KRONICK MOSKOVITZ TIEDEMANN & GIRARD
A PROFESSIONAL CORPORATION

#14

TO: Honorable Chair and Members of the Board of Supervisors, El Dorado County
CC: County Administrative Officer; Auditor-Controller
FROM: Jonathan Cristy
DATE: August 5, 2010
RE: Agenda Date: August 10
Tax Refund Claim Filed by Serrano Associates LLC

INTRODUCTION.

On August 17, 2009, the Board received from Serrano Associates LLC ("Serrano") a claim for refund of an unspecified amount of special taxes paid with respect to their property located in the County's Community Facilities District No. 1992-1 (El Dorado Hills) (the "CFD").

Serrano has asserted that the County made several errors in the calculation of Annual Costs under the Rate and Method of Apportionment ("RMA") for the CFD and in the interpretation of the Indenture under which the two series of special tax bonds currently outstanding, Series 1999 and Series 2004, were issued for the CFD.

The asserted errors have been described in letters dated September 30, 2009, and December 31, 2009, from Mike Cook of Hefner, Stark & Marois; in a letter dated July 15, 2010, from John Murphy of Stradling Yocca Carlson & Rauth; and in testimony presented to the Board in a hearing held on July 20, 2010. I have set out the asserted errors below, along with my analysis of each one.

Critical to the analysis of these asserted errors is the definition of the term 'Annual Costs' in the RMA, which I have set forth in full in a table (with my annotations) at page 12 of this memorandum.

(Serrano has also raised the tangential issue of the Board's discretion to levy taxes in the future in amounts less than the maximum allowed under the RMA. I have addressed that issue in a postscript on page 14.)

SUMMARY RECOMMENDATION.

The Auditor has made certain refunds based on the original claim. Except for those already satisfied portions of the claim, I recommend that the Board deny the claim.

SUMMARY OF ANALYSIS OF SERRANO'S CLAIMS OF ERROR IN THE TAX LEVY.

The following is a summary of my conclusions on the individual legal issues raised by Serrano. The quotations in the summary below are from the correspondence received from Serrano's attorneys.

1. Reserve Account Earnings.

Serrano's Assertion: The County has failed "to properly credit interest earnings against Annual Costs." "Years 2004-2005 and subsequent reflect no interest earnings on the Reserve Account."

Short Response: The failure to credit Reserve Account earnings was an error and has been corrected. Any claim reaching back more than four years from the date of payment is barred by Revenue and Taxation Code section 5097.

2. Reserve Requirement.

Serrano's Assertion: The Reserve Account is overfunded because the County interpreted the Reserve Requirement to be "the sum of maximum annual debt service on the Series 1999 Bonds plus maximum annual debt service on the Series 2004 Bonds," while it should be "combined maximum annual debt service on the Bonds."

Short Response: The Reserve Account is overfunded for the reason asserted by Serrano. The excess amount was funded from (i) investment earnings on the Reserve Account and (ii) from a transfer of available special tax revenues into the Reserve Account. The County did not increase Serrano's taxes for the purpose of funding the Reserve Account. An amount equal to the amount of the earnings allocable to Serrano has been refunded to them. None of the rest of the excess is owed to Serrano.

3. Administrative Expenses.

Serrano's Assertion: "The County appears to have failed to transfer monies from the CFD Fund to cover the ensuing years' expenses in every year. Had the County transferred the necessary funds, the Annual Cost calculation would have been reduced by a corresponding amount …."

Short Response: No, it would not have been so reduced. The definition of "Annual Costs" in the RMA includes the gross amount of annual expenses. It provides no credit for balances in the Expense Account or any other amounts available in the CFD Fund.

4. Redemption Account Earnings.

Serrano's Assertion: The County has failed to credit earnings on the Redemption Account against Annual Costs. Under the definition of Debt Service, such earnings are 'applicable credits' that reduce the amount of Debt Service and, thereby, lower Annual Costs.

Short Response: The definition of Annual Costs specifically includes the earnings on only the Reserve Account. The phrase 'applicable credits' in the definition of Debt Service refers to sources of funds that directly offset Debt Service, such as capitalized interest, which can only be used for Debt Service.

5. Delinquent Taxes.

Serrano's Assertion: "[T]he County fails to account for the ultimate collection of delinquent taxes in calculating the annual cost for subsequent years."

Short Response: Yes, and properly so. Nothing in the definition of Annual Costs in the RMA (or anywhere else in the RMA) provides for giving a credit against Annual Costs for delinquent taxes that are later collected. Such late-paid taxes are neither 'reimbursements' under the definition of Annual Costs nor 'applicable credits' under the definition of Debt Service.

