City of Junction City, Kansas

Independent Investigation of Housing Program
from 2005 through 2007

March 2, 2010

Prepared by

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Engagement Summary

Engagement Overview and Scope

BKD, LLP ("BKD") was engaged by the City Commission of Junction City, Kansas (the "Commission") to perform an independent investigation of the Housing Program from 2005 through 2007.

The objective of our services was to assist the City of Junction City, Kansas (the "City") in the review of the appropriateness of certain actions taken and decisions made related to the housing expansion that occurred during 2005 through 2007. The scope of our work was initially limited to specific subdivisions listed in ***Exhibit A***, and was subsequently expanded to include the review of the C.L. Hoover Opera House ("Opera House") as well.

Our services included the following:

- The analysis of the Development Agreements and petitions for the building of infrastructure related to subdivisions identified by the City Commission
- The analysis and auditing of costs paid or reimbursed by the City under each petition and Development Agreement, if applicable, for the building of infrastructure in the identified subdivisions
- The analysis of the procurement and contracting process for competitively bid infrastructure within the identified subdivisions
- The interview of appropriate parties within the City administration, the Geary County Commission during the period under review, Kaw Valley Engineering and the developer community
- Other analysis determined to be necessary based upon our findings

During our work, several individuals related a variety of concerns to us which were outside the defined scope of our work. A listing of the noted concerns and copies of documentation regarding those concerns provided to us by various individuals were given to the City Attorney.

Our services were provided in accordance with the Statement of Standards for Consulting Services promulgated by the American Institute of Certified Public Accountants and, accordingly, do not constitute a rendering by BKD or its partners or staff of any legal advice, nor do they include the compilation, review or audit of financial statements. Because our services were limited in nature and scope, they cannot be relied upon to discover all documents and other information or provide all analyses that may be of importance in this matter. For instance, any procedures we performed cannot be relied upon to give assurance that any defalcations or fraudulent transfers that might have taken place were discovered.

Scope Limitations

In response to a request for all documentation related to the subdivisions under review, the City provided its files for each subdivision. However, during the review of the file documentation, it was clear that some relevant information was not contained within the subdivision files. Further information was subsequently provided from the City Engineer's files, files maintained by Kaw Valley Engineering and from the City Attorney's files. As the City's files with regard to the subdivisions reviewed appear to be maintained in a decentralized manner, we cannot be certain that we have obtained and reviewed all relevant documents.

We did not reconcile all subdivision costs from their general ledger project accounts to their respective bonded costs. We reconciled 12 of the 39 subdivisions, representing $38 million in bonded costs.

Primary Findings

With the exception of matters already disclosed in the trial of Mick Wunder[1], we did not find that any City official inappropriately directly benefited financially from the Housing Program.

With the benefit of hindsight, it is now apparent that the initial projections of housing demand did not materialize as projected and were therefore inaccurate. Based upon those initial projections, City officials embarked on an aggressive Housing Program. In doing so, there were many risks encountered that could have been managed in a more appropriate manner. Overall, the oversight of the Housing Program was not sufficient in light of the difficult circumstances created by virtue of the ultimately inaccurate housing demand information on which the Housing Program was premised.

The War on Terror and ongoing Department of Defense ("DoD") transformation initiatives caused mission changes, which impacted Fort Riley population statistics, and in turn impacted community planning efforts. Therefore, commencing an aggressive Housing Program based upon 2005/2006 troop related population statistics and timing information resulted in a glut of infrastructure, at present, due to the Army's evolving troop related movements. Given the lack of experience of City officials with growth of the magnitude projected, prudence should have mandated the consideration of the use of the services of an experienced City Planning Consultant at the outset of the Housing Program. Community planning activities should have taken a long-term view, but with short-term benchmarks to ensure that the development activity more closely adhered to the evolving housing demand.

