from net new development will generate both new General Fund revenue and General Fund costs from additional service demand. **See Exhibit 10** for derivation of net-new residential and service population growth.

Exhibit 7 General Fund Revenues and Estimating Factors

General Fund Revenue Item	Basis		Estimating Factor		Net New Tax
General Property Tax	$525,041,797	new assessed value	1.00%	* 10% (General Fund allocation)	$525,042
Sales and Use Tax	$39,549,704	new taxable sales	1.00%		$395,497
Franchise Taxes	3,570	new daytime service pop.	$33	per new daytime service pop.[1]	$117,012
Business License Tax	792	new FTE (equivalent)[2]	$30	per new employee[3]	$23,422
Transient Occupancy Tax	$15,150,201	new room revenue	10%	of room revenue[4]	$1,515,020
Real Property Transfer Tax	$65,000	base value	13.69%	increase over base value[5]	$8,897
Total New General Fund Revenue					**$2,584,890**

(1) Factor derived by dividing 2014-15 budgeted amount by estimated 2014 Duarte Service Population
(2) FTE = Full-time employee
(3) Factor derived by dividing 2014-15 budgeted amount by 2014 Duarte city-wide employment
(4) City Transient Occupancy Tax rate
(5) Derived by increasing budgeted revenues in proportion to the increase of City total assessed value due to new Specific Plan build-out
Sources: City of Duarte; Economic & Planning Systems, Inc.

Exhibit 8 General Fund Expenditures and Estimating Factors

General Fund Expenditure Item	FY 2014-15 Budget[1]	% of Costs Variable[2]	Population Factor[3]	Budgeted Cost Per Population Basis[4]	Estimating Factor	Net New Fiscal Cost
	a	*b*	*c*	*(a * b) / c = d*	*e*	*d * e*
City Council	$106,900	5%	26,696 service pop.	$0.20	3,570 new service pop.	$715
City Council/City Clerk	$831,500	5%	26,696 service pop.	$1.56	3,570 new service pop.	$5,560
Legal Services	$155,000	20%	26,696 service pop.	$1.16	3,570 new service pop.	$4,146
Com. Promotions & Memberships	$191,000	0%	26,696 service pop.	$0.00	3,570 new service pop.	$0
Public Safety[5]	$4,267,400	90%	26,696 service pop.	$143.87	3,570 new service pop.	$513,603
Community Development[6]	$2,064,600	80%	26,696 service pop.	$61.87	3,570 new service pop.	$220,876
Field Services	$806,800	80%	26,696 service pop.	$24.18	3,570 new service pop.	$86,313
Parks and Recreation	$1,767,900	90%	21,499 res pop.	$74.01	3,051 new res. pop.	$225,802
Facilities Maintenance	$781,700	80%	26,696 service pop.	$23.43	3,570 new service pop.	$83,628
Administrative Services[7]	$2,228,400	50%	26,696 service pop.	$41.74	3,570 new service pop.	$149,000
Transfers Out	$447,600	0%	26,696 service pop.	$0.00	3,570 new service pop.	$0
Total General Fund Expenditures	**$13,648,800**					**$1,289,642**

(1) City of Duarte 2014-15 Budget (Estimated Actual Results)
(2) Source: EPS, based on general rules of thumb regarding typical city fixed and variable operating costs
(3) Service and residential population factors shown on separate exhibit. Derivation of Resident-to-Employee Equivalences from Estimated Service Population
(4) Per-cap cost multipliers calculated by dividing budgeted items by the service population factor of 26,696 or residential population factor of 21,499.
(5) Police only. Fire safety services provided by the County and billed directly to land owners.
(6) Includes Planning, Engineering/Public Works, Building and Safety
(7) Includes finance, human resources, IT, transit, risk management, and contract administration
Sources: City of Duarte 2014-15 Operating Budget; Economic & Planning Systems, Inc.

Exhibit 9 Existing Service Population (Citywide)

Service Population Category	Labor Force & Commute Patterns[1] Number	Distribution	Resident to Employee Equivalencies Weighting[2]	Weighted Average	Normalized to 100%	Estimated Service Pop.
		a	*b*	*= a * b*		
Duarte Residents						
Not in Labor Force/Unemployed	11,868	55%	100%	55%		
Employed in Duarte	804	4%	100%	4%		
Employed Outside Duarte	8,827	41%	66%	27%		
Total Residents	21,499	100%		86%	100%	**21,499**
Employees in Duarte						
Live in Duarte	804	7%	100%	7%		
Live Outside Duarte	10,693	93%	34%	32%		
Total Jobs	11,497	100%		39%	45%	**5,197**
Estimated Service Population						**26,696**

(1) U.S. Census Bureau (2013 5-year estimates) and census LEHD On The Map Application (2014)

(2) Workday weighting based on percent of annual number of 'waking' hours (5,840 = 16 hours * 365 days) relative to time at job (2,000 = 40 hours * 50 weeks)

Sources: U.S. Census; Economic & Planning Systems.

Exhibit 10 New Residential and Service Population (Town Center Plan Area)

			New Employees			**Residents**					
Net New Land Uses	**New Development**		By Use[1]		# new	Persons/ HH[2]	Occupied HHs[3]	Residents	**Hotel Guests[4]**	**Service Population[5]**
Hotel	331	rooms	7	rooms/emp.	47	0	0	0	161	182
Office	131,227	sq.ft.	300	Sq.Ft./emp.	437	0	0	0		198
Retail	100,433	sq.ft.	350	Sq.Ft./emp.	287	0	0	0		130
Multi-Family Residential	1,036	units	50	units/emp.	21	3.10	984	3,051		3060
Total					**792**		**984**	**3,051**		**3,570**

(1) Employee multipliers are rules-of-thumb based on common practice and prior EPS experience
(2) United States Census Bureau, 2013 (5 Year Estimates), ESRI Busines Analyst Online, for Duarte
(3) Assumes 5% vacancy
(4) Hotel guests reflect partial service demand compared to full-time residents and are estimated as 58% of daily hours x 76% assumed occupancy x 331 rooms x 1.1 guests/room.
(5) New employees x 45% weighting factor, new residents x 100% weighting factor. (See Exhibit 9 for derivation of weighting factors.)
Source: Economic & Planning Systems, Inc.

General Fund Revenues

This section provides further discussion of how, on a budget item-by-item basis, the proposed land use program will generate new General Fund revenue.

Transient Occupancy Tax (TOT)

The proposed program includes 331 net new hotel rooms, which are expected to capture visitors who currently uses facilities outside of the City. The net increase in Transient Occupancy Tax (TOT) revenue of $1.52 million is based on an estimated $15.2 million in new room revenues. The TOT rate is currently 10 percent, all of which goes to the General Fund. This calculation is shown on **Exhibit 12**.

Exhibit 11 Transient Occupancy Tax Calculation

Item	Calculation
Net New Hotel Rooms	331
Average Daily Rate[1]	$165
Occupancy	76%
Revenue	$15,150,201
Transient Occupancy Tax (TOT) Rate	10%
Net New TOT	**$1,515,020**

(1) Estimated 2015 LA County Average (PKF Consulting)
Sources: City of Duarte; PKF; Economic & Planning Systems, Inc.

Property Tax

Property taxes are based on the assessed value of land and on-site improvements, as well as the value of unsecured property, which refers to business property such as office furniture, machinery, equipment, etc. Though the actual assessed value of the program will be determined by market conditions and other factors at the time of assessment, the analysis uses estimated development costs as a proxy for estimating the assessed value of the new development, which is consistent with the approach used by the County Assessor's Office. EPS based all cost estimates on typical development costs for prototypical versions of the assumed uses. According to these assumptions, the Project's assessed value will be about $525 million at buildout (see **Exhibit 12**). Los Angeles County currently collects property tax based on 1.0 percent of the assessed value, and the City of Duarte receives approximately 10 percent of the 1.0 percent property tax base from the area. This share is assumed fixed going forward.