6. Large Surpluses.

Serrano's Assertion: "[T]he fact that the special tax levies have been excessive is demonstrated very dramatically by the accumulated surplus …." The "massive accumulation of surplus revenues [in the CFD accounts] is the result of at least four errors in the administration of the financial affairs of the CFD …." "[T]his result never would have been intended by the parties who approved the RMA at the time the CFD was formed." Not accounting for later-collected delinquent taxes "is obviously irrational and inequitable."

Short Response: In addition to asserting particular errors, Serrano also asserts that the unintended surplus speaks for itself and evidences both errors and inequity. The surplus actually evidences the absence of a requirement in the RMA to deduct later-collected delinquencies from Annual Costs. Equity cannot be the basis for a refund of validly collected taxes.

DISCUSSION

1. Reserve Account Earnings.

The calculation of Annual Costs in the RMA includes a deduction for "any credit from earnings on the reserve fund" (shown in item (iv) of the definition). Serrano notes that in Fiscal Year 2004-05 and following years no interest earnings on the Reserve Account were credited against Annual Costs. The issue here arose following the issuance of the Series 2004 Bonds in May 2004.

Based on an erroneous interpretation of 'Reserve Requirement' as the sum of the maximum amounts of debt service for each series of bonds taken separately, the County Auditor concluded that, as of June 30, 2004, there was a deficit of $277,431.57 in the Reserve Account. No credit for earnings on the Reserve Account was provided in the calculation of Annual Costs starting in Fiscal Year 2004-05 because of that deficit.

When there is a deficit in the Reserve Account, Annual Costs are supposed to be increased by the amount needed to replenish it. The County did not do that. Instead, the County gradually increased the balance in the Reserve Account by accumulating in the Reserve Account the investment earnings on the account. The deficit was resolved in Fiscal Year 2008-09 when there was a large inflow of taxes levied because of the high anticipated delinquency factor used in the calculation of Annual Costs.

Serrano has acknowledged that the County Auditor has refunded approximately $582,000 to Serrano to correct this error. That amount represents earnings going back to Fiscal Year 2005-06. Serrano asserts that another approximately $51,000 should be refunded, which represents earnings from Fiscal Year 2004-05.

Timeliness of Claim. Serrano's claim states that it is filed pursuant to Revenue and Taxation Code section 5096, which provides (in relevant part) that: "Any taxes paid before or after delinquency shall be refunded if they were: … (c) Illegally assessed or levied …."

Revenue and Taxation Code section 5097 provides (in relevant part) that: "(a) No order for a refund under this article shall be made, except on a claim … (2) … filed within four years after making the payment sought to be refunded, or within one year after the mailing of notice as prescribed in Section 2635, … whichever is later." [emphasis added][1]

The claim was filed in August 2009; so, if four years is as far as they can reach back, the earliest payment that would be eligible for refund is the first installment of the 2005-06 tax year (payable November 1, 2005).

Serrano asserts, however, that Revenue and Taxation Code section 2635 operates to extend the time for filing a claim for refund. Section 2635 provides (in full) that: "When the amount of taxes paid exceeds the amount due by more than ten dollars ($10), the tax collector shall send notice of the overpayment to the taxpayer. The notice shall be mailed to the taxpayer's last known address and shall state the amount of overpayment and that a refund claim may be filed pursuant to Chapter 5 (commencing with Section 5096) of Part 9." [emphasis added] (Note also that the tax collector has the duty to send such notices, rather than the auditor.)

Serrano relies on Bunker v. County of Orange (2002) 103 Cal.App.4th 542 ("Bunker") for the proposition that "if the notice required by Section 2635 is never sent, 'the statute of limitations on making a refund claim never runs.'" Serrano fails to note a critical statement in the opinion: "Section 2635….triggers [a] required notice when a taxpayer has paid more taxes than he or she should pay as reflected on the assessment roll." Bunker, at p. 549 [emphasis added].

