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Harris & Associates

# Are You Reimbursing Developers for Public Infrastructure Construction?

## *5 Things You Need to Know*

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Agencies are responsible for verifying that developers receive the appropriate reimbursement amount for building public infrastructure. This verification process is referred to as a cost reimbursement review. Not all agencies perform such a detailed review. However, it is important to determine the public improvements' actual cost and ensure the public funds are being used appropriately.

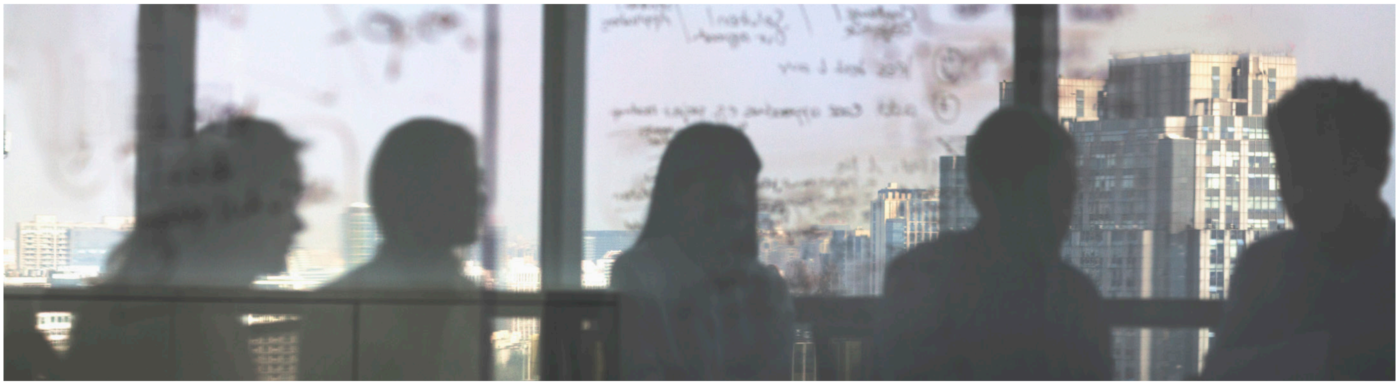
Here are five questions to consider and understand related to reimbursement verification:

1. **What is a cost reimbursement review and why is it important?**
   When a developer builds public improvements that a public agency will acquire in exchange for a reimbursement or credit from a financing mechanism, such as a CFD, EIFD, or impact fee program, the public agency must determine the true cost of those facilities with a cost reimbursement review.

**This review includes a complete assessment of:**

- Contracts
- Change Orders
- Invoices
- Checks
- Lien Releases
- Improvement Plans

It's a transparent process that protects the agency, future homeowners, and investors. Several legal guidelines also protect the investors as well as the agency—along with the tax-exempt status of the bond.



2. **What procedures and processes must agencies follow?**
A clearly defined process allows agencies to communicate their reimbursement expectations and processes while streamlining work and opening a direct line of communication for all parties involved. The agency should develop a procedures and processes manual that includes a cost reimbursement plan to define how the process will work, establish review and approval policies, and identify responsible parties throughout the process. Here are some items to consider in this manual and the cost reimbursement plan:

    - **Submittal information.** The developer should submit a formal reimbursement request indicating which facilities or discreet components they are requesting reimbursement for and the amount for each item. The request should be broken down between construction costs and soft costs (see next bullet). The developer should include all contracts and agreements, change orders, cancelled checks, lien releases, and plans associated with the requested improvements. Additional documentation, such as agency approval letters, may be required as part of the developer-agency agreement.
    - **Soft costs.** Often, the maximum allowable soft cost amount is a percentage of the total allowable construction amount. Depending on the developer-agency agreement, the soft cost amount could be automatically applied to the verified construction costs, or there may be a requirement to review the soft cost invoices to determine actual expenses. An allocation between eligible and non-eligible improvements should be provided. This information should be outlined in the policy and procedures manual.
    - **Package submission.** Agencies tend to prefer electronic submittal of documents, either via FTP site or a project share site. Developers should arrange and organize documents in folders for clear identification. Setting up a project share site keeps all information in a single place accessible all team members. Using electronic signatures, when possible, can also help streamline the process.
    - **Additional information request.** Generally, agencies use an additional information request (AIR) to obtain missing information from developers. This involves reviewing the information submitted and generating a letter that highlights additional information or clarification on requested items. The developer then re-submits a package with the additional information. AIRs are generated until the agency receives all necessary information. At that point, a final audit report is prepared that outlines the approved costs. This formal process provides a paper trail for the exchange of information and provides a detailed summary of the costs being reimbursed.
    - **Expected turnaround times.** The manual and plan should clearly define turnaround times, how long the agency has to review the payment request, turn around each AIR, and issue the final report. The timeline for these tasks typically varies from 10 to 30 days. It is important to consider a realistic turnaround time for submittals. Initial submittals contain a large amount of documentation and

can require time to review. When possible, avoid including a clause in the agreement that states an automatic payment will be made if a deadline is not met.