Exhibit 12 Property Tax Calculation

Category	Assumption	Calculation
Net new Assessed Value (AV)		$525,041,797
Property Tax Total	1.0% of AV	$5,250,418
Share of Property Tax to General Fund[1]		10%
Net New Property Tax to General Fund		**$525,042**

(1) Rate provided by the City of Duarte and represents a general estimate based on historical performance
Sources: City of Duarte; Economic & Planning Systems, Inc.

Sales Tax

The Project is expected to generate sales tax through spending at the new retail, service, and restaurant destinations, at the hotel, and as a result of spending of new residents and employees at nearby retail establishments in the City of Duarte. As shown in **Exhibit 13**, the project program overall may generate an estimated $39.5 million in new retail sales, of which the City receives $395,000 annually.

While Duarte may currently be over-retailed, there is greater long-term potential through broader "place-making efforts", expansion of the residential customer base within the walkable area, and growth in the regional economy will lead to a more robust retail mix in the Plan Area. Consequently, the retail taxable spending estimate, as shown in **Exhibit 13**, assumes that fully 75 percent of the spending at new retail outlets will be net-new to the City of Duarte.

The hotel food and beverage spending estimate, also shown in **Exhibit 13**, is based on a rule-of-thumb that such spending is generally equivalent to 25 percent of room revenue. Employee retail sales expenditures are based on ICSC data adjusted by EPS for typical worker taxable spending. And finally, household taxable spending is based on the average Duarte HH income at 29 percent taxable and 50 percent of that captured in the City of Duarte.

Exhibit 13 Sales Tax Calculation

Category	Assumptions		Taxable Spending
Retail	100,433	Sq.Ft.	
	$350	/Sq.Ft.[1]	
	75%	Net new spending in Duarte[2]	$26,363,715
Hotel Food & Beverage	$15,150,201	Estimated room revenue	
	25%	of room revenue[3]	$3,787,550
Employee Expenditures	792	New employees	
	$2,600	Annual taxable spending/employee[4]	
	25%	Duarte capture[5]	$514,804
Household Expenditures	984 [6]	Net new residential units	
	$62,250	Median Duarte HH Income[7]	
	29%	Taxable Spending/HH[8]	
	50%	Duarte capture[5]	$8,883,635
New Taxable Sales			**$39,549,704**

(1) Assumes a retail mix of restaurants, retail, and commercial services.
(2) Portion of spending that does not cannibalize existing Duarte spending
(3) EPS assumption, based on experience with prototypical hotel operating models
(4) Based on data on office worker taxable spending as reported by ICSC, with inflation adjustments and adjustments for retail workers made by EPS.
(5) EPS estimate of spending captured in the City of Duarte
(6) Includes assumed 5% vacancy
(7) U.S. Census Bureau (2013 5-year estimates)
(8) Based on the Bureau of Labor Statistics Consumer Expenditure Survey
Sources: City of Duarte, U.S. Bureau of Labor Statistics; Economic & Planning Systems, Inc.

Franchise Taxes

The Town collects Franchise Taxes for, among many items, cable television and electric utility provision. The net increase in Franchise Fees associated with the Project is estimated at $115,000 based on a cost factor of $33 per daytime service population. This calculation is shown on **Exhibit 7**.

Business License Tax

The increase in commercial area in the proposed program is expected to increase business license tax revenue to the City. These proceeds are estimated at a rate based on existing workers and the City's budget. At $30 per estimated new employee, new business license proceeds are expected to be approximately $23,000. This calculation is shown on **Exhibit 7**.

Real Property Transfer Tax

The expansion in the number of commercial properties in the City should expand the number of property transactions, and with them, real property transfer tax proceeds. These are calculated in proportion to the City's increase in total assessed value, which computes to an increase of approximately 15 percent based on the City's 2015-16 assessed value. This calculation, which generates $8,900 in net new proceeds for the City, is shown on **Exhibit 14**.

Exhibit 14 Real Property Transfer Tax Calculation

Item	Calculation
Base Value for Real Property Transfer Tax (FY 2014-15)	$65,000
Citywide Assessed Value (2015-16 Base Value)	$3,835,977,581
Project Assessed Value	$525,041,797
Net Increase in Assessed Value	13.7%
Net Increase in Real Property Transfer Tax	**$8,897**

(1) City of Duarte 2014-15 Budget (Estimated Actual Results)
Sources: City of Duarte; Economic & Planning Systems, Inc.

General Fund Expenditures

This section describes the methodology and key assumptions used for calculating various General Fund expenditure items. Certain expenditures, such as City Council and Facilities Maintenance, are assumed to consist of fixed costs that will not change with regard to the proposed new development, while others, such as Public Safety, are assumed to consist entirely of variable costs that increase in direct proportion with service demand. A summary of the approach is shown in **Exhibit 8.**

Police Services

Duarte's police department provides police protection and traffic enforcement to residents and employees in the City. The Project will generate new employees and residents in the City who will require additional law enforcement officers and/or staff time and associated equipment and training. To estimate the impact of the new development on service demand, a cost of $144 per new service population equivalent (a factor combining both new residents and new employees), based on the existing City budget, is computed, resulting in a net cost increase of $514,000. See **Exhibit 8** for the calculation.

Community Development

The Community Development Department includes all planning, engineering, public works, and buildings/safety services. The cost associated with Community Services is assumed to be $62 per service population equivalent, resulting in net new fiscal costs of $221,000 per year. See **Exhibit 8** for the calculation.

Parks & Recreation

This category includes costs associated with maintaining parks and recreational facilities. No new public parks or streets are proposed as part of the Project, but the significant increase in the residential population will incur an increase of costs associated with normal wear and tear on the City's facilities. The cost associated with Parks and Recreation services is assumed to be $74 per new resident, based on the existing City budget, for an increase of $226,000 per year in fiscal costs. See **Exhibit 8** for the calculation.

Administrative Services

This category includes costs associated with finance, human resources, IT, transit, risk, management, and contract administration. To be conservative, the analysis assumes that Administrative Services costs are fully variable with regard to service population. The cost associated with Administrative Services is assumed to be $42 per service population equivalent, resulting in net new fiscal costs of $149,000 per year. See **Exhibit 8** for the calculation.

Legal Services and Field Services

Legal and Field Services are assumed to be variable with the service population. Estimated at $1.16 and $24 respectively per service population equivalent, Legal and Field Services add $90,000 in new annual fiscal costs. See **Exhibit 8** for the calculation.

Fire Services

Fire services are provided to the Town of Duarte by the Los Angeles County Fire Department. The County receives a portion of the 1 percent basic property tax revenue to provide fire prevention and protection as well as emergency medical services. Therefore, the City would not incur increased General Fund expenses as a result of the Proposed Project and associated increased service population, and fire prevention and emergency medical services are not further addressed in this report.

Net Fiscal Impact on General Fund

Based on the assumptions and analysis described above, the annual net fiscal impact associated with the proposed development is estimated at approximately $1.3 million at Project buildout, as shown in **Exhibit 15**. The Project is estimated to generate about $2.6 million in General Fund revenues compared to $1.3 million in General Fund costs. Actual fiscal impacts will vary due to the actual timing of Project buildout and changes in economic and budgetary conditions.