Serrano did not pay more than what was reflected on the assessment roll. For that reason, the tax collector did not and does not have a duty to send a notice under Section 2635 to Serrano. The court in Bishop, McIntosh & McIntosh v. Molmen (1981) 116 Cal.App.3d 278, 282-283, said: "Since a tax collector does not exercise independent judgment or discretion with respect to the legality or propriety of particular assessment, the Legislature could hardly have intended to vest that office with broad discretion in evaluating prospective claims for the purpose of deciding whether to send a section 2635 notice. The fact that section 2635 imposes such a duty upon the

[1] Serrano refers to the four-year time limit as a "statute of limitations" and additionally requests that the Board waive it. Actually, this section functions differently than a statute of limitations. The deadline for commencement of a civil action (the limitation in a statute of limitations), which, if missed, may be asserted as a defense to the action by the defendant, may be waived by agreement of the parties. In Section 5097, however, the Legislature has forbidden the Board to make any refunds based on stale claims, and no 'waiver' is permitted.

tax collector only *where his records show* the potential for a claim within the scope of that section evidences a legislative intent to limit the tax collector duties in this regard.") [Emphasis in original.]

The Legislature confirmed that opinion expressed by the court in Bishop by adopting Chapter 1224 of the Statutes of 1983, in which it revised the language of Section 2635 from:

> "The tax collector shall give notice … where his records show that … taxes might have been … erroneously or illegally collected …"

to: "When the amount of taxes paid exceeds the amount due … the tax collector shall send notice …."

And the court in Bunker, writing in 2002, retained the interpretation that the tax collector's duty is based only on what is reflected in the assessment roll, i.e., what his records show.

Serrano's claim is filed too late to allow any additional refund of Reserve Account earnings.

2. Reserve Requirement.

Section 3.6 of the original Indenture, which was entered into at the time of the issuance of the Series 1999 Bonds, defines the amount that is to be maintained in the Reserve Account – the "Reserve Requirement" – as "an amount equal to the lesser of ten [percent] (10%) of the original principal amount of the Bonds, one-hundred percent (100%) of maximum annual debt service on the Bonds, or one-hundred and twenty-five percent (125%) of average annual debt service on the Bonds as determined and specified by the County." The least of these three quantities has always been the second one in the list – 100% of maximum annual debt service.

The original Indenture defines the term "the Bonds" to mean the Series 1999 Bonds. The First Supplemental Indenture, entered into in May 2004 at the time of the issuance of the Series 2004 Bonds, states in Section 10.03 that "the term 'Bonds' as used in the Original Indenture shall, unless the context requires otherwise, include the Series 2004 Bonds."

The question is whether the Reserve Requirement is (1) maximum annual debt service on the Series 1999 Bonds plus maximum annual debt service on the Series 2004 Bonds or (2) the maximum of the combined annual debt service on the Series 1999 Bonds and the Series 2004 Bonds. [Mathematically: (1) Max (ds1999) + Max (ds2004) or (2) Max (ds1999 + ds2004)]

Section 11.03, added to the Indenture by the First Supplement, recites that proceeds of the sale of the Series 2004 Bonds in the amount of $1,328,724.83, "representing the increase in the Reserve Requirement as a result of the issuance the Series 2004 Bonds," will be deposited into the Reserve Account. The County Auditor's records indicate that the balance in the Reserve Account as of June 30, 2004, soon after the issuance of the Series 2004 Bonds, was $4,637,962.18, which is approximately maximum annual debt service on the two series on a combined basis. Thus, Section 11.03 implies that the Reserve Requirement is to be calculated

based on the maximum of the combined debt service rather than the sum of the maximum amounts for each series.

The Reserve Account is overfunded by approximately $273,000 for the reason asserted by Serrano. The excess amount was deposited into the Reserve Account from two sources: (i) investment earnings on the Reserve Account that were accumulated therein and (ii) a transfer of available special tax revenue. The special tax revenue deposited into the Reserve Account did not come from any additional special taxes levied specifically for the purpose of funding the Reserve Account, so that amount is not the product of unauthorized taxation and is not owed to Serrano. An amount equal to the amount of the earnings allocable to Serrano has already been refunded to them, and, therefore, no additional refund is warranted.

Section 3.4 of the Indenture provides that excess amounts in the Reserve Account on the last business day of March will be transferred to the Special Tax Fund. If not needed to pay debt service on the bonds, these excess amounts will be deposited into the Facilities Account and may be used to redeem bonds (or for any of the other permitted uses of that account).

3. Administrative Expenses.

In his September 30, 2009, letter, quoting from Section 3.8 of the Indenture, Mike Cook says that "the County is obligated to 'disperse monies in the CFD Fund, as received and as needed … to the Expense Account to the extent necessary to replenish the Expense Account to the amount budgeted for annual expenses for the new fiscal year.'"

