Advisory Opinion #58

Parties: Otto Belvedere and City of Payson

Issued: December 4, 2008

TOPIC CATEGORIES:

D: Exactions on Development
J: Requirements Imposed Upon Development
N: Review of Warranty Work for Completion

Local governments may require performance bonds to guarantee completion of improvements, and they may also require warranty bonds to guarantee new construction.

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OFFICE OF THE PROPERTY RIGHTS OMBUDSMAN

ADVISORY OPINION

Performance Guarantee Requirement for Non-public Amenities

Advisory Opinion Requested by:	Otto Belvedere
Local Government Entity:	Payson City
Applicant for the Land Use Approval:	Otto Belvedere
Project:	Senior Housing Development
Date of this Advisory Opinion:	December 4, 2008
Opinion Authored By:	Elliot R. Lawrence, Attorney, Office of the Property Rights Ombudsman

Issues

May a local government require a performance bond or other security on amenities that are not dedicated to the public?

Summary of Advisory Opinion

A local government may require a developer to obtain a bond or other security to ensure completion of planned improvements. Amenities that are not dedicated to the public may be included as part of the performance bond requirement, when the inclusion is required by local ordinance. A performance bond serves legitimate public interests, and is a valid condition on new development. Continuing a portion of the bond as a contingency or warranty period also serves important public interests, and may also be required of new development, provided the amount of the warranty is roughly equal to the cost of the new development's impact. Finally, a developer may be required to complete or fund an asphalt overlay, but only to the extent that the overlay is required to address an impact of the new development, and if the cost of the overlay is roughly equal to the cost necessary to address the impact.

Review

A request for an advisory opinion may be filed at any time prior to the rendering of a final decision by a local land use appeal authority under the provisions of UTAH CODE ANN. § 13-43-205. The opinion is meant to provide an early review, before any duty to exhaust administrative remedies, of significant land use questions so that those involved in a land use application or other specific land use disputes can have an independent review of an issue. It is hoped that such a review can help the parties avoid litigation, resolve differences in a fair and neutral forum, and understand the relevant law. The decision is not binding, but, as explained at the end of this opinion, may have some effect on the long-term cost of resolving such issues in the courts.

A request for an Advisory Opinion was received from Otto Belevedere on October 30, 2008. A copy of that request was sent via certified mail to Jeanette Curtis, Payson City Recorder. The return receipt indicated that the City received the materials on November 3, 2008. The City submitted a response to the Office of the Property Rights Ombudsman, which was received on November 10, 2008. A copy of the City's response was mailed to Mr. Belvedere.

Evidence

The following documents and information with relevance to the issue involved in this advisory opinion were reviewed prior to its completion:

1. Request for an Advisory Opinion, filed October 30, 2008 with the Office of the Property Rights Ombudsman by Otto Belvedere, with Attachments.
2. Response from Payson City, submitted by David C. Tuckett, City Attorney, received on November 10, 2008.

Background

Otto Belvedere is developing a subdivision, known as "Heritage Village," within Payson City. The subdivision is intended to provide housing for senior citizens, and includes a clubhouse, trails, and other amenities for the use of the residents only, not the general public. The City also granted Mr. Belvedere additional density for the project in exchange for landscaping, entryway and fencing upgrades. The City Council granted approval of this project, and Mr. Belvedere began construction.

The City requires performance guarantees to ensure completion of required improvements. As a condition of approval, the City requires an "acceptable guarantee . . . sufficient to secure to the municipality the satisfactory construction, installation, and dedication of the required improvements." PAYSON CITY CODE, § 20.30.3.[1] The amount of the guarantee is 120% of the estimated cost of completing the improvements. *Id.* The required improvements "include roadways, municipal infrastructure, required fencing, required landscaping, required project

[1] Acceptable forms for the guarantee include bonds, letters of credit, or other types of assurance. *See* PAYSON CITY CODE, § 20.30.4.

amenities, amenities provided by the applicant in exchange for a density bonus, and any other required improvements." *Id.* If there is insufficient progress on construction after two years, the City may access the funds in the guarantee to complete the improvements. When the improvements are satisfactorily completed, the City will release the developer from a portion of the obligation.[2]

After completion of the improvement, it appears that the City requires that the developer maintain a portion of the bond for at least two more years, as a "contingency," or warranty against damage or improper construction. The amount that is required after completion is 20% of the estimated cost of the improvement. The City may access the funds if additional work on the improvement is required. After two years, the amount will be released.