Exhibit 15 Net Fiscal Impact

Category	Outputs
City General Fund Revenues	
Property Taxes	$525,042
Sales and Use Tax	$395,497
Franchise Taxes	$117,012
Business License Tax	$23,422
Transient Occupancy Tax	$1,515,020
Real Property Transfer Tax	$8,897
Total Annual General Fund Revenues (rounded)	**$2,585,000**
City General Fund Expenses	
City Council	$715
City Council/City Clerk	$5,560
Legal Services	$4,146
Public Safety	$513,603
Community Development	$220,876
Field Services	$86,313
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Facilities Maintenance	$83,628
Administrative Services	$149,000
Total Annual General Fund Expenditures (rounded)	**$1,290,000**
Net Fiscal Impact	**$1,295,000**
% of FY 2014-15 General Fund Budget	*9%*

Sources: City of Duarte 2014-15 Operating Budget; Economic & Planning Systems, Inc.

SECTION 3: INFRASTRUCTURE FINANCING AND IMPLEMENTATION

This section provides a general description of financing and implementation options and strategies to advance the goals of the Duarte Town Center Specific Plan. At this point, the specific strategies and funding sources are identified for discussion purposes to guide subsequent analytical efforts. The ultimate mix of financing mechanisms will be determined in the implementation process, based on final technical analyses of costs, benefits, and burdens, and on deliberations involving City staff, property owners, developers, elected officials, bond counsel, underwriters, finance experts, and others.

Regardless of the strategy selected, Duarte should consider implementing an incentive and infrastructure financing program that achieves the following:

- Realizes goals of Specific Plan
- Articulates trade-offs acceptable to the community
- Can be implemented without over-burdening City Staff and other resources
- Responds to the realities of Duarte’s current market position
- Is flexible enough to respond to changing market conditions

Plan Area infrastructure requirements are likely to include streetscape improvements such as the installation of bulb-outs to calm traffic and facilitate walking and biking; enhancements such as street trees and benches; and lighting improvements at key intersections such as at Brycedale, Cotter, and/or under the Highland underpass. Additional infrastructure improvements, which may be required based on increased demand resulting from new development, may include capacity expansion of utilities such as water, power, sewer, and storm drains.

Infrastructure Financing Capacity

Both the Plan Area and the City of Duarte present a number of strengths and weaknesses with respect to infrastructure financing capacity. A careful assessment of these characteristics is an important first step in the formulation of an effective infrastructure phasing and financing strategy. The EPS market study provides additional detail with regard to specific development feasibility consideration and value creation opportunities over time.

Critical strengths and weaknesses of the Project Area with respect to financing necessary infrastructure are further summarized below.

Strengths:

- **Long-Term Market:** Duarte’s accessible location within the strong San Gabriel Valley economy and recent completion of the Gold Line extension to Azusa through Duarte are strong assets for promoting future development and revitalization, which should help the City overcome current near-term market softness.

- **Fiscal Benefits:** As noted in the fiscal impact analysis above, the Plan Area at full buildout would generate an annual fiscal surplus (in 2015 dollars) of $1.3 million, which reflects a 9 percent increase in the General Fund budget that can be used to help pay for new infrastructure.
- **Entitlement:** The completion of the Town Center Specific Plan will provide supportive land use regulations for infill development and densification of the Plan Area.
- **Community Support:** The Duarte community is generally supportive of new infrastructure investment and development that would support a Town Center. The City has a business-friendly reputation.
- **Infrastructure Requirements:** As of this writing, the Plan Area does not feature any major infrastructural deficiencies or impediments that would require an extraordinary amount of infrastructure investment.

Weaknesses:

- **Short-Term Market:** As noted in the Market Assessment Study prepared by EPS in 2015, the Duarte real estate market for retail, residential, and office development is relatively soft compared with competing cities in the immediate vicinity. In the short-to-medium term, the City is most likely to attract development as a lower-cost alternative to these competing cities.
- **Size:** At approximately 55 total net acres (or 76 gross acres), the Plan Area is relatively small, which means value potential and relative creditworthiness of the area may not provide adequate or efficient scale for some public financing techniques.
- **Short-Term Fiscal Resources**: While build-out of the Town Center Specific Plan program is expected to generate substantial General Fund revenue, this resource will be realized on a gradual, incremental basis. Meanwhile, like many California cities, Duarte's current General Fund capacity is limited and focused on meeting basic City services. Moreover, as a small middle-income city with a low property tax apportionment factor of 10 percent, Duarte generates a relatively low amount of property tax with limited capacity for establishing a property-tax secured financing tool like an EIFD or CRIA.
- **Property Ownership Patterns**: The Specific Plan Area is characterized by multiple property owners with diverse objectives, time horizons, and financial circumstances. Under these circumstances, organizing and approving unified and strategic financing programs can be challenging.

Infrastructure Financing Options

There are a range of funding sources and financing options available for infrastructure development in California. While various innovative tools and techniques may be available, four primary sources will nearly always form the backbone of any financing program, as follows:

1. Development-Based Funding
2. Land-Secured Funding and Financing
3. City Funding and Financing
4. State and Federal Programs

The applicability of each of these financing categories to the Town Center Specific Plan area is further discussed below. **Exhibit 16** provides an overview of these funding categories, including a brief summary of the funding characteristics:

- **Cash or Debt:** Is the tool a new source of funding, a financing mechanism, or both?
- **Revenue Stream:** Where does the funding come from?
- **Required Approval:** Does the tool require voter approval, a new City ordinance, or other approach to implementation?
- **Role and Scale:** Is the tool the principal source of funding for an infrastructure program or one of many sources of funds required? Would the tool be appropriate for a citywide program, area program, or project-specific infrastructure?

Appendix A provides a fuller description of the funding sources and financing mechanisms that fall under these general categories.

Exhibit 16 Summary of Infrastructure Funding and Financing Tools

Funding / Financing Type	Cash / Debt	Revenue Stream	Required Approval	Infill Financing Role and Scale
Development-Based Funding				
Project Exactions	Cash	One-time investments by new development	Conditions of map approval; no voter approval	Primary Source; Project Scale
Area Development Impact Fees	Cash	Obligatory one-time fees on new development	Local ordinance; no voter approval	Primary Source; District Scale
City Development Impact Fees	Cash	Obligatory one-time fees on new development	Local ordinance; no voter approval	Supporting Source; City Scale
Private Financing, Development Agreements, and Partnerships	Cash and other contributions	Voluntary contributions by new development	No voter approval	Primary Source; Project Scale
Land-Secured Funding and Financing				
Community Facilities Districts	Cash or debt	Special taxes on real property	2/3 voter approval; Landowner vote if <12 voters	Primary or Supporting Source; District Scale
Special Benefit Assessment Districts	Cash or debt	Real property assessments	Majority landowner approval, protest proceeding	Supporting Source; District Scale
City Funding and Financing				
General Obligation Bonds	Debt	Ad valorem property tax	2/3 voter approval	Primary Source; City Scale
Revenue Bonds	Debt	Enterprise (utilities) revenue	No voter approval	Primary Source; City or District

Exhibit 16 Summary of Infrastructure Funding and Financing Tools (continued from previous page)

City Funding and Financing (Continued from previous page)				
Parcel Taxes	Cash or debt	Flat rate property tax	Majority or 2/3 voter approval (general or special purpose)	Primary or Supporting Source; City or District Scale
Sales Tax and Other Local Taxes	Cash or debt	Local-option taxes	Majority or 2/3 voter approval (general or special purpose)	Primary Source City Scale
Capitalizing Leases	Debt	General Fund obligation	2/3 voter approval	Primary Source; Project Scale
Infrastructure Financing Districts	Cash or debt	Property tax increment	2/3 voter approval	Supporting Source; City or District Scale
Enhanced Infrastructure Financing Districts	Cash or debt	Property tax increment	55% voter approval for debt	Supporting Source; City or District Scale
Community Revitalization and Investment Authority	Cash or debt	Property tax increment	No vote required; Subject to protest	Supporting Source; City or District Scale
State and Federal Programs				
Grant Programs	Cash	State and federal government funds	No voter approval	Supporting Source; City or District Scale
State Infrastructure Bank	Debt	General Fund obligation	Depends on funding source	Supporting Source; District Scale
Statewide Community Infrastructure Program	Debt	Local assessment district or CFD special tax	No voter approval	Supporting Source; District or Project Scale

Development-Based Funding

California jurisdictions have relatively broad authority to impose obligations on new development to help cover the cost of infrastructure and related community benefits. California cities have a long history of obtaining community benefits from real estate development through a variety of mechanisms, including fees, conditions of approval, and development agreements. Development impact fees, usually imposed under the Mitigation Fee Act, are probably the most common form because the can be applied to "by-right" development projects, assuming appropriate "nexus" requirements are met.