It is correct that Section 3.8 provides that the money deposited into the Expense Account comes out of the CFD Fund "from the funds transferred to the County by the Fiscal Agent from the Special Tax Fund." But those amounts, which are transferred each year on September 15, represent the amount of taxes that remain after the bond debt service in the prior year has been satisfied. And some of that remaining amount is generated by the amount that was budgeted for annual expenses and included in Annual Costs. (See the flowchart attached at page 13 of this memorandum, which shows the flow of tax revenues through the funds and accounts established by the Indenture.)

A full year's budgeted expenses are to be included in the Annual Costs (see item (ii) in the definition of Annual Costs). The RMA provides no credit against that amount for balances in the Expense Account or any other amounts that might show up in the CFD Fund (such as surpluses generated by taxes collected in anticipation of delinquencies). Nonetheless, the County actually credited $84,504.15 (the budgeted administrative costs) from amounts available in the CFD Fund against the Fiscal Year 2009-10 Annual Costs.[2]

Serrano's attorneys have not mentioned this asserted error in their most recent written and oral statements, so I assume that they have abandoned it. In any event, no refund is warranted on this basis.

[2] This credit was misleadingly labeled "Redemption Fund credit" in the tax levy worksheet prepared by the CFD administrator, NBS. That label may have prompted the assertion that Redemption Account earnings should be credited against Annual Costs.

4. Redemption Account Earnings.

The RMA defines the term "Debt Service" as follows: "Debt Service" means for each Fiscal Year or Bond Year, the total amount of principal and interest for any bonds, notes or certificates of participation of the CFD during that Fiscal Year, less any applicable credits that may be available from any other sources available to the County to pay principal and interest for the previous or current Fiscal Year or Bond Year." [emphasis added]

In his July 15 letter, John Murphy suggests that earnings on the Redemption Account are 'applicable credits' under the definition of Debt Service and, so, incorporated into the Annual Costs computation. He notes that the Indenture requires the earnings on the Redemption Account be deposited into the Special Tax Fund,[3] which makes them available to pay debt service.

These earnings are not a mandatory credit against Annual Costs. The definition of Annual Costs specifically includes a credit for earnings only on the Reserve Account. Those earnings are also deposited into the Special Tax Fund (so, mere availability for debt service is not a persuasive argument). A similar credit for Redemption Account earnings, or earnings on any other account, could have easily been explicitly included in Annual Costs in the RMA, but it was not.

The phrase 'applicable credits' must be given some meaning in interpreting the definition of Debt Service in the RMA. After all, the deduction from Debt Service does not read: "less any money that may be available." The logical candidates for 'applicable credits' are capitalized interest (interest funded from bond proceeds) and money in a defeasance escrow (funded from the proceeds of refunding bonds). Both of those sources of funds may only be used for debt service (they are perforce credits against debt service) and they directly offset the amount of scheduled debt service otherwise payable out of special tax collections.

And 'applicable' credits in the definition of Debt Service must mean something different from the types of credits that are listed in the definition of Annual Costs (such as earnings on Indenture accounts), or there would be double-counting of credits.

No refund is warranted on the basis of this asserted error.

5. Later-Collected Delinquent Taxes.

Serrano asserts that the County should take into account the ultimate collection of delinquent taxes in calculating Annual Cost for subsequent years. Item (iv) is the element of the definition of Annual Costs that addresses how actual and anticipated delinquencies are taken into account. Nothing in item (iv) provides for giving a credit against Annual Costs for delinquent taxes that are later collected.

[3] The Indenture has to include this provision, because, under federal income tax regulations, the earnings on this account have to be flushed out (except for a small carryover) at least once each year in order to maintain its status as a "bona fide debt service fund" to exempt the earnings from any rebate requirement.

Legal Argument from the Text of the RMA. In his July 15 letter, John Murphy argues that the phrase "less any reimbursements" in the definition of Annual Costs refers to later-collected delinquent taxes. It does not.

First, the word 'reimburse' means to pay back. When a property owner later pays taxes that are delinquent, he does not pay back the County for something the County had paid. The Revenue and Taxation Code does not use this word to describe late payment; it just uses the word 'pay.'

Second, as noted by John Murphy himself, the term used in the Indenture for later collections is 'reinstatement' – the notion being that the property owner's account is brought current or reinstated to good standing.

Third, note where the phrase 'less any reimbursements' appears in the definition of Annual Costs. It does not appear immediately after the two delinquent tax items (last year's delinquencies and next year's anticipated delinquencies). Instead, two other items intervene. And, most telling, it appears after the phrase 'less credit for applicable development fees.' It appears there because it is not an additional credit (it does not read "less credit for any reimbursements"); instead it is an offset to any credit given for applicable development fees.

