



## City of Homer

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### Memorandum 14-175

**TO:** Mayor Wythe and Homer City Council

**FROM:** Walt Wrede

**Date:** November 24, 2014

**SUBJECT:** Natural Gas Distribution System

#### ***STATUS REPORT***

#### ***HOMER NATURAL GAS DISTRIBUTION SYSTEM SPECIAL ASSESSMENT DISTRICT***

#### Introduction / Background

The Homer Natural Gas Distribution System project has a history of public discussion and Council action that goes back to 2009 when the possibility of a gas line extending to Homer from the North Fork looked more and more realistic. I will not attempt to rehash all of that history here, but it did seem useful to highlight the significant Council actions that got us to where we are today.

- When it adopted Resolution 12-069, the City Council initiated a Natural Gas Distribution System Special Assessment District. The Resolution contained a finding that all parcels of real property would be assessed equally because they would be provided access to gas.
- Resolution 12-081 contained and endorsed an improvement plan for the Special Assessment District. The plan included a per-lot assessment estimated to be \$3,283.30. This amount was a preliminary estimate and was subject to adjustment based upon the City's actual costs incurred for the improvement and the number of parcels on the final assessment roll.
- Ordinance 12-46 appropriated \$50,165 for the first round of assessment district administrative costs and for public outreach and education. The funds were to be recovered later through property assessments.
- Ordinance 13-02 formally created the Homer Natural Gas Distribution System Special Assessment District.
- Ordinance 13-03 (S) (2) authorized the City to issue Natural Gas Distribution System Special Assessment Bonds in an amount not to exceed \$12,700,00 to finance the project.

- Ordinance 13-09 appropriated funds in the amount of \$539,368 for administration and direct services provided in support of the assessment district and established a project budget. The funds were to be recovered over ten years through property assessments.
- Resolution 13-017 (S) authorized and approved a construction contract between the City of Homer and Enstar Natural Gas Company in an amount not to exceed \$12,160,632.

### Construction Summary

The gas distribution system construction project was completed in two seasons. This is impressive because there were many knowledgeable and experienced parties who were skeptical that a job of this size and scope could be done in two seasons. The original plan was for the “Core Area” in downtown to be constructed in 2013 and the East End, Spit, and Bluff areas to be completed in 2014. The warm winter in 2013-2014 enabled the contractors to accelerate the schedule and work on the Spit was completed during the winter months. Work in parts of the West Hill area began earlier in the season than originally anticipated.

The end result was that the entire project was completed several months early. Again, we cannot say enough about the contractors who worked for Enstar. They did an excellent job and responded quickly to City or citizen inquiries. Enstar, the contractors, and the City staff worked very well together and coordinated their efforts toward a common goal. Problems were resolved quickly and efficiently. Our early concerns about traffic disruptions, dust, property owner complaints, and general public inconvenience did not materialize except for a very few isolated incidents. In summary, the project went about as smoothly as anyone could have hoped for.

The contract between the City and Enstar contained a preliminary estimate that the project would consist of 392,000 linear feet or 74.24 miles of pipe. Those numbers were refined later when the engineered / design plan was completed in preparation for the bidding process. The designed plans called for 377,054 linear feet or 71.41 miles of pipe. The final constructed / installed number is 375,835 linear feet or 71.18 miles of pipe.

There are many reasons for the differences between the estimates in the contract, the engineered plans, and the final construction numbers. First, estimates became much more precise as Enstar moved from the preliminary drawings used for project planning and contract discussion purposes to the engineered, bid ready documents used later. Most of the adjustments were mutually agreed upon. For example, there were instances where the alignment of a section of pipe was changed because a more direct and shorter route was identified. There were times where it was decided not to construct sections of pipe that were in the original design because the right of way was not cleared or constructed, there were no other utilities present, no structures to be served, and construction would have been expensive with little or no benefit. There were instances where pipe was eliminated because all of the adjacent lots could be served from different directions and the pipe was redundant (Poopdeck ROW). There were also instances where additional pipe was installed due to unforeseen circumstances such as the Enstar’s inability to obtain easements.

One of the major reasons this project went far more smoothly than anyone anticipated was the fact that much more of the project was “bored” than the design or bid documents anticipated. Boring costs are significantly more per unit than “trenching”. The original design and cost estimate

anticipated that boring would only be used to avoid or mitigate damage to sensitive areas like streams, wetlands, or steep trenches. It would also be used in downtown areas where there would be potential conflicts with other utilities or infrastructure and/or restoration costs (pavement, sidewalks) would be high if trenching were employed. In short, the plan was to trench as much as possible to keep costs and ultimately assessments as low as possible.