However, when the public sector creates value through up-zoning and infrastructure development, landowners enjoy a financial gain in the form of higher land value, which is realized when they sell or develop their land. This increase in land value is an unearned financial benefit that accrues to the private sector, though it is generated (and commonly paid for) by tax-payer funded public entities. At the same time, this benefit may provide an economic incentive in a sluggish market to transition land to a higher use or a use more consistent with a city's goals. Community Benefit Incentive Zoning is a particular variety of development-based funding with potential application to the Town Center Specific Plan, as described further below.

Community Benefit Incentive Zoning

Community Benefit Incentive Zoning (CBIZ) programs are structured around an exchange in which municipalities offer optional increases in development potential in return for public assets (or funds) desired by the community. The development incentive must be above what normally would be allowed and the public benefit must be beyond what otherwise would be required. Because these programs are optional, development outcomes vary based on the degree of participation in the plan. That is, some developments may not take advantage of the incentive while others will. The optional nature of the program creates increased uncertainty regarding the final urban form that ultimately will be achieved.

Additionally, the magnitude of the community benefit sought/expected must be equal to or less than the value of the incentive offered. In order to receive community benefits, the public sector creates value through the provision of an incentive (commonly increased development density). CBIZ programs are founded on the concept of "value capture." CBIZ programs must be carefully tailored to be attractive to project proponents and simultaneously achieve quality of life goals of the community. Program design and development should evaluate the range of potential development outcomes, including the built form and magnitude of expected community benefits, to ensure that the exchange of development rights for community benefits is desirable.

<u>The Concept of Value Capture</u>

Cities and government agencies create real estate value with investments in public facilities and services (e.g., transit and utilities upgrades) as well as through changes to zoning code that increase the value of land. As noted above, this creates an unearned financial benefit that accrues to landowners. The term "value capture" reflects the situation in which the public sector reclaims some of this unearned value created for the private sector by public sector activities.

If the public sector seeks/expects to collect more value than is created, in the form of community benefits, it is unlikely that project proponents will use the program. Since the value of development incentives varies with market conditions, development incentives may be very valuable in a strong market but of lesser or no value in a weak market. Therefore, CBIZ programs respond to market conditions or anticipate that the program will not be used during periods of market weakness.

CBIZ requires a healthy real estate market with sufficient market value to support the incentives. For example, in order for a CBIZ program that seeks to capture value from an incentive (such as increased density or greater development potential) to be successful, there must be market demand to support the higher-density, higher-cost real estate products that are made available through the zoning change.

<u>CBIZ Program Basics</u>

There are two primary types of CBIZ programs: “negotiation-based” and “plan-based” programs. Negotiated community benefits may occur in the context of a Development Agreement or other negotiation process. Plan-based programs are “formulaic” (the term used here) and typically are implemented in a “ministerial” fashion, without discretion.

- In a **Negotiation-Based CBIZ Program**, development incentive and associated community benefits package are jointly agreed upon between the municipality and the project proponent. That is, the CBIZ program does not define fixed relationships between incentives and required community benefits. Negotiated programs are relatively costly to administer, may be perceived by the community as opaque processes, and may be viewed as risky by the development community. However, these programs offer the flexibility to increase or reduce community benefit requirements to reflect changing market conditions. The primary advantage of negotiation-based programs is that the potential for the community benefits requirement may be crafted to reflect the economics of the proposed project and the current real estate market, while the disadvantage is that the negotiation process can be labor intensive and may not be practical (particularly for smaller projects).
- Under a **Formulaic (Plan-Based) CBIZ Program,** specific development incentives are made available in return for the provision of pre-defined community benefits. The principal advantage of a formulaic approach is reduction of project risk, for both the development community and the municipality and community, due to program certainty and lower program administration costs. The key disadvantage is that the program cannot respond to unique project challenges or fast-changing market conditions. The concept of a **Development Opportunity Reserve** is one potential variation of the formulaic CBIZ that might be well suited to the Town Center. A Development Opportunity Reserve establishes a particular level of additional density or additional land use entitlement that may be allowed in a plan area but isn’t assigned to particular parcels. Allocation of the “reserve account” may be done on a competitive basis, with petitioning development projects qualifying on the basis of compliance with pre-set “community objectives,” which could include parcel assembly, development of catalytic or preferred project types, and / or participation in infrastructure financing efforts.

<u>Applicability to Town Center Specific Plan</u>

CBIZ programs are successful when there is strong enough market demand for the higher-density products made available through the zoning change to pay for expected benefits. In addition, administration of CBIZ programs can be labor-intensive for City Staff, especially where competitive applications for a limited supply of reserve or benefit is entailed. Currently, because the Town Center sub-market real estate market remains relatively “soft” for many of the development prototypes envisioned for the Plan, CBIZ may not be an effective short-term tool for the City. Nevertheless, the structure and elements of a CBIZ can be advanced as part of the planning process to set expectations and ground rules for when development becomes more viable. For example, the terms, conditions, and mechanisms for a CBIZ Program such as a Development Opportunity Reserve program could be developed and incorporated into the Specific Plan to support long-term implementation of desired public facilities and infrastructure.

Land-Secured Funding and Financing

There is a long history in California and elsewhere in the United States of using land-secured financing methods to fund local infrastructure or provide services that benefit a particular area (ranging from an entire jurisdiction to sub-areas of all sizes). While increased voting requirements from Proposition 218 have created limitations on these mechanisms, the Mello-Roos Community Facilities District (CFD) remains a relatively flexible and well-used infrastructure finance tool. In addition, the State has recently increased the ease in which jurisdictions can leverage property tax increment through the Enhanced Infrastructure Financing Districts. However, several issues may limit the application of these tools in within the Town Center:

- Multiple property Owners: In the case of a CFD, a two-thirds voter approval is needed in areas that have more than 12 residents (landowners can approve special taxes in areas with 12 or fewer residents). This can be a difficult threshold in areas with numerous property owners.
- Low Property Tax Allocation Factor: The City has a relatively low property tax apportionment factor of 10 percent. Consequently, Duarte generates a relatively low amount of property tax with limited capacity for establishing a property-tax secured financing tool like an EIFD or CRIA.

City Funding and Financing

Cities have a number of ways in which they can raise money for capital projects, including seeking voter approval of general obligation bonds or special tax bonds, use of enterprise revenues (i.e., revenue-generating services) for enterprise investments (e.g., water and sewer utilities), and through "capitalizing leases" funded with general fund revenue sources. (City use of various State and federal grant program funds that continue to be available, as discussed separately below).

The long-term General Fund surplus associated with build-out of the Town Center area may present some opportunities for infrastructure financing. In most cases, this can be accomplished through a vote by City Council to obligate General Fund revenue for a particular purpose or period of time. For example, the City can vote to obligate sales tax increment from the Project Area to certain types of infrastructure and related improvements.

Another opportunity is the use of revenue from City-owned property, either through long-term lease or sale. For example, should the City choose to sell existing vacant properties within the Plan Area, or redevelop any part of the Civic Center and re-allocate any portion of it for commercial uses, the disposition or ground rent proceeds could be re-directed to support infrastructure development.

