
OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Item #: 202

Mills Act Program Reforms and Cost Recovery Fees

OVERVIEW

On Monday, November 24, 2008 the City Council will be asked to approve amendments to the Land Development Code and Council Policy 700-46 “Mills Act Agreements for Preservation of Historic Property,” to reform the City’s Mills Act Program. The City Council is also asked to implement cost recovery fees for the administration of the program.

The Mills Act was enacted in 1972 by the State of California to enable local governments to enter into contracts with owners of qualified historic properties who actively participate in the restoration and maintenance of their historic properties while receiving property tax relief. The State of California’s Office of Historic Preservation identifies the benefits to the local government of having a Mills Act program as the “conserving of resources and reinvestment as well as the important role historic preservation can play in revitalizing older areas, creating cultural tourism, building civic pride, and retaining the sense of place and continuity with the community’s past.” Mills Act contracts are between the property owner and the local government granting the tax abatement. Each local government establishes their own criteria and determines how many contracts they will allow in their jurisdiction.

In 1995 the City of San Diego established a Mills Act program. In their November 18, 2008 (Report # 08-176) report to the City Council, staff states that the current program is “Very informal” and “Only a limited number of agreements include additional preservation or rehabilitation requirements and there is no requirement that the tax savings realized through this program be invested in the historic property.” Staff also states that “There is no formal inspection schedule or monitoring of agreements for

compliance with the contract requirements.” Over the last two years there has been a desire by the Mayor and the City Council to review the current program to ensure its effectiveness and to propose a cost recovery fee proposal. In addition, the effectiveness of the City’s Mills Act program has recently come under scrutiny from the San Diego County Grand Jury.

The City of San Diego currently has 901 Mills Act contracts resulting in an annual reduction of \$1.1 million in property tax revenue. As pointed out by the San Diego County Grand Jury, the City San Diego has substantially more Mills Act contracts when compared to other California jurisdictions.

FISCAL/POLICY DISCUSSION

The reform of the City’s Mills Act program can be simplified into one overarching question - How does the City balance protecting our historical properties while limiting the fiscal impact to the General Fund? It is the opinion of the IBA that staff has proposed sensible modifications to the Mills Act program that addresses this question. The modifications proposed by staff include:

- Requiring a formal application process with a set deadline;
- Establish an inspection schedule for monitoring Mills Act properties;
- Establish a fiscal threshold for tax revenue reduction to the General Fund;
- And establish a cost-recovery fee.

The following sections provide comments, additional information, and recommendations that our office has on the staff’s recommendations.

Staffing for the City’s Historical Resources Section

For the proposed reforms to the City’s Mills Act program to be successful, adequate staffing in the Historical Resources Section is essential. The following chart details staffing levels for the City’s Historical Resources Section over the last four fiscal years:

Fiscal Year	Staff
2006	1.00 Senior Planner 1.75 Senior Planner “borrowed” from Community Planning. 1.00 Associate Planner Total Staff: 3.75
2007	2.00 Senior Planner 1.75 Senior Planner “borrowed” from Community Planning. 1.00 Senior Clerk Typist Total Staff: 4.75
2008	2.00 Senior Planner 1.75 Senior Planner “borrowed” from Community Planning. 1.00 Senior Clerk Typist Total Staff: 4.75
2009	3.75 Senior Planner 1.00 Senior Clerk Typist Total Staff: 4.75

Staff has indicated that if the proposed reforms are approved they will expect to complete an average of 200 inspections per year and process 3-6 applications per month or an estimated 50 per year. They have also stated that the existing staffing levels should allow them to meet their goals. However, some delays could occur due to the impacts of reductions to the City Planning and Community Investment Department that have been proposed to help solve the City’s Fiscal Year 2009 budget deficit. These reductions include a cut of (\$200,000) to the Uptown Cluster Community Plan Update. Prior to the proposed reduction, the department was expecting to hire consultants to help with various components of the Uptown Cluster Community Plan Update. If the reduction is approved, the Historical Resources Section will assume some of the responsibilities for completing the Uptown Cluster Community Plan. ***It is important to note that if staff is reduced from the Historical Resources Section, the effectiveness of the reforms and the program will be severely impacted.***

Cost Recovery Fee Proposal

Currently the City of San Diego charges a maximum fee of \$400 to process a Mills Act Program Agreement and no fee for the processing of historical designation nominations. As pointed out by staff in their November 18, 2008 (Report # 08-176) report, the majority of the City’s cost to process Mills Act applications and historical designation nominations is absorbed by the General Fund. To ensure cost recovery of the program, staff has proposed the implementation of the following fee schedule:

Fee Description	Fee Amount
Individual Historical Resource Nomination Fee (To be paid upon submittal of nomination)	\$1,185
Mills Act Program Agreement Fee (To be paid at the time of request for a Mills Act Program Agreement following the historic designation)	\$590
Mills Act Monitoring Fee (To be paid upon submittal of a signed and notarized Mills Act Program Agreement)	\$492

Staff has developed the proposed fee amounts based on the tasks associated to complete the designation, agreement, and monitoring. When developing the fees, staff factored in the fully loaded salary amounts for the positions responsible for each task and the time associated with each project. Staff provided the IBA with their back up information for our review and we concur with the methodology that they used to develop the fees. It should be noted that the proposed fees are based on current salary data. In the resolution before Council, staff has requested the authority to adjust the Fee Schedule from time-to-time to recover increases in the administrative costs of the program.