The project design and bid documents called for 7.8 miles or 10% of the project to be bored and 64.33 miles or 90% of the project to be trenched. In the end, 46.02 miles or 65% of the pipe was installed using boring technology and 25.16 miles or 35% was installed by trenching. As you can see, this is a significant difference. There are a number of reasons for this. They include:

- Preliminary engineering and fieldwork, conducted mostly in winter and without the benefit of field locates, did not anticipate or identify all of the areas where boring was preferred or necessary.
- Most of the decisions to bore were made independently by the contractors because they found it to be in their best interest to do so. For example, UTI received a discount on the normal per unit cost of boring in year one because of the anticipated volume of work. Other times contractors determined that it was cheaper and easier to bore because they could avoid permitting, mitigation, and restoration costs that might be associated with trenching. In all cases where the contractors decided independently to bore, they were paid the trench price.
- In some cases the City agreed to boring in advance due to special circumstances. For instance, on Kachemak Drive and on Skyline Drive, there were areas where Enstar could only obtain vital easements if it agreed to bore. If we had refused, important gas loops would not have been completed and we would have been left with dead end lines. In addition, a significant number of parcels that were included in the assessment district and whose owners wanted gas would not have been served. We determined it was worth the extra money in those cases.

### Property Served

A benefited or served property in the Homer Natural Gas Distribution System Assessment District is defined as a property that has a gas line fronting its property line or one that is close enough, as in the case of a cul-de-sac, to be accessed with a normal service line. The preliminary assessment roll contained 3,855 properties to be assessed. This number was used to calculate the estimated assessment per property. Assessment rolls are often changing and evolving based upon new information and circumstances and this one is no exception. It will likely change several more times between now and the time Council approves the final roll. The Council has already amended the preliminary assessment roll several times by resolution, most recently through adoption of Resolution 14-092-A.

The current, amended roll contains 3,816 properties to be assessed. This is a reduction of 39 properties. This is important to note because 39 fewer properties at an estimated assessment of \$3,283 per property results in a \$128,037 reduction in revenue; revenue that is needed to repay the City's loan. Following is break down of those 39 properties:

- 11 properties were removed from the roll due to lot line vacations which occurred prior to the deadline established by Council.
- 9 properties were exempted from assessment because they were not benefitted. These are properties that are not developable for some reason, pursuant to criteria established by Council resolution.
- 19 properties were excluded from the assessment district because they were not served due to mutual decisions by the City and Enstar (See Construction Summary Above).

As requested by Council, the Planning Department will produce a large map that can be placed on the wall for the next meeting on December 8, 2014. This map will show where the gas lines are constructed, which properties are served, and which properties are either exempted or not served.

### Project Cost

The estimated total project cost prior to construction was \$12,700,000. This number includes the not to exceed contract price with Enstar (\$12,160,632) plus the City budgeted administration and direct costs (\$539,368). The news is good with respect to both components of the budget. The final negotiated post construction project cost was \$12,085,632 or \$75,000 below the not to exceed contract amount. The City's costs are \$273,756 or \$265,612 below the approved budget. This figure includes anticipated administrative expenses that will accrue during the next phase of assessment district approval and finalization in 2015.

Therefore, the final project cost is \$12,359,388. This is \$340,612 below the total project budget. So, the news so far is good. The project was completed on time and under budget. An added financial benefit is the fact that the City will not have to draw down as much money on its loan with the Borough as expected.

### Condominiums

The preliminary assessment roll included full assessments for each individual condominium unit within a condominium building or complex. Kenneth W. Castner III sued the City (3HO-13-38 CI) and argued that the condominium complex he had an ownership interest in should only receive one assessment for the parcel it was located on. The City argued otherwise based upon the clear language of the relevant statute and second opinions obtained by attorneys experienced in this area of law. The judge ruled in favor of Castner and against the City. The City believes this was a flawed decision for many reasons but decided that on balance, it was not worth the time, effort, and expense to appeal. It is not my intent to rehash this case here.

The judge's decision had the potential to have very significant impacts upon the assessment roll and the assessment amount ultimately paid by the remaining property owners. For example, if the City only levied one assessment per lot for condominium units, approximately 102 properties would be dropped from the assessment roll. One hundred and two properties times the projected per property assessment is \$334,000 in lost revenue needed to repay the Borough loan. This lost revenue and additional cost would have to be shifted to the remaining property owners in the assessment district.