Mr. Belvedere and the City entered a Development Agreement governing the construction of Heritage Village. This Agreement described the required amenities, and stated that those amenities were a concession from Mr. Belvedere in exchange for increased density from the City. *See* "Heritage Village Development Agreement," § 11. The Agreement also required Mr. Belvedere to obtain a performance guarantee for all improvements, required landscaping, and project amenities. The amount of the guarantee was 120% of the estimated cost of the improvements, and the Agreement also required that Mr. Belvedere complete a one-inch asphalt overlay on all roads, when the project is 90% complete. *Id.* § 16. The Agreement was executed and signed in October, 2007.

In addition to the bond requirement, the City also charges fees for building permits and inspections. Evidently, the City miscalculated the fee amount for part of Heritage Village, resulting in an overcharge. The City recalculated the fee, and refunded the excess amount to Mr. Belvedere.

Analysis

I. The City Validly Imposed the Performance Guarantee Requirement on the Project.

The Utah Code requires that all conditions on development must be expressed at the time a land use application is approved.

> A municipality may not impose on a holder of an issued land use permit a requirement that is not expressed:
>
> (i) in the land use permit or in documents on which the land use permit is based; or
>
> (ii) in [chapter 10-9a] or the municipality's ordinances.

[2] The City may release partial amounts of the guarantee obligation as improvements are completed. In October of 2007, Mr. Belvedere obtained a $1,958,607.28 bond for the project. The bond amount included the estimated costs for the clubhouse, trails, fencing, and landscaping, along with other required infrastructure. The City states that portions of the bond have already been released.

UTAH CODE ANN. § 10-9a-509(e).[3] This section restricts a local government from imposing unannounced requirements or conditions, and it helps ensure certainty in applications and approvals.

Subdivision or development bonds are valid means to guarantee that public improvements will be built to completion when new development is approved. Performance or development bonds are commonly used to guarantee construction of improvements that will be dedicated to the public upon completion.[4] The bond amount is determined by the estimated costs of unfinished public improvements. If a developer is unable to finish such improvements as streets or water systems, the bond furnishes money for completion. Payson City properly required a performance guarantee as a condition of approval of Heritage Villa, because the surety requirement is expressed in § 20.30.3 of the City's ordinances, with specific requirements included in the Development Agreement.

Mr. Belvedere objects to the City's bond because it includes amenities that will not be dedicated to the public, such as the clubhouse, walking trails, fencing, and landscaping. He argues that because these "non-dedicated" improvements will not be turned over to the public, or even be available for public use, the bond requirement should not apply to them. However, amenities provided in exchange for a density bonus are among the improvements subject to the performance bond requirement of § 20.30.3 of the Payson City Code. The Development Agreement identifies the clubhouse, trails, fencing, and landscaping as amenities provided in exchange for additional density, so they are also subject to the performance bond requirement. Although these amenities are not to be dedicated to the public, the City is entitled to some assurances that these amenities will be completed, because the City agreed to density concessions in exchange for them.

The Development Agreement requires a performance guarantee "for all improvements that will be dedicated to Payson City." This does not exempt the "non-dedicated" amenities from the performance guarantee requirement. Nothing in the language of Section 22 of the Agreement indicates such an exemption was intended. Although the Agreement may only require a performance guarantee for dedicated amenities, Payson City ordinance requires a performance guarantee for the non-dedicated amenities in this situation. Section 18 of the Agreement states that the Agreement does not relieve the Applicant from complying with City ordinances. In order to comply with City ordinances, the Applicant must provide a performance guarantee on the non-dedicated amenities. Where a conflict between the Agreement and ordinance arises, the ordinance controls, according to the terms of the Agreement. The "non-dedicated" amenities are subject to the performance bond requirement.[5]

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[3] A parallel provision, applicable to counties, is found at § 17-27a-508 of the Utah Code.

[4] The City notes that § 10-9a-604.5 of the Utah Code specifically authorizes cities to require "improvement assurance," or a performance bond, as a condition of development approval. However, that section was adopted by the 2008 Utah Legislature, with an effective date of May 5, 2008, after Mr. Belvedere had obtained his bond.

[5] The City indicates that it will release the full bond amount for the "non-dedicated" amenities upon completion, and will not retain the 20% contingency required of dedicated improvements.