State and Federal Programs

Local and regional government entities commonly participate in a range of State and federal grant programs, compete for special grants, and partner with other public agencies on strategic infrastructure improvements. These grant programs and cooperative efforts, while mainly focused on maintenance of existing infrastructure, can be managed in a way that supports revitalization and infill development efforts. While the availability and level of funding from these sources are generally difficult to predict a-priori, the City should continue explore and pursue these opportunities as they arise.

Recommended Next Steps

Given the opportunities and constraints of the Town Center plan area discussed above, the following approach to infrastructure development strategy is recommended:

1. Continued progress towards improving the project area's development readiness by finalizing the Specific Plan, pursuing individual project opportunities, and supporting on-going re-tenanting and property re-investment activity. Indeed, approval of the Specific Plan itself represents one of the most important steps to improving the feasibility of infrastructure financing because doing so provides the guidance, certainty, and authority needed to induce further private sector investment.

2. Consider expanding Plan Area geography and/or coordination with related planning efforts. The City may consider pooling the Town Center Specific Plan with Duarte Station and City of Hope Master Plan (under development) areas for the purpose of infrastructure financing, as the relatively small size of the Town Center Area alone may constrain the range of financing options. Together, the City of Hope Master Plan and Duarte Station plans anticipate a substantial growth in the employment and residential bases of the City, which will increase demand for commercial and residential uses in the Town Center area and lead to greater area-wide motorized and non-motorized circulation. Coordinated development and financing of supportive infrastructure improvements could allow for cost sharing, implementation scale economies, access to TOD-oriented financing resources, and possibly also the establishment of a tax-increment-secured tool such as an EIFD or a CRIA.

3. Develop a detailed infrastructure financing plan. The City should initiate further analysis related to the scope, feasibility and capacity of the specific financing mechanisms identified in **Exhibit 16** and described further in **Appendix A**. The optimal financing plan will likely include a number of complementary tools reflecting the following interrelated analyses:

    a. **Estimate market value, timing, and feasibility for proposed Plan Area uses.** Strong market support is a precondition for generating financing capacity for a wide range of developer-sourced forms of financing, including developer impact fees, Community Benefit Incentive Zoning programs, and developer exactions. Such financing tools capture residual surplus value that remains after the developer's expected return, so without sufficient market support, these resources may not materialize.

    b. **Determine city willingness and ability to fund catalytic new infrastructure up-front.** Infrastructure development can create conditions that help stimulate new development, but many financing mechanisms capture value after the fact, which presents timing and phasing challenges as well as repayment risks. The City's willingness and ability to fund infrastructure bonds up front, based on General Fund capacity (including expected fiscal benefits discussed above in Chapter 2) and other potential sources, is a key component in providing this catalytic infrastructure.

c. **Consider increasing the size of the plan area and the scope of proposed infrastructure improvements.** As noted above, an infrastructure strategy that combines the Town Center, Duarte Station, and City of Hope plan areas will increase potential for implementing land-secured tools, such as an EIFD or CRIA, or obtaining certain transit- or complete streets-oriented grants. As noted above, scale and scope economies are an important pre-condition for use of many of these tools.

d. **Assess potential public and stakeholder support for voter- or property-owner-approved sources of financing.** Tools such as special assessment and community facilities districts, ad valorem tax-funded GO bonds, and development-supporting sales and property tax increases, require voter approval. Considerations such as the location of district boundaries, size of expected voter contributions, and general political sentiment can determine the efficacy of these tools and whether they are even worth pursuing.

APPENDIX A

Infrastructure Funding Tools

APPENDIX A: INFRASTRUCTURE FUNDING TOOLS

The infrastructure and development funding and financing options currently available to California cities fall into four general categories:

1. Development-Based Funding
2. Land-Secured Funding and Financing
3. City Funding and Financing
4. State and Federal Programs

The following section describes each of the funding sources and financing mechanisms that fall under these general categories. Without Redevelopment, development-based funding, including citywide and area development impact fees, project-specific exactions, private financing, and land-secured taxes and debt, are the primary tools for funding new development-required infrastructure. These sources in some cases may be layered or augmented with local sources that offer “bridge” financing and/or provide funding for specific infrastructure projects.

1. Development-Based Funding

Development Impact Fees

A development impact fee is an ordinance-based, one-time charge on new development designed to cover a “proportional-share” of the total capital cost of necessary public infrastructure and facilities. The creation and collection of impact fees are allowed under AB-1600 as codified in California Government Code Section 66000, known as the Mitigation Fee Act. This law allows a levy of one-time fees to be charged on new development to cover the cost of constructing the infrastructure needed to serve the demands created by the new development. To the extent that required improvements are needed to address both “existing deficiencies” as well as the projected impacts from growth, only the portion of costs attributable to new development can be included in the fee. Consequently, impact fees commonly are only one of many sources used to finance a city’s needed infrastructure improvements. Fees can be charged on a jurisdiction-wide basis or for a particular sub-area of the jurisdiction (such as a specific plan area).

<u>Establishment</u>

Development impact fees can be imposed through adoption of a local enabling ordinance supported by a technical analysis showing the “nexus” between the fee and the infrastructure demands generated by new development. Fees may be charged for a particular improvement (e.g., transportation improvement) or include multiple infrastructure improvement categories in a comprehensive program. Impact fee programs must be reviewed annually and updated periodically to assure adequate funding and proper allocation of fee revenues to the infrastructure for which the fees are collected.

<u>Cost Burden</u>

The burden incidence of development impact fees is upon the project developers and builders who pay the fees. Fees are a cost of development and are “internalized” into project costs in the same manner as all other development- and construction-related costs. There is no direct effect of fees on development pricing, because the markets set pricing independent of costs. However, when costs are too high for the market to bear, development may be deterred until such time as prices justify costs. All costs will influence land value, so it is often the case that landowners bear a portion of the cost of fees through lower land values (prices paid by developers or builders). So long as total development costs fall within a reasonable level, potential negative effects on development feasibility effects are manageable.

Economic Considerations

There are a number of specific economic considerations of development impact fees including:

- The effects of fees on the financial feasibility of new development and potential to deter otherwise desirable development (due to excessive costs); and
- The competitiveness effects of higher development costs (compared to neighboring jurisdictions) leading to dislocation of desired development.

A benefit of impact fees is that they provide a comprehensive and programmatic framework for identifying and allocating infrastructure costs to new development based on a demonstrated nexus between the new development and infrastructure need. In addition, there is no discretion on the part of developers subject to the fees nor is voter approval required.

The key limitation of development impact fees (in addition to the nexus requirement) is the timing of funding. Infrastructure often is needed "up-front" while fees are paid over time as development occurs. This means that other funding or financing methods are needed to close the timing gap. Fees also are irregular, as they depend on development activity that varies with economic conditions. During the 2008-09 recession, when development around the State and in the Bay Area slowed dramatically and prices fell precipitously in many locations, fee program revenues fell proportionately. Fees also require ongoing management including annual review, fund accounting, and updating to assure the efficacy and transparency of the fee program.

Related to the economic concerns discussed above, it is important to recognize that there are methods for moderating or deferring fees. Though individual development impact fee ordinances must be consistently applied and coordinated, they may contain features that can reduce potential negative economic effects and to avoid unnecessarily inhibiting otherwise desirable development. Also, there can be features of development impact fees that address economic concerns generally or on a case-by-case basis.

- Fee Deferrals: While the statute allows a levy of fees at issuance of building permit, many development impact fee ordinances allow a deferral until the "certificate of occupancy" is issued.
- Fee Waivers: Fee waivers provide the local government the ability to waive the fee for a particular project when it is determined that without such reduced costs a project that has substantial public benefit may otherwise not occur. Lacking such community benefits, waivers may be regarded as a "gift of public funds." Examples of such partial or total waivers include projects with the potential to generate substantial municipal revenue or community amenities, affordable housing projects, and employment-generating uses. Fee waivers reduce funding in a fee program proportional to the aggregate amount of waivers or exemptions

granted. Such revenue reductions must be "made up" by the city from other funding sources, or risk falling short on funding for infrastructure in the fee program.