Since the judge rendered his decision, Tom Klinkner and I have spent time weighing the costs and benefits of various alternative approaches to assessing Condos. We have tried to balance the

competing requirements of the judge's decision, the statutes, the desire to achieve a degree of proportionality and fairness for all property owners, and other financial, legal, and political considerations.

A recommendation from Tom on how to proceed with the assessment of condos is attached and Tom will be available to discuss this with you in person at the November 24 meeting. In short, Tom concludes, all things considered, that the City would be best served by issuing one assessment per lot for condo buildings and dividing the assessment by the number of condos in the building. Exceptions to this approach would include condos with individual service lines and/or meters. So for example, in Mr. Castner's case, if we apply one assessment to the property, subtract the separate tax parcels that are owned in common, and divide it by the number of condo units (assuming 5), you wind up with an assessment for each condo of about \$657.00. This approach complies with the law and assigns individual assessments to each condo. Therefore, the assessment roll does not lose 102 properties. However, the bottom line is still the same. Approximately \$334,000 in assessment revenue is lost which will have to be made up somehow. This amount may be reduced somewhat when condos with individual service lines or meters are accounted for.

The discussion in the next section on projected assessments assumes that the Council will accept Tom's recommendation. We understand that may not be the case. If the Council wants to discuss this further in more detail, including legal strategies and the potential legal costs, benefits, and risks associated with other alternatives, I would suggest an executive session soon, before the final assessment roll is produced for public consumption in late January. If Council does not object or question the recommendation, this is the approach the administration will take in preparing the final assessment roll. Remember that Council will still have public hearings on the final roll and the opportunity to hear property owner objections. The Council will have additional opportunities to amend the roll at that time as it sees appropriate before final approval.

### Projected Assessments

Following is a chart that shows what the estimated property assessment will be using the new, updated information we have on total project costs and the number of properties to be assessed. Keep in mind that this will likely change slightly before the final roll is produced as new information on individual condos is produced and other information emerges during the public comment and objection period. For information purposes, this chart contains a comparison of the original assessment estimate vs. the current, post project estimate and a comparison of what assessments will be if each individual condo unit receives a full assessment rather than one assessment per lot divided by the number of condos.

Original Cost Estimate: \$12,657,147 (This is the first estimate that was used to calculate estimated assessments)

Final Total Project Cost: \$12,359,388

	<u>Number of Parcels</u>	<u>Assessment</u>	<u>Difference from original</u>
Original Estimate	3855	\$3,283.31	
Condos Fully Assessed	3816	\$3,238.83	-- \$44.48
Condos Assessed Per Lot	3714	\$3,327.78	+ \$44.47

It should be noted that the City will be receiving quarterly Free Main Allowance rebate payments from Enstar for the next ten years. The City receives rebates every time a property owner hooks up to natural gas. The rebate is a way to partially reimburse the City for its initial investment in the distribution system infrastructure. Kachemak City has been receiving rebates that average in the neighborhood of \$800.00 per property. If Enstar's projections on future customers are close to accurate, the City should be receiving Free Main Allowance payments that total \$1.2 Million or more. The Council has talked about applying the FMA toward reducing property assessments. If it does so, the assessment in the end could be less than \$3,000.

#### Next Steps

Between now and January, the staff will be working on tuning up the final assessment roll and making sure the new assessment software program is operational. The final assessment roll is scheduled to be on the Council agenda the second meeting in January. Once the final roll is introduced, Council will follow the process prescribed in Title 17 of the code. The process will include opportunities for the landowners in the assessment district to object and to point out errors and omissions.

In the interim, it would be good for the Council to consider several other items:

- Confirm and formalize how the FMA payments will be used and allocated.
- Consider a set of recommendations, still to be submitted, regarding SAD code changes that will streamline administration.
- Consider incentives for payment in full. For example, it is my understanding that for Borough USADs, if property owners pay the assessment in full within 60 days of billing, there is no interest charged and no lien against the property is recorded. This works to the advantage of both the City and the property owner.