"Applicable" development fees must be those that are available to be applied to pay the costs of facilities the CFD is authorized to acquire. This credit is net of the amount of any reimbursements that are made to developers from those same development fees (which are, therefore, not available to the County to pay facility costs). This is the standard way the term 'reimbursement' is used in development mitigation practice – a payment to one developer who constructs more than its share of necessary infrastructure from development fees collected from other developers is called a reimbursement. (See, for example, Government Code sections 66485-7, which require such reimbursements and use the terms 'reimburse' and 'reimbursement.')

(John Murphy also attempts to use the 'any applicable credits' phrase in the definition of Debt Service as a second way of roping in later-collected delinquent taxes. If that phrase is as all-inclusive as he claims, there was no need to have itemized all the credits that appear in the definition of Annual Costs. This secondary argument advanced by John Murphy is also erroneous.)

Non-legal Argument. Attached as Exhibit B to Mike Cook's September 30, 2009, letter are examples of other RMAs that do credit delinquent taxes that have been collected – what those RMAs provide, of course, is irrelevant to the question of what this RMA provides. In Exhibit C to that letter is a flowchart prepared by Economic & Planning Systems (EPS), the authors of the RMA for CFD 1992-1 (El Dorado Hills), that purports to show that such a credit is part of this RMA. It is not. Likewise, the testimony presented by special tax consultants Tim Youmans (of EPS) and David Taussig at the hearing on July 20 that they would have administered this CFD so as to minimize taxes proves nothing about whether the RMA for this CFD authorizes levying taxes in the amounts that were actually levied by the County. Essentially, the argument they made is that the County had discretion to take later-collected

delinquent taxes into account and should have exercised that discretion to achieve a better result. That is not a argument that the County was required by the terms of the RMA to take them into account.

No refund is warranted based on these assertions and arguments.

6. Large Surpluses.

In his July 15 letter, John Murphy makes an over-arching argument that, because large amounts of surplus tax revenues have accumulated and the parties in 1994 never would have intended that such large surpluses would accumulate, something must be wrong. On the contrary, unintended consequences often result from systems designed by mortals. The mere accumulation of surpluses is not proof that any error was made in application of the RMA, i.e., that the County failed to follow the rules and levied more than it was legally entitled to collect. Surpluses may, instead, be evidence that the RMA was defective in not taking into account later-collected delinquent taxes when calculating Annual Costs.

While the absence of a credit for later-collected delinquencies may be a flaw in the RMA, it might be a valuable feature, instead. It provides the potential for larger tax collections that would provide greater security for the bonds.[4] The "excess" amounts collected that are not needed for debt service or administrative expenses flow into the Facilities Account, where they may be used to pay for additional public facilities or to redeem bonds. Regardless of whether it is a flaw or a feature, the RMA simply does not take into account subsequent collection of delinquent taxes.[5]

The possibility of surpluses was anticipated by the Indenture, which provides that accumulated surpluses may be used to redeem bonds. By redeeming bonds, these tax revenues are recognized in a way that will lower future taxes paid by homeowners but may not directly benefit Serrano.

The mere existence of surpluses does not justify any refund.

BOARD'S AUTHORITY TO MAKE REFUNDS.

Correction of Errors. Serrano filed its claim for refund under Revenue and Taxation Code section 5096 and Section 8 of the RMA. Revenue and Taxation Code section 5096 (in relevant part) provides that:

> Any taxes paid before or after delinquency shall be refunded if they were … illegally assessed or levied.

[4] On this point, at the hearing, Supervisor Santiago inquired about John Murphy's statement that maintaining some amount of surplus would be prudent. When pressed, he ventured a figure of $2-300,000 as a prudent buffer, thereby implying that generating some amount of "excess" must be appropriate.

[5] More recent RMAs prepared by Economic & Planning Systems have added the sentence: "Collections from prior delinquencies should be used to offset the amount needed for current and future delinquencies if available." Even that is not a requirement to use them for that purpose.

Section 8 of the RMA (in relevant part) provides:

> Any taxpayer who feels the amount of Special Tax assigned to a Parcel is in error may file a notice with the County appealing the levy of the Special Tax. … If the County verifies that the tax should be modified or changed, a recommendation at that time will be made to the Board and, as appropriate, the Special Tax levy shall be corrected and, if applicable in any case, a refund shall be granted. [emphasis added]

Both provisions empower the Board only to correct illegalities or errors in the application of the RMA, i.e., failures to follow the rules that result in more taxes being levied than the County was legally entitled to collect.

