TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER

DATE: SEPTEMBER 19, 2005

DEPARTMENT: UTILITIES

CMR: 377:05

SUBJECT: FINANCING ALTERNATIVES TO FUND SERVICE CONVERSION COST FOR PROPERTY OWNERS IN UNDERGROUND DISTRICTS

REPORT IN BRIEF

During the public hearing for the formation of Underground Utility District (UUD) No. 41 on July 25, 2005, property owners expressed concerns about the high cost for the service conversion work on their properties. In response to this request, Council directed staff to present alternative financing plans to assist property owners with the costs. In addition, staff was requested to report on the current cost of underground service conversion work in relation to past underground districts.

The following report discusses: financing options that are currently available, alternates to the current financing, possible changes in current policy to reduce service conversion costs in Underground Districts, and the current cost of underground service conversion as compared to those in previous districts.
**RECOMMENDATION**

Staff recommends that the Council direct staff to: Return with amendments to the Municipal Code to allow the repayment of Underground Utility District loans and release of lien, with interest, as follows: Repay with current 10-year loan program, or repay at the time the home is sold or transferred to a person or persons other than the present owner, the loan amount is repaid, or the ownership is changed.

Provide an additional service to property owners in underground districts the management of all or part of the service conversion work and direct staff to establish a fee for managing and administering the contract, to be included in the Utilities Rates and Regulations.

Staff also recommends that the Council meeting of October 17, 2005 be set as the date of the public hearing for the adoption of the Ordinance Establishing Underground District No. 41.

**BACKGROUND**

One major activity in the completion of an underground district is the underground service installation from the street to the house. In accordance with current policy as established in Palo Alto Municipal Code Chapter 12.16, the property owner is responsible for completing and paying for this work. The work required at a typical property consists of installing three or more conduits (electric, telephone, and CATV) from the designated service point to the building or present meter location and installing the electric service cables. Various types of restoration/reconstruction work may also be required, e.g. lawns and landscaping, sprinkler systems, driveways and walkways (concrete, asphalt, exposed aggregate and/or brick). Although some property owners may be able to perform this work, the majority hire a contractor.

**DISCUSSION**

The discussion section is divided into three main areas: Currently Available Options, Providing Additional Support to Assist Property Owners with Service Conversion Work, and Comparison of Service Conversion Cost of past Underground Districts.

Currently Available Options
There are several programs currently available to assist property owners with the costs associated with the underground service conversions.

*Underground District Loan Program*
When Municipal Code Chapter 12.16 was adopted, it was anticipated that some property owners would have difficulty paying the service conversion cost in a one-time fee. To alleviate this burden on the property owners, the Council authorized 10-year loans at an interest rate set in the Municipal Code.

The current 10-year financing program established in the Municipal Code for underground districts is a special assessment against the property that is secured by a property lien. The loan is repaid over 10 years and is collected as a special assessment on their property tax bill. The
financing program is funded by ratepayers through a reserve in the Electric Fund. Currently the reserve fund has a balance of $636,000. In past districts, 2 to 3 percent of homeowners have opted to take the loan.

The loan program is administered by the City. To qualify for the financing, property owners are required to request financing at the time of the formation of the district. Once the district is formed and the utility portion of the work is nearing completion, a resolution to approve the loan payments is sent to Council. Property owners who have elected to finance their utility services are required to install their facilities and pay the contractors for the work performed. They then send a request for financing to the City. The City establishes a lien with the County and the property owners are reimbursed for their expense. The special assessment is then paid back over 10-years through the bi-annual property tax bill.

Property owners can defer or reduce the costs associated with their property tax bill with the following programs administered by the State.

Property Tax Deferment
The State Controllers Office (SCO) has a property tax deferment program for people that qualify for the program. The program defers the entire amount of the tax bill including any assessments against the property. Requirements are as follows:

- 62 years of age or older by December 31, 2004 or
- Blind or disabled at the time of filing (for a continuous period of at least one year) and
- Total household income for the prior year of $24,000 or less ($34,000 for those who filed and qualified for tax postponement in 1983);
- 20 percent equity in their home at the time of filing; and
- Have owned and occupied their home, mobile home or floating home as of December 31, 2003.

An application must be submitted to the SCO. If it is approved, the State will issue certificates that may be used to pay all or part of the property taxes to the county.

An account is set up by the SCO for the amount of taxes postponed. This account must be paid, with interest, when the claimant: (a) moves out, (b) sells the home, (c) allows future property taxes or other senior liens to become delinquent, or (d) dies and there is no spouse, domestic partner, or other qualified individual who continues to reside in the home.

A security document or lien is placed on the property to protect the State's interest and ensure eventual recovery of the amount of taxes the State has paid, plus interest.

Homeowner Assistance Program
In addition to the property tax deferment program, the State Franchise Tax Board administers a homeowner assistance program. This program allows a once-a-year payment from the State of California to qualified individuals based on part of the property taxes assessed and paid on their homes. For the 2005 claim year, eligible homeowners may claim up to 96% of the property taxes they paid in 2004. The maximum assistance payment is $472.60.
Homeowners may be eligible to file a 2005 claim if they are a citizen of United States, designated alien or qualified alien when they file a claim and they have met the following criteria on December 31, 2004:

- 62 years of age or older, blind, or disabled,
- Owned and lived in your own home, and
- Had a total household income of $39,699 or less.

The Homeowner Assistance Program does not create a lien against the house. However, if homeowner assistance is granted and the State Controller grants a claim for property tax postponement for the same fiscal year, the amount of the homeowner assistance will be sent to the State Controllers office to reduce the balance due on the postponed tax payments.

**Proposed Additional Financing Options**

As directed by Council, staff looked for additional ways to augment or change the existing programs to provide assistance to property owners in underground districts to reduce the burden of the service conversion costs.