II. The Performance Guarantee Requirement is an Exaction, Which Must Comply with Section 10-9a-508 of the Utah Code.

A. The Security Requirement is an Exaction, and must Satisfy both Parts of Section 10-9a-508.

The City's requirement that a developer acquire a performance guarantee to ensure completion of public improvements constitutes an exaction under Utah Law. "Exactions are conditions imposed by governmental entities on developers for the issuance of a building permit or subdivision plat approval." *B.A.M. Development, LLC v. Salt Lake County,* 2006 UT 2, ¶ 34, 128 P.3d 1161, 1169. Exactions include mandatory dedication of property, as well as fees. *Id.* Payson's guarantee requirement is an exaction, because a bond or other surety is required before the City will grant approval of a final subdivision plat.

In 2005, the Utah Legislature enacted § 10-9a-508 of the Utah Code, which authorizes counties to impose exactions on new development, and also prescribes limits on that authority:

> A municipality may impose an exaction or exactions on development proposed in a land use application provided that:
>
> (a) an essential link exists between a legitimate governmental interest and each exaction; and
>
> (b) each exaction is roughly proportionate, both in nature and extent, to the impact of the proposed development.

UTAH CODE ANN. § 10-9a-508(1).[6] The Utah Supreme Court observed that the language of this statute was borrowed directly from the U.S. Supreme Court analyses in *Nollan v. California Coastal Comm'n,* 483 U.S. 825, 107 S.Ct. 3141 (1987) and *Dolan v. City of Tigard,* 512 U.S 374, 114 S.Ct. 2309 (1994). *See B.A.M.*, 2006 UT 2, ¶ 41, 128 P.2d at 1170. In those two cases, the Supreme Court promulgated rules for determining when an exaction is valid under the federal constitution's Takings Clause.[7] This has come to be known as the *Nollan/Dolan* "rough proportionality" test, and that two-part analysis is reflected in § 10-9a-508.

The *B.A.M.* decision indicates that the Utah Supreme Court—as well as Utah Legislature—agrees that any condition imposed on development approval is an "exaction," whether the local government requires dedication of a property right or not. *See B.A.M.*, 2006 UT 2, ¶ 46, 128 P.3d at 1171. It should be noted that in *Monterey v. Del Monte Dunes at Monterey, LTD*, the United States Supreme Court held that the "*Nollan/Dolan*" rough proportionality analysis did not extend exactions that did not require dedications of property. *Del Monte Dunes*, 526 U.S. 687, 703, 119

[6] There is a corresponding statute applicable to counties found at § 17-27a-507 of the Utah Code.

[7] *See* U.S. Const., amend V. The Supreme Court has interpreted the Takings Clause as limiting a government's ability to impose conditions on development. Furthermore, "[t]he Utah Constitution reinforces the protection of private property against uncompensated governmental takings . . ." *B.A.M.*, 2006 UT 2, ¶ 31, 128 P.3d at 1168. *See also* Utah Const. art. I, § 22.

S.Ct. 1624, 1635 (1999). However, state courts have applied the rough proportionality test to "non-dedicatory" exactions, such as fees and payments for improvements.[8] Based on the language in *B.A.M.*, as well as § 10-9a-508, it appears that the rough proportionality test applies to all conditions imposed on new development, including Payson's guarantee requirement. Thus, in order to be valid, the City's security requirement must meet both parts of § 10-9a-508(1).

The Utah Supreme Court further honed the "rough proportionality" analysis in *B.A.M. Development, LLC v. Salt Lake County*, 2008 UT 45 ("*B.A.M. II*"), which was a second appeal stemming from the same development project at issue in the earlier decision. This opinion explained that rough proportionality analysis "has two aspects: first, the exaction and impact must be related in nature; second, they must be related in extent." *B.A.M. II*, 2008 UT 45, ¶ 9. The "nature" aspect focuses on the relationship between the purported impact and proposed exaction. The court agreed that the approach should be expressed "in terms of a solution and a problem . . . . [T]he impact is the problem, or the burden which the community will bear because of the development. The exaction should address the problem. If it does, then the nature component has been satisfied." *Id.*, 2008 UT 45, ¶ 10.

