

Are You Reimbursing Developers For Construction of Public Infrastructure?

5 things you need to know.

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When a developer seeks reimbursement for construction of public infrastructure, it is the responsibility of the agency to verify the appropriate cost of the facilities. This process is referred to as an acquisition audit. Not all agencies perform such an audit; however it is a process that should be followed.

1. What is an Acquisition Audit and why is it important?

When a developer constructs public improvements that are to be acquired by a public agency in exchange for a reimbursement or credit from a financing mechanism such as a CFD or impact fee program, the public agency must determine the true cost of those facilities. The acquisition audit is a process by which the appropriate acquisition cost is determined. This is done through a complete review of contracts, change orders, invoices, checks, lien releases and improvement plans. This process is imperative as it provides a transparent process that protects the agency, future home owners and investors. There are also several legal guidelines that must be adhered to protect the investors as well as the agency.

2. What are the procedures and processes that must be followed?

Having a clearly defined process enables the agency to communicate clearly the expectations and processes for reimbursement. It also streamlines the process and opens up a clear and direct line of communication. The agency should develop a procedures and process manual to define how the process will work. Here are some items to consider in this procedures and processes manual:

- What information should be submitted? The developer should submit all contracts, approved change orders, cancelled checks, lien releases, plans, and a formal reimbursement request. The request should indicate which discreet components are being requested for reimbursement and how much for each item. This should be broken down between construction costs and soft costs.
- How will the package be submitted to the agency? Electronic submittal of the documents tends to be the preferred method. The developer should use an FTP site for transmittal of the documents. The documents should be arranged in folders so that the information is clearly identifiable. Setting up a project share site is a great way to keep all information in a single place and accessible for all team members. Utilizing electronic signatures when possible can also help streamline the process.

- What is the process for requesting more information? Generally an additional information request (AIR) is used. This involves reviewing the information submitted and generating a letter that highlights additional information needs or clarification on items being requested. The developer then re-submits a package with the additional information. Additional AIR's are generated until all information has been received. Once all information is received a final audit report is prepared and submitted to the City for documentation of the approved costs. This formal process provides a paper trail and keeps the exchange of information well documented.
- What is your expected turnaround time for a submittal? This should be clearly defined in the process and procedures manual. These timelines should define how long the agency has to turn around each AIR as well as the final audit report. The timeline for these tasks typically vary 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 it can take time to review that data. An automatic payment which provides payment if a deadline is not met, should not be included.
- What soft costs are allowed and how will these costs be allocated to each discreet component? This information should be outlined in the policy and procedures manual to provide a clearly defined allowance. This takes the guess work out of the equation later.

3. How will you define what is public versus what is private?

Being able to clearly separate out what items of work are related to reimbursable improvements is a critical element in the reimbursement process. If this information is clearly defined in the beginning, it will save everyone time and money over the long run. Here are some items to consider:

- Define discreet components clearly in the acquisition audit. It should be clear what is covered under each and each discreet component should be an item that can easily be defined as a separate item of work in the contract.
- In the contract, the pay items should match the discreet components and should be broken down to clearly distinguish between public versus private infrastructure.
- Any change orders should also be broken down by discreet component and clearly define public versus private. The eligibility of these items should be verified as the change order occurs.

4. Who should perform the audit?

There are many nuances involved in processing reimbursement audits. A firm should who is experienced in processing audits will understand the laws associated with bonds, will have a clearly defined process in place and will understand how to read plans, contracts, and invoices to accurately verify reimbursable costs. Getting a well-qualified firm involved early in the process to help develop the process and procedures manual and assist in developing the acquisition agreement will set the process up for success. The consultant should also have an established

method for tracking reimbursements and submitted costs to ensure that the developer does not get reimbursed more than they are eligible for.

5. Are there any legal issues to consider?

There are many legal issues that an agency must be aware of as it relates to reimbursement audits.

- Prevailing wages must be paid for any work that is to be reimbursed from public funds. Recent rulings made 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,” and (3) once a project is deemed a “public work” under Prevailing Wage Law, the entire project is subject to the law – including those improvements which are privately financed.
- Improvements that are acquired prior to the CFD being formed are not eligible.
- 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 how this will be stored.

Summary

Performing reimbursement audits is a key step in the acquisition of public improvements by an agency. Too often this process is overlooked due to the fact that the legal framework for acquiring public improvements is not thoroughly understood by the administer of the program. Not performing reimbursement audits can open the agency up to legal ramifications and public scrutiny. Allowing developers to use public financing as a method of financing infrastructure places a responsibility on the agency to ensure that the bonds placed on the home were used in the manner in which they were intended. The agency should take the time up-front to establish the process by which the public infrastructure is to be acquired. This process should be funded by the developer as it is part of cost associated with using the public financing mechanism.

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