Posted on: Sunday, September 16, 2007

Another way to pay for Hawaii infrastructure

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People who buy homes in Hawai'i subdivisions built in the next few years and beyond may be assessed a special tax to help pay for new roads, utilities and schools under a public facilities financing tool being promoted by government officials and pursued by developers.

Financing tool used in California for years could become 'new reality' in Hawai'i by lowering new-home costs.

Gentry Cos. is considering using CFD financing for its Waiawa Ridge project, which includes an upgrade to H-2's Waipi'o interchange.

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The arrangement, called Community Facilities District financing, likely will see its first local test case at a Big Island project called Kamakoa at Waikoloa, though developers of several planned communities around the state are studying or setting up so-called CFDs.

It remains to be seen how much or little the tool ultimately will be used, though some industry observers view it as essential to help provide needed roads, schools and other public facilities without raising general taxes or forcing up prices for new homes.

"We think it's going to become a new reality," said Harry Saunders, operations president of one of the state's oldest and largest housing developers, Castle & Cooke Hawaii.

In one sense, CFDs are a twist on the way subdivision developers now pay for public infrastructure by folding such costs into the price of homes.

According to developers, CFDs can reduce the infrastructure expense passed on to homebuyers, because homeowners pay for the infrastructure over about 25 years or as long as they own the home.

But the tool could result in more costs for public facilities being paid for by homeowners in new communities as opposed to homeowners in existing communities and taxpayers in general.

There also is a concern that homebuyers within CFDs might view the special assessment as a new county tax since counties would collect the payments as an extra item on property tax bills.

The pursuit of CFDs in large part is a result of state and county officials trying to ensure that regional infrastructure is developed concurrently with new neighborhoods, as opposed to past practices that often resulted in inadequate or delayed construction of roads, schools and other public facilities.

Historically, the government funded development of public facilities necessitated by growing communities, relying on the additional tax base generated by more residents to pay for infrastructure such as roads and schools.

In more recent history, however, government has required developers to provide land and/or money for more public facilities, though in some cases troubled projects failed to deliver facilities as required. On the other hand, the state and counties have sometimes cut or delayed its construction projects.

CFDs are a way to accelerate public facility development, but in a way that also more transparently shifts the cost onto homeowners in new communities.

"They're basically user fees," said Gary Painter, associate professor at the University of Southern California's School of Policy, Planning and Development. "People are sort of paying for what they're getting."

USED IN CALIFORNIA

Henry Eng, director of Ho-nolulu's Department of Planning and Permitting, said CFDs are a creative financing mechanism for land development infrastructure needs. "(We) are hopeful that developers will take advantage of this method," he said.

CFDs are not new. California has used them successfully for more than 20 years, after a property tax cap passed in 1978 severely limited the ability of local governments to pay for public facilities.

In Hawai'i, CFDs only became an option in recent years. The state Legislature gave counties the power to create such districts in 1992, leading to county ordinances, including one for Ho-nolulu established in 1996 and modified in 2000.

Under the ordinance, a developer can use a county's power to issue tax-exempt bonds for financing facilities that will be owned and maintained by the government, including roads, parks, schools, libraries, museums, police and fire stations, water and sewer systems, public parking and public transportation.

The bonds are sold to investors and paid off by buyers of homes in the district through a special levy attached to biennial property tax bills. In some cases, commercial property owners in a project also could be assessed.

Developers say paying for public facilities with tax-exempt bonds reduces a project's development cost, a savings that can be passed on to homebuyers. Also, the initial cost of a home is typically lower because public facility costs are paid over about 25 years.

For a hypothetical community of 5,000 homes and $100 million in public facilities, each home cost might be reduced by $20,000.

HOMES SELL FOR LESS

Painter at USC said that in California, homes within CFDs typically sell for less than comparable homes outside CFDs as an adjustment for the extra tax liability. He also said CFD homes aren't as popular with buyers as non-CFD homes, so sale prices are often lower.

One pioneer in Hawai'i working to establish a CFD is developer Gentry Cos., which said the city around 1996 encouraged the company to use the tool for its Waiawa Ridge project envisioned for up to 10,000 homes on 3,700 acres in Central O'ahu.

After nearly eight years of research and planning, Gentry in 2004 applied to establish the first phase of its Waiawa project slated for 5,440 homes as a CFD eligible for up to $150 million in bond financing.

Gentry said the financing arrangement would allow more public infrastructure to be developed earlier in the life of the project, benefiting residents at Waiawa Ridge and neighboring communities.