The "extent" aspect of the rough proportionality analysis measures the impact against the proposed exaction in terms of cost:

> The most appropriate measure is cost—specifically, the cost of the exaction and the impact to the developer and the municipality, respectively. The impact of the development can be measured as the cost to the municipality of assuaging the impact. Likewise, the exaction can be measured as the value of the land to be dedicated by the developer at the time of the exaction.

Id., 2008 UT 45, ¶ 11. The court continued by holding that "roughly proportional" means "roughly equivalent." Thus, in order to be valid, the cost of an exaction must be roughly equivalent to the cost that a local government would incur to address (or "assuage") the impact attributable to a new development.

B. The City's Security Requirement Satisfies Section 10-9a-508(1)(a), Because There is a Link Between the Requirement and a Legitimate Governmental Interest.

The City has a legitimate interest in seeing that proposed improvements are completed in a timely manner. A requirement that a developer provide a source of funding for completion of improvements supports that objective, and is within the power of local governments. In addition, a contingency period during which the builder warrants construction is another reasonable means of guaranteeing that the public improvements will be properly constructed. There is thus an essential link between requiring a developer to provide some form of security for completion of

[8] *See e.g., Town of Flower Mound v. Stafford Estates LP*, 135 S.W.3d 620 (Tex. 2004) (requirement that developer pay for improvements to streets not directly serving subdivision). The Texas Supreme Court cited to "non-dedicatory" cases from California, Illinois, and Ohio. *See also Town of Flower Mound v. Stafford Estates, LP*, 71 S.W.3d 18 (Tex.App. 2002)(lower court decision upheld by supreme court).

improvements and the legitimate governmental objective of having the improvements completed, as well as the requirement that developers guarantee the improvements for a period of time.[9]

C. The City's Performance Guarantee Requirement Must be Evaluated Under the "Rough Proportionality" Aspect of § 10-9a-508(1)(b).

The "nature" aspect of § 10-9a-508(1)(b) requires that the City's requirement address a "problem" derived from the impact of the development. In this particular situation, this analysis is basically the same as that for the "essential link" aspect described above. The City may fulfill its legitimate interest that the improvements be completed by requiring a performance bond. The "non-dedicated" improvements may legitimately be included in the bond, because the City has an interest in seeing that those improvements also be completed. The City's interest in these improvements is greater than other non-public improvements, because it allowed a greater density for Heritage Village in exchange for the proposed amenities. Because the City's legitimate interests are served by the performance guarantee, the requirement satisfies the "nature" aspect of the rough proportionality analysis.

The required amount of the performance guarantee also satisfies the "extent" aspect of the analysis. As stated above, extent is measured by comparing the cost to the developer against the cost to the local government. The amount of the bond is set at the estimated cost to complete the improvements, which would be the same for both the developer and the City. Therefore, insofar as the amount of the bond is concerned, the "extent" aspect is satisfied.

Maintaining a portion of the bond as a two-year "contingency fund," presumably to provide funds for repairs and damage, also must satisfy rough proportionality analysis. Ensuring that public improvements are properly constructed is a legitimate governmental interest. Requiring contingency funds for a period following completion of the improvements promotes that interest by providing some funds for problems that might not be apparent when the improvement is completed and accepted.

This does not mean, however, that a developer may be expected to fund repairs to all damage without regard to the cause. The U.S. Supreme Court agreed that proportionality "animates" the Takings Clause: "The Fifth Amendment's guarantee . . . was designed to bar the Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *Del Monte Dunes*, 526 U.S. at 703, 119 S.Ct. at 1635 (*quoting Armstrong v. United States*, 364 U.S. 40, 49, 80 S.Ct. 1563, 1569 (1960)). Fairness and

[9] Payson City has chosen a contingency period of 24 months. Section 10-9a-604.5, enacted by the 2008 Utah Legislature, only authorizes a one-year warranty period, which may be extended under certain circumstances. *See* UTAH CODE ANN. § 10-9a-604.5. However, that section cannot be applied retroactively to performance guarantees required under local ordinances. *State v. One Lot of Personal Property*, 2004 UT 36, ¶ 10, 90 P.3d 639, 641 ("[I]t is a long-standing rule of statutory construction that a legislative enactment which alters the substantive law or affects vested rights will not be read to operate retrospectively unless the legislature has clearly expressed that intention.") The performance bond for Heritage Village was required before § 10-9a-604.5 was adopted, and is therefore subject to the two-year contingency period.

justice dictate that the City may only use contingency funds to the extent that the funds are roughly equivalent to the impact caused by the development.