Additional findings include the following:

- Accounting practices with regard to the individual subdivisions were lacking in appropriate structure. We noted several instances of costs for one subdivision being billed to another subdivision. The time necessary to correctly identify and track down appropriate supporting documentation added significantly to the time and costs of this investigation.
- Supporting documentation requirements for pay estimates paid by the City to contractors were unsubstantial. The failure to require detailed pay estimates and associated supporting documentation can create a risk of overpayment by the City. Additionally, the City's files were missing some pay estimate forms, and some forms reviewed did not contain all necessary approvals.
- Reconciliations performed between the general ledger project costs and bonded costs for selected subdivisions did not tie-out. Our analysis revealed instances of costs that were either in the bonded costs or the general ledger costs for a subdivision, but not both. To the extent that bonded costs for a subdivision may not be accurate, the Special Assessments for that subdivision would not be accurate as well.
- The methodology for calculation of the City at large percentage for City requested infrastructure upgrades was not consistently applied among the subdivisions under our review.
- The Special Assessments for Sutter Woods and Sutter Highlands are too high. Over $692,000 in City requested infrastructure upgrades were not removed from costs allocated to the Improvement Districts prior to the calculation of the Special Assessments. Therefore, 90% of the City requested upgrading costs have been allocated to the Improvement Districts.
- Construction of infrastructure for Sutter Woods, Sutter Highlands and Olivia Farms commenced prior to the City Commission's approval of the petitioned costs that the City would be obligated to pay.

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[1] As Mr. Wunder's trial was public and was reported upon by various public news outlets, we will not recount those charges and their details in this report.

- Subsequent to the withdrawal of the application for the creation of a Kansas Rural Housing Improvement District for Olivia Farms, its Special Benefit District was enlarged to include Block 12, Lot 31. This parcel of land was allocated 16.5971% of the Improvement District assessed infrastructure costs, or approximately $1.7 million, through an amended petition dated January 13, 2009. However, that lot is reportedly an eight acre ravine which could be difficult to build on. If the property were to be abandoned by the developer, it is possible that the infrastructure costs allocated to that lot would become the responsibility of the City at large.
- The $87,656.50 cost of hauling dirt that was to have been provided by the City free of charge for Phase 1 of Village at Freedom Place was included in the Special Assessments for Phase 2 of Village at Freedom Place. However, Phase 1 of Village at Freedom Place was not financed through the use of a Special Benefit District. Therefore, the Special Assessments against Phase 2 of Village at Freedom Place may be too high.
- The City is not in compliance with its Debt Management Policy. The City is exceeding some of the debt affordability limits established within the policy.
- In some instances, the City Manager appears to have violated standing City policies related to the approval limits of the City Manager.
- The relationship between Kaw Valley Engineering ("KVE") with regard to services performed for the City and services performed for a majority of the developments creates the appearance of a conflict of interest. In addition, during the course of the Housing Program, a principal of KVE involved in the services provided to the City had an ownership interest in one of the development companies that utilized City assistance to build subdivision infrastructure.
- Fees paid by the City to KVE for engineering services are based on a percentage of the Engineering Cost Estimate rather than a percentage of the actual costs incurred. As a representative for KVE indicated that KVE builds a cushion into its cost estimates, this can result in an overpayment by the City.

Recommendations

The Commission should consider hiring a chief financial officer to oversee the City's accounting function and ensure that all City staff involved in the accounting process are appropriately trained and properly performing their job duties.

All future pay estimates for construction paid for or reimbursed by the City should require a completed pay estimate form with the required approvals as well as adequate supporting documentation. Supporting documentation should include copies of subcontractor contracts and invoices and invoices or receipts for materials.

Reconciliations of general ledger project costs to bonded costs should be performed for all subdivisions not reconciled by BKD.

The Commission should formalize a consistent methodology to be used to calculate the City at large percentage for City requested infrastructure upgrades. Furthermore, the Special Assessments for Sutter Woods and Sutter Highlands should be reviewed for accuracy with regard to the City requested infrastructure upgrades and amended accordingly.

All required approvals should be in place prior to the construction of any infrastructure to be paid for by the City, as a risk management control.

The Commission should consider conducting further investigations into the propriety of the expansion of the Improvement District for Olivia Farms to include Block 12, Lot 31.