The company also said a planned sewer trunk line would allow the city to make other connections that would eliminate the need for two existing pump stations for $2 million in city savings, while avoiding the eventual replacement of an existing line for additional city savings of many millions of dollars.

'STILL LOOKING AT IT'

Under Gentry's initial projection, homeowners, depending on a home's size, would pay from $465 to $3,196 annually for about 25 years, with a maximum 2 percent annual increase. The long-term cost roughly adds up to $16,000 to $108,000 per home.

However, Gentry today is still assessing whether to use CFD financing for Waiawa Ridge infrastructure that includes a $25 million extension to Ka Uka Boulevard, a $30 million sewer line and a $40 million upgrade to H-2 Freeway's Waipi'o Interchange.

"We are still looking at it very seriously as an option," said Alan Arakawa, president and CEO of Waiawa Ridge Development LLC, a joint venture of Gentry and Alexander & Baldwin Inc.

Gentry took the first of three steps to set up a CFD in 2004, obtaining a City Council resolution of intent to establish a CFD. If Gentry and A&B decide to go forward, the partners would have to establish an ordinance forming the CFD followed by another ordinance to issue bonds.

Joe Fadrowski, vice president for Gentry subsidiary Gentry-Pacific Ltd., said that the last step wouldn't need to happen until late 2008, given Waiawa Ridge's development schedule.

At least one other private project has obtained an initial county resolution for establishing a CFD — a planned Big Island community called Villages of Aina Le'a designed for 1,900 homes, two golf courses, a public school and 26 acres of parks and walking and biking paths.

Aina Le'a developers intend to establish a CFD for up to $100 million in public facilities — roads, parks, water system and sewer system — and project annual special taxes of roughly $2,800 to $5,900, depending on a home's size.

"It's a great tool for bringing in regional improvements," said Jim Baldwin, Aina Le'a project manager. "Generally, the people who benefit are the ones who pay."

OTHERS CONSIDERING IT

On O'ahu, other developers considering CFDs include the 4,100-home Makaiwa Hills project near Makakilo planned by a venture led by the James Campbell Co.; the 11,700-home 'Ewa project Ho'opili by D.R. Horton Inc.'s Schuler Division; and Waiawa and Koa Ridge projects slated for roughly 7,000 homes by Castle & Cooke.

Saunders of Castle & Cooke said the challenge has been assessing the costs and benefits of CFDs, including the process of establishing them and gauging public acceptance.

"Nobody's done it yet," he said.

Hawai'i's first CFD is likely to be Kamakoa at Waikoloa, a Hawai'i County-sponsored affordable workforce housing community on the Big Island.

The project is designed for 1,200 homes, including 400 rentals, and largely targets employees of West Hawai'i resorts, many of whom commute from East Hawai'i and contribute to nightmare rush-hour traffic.

The county turned to CFD financing because project infrastructure costs are estimated at about $90 million — too much to swallow for the county and its nonprofit development partner, UniDev LLC.

Under the CFD, Kamakoa homeowners would pay a maximum annual special tax of $3,600 to $6,000 for homes estimated to cost $230,000 to $375,000 on leasehold land, though costs have not been finalized.

Kamakoa is expected to break ground in November and deliver initial homes in 2009.

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How a CFD works
Property owners in a defined district pay for public facilities as part of their biennial property tax bill, typically for up to 30 years.

Who sets up CFDS
Developers generally are forming CFDs for new master-planned communities, financing CFD work using tax-exempt bonds issued under county power and paid back by community homeowners.

How a CFD is established
An initial petition with information including a CFD's boundaries, public facilities and costs must be submitted to and approved with a resolution by a county council. Later, an ordinance forming the district is needed. The approval process requires a public hearing, and a CFD can be blocked if at least 55 percent of landowners in a proposed district object.

What facilities can a CFD finance
Anything owned and maintained by the government with a useful life of more than five years. Examples include roads, parks, schools, libraries, museums, police and fire stations, water and sewer systems and public parking.

Who pays for the CFD
Any property owner designated by the district, which could include homeowners as well as

owners of commercial or other property. The tax is assessed on the property, making it a liability of any subsequent owners.

How CFDs affect home prices

Theoretically, the initial price of a home in a CFD is less because public infrastructure costs are being paid for through a tax over as many as 30 years. But a CFD homeowner could pay more over the long term depending on how many years they own the home. If a CFD home is sold, the new owner has the tax liability.

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