- Credits and Reimbursements: Credits and reimbursements are mechanisms that allow developers subject to an impact fee to build infrastructure in-lieu of paying the fee. Credits provide proportional fee forgiveness for the value of that construction against the fee obligation. Reimbursements occur in the case where construction value exceeds the particular developer's fee obligation.

- Short-Term Fee Financing (interest bearing installment payments): Ordinances can provide for a developer to pay fee obligations over a period of time subject to an interest bearing and secured note.

Private Financing, Agreements, and Partnerships

Developers commonly fund infrastructure requirements privately, for example virtually all "in-tract" improvements (infrastructure improvements within a subdivision) are privately financed. In some cases area-serving infrastructure (not fully the responsibility of a particular developer) can be privately financed. These cooperative arrangements are typically structured in development agreements or reimbursement agreements. This upfront infrastructure development may be fully or partially refunded, using subsequently collected development impact fees, special tax bond proceeds, or other city funding sources. These arrangements tend to be available during times of strong market performance. In weaker markets or locales it may be difficult to obtain such private financing.

Project-Specific Conditions and Exactions

Before the advent of ordinance-based development impact fees, it was common for infrastructure to be funded by the developer through project-specific exactions imposed by the local jurisdiction, including direct payments for or construction of infrastructure required as a condition of subdivision or project approval. While development impact fees have reduced the use of exactions, exactions remain an important part of development-based infrastructure financing as there are often infrastructure requirements of a new project that are not included in the applicable fee programs. Determination of the need for such additional infrastructure is based on "rough proportionality" (i.e., nexus) with the development itself and is often derived from CEQA-based mitigation measures.

Development Agreements

A development agreement (DA) is a legally binding agreement between a local government and developer authorized by State statute (Government Code Section 65864 et seq.). A DA is a means for a developer to secure a development entitlement for a particular development project for an agreed upon period (often long-term approvals) in exchange for special considerations by the city (or county), generally including infrastructure improvements, amenities, or other community benefits that cannot be obtained through the normal conditions applicable to the project. DAs are entirely discretionary on the part of local government (there is no nexus requirement) and must be individually adopted by local ordinance. Development agreements vary widely and cities often establish their own policies and procedures for considering development agreements.

Incentive Zoning

Land use regulations can be configured in a manner that can provide incentives for additional private investments in local infrastructure and community benefits beyond that obtainable through the normal regulatory procedures. Community Benefit Incentive Zoning (CBIZ) programs are founded on the concept of "value capture." Public entities commonly create value with investments in public facilities and services (e.g., transit and utilities upgrades) as well as through changes to zoning code that increase the value of land. Typically, when the public sector creates value in these ways, landowners enjoy a financial gain. Value capture occurs when the public sector reclaims some of the value created by its activities. The State of California's Affordable Housing Density Bonus Law is an example of a CBIZ value capture program. Under this law, developers are granted additional density (i.e., the right to build additional market rate units) in return for their development of affordable housing units. A key limitation of CBIZ is the requirement for a strong real estate market in which developers are seeking to take advantage and pay for the incentives offered.

2. Land-Secured Funding and Financing

Special Benefit Assessment Districts and Community Facilities Districts

There is a long history in California and elsewhere in the United States of using land-secured financing methods to fund local infrastructure or provide services that benefit a particular area (ranging from an entire jurisdiction to sub-areas of all sizes). Traditionally, special assessment bonds as authorized by the Improvement Bond Act of 1915 and other related legislation were issued and funded by annual property tax assessments from benefitting properties. Increased voting requirements created by Proposition 218 largely eliminated the use of Special Benefit Districts in the mid-1990s. However, since the mid-1980s the Mello-Roos Community Facilities District (CFD) has been a well-used infrastructure finance tool, though it is not well suited for most infill applications due to voting requirements.

Establishment

California's land-secured funding districts can fund a wide range of infrastructure improvements that generate direct and measurable benefits to specific properties. The districts require (resident) voter or landowner approval. In the case of assessment districts, majority landowner approval is typically required. In the case of a CFD, a two-thirds voter approval is needed in areas that have more than 12 residents (landowners can approve special taxes in areas with 12 or fewer residents).

Cost Burden

The owners or users of real estate pay assessments or special taxes. By adding to the cost of ownership, the assessment or tax may affect the price a buyer is willing to pay for a home or commercial property, in which case the cost incidence is shared with the builder, land developer, or landowner. Experience suggests that less than 100 percent of the financing burden is recognized by buyers.

Economic Considerations

Land-secured financing provides a well-established method of securing relatively low-cost tax exempt, long-term, fixed rate, fully-assumable debt financing. However, there can be challenges associated with establishing measurable and specific benefits to particular properties. In addition, land-secured financing adds financing costs (e.g., cost of issuance and program administration).

Further, the financing capacity of a district may be limited in early phases of development and it may be necessary to rely on other sources of infrastructure funding during initial years. Finally, while land-secured financing has been widely used in greenfield development where landowner approval is the norm, achieving a two-thirds voter approval in infill areas typically is a barrier to use of the tool.

<u>Special Benefit Assessment Districts</u>

Special benefit assessment districts are a way of creating a property-based assessment upon properties that benefit from a specific public improvement. The formation of assessment districts requires majority approval of the affected property owners. Benefit assessments can fund a wide range of infrastructure improvements so long as a direct and measurable benefit can be identified for the benefitting properties. There are numerous forms of special benefit assessments in the California statutes, including the Municipal Improvement Act of 1913, Lighting and Landscape Maintenance Districts, and others. However, in 1996, Proposition 218 effectively curtailed the use of Assessment Districts in California by limiting the methods by which local governments may exact revenue from taxpayers without their consent. In addition, recent court rulings (Silicon Valley Taxpayers' Assn., Inc. v. Santa Clara County Open Space Authority, 44 Cal. 4^{th} 431 (Cal. 2008)) have further tightened the requirements for demonstration of "special benefit" thus further reducing the flexibility and utility of assessment districts.

<u>Community Facilities District Act</u>

The Mello-Roos Community Facilities Act of 1982 *(authorized by Section 53311 et. seq. of the Government Code)* enables the formation of a CFD by local agencies, with two-thirds voter approval (or landowner approval when there are fewer than 12 registered voters in the proposed district), for the purpose of imposing special taxes on property owners. The resulting special tax revenue can be used to fund capital costs or operations and maintenance expenses directly, or they may be used to secure a bond issuance, the proceeds of which are used to fund capital costs. Because the levy is a tax rather than an assessment, the standard for demonstrating the benefit received is lower, thus creating more flexibility. Despite limited use in populated infill areas, CFDs have become the most common form of land-secured financing in California.

3. City Funding and Financing

Cities have a number of ways in which they can raise money for capital projects, including seeking voter approval of general obligation bonds or special tax bonds, use of enterprise revenues (i.e., revenue-generating services) for enterprise investments (e.g., water and sewer utilities), and through "capitalizing leases" funded with general fund revenue sources. Cities also have discretion over the use of various State and federal grant program funds that continue to be available.

General Obligation Bonds

A general obligation bond is a type of municipal bond that is secured by a state or local government's pledge to use legally available resources, most typically including property tax revenues, to repay bond holders. General obligation bonds are restricted to defined capital improvements. Credit rating agencies often consider a general obligation pledge to have very strong credit quality and frequently assign them investment grade ratings. In California, cities must secure a two-thirds voter approval to issue general obligation bonds.

Establishment

Creation of general obligation bonds requires two-thirds voter approval if the issuance is for non-educational purposes.