The inclusion of the cost of the dirt for Phase 1 of Village at Freedom Place, which phase was financed by the developer, in the bonded costs for Phase 2 of that development, which is being reimbursed to the City through Special Assessments, should be reviewed by the City Attorney for appropriateness and compliance with all applicable laws, statutes and ordinances.

The Commission should review all standing City policies to ensure their continued appropriateness. City staff should acquaint themselves with all City policies and controls should be installed to ensure that policies are not breached without the pre-approval of a formal exception to the policy by a vote of the Commission.

Appropriations Ordinances should not be approved by the Commission unless the individual Commissioners have received and have taken the time to adequately review the listing of expenditures prior to the Commission meeting.

Commissioners and City staff should be mindful of the appearance of conflicts of interest. Potential conflicts of interest should be carefully considered and managed to ensure the legitimacy of transactions and to avoid perceptions of possible self-dealing or mismanagement.

The Commission should consider amending the practice of paying engineering related fees equal to a percentage of the original Engineering Cost Estimate to a percentage of the actual costs. This would avoid the possibility of the inflation of the amount of the Engineering Cost Estimate for the sole purpose of a higher fee.

Engagement Approach

Approach

In performing our work, we reviewed minutes of the City Commission meetings and agenda items related to the subdivisions under our purview. For the individual subdivisions, we reviewed bid documentation, Engineering Cost Estimates, pay estimates and associated supporting documentation, where available. For each subdivision, we reviewed the City's accounting general ledgers and documentation related to costs paid by the City. For selected subdivisions, we reconciled the general ledger project costs to the bonded costs. In addition, we performed general public research, and interviewed various parties to gain an understanding of the history of the Housing Program to try to determine what information was the basis for pivotal decisions.

Interviews

The following individuals were interviewed by or provided information to BKD: Terry Heldstab, Mike Rhodes, Ken Talley, Jack Taylor, Scott Johnson, Rod Barnes, Catherine Logan, Christina Cook, Joleen Schnurr, Sarah Talley, Leon Osborn, and County Commissioner Ben Bennett. BKD also spoke with a representative of the City's bond counsel, Gilmore & Bell, as well as representatives of Big D Development ("Big D"), Fort Development, LLC, Mann's Ranch, Doc Hargreaves, Village at Freedom Place, Western Frontier Developers, LLC and other developers that participated in the Housing Program.

In addition, a number of private citizens met with, emailed and called BKD to provide additional information and/or express a variety of concerns. As previously stated, many of the concerns raised by the private citizens and developers were outside of the scope of work BKD was hired to perform. Their comments and copies of any information provided to BKD have been passed on to the City Attorney for future consideration by the appropriate parties within the City.

Findings and Recommendations

Overview of Housing Program

Anticipated Housing Demand

In 2005, it was announced that Fort Riley would have significant gains in personnel between 2006 and 2011 due primarily to the effects of the Base Realignment and Closure ("BRAC") process and the return of the Big Red One from Germany. In March 2006, Fort Riley officials estimated an influx of 8,500 soldiers and 13,000 family members[2]. Fort Riley officials indicated that 9,000 housing units in total would be necessary for the military personnel and their dependents and looked to the surrounding communities to provide approximately 6,000 units of off-base living quarters to house the expected influx. Most of the soldiers were enlisted at the lower end of the pay scale, so the Army asked developers to focus on affordable, single-family homes in the $120,000 to $150,000 price range[3].

As a result, the City committed to build or purchase infrastructure to support approximately 6,000 housing units. Although Junction City traditionally housed approximately 45% of the soldiers living off-base, City officials wanted to position the City to attract the vast majority of new military households moving into the area. The City Commission annexed 1,400 acres of land and work began on 56 housing subdivisions[4].

Early on, a shortage of housing was a concern. News articles in March 2006 indicated that homes were not being built fast enough to meet the growing military population[5]. However, by November 11, 2006, *The Daily Union* reported that Junction City had 6,276 housing units constructed or under construction[6]. Therefore, the City's commitment to the Housing Program appears to have been immediate and significant.