## MEMORANDUM

**TO: WALT WREDE, CITY MANAGER  
CITY OF HOMER**

**FROM: THOMAS F. KLINKNER**

**RE: NATURAL GAS DISTRIBUTION SYSTEM ASSESSMENTS FOR  
COMMON INTEREST COMMUNITIES**

**FILE NO.: 506,742.205**

**DATE: NOVEMBER 7, 2014**

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### **1. Introduction.**

By Resolution 12-069, the Council initiated a natural gas distribution system special assessment district ("District") and found that "the natural gas distribution system will benefit equally all parcels of real property in the City that will receive access to natural gas service ... and that all parcels so benefited should be assessed equally for the cost of the natural gas distribution system." In the improvement plan for the District adopted by Resolution 12-081, the amount of this per-lot assessment was estimated to be \$3,283.30; however this amount is subject to adjustment based on the actual costs incurred by the City for the natural gas distribution system improvements.

In *Castner v. City of Homer*<sup>1</sup> the Superior Court held that levying natural gas distribution system assessments on condominium units in the Kachemak Bay Title Building as though the units were individual parcels would result in assessments that were invalidly disproportionate to the benefit the units would receive from the improvements. The following updates and completes our analysis of the effect of the *Castner* decision on the City's assessment of condominiums for natural gas distribution system improvements.

### **2. The Assessment of Condominiums**

As we have explained previously, the assessment of condominiums is regulated by the Uniform Common Interest Ownership Act, Alaska Statute Chapter 34.08 (the "Act"). A condominium consists of separately owned units each of which holds an

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<sup>1</sup> Superior Court No. 3HO-13-38CI.

undivided interest in common elements.<sup>2</sup> The Act provides for the treatment of units in a condominium as separate parcels of real estate:

(b) In a condominium or planned community,<sup>3</sup>

(1) if there is a unit owner other than a declarant, each unit that has been created, together with its interest in the common elements, constitutes for all purposes a separate parcel of real estate;

(2) if there is a unit owner other than a declarant, each unit shall be separately taxed and assessed, and a separate tax or assessment may not be rendered against any common elements for which a declarant has reserved no development rights.<sup>4</sup>

On the basis of the rules in AS 34.08.720(b), the City proposed to assess each condominium unit in the District the same per lot assessment amount as other benefited real estate parcels.

### **3. The Decision in the *Castner* Case**

In *Castner*, the Superior Court observed that the City's improvement plan called for all parcels of real property in the District to be assessed an equal amount, regardless of a parcel's use or other characteristics, and that each parcel of real property in the District other than a condominium typically would receive natural gas service through a single service connection to the distribution system.<sup>5</sup> The Superior Court contrasted this state of affairs with the assessments proposed for property in which *Castner* owned condominium units:

Kachemak Bay Title Building is located within the city limits of Homer, and is comprised of five condominium units and a 30% ownership of all common property associated with the units. The plaintiff owns [interests in] three condominium units located in the Kachemak Bay Title

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<sup>2</sup> AS 34.08.990(8). Common elements consist of the exterior walls and structural elements of a multi-unit building, shared interior facilities such as lobbies and elevators, and exterior areas used for such purposes as parking and landscaping.

<sup>3</sup> A planned community typically consists of separately owned units with common elements owned by an association. A subdivision of single family dwellings with common open space owned by a homeowners' association would be a planned community.

<sup>4</sup> AS 34.08.720(b). These rules in apply "if there is a unit owner other than the declarant." "Declarant" refers to the developer of the condominium project. Thus, the rules in AS 34.08.720(b) apply from the time that the developer of a condominium project has sold at least one unit in the project.

<sup>5</sup> Memorandum Decision and Order dated January 8, 2014 ("Order"), 9.



Building. ... The City of Homer included the Kachemak Bay Title Building's five condominium units, the lot on which the building is located, and the parking area within the gas improvement district and assessed each "property" \$3,283.30 for the benefit they would receive by the gas line. In sum, the Kachemak Bay Title Building parcel is being assessed nine times for a total of \$29,549.70, which includes the plaintiff's assessed costs of \$9,849.90.

Thus, the Superior Court found that although the Kachemak Bay Title Building received natural gas service through a single service connection, it was subject to nine separate assessments.<sup>6</sup>

In its analysis, the Superior Court relied heavily on a Wisconsin court decision that each property receiving sewer service through an individual service connection should be assessed equally, regardless of whether the property was owned singly or in separate condominium units:

The Wisconsin Supreme Court noted that "other lots that [had] multiple habitable units and were provided access to the sewer main through one four-inch stub to the lot were charged only one availability charge. Yet the Petitioners' lot was assessed an availability charge 18 times higher for the same, single four-inch stub. The court held that assessment costs was [sic] not levied uniformly, because the condominiums were not treated the same as the other lots that received one access stub to connect each lot to the sewer main ...