Other alternative fee proposals have been reviewed by staff and our office. In a July 21, 2005 letter from The Save Our Heritage Organisation, they proposed a graduated processing fee of \$200 per \$100,000 of assessed value of the home with a cap of \$3,000. The IBA has reviewed this method but felt that depending on the assessed valuation of the home, the fees collected would not cover the costs to administer the program and for some homeowners they would end up paying more than what is cost recoverable. It is also important to note that the City’s Administrative Regulation on fees (Administrative Regulation 95.25 – “Processing new and revised fees and charges for current services,”) states that the policy on fees is to **recover the cost** of providing certain services.

Finally, it should be pointed out that the proposed fee policy does not factor in an economic hardship waiver for those that cannot afford to pay the fees. Although the Mills Act Program is voluntary, it is the opinion of the IBA that homeowners who qualify and are willing to adhere to the program guidelines should be given the opportunity to participate regardless of their ability to pay the fee. Staff has indicated that because the program is voluntary, they do not have statistics on homeowners who would like to participate in the program but are precluded from doing so because of financial constraints. However, they estimate that the number is a small percent of the overall applications. Although not included in their formal proposal to the City Council, staff does discuss a possible option to incorporate an economic hardship waiver for property owners that can satisfactorily demonstrate that their annual income is less than the Area Median Income. If the homeowner qualifies, all fees would be waived. If the fees were waived, the General Fund would assume the costs for these homes. ***The IBA supports the inclusion of an economic hardship waiver in the updated City Council Policy. If***

an economic hardship waiver is approved by the City Council, the IBA recommends that staff reports on the number of economic hardship waivers granted annually.

Annual Threshold

As staff points out in their November 18, 2008 report, the City currently experiences an annual reduction of \$1.1 million in Property Tax Revenue related to Mills Act agreements. Based on the need to manage the fiscal impacts of the program to the City's General Fund, staff is proposing to implement an annual threshold amount of \$100,000 in additional Property Tax reductions from the approval of new Mills Act agreements. The IBA supports the implementation of a threshold. The implementation of a threshold will put into place a process where the City Council is annually informed of the impacts of new Mills Act agreements and can choose to increase the threshold based on the financial condition of the City. The IBA does offer the following suggestions and changes to the threshold implementation language included in the strike-out version of City Council Policy 700-46.

IMPLEMENTATION

Proposed Language

E) Exceeding the Threshold: If in any calendar year, the projected reduction in property tax revenue to the City from Mills Act Agreement applications exceeds \$100,000, the City Manager or designee shall present those applications to the City Council as part of that year budget process. The City Council may authorize the processing of Mills Act Agreements exceeding the \$100,000 threshold by making a finding that the fiscal health of the City is such that additional reduction in tax revenue can be supported by the budget.

If in any calendar year, the projected reduction in property tax revenue to the City from Mills Act Agreement applications exceeds \$100,000, and the City Council does not make a finding to authorize the processing of those Agreements, the property owner may choose to apply for an Agreement in a subsequent year.

It concerns the IBA that the "Exceeding the Threshold" language proposed by staff confuses calendar year with fiscal year. The City's fiscal year runs from July 1st to June 30th and transcends multiple calendar years. The calculation of the impact to the General Fund should be based on fiscal year and not calendar year to be consistent with the City's annual budget process. In addition, the IBA is concerned that once the \$100,000 threshold is reached, the City Council will be asked to approve the *applications* that are over the threshold and not just an increase to the threshold. The IBA believes that the intent should be for the City Council to approve increasing the threshold, not specific applications. The proposed process for applications that are submitted after the threshold could result in applicants being treated differently. The proposed language states that the property owner may choose to apply for an Agreement in a subsequent year but does not state if they have to pay additional fees. It seems unfair that an applicant would have to re-apply because they are over the City's threshold. The IBA believes if the Council does not approve an increase to the threshold, then applications that have already been

submitted should be rolled over to the next fiscal year. Based on these concerns the IBA offers the following suggestions to clarify the proposed language:

E) Exceeding the Threshold: If in any ~~calendar year~~ **Fiscal Year**, the projected reduction in property tax revenue to the City from Mills Act Agreement applications exceeds \$100,000, the City Manager or designee shall ~~present those applications to the City Council as part of that year budget process~~ **seek Council authorization to exceed the threshold.** The City Council may authorize the processing of Mills Act Agreements exceeding the \$100,000 threshold by making a finding that the fiscal health of the City is such that additional reduction in tax revenue can be supported by the budget.

If in any ~~calendar year~~ **Fiscal Year**, the projected reduction in property tax revenue to the City from Mills Act Agreement applications exceeds \$100,000, and the City Council does not make a finding to authorize the processing of those Agreements, the property ~~owner may choose to apply for an Agreement in a subsequent year.~~ **owner's application will be rolled over to the next Fiscal Year.**

CONCLUSION

Overall the IBA supports the proposed reforms to the City's Mills Act program. The reforms proposed by staff balance protecting our historical properties while limiting the fiscal impact to the General Fund. The IBA does recommend the following:

- *The inclusion of an economic hardship waiver in the updated City Council Policy. If an economic hardship waiver is approved by the City Council, the IBA recommends that staff reports on the number of economic hardship waivers granted annually.*
- *Recommend language changes to the modifications to Council Policy 700-46 as proposed by staff and discussed in the Annual Threshold Section of this report.*

[SIGNED]

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APPROVED: Andrea Tevlin
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