Anticipated Housing Demand Did Not Materialize as Projected

The demand for housing did not materialize as originally projected and by February 2007, the news media reported that there were growing concerns regarding possible overbuilding in Junction City[7]. The reasons for the slowdown in housing demand were many. However, there appear to be three major contributing factors.

First, the Army's plans regarding troop movements evolve continually. Therefore, the number of expected troops and the timing of their arrival is always subject to change. To date, troop deployment and reassignments have been impacted by overseas combat operations related to the Global War on Terror and other contingency operations, reducing the number of military personnel and their dependents moving to the community. Furthermore, these operations have countered the military's announced intention to station soldiers at Fort Riley for five to seven-year stints. Instead, many soldiers have been assigned to Fort Riley for a two or three-year tour and then have been sent to other installations. Some soldiers may have decided to rent rather than buy given the uncertainty of the length of their assignment to Fort Riley.

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[2] At that time, Fort Riley's population, including soldiers, family members, civilian workforce and retirees and their families, was estimated at 48,000.

[3] *Housing Summit Conducted on Fort Riley.* IMA Headquarters New, March 21, 2006. www.ima.army.mil/sites/newsletter/ftrileysummit.asp (9/21/2009).

[4] "Updates from the City Manager", 12/14/2007. www.jcks.com/rodupdates/archives/2007.1214.html.

[5] http://www,ktka.com/news/2006/mar/26/home_sales_continue_plague_manhattan/.

[6] *MPC to Increase Scrutiny of Housing,* The Daily Union, November 22, 2006.

[7] Ibid.

Second, troops that were assigned to Fort Riley tended to be younger than originally expected as brigades have been going through rebuilding efforts[8]. The greater than expected number of younger, single soldiers has resulted in fewer dependents and a higher demand for rental housing than the community originally anticipated. Furthermore, it is reported that soldiers are arriving with a very high debt load and highly leveraged, possibly impeding their ability to qualify for a home loan[9].

Lastly, it has been suggested by Fort Riley that an additional significant factor may be the affordability of the housing being built. Affordable housing is cited by the military as a "key component" of families following their soldier to Fort Riley[10]. Affordable housing is defined by the soldiers as housing expense that does not exceed the Basic Allowance for Housing ("BAH"). The BAH is intended to cover 100% of the median *rental* cost (rent, utilities and renter's insurance with $0 out-of-pocket) for an area[11]. However, it appears that the developer community may have been ascribing to the generally accepted definition of affordability, which indicates that a household should spend no more than 30% of salary on housing. Thus, it appears the developers were expecting soldiers to be willing to utilize part of their salaries in addition to their BAH to meet their monthly mortgage expense.

Several of the housing developments in Junction City had price points of $160,000 and up[12], which were above the affordability guidelines of $120,000 to $150,000 stated by the Army. It is possible that the housing shortage experienced in the late winter and early spring of 2006 may have induced some developers to build more expensive housing, anticipating that the demand would move up in price point due to the shortage. A City official indicated that although the City approved infrastructure for housing developments, the City ultimately had no control over the floor plans and finishes or price points of homes ultimately built by a builder.

Current Housing Need Projections

Fort Riley's most recently published troop strength and housing need assessment is contained in the September 9, 2009 Central Flint Hills Region Community Partnership Conference presentation[13]. In that document, current soldiers assigned to Fort Riley total 16,528, although soldiers projected to be on base are expected to average 11,750 over the next two years due to deployments. Currently, 8,169 families or approximately 50% of the number of assigned soldiers have accompanied their soldiers to Fort Riley. The presentation indicates that 4,251 soldiers live in local communities, with 1,824 of those soldiers, or 43%, residing in Junction City.