With the exception of the failure to apply some earnings on the Reserve Account as a credit against Annual Costs and the use of stale delinquency data in two years (both of which the Auditor has corrected), the County has correctly calculated the Annual Costs and has legally and correctly levied the special tax. Thus the Board does not have legal authority under the Revenue and Taxation Code or the RMA to make further refunds to Serrano.

Board's Power to Interpret the RMA. In his July 15 letter, John Murphy urges the Board to exercise its interpretive authority under the second paragraph of Section 8 of the RMA to adopt his proposed interpretations of the RMA and apply them retroactively to provide a basis for the requested refunds. The paragraph in question provides:

> Interpretations may be made by Resolution of the Board for purposes of clarifying any vagueness or ambiguity as it relates to the Special Tax rate, the method of apportionment, the classification of properties or any definition applicable to the CFD.

The arguments advanced by John Murphy in connection with the two asserted errors still in contention – the asserted failures to credit Redemption Account earnings and to take into account later-collected delinquent taxes – do not demonstrate any ambiguity or vagueness that needs clarification, as I have argued above in Parts 4 and 5 under the heading "Discussion." Instead, his arguments urge unnatural readings of the definitions in the RMA, which amount to revisions.

Although this paragraph is lodged under the heading "Appeals" in the RMA[6], which would suggest that the interpretive power may be applied when considering whether the tax was correctly applied in the past, its retrospective application to revise the RMA is invalid on the ground that it violates the constitutional prohibition against making a gift of public funds. As stated by the Supreme Court in Estate of Skinker (1956) 47 Cal.2d 290, 296: "The Legislature cannot by a subsequent act increase or decrease the rate, remit the tax or in any way surrender, impair or limit rights that have become fixed. [Citations] Where a tax has become due, a subsequent act of the Legislature reducing the tax by reason of the change in exemptions, tax

[6] Other special tax consultants do not include an "Appeals" section in their RMAs, leaving that to the ordinance that first levies the tax, but do include a provision authorizing the governing board to clarify ambiguities prospectively.

rates, or for that matter in any way, is held to be a gift of state monies and is prohibited by article IV, section 31 [now article XVI, section 6], of the California Constitution."

These prohibitions apply equally to the Board, so no refund may be based on a retroactive revision of the RMA.

BOARD'S AUTHORITY TO REBATE TAXES VALIDLY COLLECTED.

The legal arguments advanced by Serrano on the remaining items in contention are not valid. If there were some validity to their claims, the County could enter into a settlement agreement with Serrano.

"[T]he settlement of a good faith dispute between the State and a private party is an appropriate use of public funds, neither wasteful within the meaning of [Code of Civil Procedure] Section 526a, nor a gift barred by article XVI, section 6 [of the Constitution], because the relinquishment of a colorable legal claim in return for settlement funds paid by the State is good consideration and accomplishes a valid public purpose. … A promise to compromise an invalid or unfounded claim, however, is not valuable consideration." Orange County Foundation v. Irvine Co. (1983) 139 Cal.App.3d 195, 200, 201.

In addition to its legal arguments, Serrano has made an appeal based on equity. However, equity provides no basis for justifying a payment made on an invalid legal claim, which would be a gift of public funds. The California Supreme Court had this to say on the subject in Conlin v. Board of Supervisors (1893) 99 Cal. 17, 21-22, 33 P. 753:

> The 'gift' which the legislature is prohibited from making … includes all appropriations of public money for which there is no authority or enforceable claim, or which rest upon some moral or equitable obligation, which in the mind of a generous or even a just individual, dealing with his own moneys, might prompt him to recognize as worthy of some reward. The legislature is to be regarded as holding the public moneys in trust for public purposes, and this limitation of the constitution is directed against its disposal of these funds except in accordance with such purposes. All those moral considerations or demands resting merely upon some equitable consideration or idea of justice … are insufficient as a basis for making an appropriation of public moneys.

RECOMMENDATION.