The court finds the reasoning of the Wisconsin Supreme Court's holding in *Steinbach* to be compelling. First, there is no nexus between the charge to an owner of a "parcel of record" or "lot" who shares access to the gas line through one two-inch high density polyethylene pipe and the City of Homer's cost to provide that access. Second, lots or parcels that have multiple habitable units and leases were provided with the same access to the gas line through one two-inch high density polyethylene pipe to the lot were charged only one assessment charge per lot or parcel. ... Third, there is no showing that each condominium owner received a greater benefit than was provided to other properties affected by the gas line extension.<sup>7</sup>

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<sup>6</sup> Order, 2-3. The reference to nine assessments is based on the City's initial draft assessment roll. The City later found that the division of the Kachemak Bay Title Building property into nine separate tax parcels was incorrect. One difficulty with the *Castner* decision is that the Superior Court did not allow the City to complete the administrative process of correcting this sort of error in the assessment roll for the District. It is unclear whether correction of the assessment roll would have affected the Superior Court's decision.

<sup>7</sup> Order, 11-12.

On the basis of this analysis, the Superior Court concluded that “[t]he per lot assessment is, however, disproportionate to the benefit conferred upon unit owners as opposed to other assessed properties within the assessment district.”<sup>8</sup>

#### **4. The ENSTAR Tariff.**

ENSTAR provides service under the terms in its tariff on file with the Regulatory Commission of Alaska. An additional consideration in implementing the *Castner* decision is the ENSTAR tariff provision regarding service connections. The tariff provides for the installation of one service connection and meter connecting ENSTAR’s distribution system to each customer. A customer is the person or entity that contracts with ENSTAR for natural gas service. Thus, if there is one service connection to a condominium property, the entire condominium property (or its related homeowners’ association) would be the customer. It also is possible that ENSTAR could install a separate service connection and meter for each unit in a condominium, or for each building in a multi-building condominium project. The number of service connections and meters that will be installed in each case is determined by the contractual relationship between ENSTAR and its customer, and not by the City.

#### **5. Assessing Condominiums.**

The City could apply the *Castner* decision at various levels of generality. At a minimum, it binds the City in its assessment of *Castner*’s condominium property. The City may levy an amount equal to only one per-lot natural gas distribution system assessment against the entire Kachemak Bay Title Building. To do so consistently with the Act, the City should determine the actual number of condominium units in the building, excluding all parts of the property that are properly characterized as common elements, divide the per-lot assessment amount by the number of condominium units, and levy the resulting amount against each of those units.

While the *Castner* decision does not strictly bind the City in assessing condominiums other than the Kachemak Bay Title Building, we recommend that the City apply the same assessment method to any other condominium where more than one unit is served by a single service connection to the natural gas distribution system. If a condominium project consists of only one building that is served by a single service connection, the City should levy assessments against the condominium units in the building in the manner described for the Kachemak Bay Title Building. If a condominium project consists of multiple buildings, each of which is served by its own service connection, the City should allocate a single per-lot assessment to each service connection, divide it by the number of condominium units in the related building, and levy an assessment equal to the resulting amount against each condominium unit in that building. If there is a separate service connection for each unit in a condominium, the City should levy the per-lot assessment amount against that unit.

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<sup>8</sup> Order, 13.

I also recommend that the City adopt the following process in assessing condominiums.

- Correctly correlate the actual elements of the condominium with the Kenai Peninsula Borough's tax assessment records. As the *Castner* case illustrates, the Borough tax assessment records are only a starting point for levying assessments against condominiums. Each tax parcel that corresponds to a condominium unit should be identified as such. Any tax parcel that corresponds only to a common element (open space, parking area, etc.) should be excluded from the assessment roll. In cases where there is doubt about the nature of a tax parcel in a condominium, a review of the recorded declaration for the condominium or an inspection of the condominium property may be required.
- For condominium units currently receiving natural gas service, identify the customer receiving gas service, and the facilities through which gas service is provided. If the customer is an individual unit owner, and the unit receives gas service through a separate service connection and meter, the unit may be treated as a separate lot for assessment purposes. If the customer is a representative of multiple unit owners (such as a homeowners' association), and the units receive gas service through a single service connection and meter, the multiple units receiving service should be treated as a single lot for assessment purposes, as described above.
- For condominium units in the District that do not currently receive natural gas service, the City, with advice from ENSTAR, should determine the manner in which ENSTAR would be most likely to provide service to the condominium. Based on that determination, units in the condominium should be assessed as described above.