Cost Burden

The incidence of burden of general obligation bonds is upon all property owners in the issuing jurisdiction proportional to the value of their property. It is this very broad base of funding that provides excellent security for general obligation bonds, thus typically garnering the lowest interest rate of any municipal debt instrument.

Economic Considerations

General obligation bonds allow public entities to finance at a low fixed rate over the useful life of the asset. However, general obligation bonds are limited to capital improvement expenditures and also are limited in their use to the precise purposes outlined in the authorizing ballot measure. General obligation bonds are commonly restricted to particular capital uses (e.g., street improvements, drainage improvements, parks and recreation).

Revenue Bonds

Cities and other local governments typically issue revenue bonds when they have access to a stable source of revenue such as municipal utility rates. Commonly, revenue bonds fund improvements to water and sewer facilities. Utility rates that fund revenue bonds can vary within a given jurisdiction if there are substantial differences in the costs of providing services. There also can be rate surcharges if unique improvements are needed to serve the area.

Establishment

Revenue bonds are issued by the municipal enterprise and require no voter approval. Revenue bonds may provide improvements for an entire jurisdiction or a sub-area.

Cost Burden

The incidence of burden of revenue bonds is upon rate payers.

Economic Considerations

Revenue bonds typically have a good risk profile and therefore garner comparatively low interest rates. Because they are secured exclusively by enterprise revenue, they are not general obligations of the city and do not require ballot approval. The ability to adjust rates to cover debt service costs and the ability to charge such rates differentially (given differing costs and benefits in service sub-areas) creates flexibility and appropriate cost allocation.

Revenue bonds are limited to enterprise-related expenditures and to the precise purposes outlined in the authorizing bond instrument. Revenue bonds also are limited by the rate base, which is a constraint when rates must conform to Constitutional and statutory requirements (e.g., Proposition 218).

Parcel Taxes

Citywide parcel taxes can be imposed with voter approval to fund municipal services and infrastructure. In practice, they typically are used to provide a broad-based source of funding for citywide-serving services. Due to the voter approval requirements and similar to general obligation bonds, jurisdiction-wide parcel taxes or special taxes typically are only successful if they fund highly-desirable public services and improvements, such as improved public safety services. Parcel taxes differ from general obligation bonds in that they can be used for maintenance and operations and they are not levied "ad valorem" (i.e., they typically have a flat or escalating rate structure applied to particular classes of properties).

<u>Establishment</u>

Parcel taxes, if used for general purposes including infrastructure investments, can be imposed with majority voter approval. If used for special purposes, parcel taxes will require two-thirds voter approval. They may be used for funding ongoing services or pledged to debt service.

<u>Cost Burden</u>

The incidence of burden of parcel taxes (and special taxes) falls upon property owners. Typically such taxes are "flat rate" charged per parcel, sometimes with use-related variation and exemptions.

<u>Economic Considerations</u>

Parcel taxes (and special taxes) create an opportunity for voters to decide to pay for municipal services or facilities that they deem important. With a broad funding base and strict allocation rules, the taxpayers can assure that funding will be used as intended. However, parcel taxes (and special taxes) are limited to the purposes for which they were approved. They also are commonly subject to a "sunset" date, and must be re-authorized periodically to maintain funding.

Sales Tax and Other Local Taxes

Subject to a vote, cities and counties can use a variety existing or new funding sources to fund infrastructure directly or provide interim financing for development-based obligations. For example, local sales tax increases, transient occupancy taxes, utility user taxes, development taxes, and (local option) real estate transfer taxes (charter cities only) all can be created or increased for this purpose. By enhancing General Fund revenues, the City gains the ability to divert some funds to infrastructure projects. A commitment to fund specific types of projects can be made in the ordinances that create new taxes or can be made as a matter of city policy. City funding can be used to fund infrastructure using a "pay-as-you-go" approach, as a source of reimbursement, or to support a municipal bond issue (e.g., to fill an initial funding gap associated with development impact fee programs or land secured financing programs).

General Taxes versus Specific Taxes

<u>General Tax</u>

- Expended at the discretion of the local government's governing body on any programs or services
- *Simple majority (50% +1) approval is required for General Taxes*

<u>Special Tax</u>

- Tax levied by a city or county that is dedicated to a specific purpose
- Taxes (other than property taxes for infrastructure bonds) levied by special districts, school districts, and community college districts (i.e., Special–Purpose District Tax)
- All taxes levied on property other than the property tax
- *Two–thirds voter support is required to approve special taxes.*

Source: Legislative Analyst's Office

Establishment

Creation of new general or special revenues and any related issuance of bonds supported by such revenues are limited by State constitutional requirements and statutes that require voter approval of greater than 50 percent for general taxes and two-thirds approval for special taxes (i.e., those earmarked for particular uses).

Cost Burden

The incidence of burden falls to those paying the taxes or rates. For example, sales taxes are paid by residents, businesses, employees, and visitors, while transient occupancy taxes are paid by visitors. The rationale for this payer burden is that these residents, businesses, employees, and visitors will benefit from the investments made in infrastructure and development.

Economic Considerations

Use of various general fund sources to support infrastructure investments including repair and replacement of existing infrastructure, as well infrastructure that serves new development, requires little additional administrative effort and is typically secure given the broad range of revenue sources pledged to the financing. However, the use of existing General Fund revenue is limited by current demands to support municipal operations.

Capitalizing Leases

Capitalizing leases, most commonly Certificates of Participation (COPs), are typically used by government agencies for construction or improvement of public facilities. Through the use of a lease-type repayment structure, the monies needed to fund these building projects do not (by California State law) constitute public debt and do not require voter approval. Usually, a public entity enters into a tax-exempt lease-purchase with a lessor and the lessor provides the agreed-upon the public facility. In this way, government agencies may use their leasing powers to provide more expedient access to the capital markets than the more restricted powers to incur debt. Agencies typically use tax-exempt leases to finance non-enterprise projects, such as schools, courthouses, jails, and administration buildings.[2]

Infrastructure Financing Districts and Enhanced Infrastructure Financing Districts

Infrastructure Financing Districts (IFDs) and Enhanced Infrastructure Financing Districts (EIFDs) are forms of Tax Increment Financing (TIF) that currently are available to local public entities in California. Local agencies may establish an IFD or EIFD for a given project or geographic area in order to capture incremental increases in property tax revenue from future development. In the absence of the IFD or EIFD, this revenue would accrue to the city's General Fund (or other property-taxing entity revenue fund). EIFD funds can be used for project-related infrastructure, including roads and utilities, as well as parks and housing. Unlike prior TIF/Redevelopment law in California, IFDs and EIFDs do not provide access to property tax revenue beyond the local jurisdiction's share (AB-8 tax allocation, see "Local Property Tax" text box below).

Largely because IFDs can be difficult to enact, Senate Bill 628 created a similar but more flexible tool, the EIFD. The EIFD bill expands the scope of eligible projects considerably, and lowers the

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[2] California Debt Advisory Commission 1993.

voter/landowner threshold to pass a bond from two-thirds to 55 percent. In addition, EIFDs can be formed and gain access to unlevered (debt free) revenue without a vote.

While any tax increment, no matter how small, could benefit a marginally financially feasible project, it is important that in most cases the local property tax available is very limited (California cities typically get between $0.10 and $0.20 of a property tax dollar). Moreover, the use of local property tax to support infrastructure financing has fiscal implications for California cities. Dedicating tax revenue to infrastructure limits funding for new public services costs associated with development.

Establishment

The establishment of an IFD or EIFD requires approval by every local taxing entity that will contribute its property tax increment. The IFD also requires two-thirds voter approval (within the specific geographic area) to form the IFD. EIFDs only require a vote when debt issuance is sought.

Cost Burden

The incidence of burden of an infrastructure financing district is local taxing jurisdiction that foregoes property tax revenue for services and dedicates these funds to infrastructure or other eligible investments.