**Loan Secured by Property Lien with No Repayment Schedule**

In this option, the City would finance the cost of the conversion and secure repayment by placing a lien against the property. This differs from the current program in that property owners would not be required to meet a repayment schedule. The lien would remain against the property collecting interest until the property is sold or transferred to a person or persons other than present owner, the ownership is changed, or the amount is repaid.

This program would be available to all property owners in the UUD. Council, in order to minimize the financial risk, may chose to limit this loan program to property owners who meet certain criteria that could be established. However, staff is not recommending establishing qualification criteria because of the amount of staff time required to qualify homeowners for the program. Also, based on the low number of loans given in the past, staff does not anticipate significant exposure to financial risk.

One issue that might arise during repayment of the loan at the time of sale or transfer of the property is the realization by property owners that a large payment is due to pay off the accumulated interest on the loan amount.

Staff is recommending that this program be implemented because it provides the most benefit to property owners without increasing administration costs significantly. Property owners have the benefit of no out-of-pocket expense and the City will secure repayment with interest by a lien placed against the property.

**Direct Assistance**

The direct assistance proposal would pay 20% of qualifying homeowners’ service conversion cost. This proposal is based on the current Utilities Rate Assistance Program that pays 20% of the cost of qualifying ratepayer’s monthly bills. Homeowners in the underground district that
already qualify for the Ratepayer Assistance Program would automatically qualify for the underground district assistance program. Anyone wanting to apply who is not currently in the program would be required to submit an Application for Utility Rate Assistance to determine eligibility.

This program could be offered in conjunction with the current loan program, which would result in a 20% reduction in the annual assessment.

Staff does not recommend this alternative for the following reasons:

- The qualifying criterion for the Rate Payers Assistance Program is similar to the Home Owners Assistance program administered by the State of California. In most cases the direct assistance would provide fewer benefits than the State’s program.
- The program would increase the City’s costs by adding an additional program to be administered by staff.

*Service Conversion Policy Change*

It has been the City’s policy that homeowners are responsible for the installation and maintenance of conduits and for the installation of electric conductors on their property for electric service. This policy is in place for all new services including those that are established during an underground project. This policy could be changed and the ratepayers could assume the costs of installing facilities on the customers’ property.

Staff does not recommend this policy change for the following reasons:

- The additional costs would reduce funds available for the underground program by about one-third.
- Underground service conversion work on the property is a shared asset for electric, cable, and telephone. It would be difficult to separate the cost so that the electric ratepayers were paying only for the electric assets.

*Provide Additional Support to Assist Property Owners with Service Conversion Work*

The extent of involvement of Utilities staff in assisting property owners with service conversion work is typically limited to providing specifications for the scope of work and a list of contractors who have performed similar work in previous underground districts. The property owners are then responsible for obtaining price quotes from one or more contractors and coordinating the work with the selected contractor. City staff has provided assistance, within reasonable limits, to help with the process of hiring the contractor or explaining the work to be performed. Although following this process has worked for some property owners, it has in some cases presented a perceived problem or inconvenience to the property owners, especially for the senior citizens or for people with little or no experience dealing with contractors. Property owners have expressed concerns and have requested the City in the past to handle the service conversion work by taking the lead and representing the property in hiring a contractor to get the work completed.

In order to address the property owners’ concern about service conversion costs, Utilities staff implemented a pilot program in Underground District 40 to perform the service lateral conduit
installation portion of service conversion work using the contractor that was hired to install the utility substructure in the street. The service was offered to the 18 property owners and 100% of the property owners opted to have the City’s contractor install the service lateral conduits. The same contractor also provided estimates for the electrical portion of the work. It is staff’s understanding that the majority of the property owners are planning to use the same contractor to complete the electrical work. The service conversion cost (both conduits and electrical work) based on the bid submitted by the City contractor ranged from a low of $3,380 to a high of $5,988 with an average of $4,200.

Managing and administering the service lateral conduit installation did not significantly impact staff’s time or workload in Underground Utility District 40 due to limited number of property owners. Providing similar service in large districts, such as Underground Utility District 41, which has 175 properties, however, will require significant staff time and the establishment of new administration and management policies and fees for the service conversion work. Staff believes that working with the homeowners to develop a City-administered contract for service conversion work will reduce the costs for homeowners due to the efficiency gained by work consolidation.

Service Conversion Cost Comparison of Past Districts
Service conversion costs were reviewed from the limited data that staff has available. It appears that the costs in the last four or five similar underground districts have escalated faster than the rate of inflation. Staff attributes this to the lack of competition in the market place for this work and generally the higher cost of providing service in the Palo Alto area. Implementing a City-managed contract for service conversion work to assist property owners could help mitigate the high cost experienced by other districts.

**RESOURCE IMPACT**
These proposals will increase staff time for the administration of the loan program and coordinating contracting work. Depending on the number of property owners, it is estimated that 1 to 2 percent of the project cost will be required to implement the recommendations. All additional costs will be reimbursed through fees charged to property owners obtaining loans and or requesting City to manage the service conversion work.

If a large number of property owners opt into the City loan program additional funding will need to be added to the Underground Reserve Fund. This could have a minimal impact on rates.

**POLICY IMPLICATIONS**
Staff’s recommendations will change existing policy on the City’s role in the contracting for service conversion work. In the proposed change, the City will act as the contracting agent for the service installation on the homeowner’s property.

In addition, the recommendations will also require changes to the loan policies in the Palo Alto Municipal Code. The impact of this policy change could result in an increase in the amount of
reserves required to fund the loan program and the amount of funds tied up in outstanding loans would not be collected until the liens are cleared.

ENVIRONMENTAL REVIEW
This project is categorically exempt from CEQA under Section 15302.

ATTACHMENTS

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