

# Commentary

## “Can’t Get No Satisfaction?”

### Getting Reimbursement from Reimbursement Agreements

by Carla K. Ryhal

The California Subdivision Map Act allows a local government not only to require a subdivider to construct improvements which benefit the subdivision, but may also require that the size or capacity of the improvements be larger than necessary for the subdivision in order to benefit property that is not within the subdivision. For example, roadway, sewer, water or drainage facilities may be required to be large enough to be used by future subdivisions of nearby property. In that case, the subdivider is required to pay the additional costs of the enlarged facilities, but the local government is required to enter into an agreement to reimburse the difference between the costs incurred in constructing the enlarged facilities and the costs that would have been incurred to construct the facilities to serve only the subdivision.

Unfortunately, reimbursement agreements are frequently so casually negotiated that the subdivider rarely recoups his excess costs. Compounding the problem, there have been no reported court cases dealing with the local government's obligation to reimburse a subdivider for enlarged facilities. Therefore, if a subdivider will be required to oversize subdivision improvements, negotiating and drafting an effective reimbursement agreement is well worth the effort.

#### **Timing of Negotiations**

Of course, given the paucity of construction financing in the current economy, it is preferable to avoid conditions on a subdivision map requiring the oversizing of improvements.

Barring that, however, the best time to negotiate the terms of reimbursement is concurrently with the subdivision conditions themselves. Since the ability to receive reimbursement influences the economic feasibility of a subdivision condition requiring oversizing of an improvement, and since a subdivider is prohibited from challenging a condition that he does not contest through the local government's approval of the subdivision map, much of the subdivider's negotiating leverage is lost after approval of the subdivision map imposing the oversizing requirement.

The second best time to agree upon the terms of reimbursement is before constructing the enlarged improvement, when the local government is still motivated by its desire to get the subdivider to install the improvement. The common but least desirable time to try to seek reimbursement is after the enlarged improvements are in place, at which time the local government has no self-interest in giving reasonable reimbursement terms.

#### **Identifying Source of Reimbursement**

The Subdivision Map Act identifies three primary sources from which reimbursement may be obtained. The local agency may: (1) collect user or connection fees from other persons using the enlarged facilities; (2) levy a charge upon the property outside the subdivision that is benefited by the enlarged facility; and (3) establish a local benefit district.

Connection charges or development fees are collected when the benefited property is developed, and thus can be virtually non-existent sources of reimbursement if a significant amount of the benefited property has already been developed. Depending on the particular type of improvement and area of benefit, a financing district *may* be available as a source of reimbursement and, under some circumstances, *can* be collected upon completion of the improvement, whether or not the benefited property is developed.

In addition to the reimbursement methods identified in the Subdivision Map Act, some jurisdictions have been willing to give subdividers credit against fees for the same type of facilities as those constructed by the subdivider, or even against unrelated fees. Finally, a local government is free - though usually unwilling - to reimburse a subdivider from its own funds and then be reimbursed itself from the sources identified above. These possibilities should be explored as the first source for reimbursement, as they are guaranteed, are immediate, and reduce the developer's need for construction cash.

#### **Defining Reimbursable Costs**

Whichever of these reimbursement sources is to be used, it is important that a legally supportable study be prepared, showing the benefit bestowed on the benefited property by the oversized improvement and justifying the fair share assessment on the benefited property. Conversely, it is important to identify what portion of the cost of the enlarged facility is attributable to the subdivision and limit the developer's responsibility.

The reimbursement agreement should specify what costs the subdivider anticipates in constructing the oversized improvement would be reimbursable. Types of expenses frequently disputed include design and engineering costs, plan check and permit fees, the cost of the subdivider's employees supervising the contractor and subcontractors, insurance and bonding costs, legal fees in drafting the reimbursement agreement, and consultant fees in preparing an area of benefit study.

Local jurisdictions frequently refuse to pay the subdivider interest for the time between construction of the improvement and reimbursement. However, the Subdivision Map Act clearly requires a reimbursement agreement to include interest.

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## Assuring Collection of Reimbursement

A reimbursement agreement should establish the procedures the local government will follow to collect reimbursement from benefited property on behalf of the subdivider. The local government should commit to begin collecting the reimbursement assessments immediately after the reimbursement agreement. If reimbursement assessments are collected before the subdivider constructs the enlarged facility, the money should be maintained in a separate account. In such an enviable case, whether partial reimbursement will be paid to the subdivider throughout construction of the improvement should be considered.

Generally, a residential subdivision cannot be required to pay development fees for the construction of public improvements until the final inspection or certificate of occupancy. However, development fees may be collected earlier if they are to reimburse expenditures already made. A reimbursement agreement should obligate the local government to collect the reimbursement charges at the time the first discretionary or ministerial permit is granted to a benefited property.

Finally, the term of the reimbursement agreement should be as long as possible in order to capture reimbursement from benefited property that is not promptly developed. Local governments typically insist that reimbursement agreement expire after a number of years (typically ten), after which the subdivider loses any remaining reimbursable costs. There is no legal basis for limiting the life of reimbursement agreements, and short terms represent a windfall to the benefited property owners.

## Public Contracting Requirements

Local governments frequently include provisions in reimbursement agreements requiring the subdivider to competitively bid contracts and to pay prevailing wages for construction of the enlarged improvement. Such provisions should be resisted. Reimbursement agreements should neither expand nor narrow the competitive bidding and/or payment of prevailing wages otherwise required by law.

By way of background, state law requires the payment of prevailing wages on "public works" contracts. Although there is no judicial authority on the issue yet, a 1986 opinion of the California Attorney General did conclude that a private developer must pay prevailing wages when constructing facilities pursuant to a development contract with a public entity that retained the public entity's control over the construction and obligated the developer to convey the completed facilities to the public entity. Thus, even without an express provision in a reimbursement agreement, a subdivider constructing an enlarged improvement pursuant to a reimbursement agreement may be required to pay prevailing wages. A subdivider who wants to minimize the risk of being required to pay prevailing wages may want to include a statement that the reimbursement agreement gives the local jurisdiction no greater right to approve the design and specifications for the improvement or to inspect the improvement during the construction process than it would have had the improvements not been required to be oversized so as to necessitate the reimbursement agreement.

State law also requires that contracts by public entities for public projects be competitively bid. The party awarding the contract, not the source of the funds, is determinative of whether competitive bidding is required. That is, a developer is not subject to competitive bidding requirements in awarding contracts for the construction of public improvements merely because the cost of the facilities may be reimbursed by the public entity at a later date. Thus, a reimbursement agreement should not impose competitive bidding requirements since they would not otherwise apply.

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