Economic Considerations

IFDs and EIFDs, a form of TIF, redirect property taxes otherwise accruing to the city General Fund. The value created by the project is captured and invested in a manner that helps realize the project. However, only specific types of public investments of community-wide significance may be financed through an IFDs and EIFDs. IFDs and EIFDs cannot be used to finance operations and maintenance expenses. Unlike former Redevelopment TIF, IFDs only can utilize local government's share of property tax (along with other agencies who agree to forego their share of tax increment).

Local Property Tax

The county auditor is responsible for allocating property tax revenue to local governments pursuant to state law. The allocation system (referred to as AB 8) defines the share of property tax that accrues to local government and services districts.

The county auditor allocates the revenue to local governments by Tax Rate Area (a single county may have thousands). Each local government's share is based on its share of countywide property taxes during the mid-1970s.

The most significant factor in explaining the differences among local governments' shares of property tax is the difference in service responsibility. Local governments that provide a full range of governmental services typically receive a greater share of property tax.

Source: Legislative Analyst's Office; Elledge 2006

Community Revitalization and Investment Authority

The Community Revitalization and Investment Authority Law (AB 2) allows cities (and other property-taxing entities, except school districts) to establish a Community Revitalization and Investment Authority (CRIA) in disadvantaged communities (defined by the legislation). The CRIA area may adopt a resolution to allocate its share of property tax increment to the CRIA for funding of affordable housing and other redevelopment-related costs (e.g., infrastructure, environmental remediation, property). CRIA powers are similar to the authority of former Redevelopment agencies, including eminent domain.

Establishment

A CRIA is formed by City resolution or through entering into a joint powers agreement. The actions of the CRIA are governed by a community revitalization plan. To adopt an AB2 community revitalization plan, the CRIA must hold hearings. If there is a majority protest, the CRIA must terminate proceedings. A majority protest exists if protests have been filed representing over 50 percent of the combined number of property owners and residents in the area (who are at least 18 years of age). If between 25 percent and 50 percent of the combined number of property owners and residents in the area who are at least 18 years of age file a protest, then an election must be held. If an election is required, a majority vote is required to adopt the revitalization plan.

Cost Burden

The incidence of burden of CRIA tax increment funds falls to the local taxing jurisdiction that foregoes property tax revenue for services and dedicates these funds to the CRIA.

Economic Considerations

CRIAs create a new opportunity to redirect property taxes otherwise accruing to the city General Fund to infrastructure. However, similar to IFDs and EIFDs, the CRIA only may utilize local government's share of property tax (along with other agencies who agree to forego their share of tax increment). Furthermore, the CRIA area must include at least 80 percent of land that has an annual household income that is less than 80 percent of the statewide annual median income, as well as three out of the four additional criteria defined in the statute (high unemployment, high crime rates, deteriorated or inadequate infrastructure, deteriorated commercial or residential structures, including a former military base).[3] A key concern related to the potential for CRIAs is that they are targeted for use in areas that likely, given these eligibility requirements, typically will have weak market conditions and local jurisdictions with minimal flexibility to give up property tax revenue that is otherwise needed to support municipal service costs.

4. State and Federal Programs

Grant Programs

Local and regional government entities commonly participate in a range of State and federal grant programs, compete for special grants, and partner with other public agencies on strategic infrastructure improvements. These grant programs and cooperative efforts, while mainly focused on maintenance of existing infrastructure, can be managed in a way that supports revitalization and infill development efforts.

State Infrastructure Bank (IBank)

The IBank was created in 1994 to finance public infrastructure and private development that promote a healthy climate for jobs, contribute to a strong economy and improve the quality of life in California communities. The IBank operates pursuant to the Bergeson-Peace Infrastructure and Economic Development Bank Act (Government Code Sections 63000 et seq.). The IBank is administered by the Governor's Office of Business and Economic Development and is governed

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[3] See AB-2 Community revitalization authority full text here: https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=201520160AB2.

by a five-member Board of Directors. Since its inception, the IBank has financed more than $32 billion in infrastructure and economic development projects around the State.

The IBank has broad authority to issue tax-exempt and taxable revenue bonds, provide financing to public agencies, provide credit enhancements, acquire or lease facilities, and leverage state and federal funds. The IBank's current programs include the Infrastructure State Revolving Fund (ISRF) Program, 501(c)(3) Revenue Bond Program, Industrial Development Revenue Bond Program, Exempt Facility Revenue Bond Program and Governmental Bond Program.

The ISRF Program provides very low-interest rate loans up to $25 million (per applicant) to municipal governments for a wide variety of municipal infrastructure, including infrastructure needed to serve new development. An application is required for these loans, and loans require a stable and reliable source of repayment. If approved, loan repayment can be funded through a commitment of city general fund revenues or a pledge of a particular revenue source, including a citywide tax, land secured assessment, or special tax levied on a particular area.

Common criticisms of the IBank ISRF Program have included its cumbersome program application process, its strict credit standards and related risk aversion, and limited financial incentive to participate. However, recent changes to the program may increase IBank lending to cities without other credit options. Pursuing further opportunities to modify or expand the Program, or to create an entirely new program, could make State-sponsored lending a useful tool for assisting and incentivizing infill development.[4]

Statewide Community Infrastructure Program

The Statewide Community Infrastructure Program (SCIP) is a program of the California Statewide Communities Development Authority (CSCDA) that makes use of a local government's ability to create land-secured financing districts. The Program "pools" debt obligations to gain a comparatively lower interest rate and issuance costs (particularly if the issue is less than $5 million). SCIP can benefit developers because it provides low-cost, long-term financing of fees and improvements, which can otherwise entail substantial upfront cash outlays. Local agencies benefit from SCIP when fee funds are made available upfront or infrastructure is financed with attractive terms. Typically, most public improvements required as conditions of project approval are eligible, including roads, street lights, landscaping, storm drains, water and sewer facilities, and parks. Further, the availability of low-cost, long-term financing also can soften the burden of rising fees and improvement costs, which benefits developers and local agencies. According to CSCDA, the SCIP program has assisted communities and developers throughout California to finance over $150.2 million in impact fees since 2003.

CSCDA is a Joint Powers Authority sponsored by the League of California Cities and the California State Association of Counties. Membership in the Authority is open to every California city and county, and most are members. SCIP financing is available for development projects situated within cities or counties (local agencies) which have elected to become SCIP participants. Eligibility to become a local agency requires only (a) membership in the League of Cities or

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[4] Find more information concerning California Infrastructure and Economic Development Bank programs available here: http://www.ibank.ca.gov/programs_overview.htm.

California State Association of Counties, (b) membership in the Authority, and (c) adoption of a resolution making the election (the “SCIP Resolution”).

Participation in SCIP entails the submission of an application by the property owner of the project for which development entitlements either have been obtained or are being obtained from a local agency. For projects determined to be qualified, SCIP provides non-recourse[5] financing of either (a) eligible development impact fees payable to the local agency or (b) eligible public capital improvements (or both). Under certain circumstances, determined on a case-by-case basis, development impact fees payable to local agencies also may be used as repayment for upfront SCIP funding.

SCIP funding awards are aggregated for inclusion in a round of financing authorization. Periodically, as warranted by the accumulation of approved funding applications, the California Statewide Communities Development Authority issues tax-exempt revenue bonds. For projects involving a sufficient amount of financing (generally $5 million or more), a special series of bonds may be issued to fund the project separately if the timing of issuance of a pooled financing does not suit the project. Revenues to pay debt service on the SCIP bonds are derived from special assessments pursuant to the Municipal Improvement Act or through the levy of special taxes by establishing a CFD pursuant to the Mello-Roos Community Facilities Act.

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[5] Non-recourse financing is a loan structure in which the lending bank is only entitled to repayment from the proceeds of the project, not from other assets of the borrower.