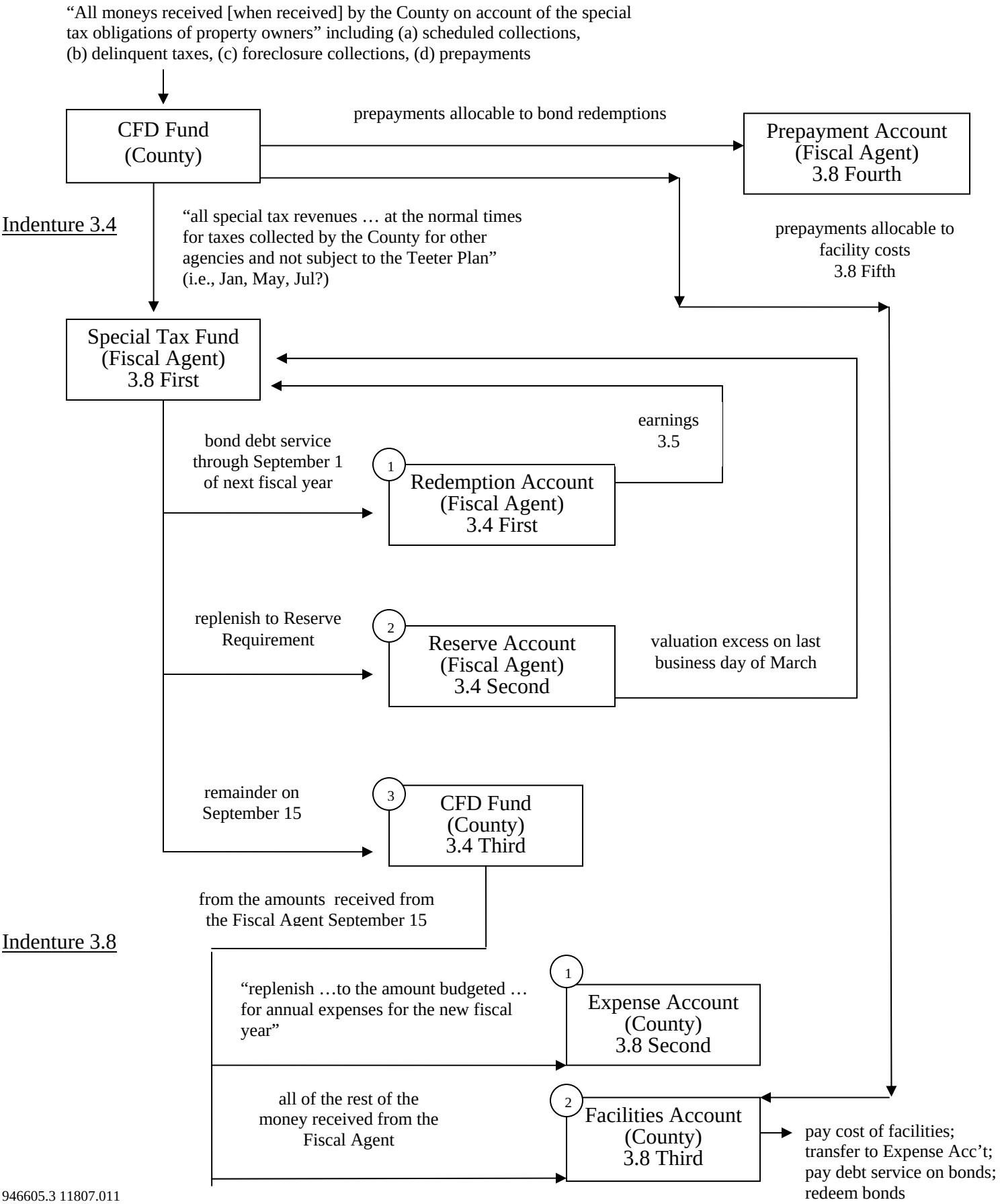
Deny the Claim. As described above, the Auditor has made certain refunds with respect to those elements of the original claim that were valid. Except for those already satisfied portions of the claim, the Board should deny the rest of the claim, because it is without legal foundation and the Board lacks discretion to make a refund on equitable grounds.

Government Code section 23006 provides that "any contract, authorization, allowance, payment, or liability to pay, made or attempted to be made in violation of law, is void, and shall not be the foundation or basis of a claim against the treasury of any county."

definition of Annual Costs from the Rate and Method of Apportionment (RMA)