- **Developer and agency responsibilities.** Cost reimbursement plans should clearly define each party's roles and responsibilities, for the completion of specific tasks throughout the process and the related deadlines. An acquisition agreement (or similar governing documents) often outlines the roles and responsibilities, which are then further defined by agency policies.

3. **How will you define what is public versus what is private?**
Items of work that are related to reimbursable improvements at the outset will save everyone time and money over the long run. Here are some items to consider in differentiating public and private improvements:

- Define discreet components clearly in the acquisition agreement or funding documents to articulate what each component covers. Each discreet component should be easily defined as a separate item of work in the contract.
- Make sure your pay items in the contract match the approved discreet components and break them down to clearly distinguish between public versus private infrastructure.
- Break down any change orders by discreet component and clearly define public versus private. The eligibility of these items should be verified as the change order occurs, which ensures the supporting documentation for the change order is readily available.

4. **Who should perform the cost reimbursement review?**
Processing reimbursement requests involves many nuances. An experienced firm will understand the laws associated with bonds, have a clearly defined process in place, and know how to read plans, agreements, contracts, and invoices to accurately verify reimbursable costs.

**Involving a well-qualified consulting firm early in the process to help...**

Assist in Developing the Acquisition Agreement

Develop the Process and Procedures Manual and

Create a Cost Reimbursement Plan

**...will set the entire process up for success!**

The consultant should also have an established method for tracking reimbursements and submitted costs to ensure the developer receives no more than the reimbursement for which they are eligible.

5. **Are there any legal issues to consider?**
Agencies must understand and consider many legal issues related to reimbursement audits. Among them:

   - Per the California Code of Regulations, title 8, section 16001, subdivision (a), prevailing wage rates must be applied to all public works contracts. California Code of Regulations defines public works as the "construction, alterations, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds."

In recent rulings in the court case of
**Azusa Land Partners v. Department of Industrial Relations**
*the court upheld that:*

**1**

A master planned community project is a **"public work"** subject to prevailing wage laws applicable to public improvement work performed by private contractors where such work was a condition of project approval.

**2**

Mello-Roos proceeds are **"public funds"**.

**3**

Once a project is deemed a **"public work"** under prevailing wage law, the entire project is subject to the law, including those improvements privately financed.

   - Improvements acquired by the agency prior to the CFD being formed are not eligible for reimbursement from bond proceeds.
   - Private utility payments that exceed 5% of the bond amount are not reimbursable. This needs to be considered when reimbursing for items such as joint trench. If the reimbursement exceeds this amount, the bond loses its tax-exempt status.
   - All documentation must be retained for the life of the bond. Consideration should be given to storage methods.
   - Bond proceeds must be held in a deposit account. Any bond proceeds placed in an impact fee fund need to be spent within three years.

## Summary

Performing reimbursement reviews is a key step in the acquisition of public improvements by an agency. Too often, agencies overlook this process because the program administrator lacks a thorough understanding of the legal framework.

Not performing cost reimbursement reviews can open your agency up to legal and tax ramifications as well as public scrutiny. After all, by allowing developers to use public financing as a method of funding infrastructure, agencies assume responsibility to ensure the bonds are used in their intended manner. That's why your agency should take the time up front to establish the public infrastructure acquisition process—a process that the developer should fund since it's part of the cost associated with using the public financing mechanism.

**For support with cost reimbursement reviews, developing procedures manuals, and other critical steps, contact Alison Bouley, PE.**

### About the Author

Building rapport with clients is one of Alison's specialties. She has worked at Harris for most of her 20 years in the industry, so it's no surprise that Alison has developed long-term relationships that have benefited communities across California.

As a Vice President in the municipal funding and special district finance practices, Alison is an expert in the intricacies of AB1600 requirements and has been an integral player in guiding new developments through the specific plan, EIR, and finance plan process. She's also skilled at acquisition audits—ensuring that public agencies understand the legal aspects of reimbursing developers for constructing public infrastructure. This understanding is essential when precious public funds are involved.

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### About the Author

Through her impressive career spanning more than 17 years, most with Harris & Associates, Anna Tan-Gatue has helped numerous clients navigate the intricacies of municipal funding challenges.

As a project manager, Anna has provided municipal finance services to cities, counties, and special districts on a wide variety of project types. Her many proficiencies include compiling district databases, researching and analyzing the different attributes of the district, confirming database accuracy, ballot tabulation, and coordinating with the Count Auditor-Controller's offices for annual levy submittals for inclusion on property tax bills.

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