Finally, requiring a new asphalt overlay is also an exaction that must meet § 10-9a-508(1).[10] There is an essential link between the overlay requirement and the City's legitimate interest in safe roadways. However, there has been no showing that repaving or resealing the roadways is roughly proportional to the impact of the development. There has been no showing that repaving is necessary due to a defect in construction, or is required because of damage caused by the developer. Without such a showing, the overlay requirement is not a valid exaction.[11]

Conclusion

The City may validly require a performance bond for the improvements in Heritage Village. The requirement was imposed by the City's ordinances, and serves a valid public purpose by providing funds to complete the public improvements in the event that Mr. Belvedere cannot. The City may include the "non-dedicated" amenities as part of the bond, because they were included as part of the project in exchange for density concessions from the City, which is anticipated by the City's ordinance.

The performance guarantee requirement is a type of exaction, because it is a condition on approval of the development. As an exaction, it must satisfy the "rough proportionality" analysis required by § 10-9a-508 of the Utah Code. There is an essential link between a bonding requirement and the City's legitimate interest in guaranteeing that public improvements be completed. The performance guarantee also "solves" the "problem" by providing a ready source of funds to complete improvements. Since the bond amount is based on the estimated cost to complete the improvements, the value of the bond satisfies the "extent" aspect of the rough proportionality analysis.

Using bond funds as a contingency or warranty for completed improvements is valid to the extent that the funds used are roughly equal to the costs related to the impact of the development. Funds to overlay roadways may be required of developers, again only to the extent that the funds are roughly equivalent to the impact caused by the development.

Brent N. Bateman, Lead Attorney
Office of the Property Rights Ombudsman

[10] The Development Agreement requires Mr. Belvedere to fund a one-inch asphalt overlay on all roadways. *See* Development Agreement, § 16.

[11] If the City shows that the cost of the overlay is roughly equal to the impact attributable to the development, it may validly require the funds to be paid.

NOTE:

This is an advisory opinion as defined in § 13-43-205 of the Utah Code. It does not constitute legal advice, and is not to be construed as reflecting the opinions or policy of the State of Utah or the Department of Commerce. The opinions expressed are arrived at based on a summary review of the factual situation involved in this specific matter, and may or may not reflect the opinion that might be expressed in another matter where the facts and circumstances are different or where the relevant law may have changed.

While the author is an attorney and has prepared this opinion in light of his understanding of the relevant law, he does not represent anyone involved in this matter. Anyone with an interest in these issues who must protect that interest should seek the advice of his or her own legal counsel and not rely on this document as a definitive statement of how to protect or advance his interest.

An advisory opinion issued by the Office of the Property Rights Ombudsman is not binding on any party to a dispute involving land use law. If the same issue that is the subject of an advisory opinion is listed as a cause of action in litigation, and that cause of action is litigated on the same facts and circumstances and is resolved consistent with the advisory opinion, the substantially prevailing party on that cause of action may collect reasonable attorney fees and court costs pertaining to the development of that cause of action from the date of the delivery of the advisory opinion to the date of the court's resolution.

Evidence of a review by the Office of the Property Rights Ombudsman and the opinions, writings, findings, and determinations of the Office of the Property Rights Ombudsman are not admissible as evidence in a judicial action, except in small claims court, a judicial review of arbitration, or in determining costs and legal fees as explained above.

MAILING CERTIFICATE

Section 13-43-206(10)(b) of the Utah Code requires delivery of the attached advisory opinion to the government entity involved in this matter in a manner that complies with Utah Code Ann. § 63-30d-401 (Notices Filed Under the Governmental Immunity Act).

These provisions of state code require that the advisory opinion be delivered to the agent designated by the governmental entity to receive notices on behalf of the governmental entity in the Governmental Immunity Act database maintained by the Utah State Department of Commerce, Division of Corporations and Commercial Code, and to the address shown is as designated in that database.

The person and address designated in the Governmental Immunity Act database is as follows:

Jeanette Curtis, City Recorder
Payson City
439 W. Utah Ave.
Payson, Utah 84651

On this _____ Day of December, 2008, I caused the attached Advisory Opinion to be delivered to the governmental office by delivering the same to the United States Postal Service, postage prepaid, certified mail, return receipt requested, and addressed to the person shown above.

_____
Office of the Property Rights Ombudsman