"**Annual Costs**" means, for any Fiscal Year, the total of	**Notes** (examples from FY 2009-10)
(i) **Debt Service** for the Calendar Year commencing January 1 for such Fiscal Year through December 31 of the following Fiscal Year	Annual Costs for FY 2009-10 would include debt service for Calendar Year 2010, which includes the interest due March 1, 2010, and the principal and interest due September 1, 2010
[Note: **"Debt Service"** is itself defined in the RMA as scheduled payments "less any applicable credits that may be available from any other sources available to the County to pay principal and interest"]	["Applicable" credits must mean something different from the types of credits that are listed in the definition of Annual Costs, or there would be double-counting. This phrase refers to money in a capitalized interest account or a defeasance escrow, which are directly related (applicable) to debt service.]
(ii) **Administrative Expenses** for such Fiscal Year	This element of the Annual Cost calculation is not stated to be net of any existing balance in the Expense Account as of July 1
(iii) Any amounts needed to replenish any **bond reserve fund** for bonds of the District issued for the CFD to the level required under the documents pursuant to which such bonds were issued	The required level is "maximum annual debt service on the Bonds" (Indenture §3.6). Based on the statement in Section §11.03 of the First Supplement, the required level is the maximum of the combined debt service, i.e., Max (ds1999 + ds2004).
(iv) An amount equal to [1] the amount of **delinquencies** in payments of Special Taxes levied in the previous Fiscal Year **and** [2] an amount for anticipated **delinquencies** for the current Fiscal Year	The NBS materials show this as the "reserve for delinquencies." However, it is deposited into the CFD Fund with other taxes and not into a reserve fund. If not needed for debt service, it winds up in the Facilities Account. No credit is given against these amounts for delinquent taxes actually collected.
less any credit from **earnings** on the reserve fund	"any credit" suggests this might be optional, but it was read pre-2004 as "any earnings"; estimated earnings for FY 2009-10 based on actual earnings from FY 2008-09
less credit for applicable **development fees**, less any **reimbursements**	"Applicable fees" are those collected in FY 2008-09 and available for facility costs, which would offset the amount needed for pay-as-you-go expenditures in (v) below. The amount of the credit for developer fees is net of any reimbursements made by the County to developers from those fees.
less any funds available from **prepaid Special Taxes** as prescribed in Section 7	One component of prepaid Special Taxes is used to redeem bonds – this would offset the amount needed for debt service in (i) above. The other component is retained to be used to pay facility costs – this would offset the amount needed for pay-as-you-go expenditures in (v) below.
(v) **Pay-as-you-go expenditures** for authorized facilities to be constructed or acquired by the CFD	As determined by the County for FY 2009-10

Indenture 3.8



OTHER ISSUE RAISED AT HEARING.

Serrano raised an issue tangential to their claim for refund at the hearing on July 20. Serrano requested that the Board exercise its discretion to levy taxes in amounts less than the maximum allowed under the RMA. The following is an analysis of the extent of the Board's discretion with respect to future tax levy amounts.

Board's Authority to Lower Taxes in Future Years.

Government Code section 53340 provides, in pertinent part:

> (a) After a community facilities district has been created and authorized to levy specified special taxes pursuant to Article 2 (commencing with Section 53318) [or] Article 3 (commencing with Section 53330) …, the legislative body may, by ordinance, levy the special taxes at the rate and apportion them in the manner specified in the resolution adopted pursuant to Article 2 (commencing with Section 53318) [or] Article 3 (commencing with Section 53330).
>
> (b) The legislative body may provide, by resolution, for the levy of the special tax in the current tax year or future tax years at the same rate or at a lower rate than the rate provided by the ordinance ….

The Board, in Ordinance No. 4648, adopted May 4, 2004, provided:

> a special tax is hereby levied on all taxable parcels within the [CFD] for the 2004-2005 fiscal year and for all subsequent fiscal years in the amount of the maximum authorized tax, provided that this amount may be adjusted annually, subject to the maximum authorized special tax limit, by resolution of this Board.

The RMA represents the special taxes specified in a resolution adopted pursuant to Article 3 (commencing with Section 53330). The RMA specifies the tax to be levied by describing a process of calculating Annual Costs and then apportioning them among the parcels in the CFD by formula. The Ordinance (as authorized by Section 53340(b)) authorizes the Board to adopt resolutions that levy the tax at amounts lower than those that would be produced by application of the tax formula.

Section 5.3 of the Indenture establishes a minimum tax rate. The County promises the bondholders that it will levy taxes that will be sufficient, after making a reasonable allowance for delinquencies, to pay debt service, pay administrative expenses, cure actual or anticipated debt service delinquencies, and replenish the Reserve Account.

Government Code section 53340 permits the County to levy the special taxes in any year in an amount less than the amount authorized by the Ordinance. So, in future years, the County will have the discretion to levy less than the maximum amount permitted by the RMA (and, therefore, totaling less than the full amount of the Annual Costs), as long as what is levied is at least as much as required by the Indenture.

Taxpayers in the CFD do not have the right to require the County to levy the full amount of the Annual Costs. Nothing in the Government Code limits the Board's authority to levy the special taxes at a rate lower than the rate the RMA and Ordinance permit because of the effect of that action on the taxpayers (perhaps on the theory that no one would object to paying less).