The military projects that by Fiscal Year 2013, there will be 19,002 soldiers assigned to Fort Riley. Based upon current projections, 50% of the families are expected to accompany their soldiers to the area. Therefore, Fort Riley projects that it will need 9,392 available housing units by 2013. Projected on-post inventory in 2013 is 3,307 housing units. However, utilizing current available off-post housing numbers, a shortfall of 485 housing units is projected. As detailed below, that number is comprised of a shortfall of 1,610 two-bedroom units and a surplus of 739 three-bedroom units and 386 four-bedroom units. Therefore, Fort Riley's need going forward is anticipated to be in the area of affordable two-bedroom town homes or rental units.

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[8] www.oea.gov/OEAWeb.nsf/Summit+Profile?readform.

[9] www.oea.gov/OEAWeb.nsf/Summit+Pres?readform.

[10] The Central Flint Hills Region Community Partnership Conference, May 20, 2009.

[11] The Central Flint Hills Region Community Partnership Conference, September 18, 2008.

[12] Moon, Chris, "Malone hopes to ride Junction City housing wave as troops return to post." *Wichita Business Journal*, February 23, 2007.

[13] http://www.riley.army.mil/Documents/CPC_Housing/090908165009.pdf.

	2013 Requirement	2013 Projected On-Post Inventory	2013 Projected Off-Post Inventory	2013 Projected Demand
Two-Bedroom	4,226	735	1,881	-1,610
Three-Bedroom	2,911	1,157	2,493	+739
Four-Bedroom	2,255	1,415	1,226	+386
Total	9,392	3,307	5,600	-485

However, these projections represent a snapshot in time. At this writing, news media are reporting the possibility of a significant change in troop strength overseas, which could significantly impact these projections.

Junction City's Housing Plan

Junction City officials quickly moved to capitalize on the potential economic opportunity presented by the projected population growth. Although Junction City had traditionally housed approximately 45% of the soldiers living off-base, City officials expected Junction City to attract the vast majority of new military households moving into the area. The projections in the 2005/2006 timeframe were that 60% of the soldiers would be married and many would have school-age children. Historically, that demographic had tended to chose to reside in Junction City. Although it was known to City officials that the projected housing would be needed over a five-year period, a City official told us that Junction City took an aggressive stance due to the existing housing shortage at that time and to, in effect, be at the forefront of the housing boom in relation to other surrounding communities. Furthermore, we were told by many City officials, City staff and members of the development community that Fort Riley had made it known that the housing was needed immediately and that if the communities did not supply the housing, the anticipated military personnel might not be stationed at Fort Riley.

Due Diligence

In December 2005, a Tri-County Congress retreat was held that included city and county officials from Riley, Geary and Pottawatomie Counties. Emphasizing a regional approach, stakeholders formed the Flint Hills Regional Task Force. This task force used grants from the Department of Labor and the DoD to conduct joint planning studies such as the Land Use Study and the Strategic Action Plan and Growth Impact Assessment ("SAP") for the communities near Fort Riley. To further the planning efforts, a planning assistance management grant from the Office of Economic Adjustment was secured to conduct the Flint Hills Regional Growth Plan ("FHRGP"). Information from the studies was to be used by all three counties and their communities to assist in planning for infrastructure needs inclusive of housing, education, transportation, workforce and childcare. Representatives of Junction City were members of the task force.

Based on data collected in April 2006, the SAP projected a surplus of single-family housing and a need for more multi-family housing. The FHRGP found that as of June/July 2007, the housing market was already cooling. Developers and builders were voicing concern over data related to troop movements and had requested that the DoD provide consistent and timely information. It was noted that many developers were not fully aware of the total supply of units within the region, and that this lack of accurate data increased the possibility of over-development.

However, due to the City officials' perceived urgency of the housing need based upon initial information released by Fort Riley in 2005/2006, Junction City commenced its Housing Program well in advance of the release of the results of the studies. It was noted that the results of these studies were not publicly available until the 2007/2008 timeframe. A City official who served as a representative on the task force indicated that he did not have access to preliminary information from the studies, and that the timing of the release of the studies was too late in the development process to allow for a change in direction.

Junction City officials were relying heavily upon Fort Riley for the troop numbers and timing of their arrival. City officials told us that no other due diligence was done by the City prior to the implementation of the Housing Program as the State of Kansas was taking the lead on due diligence. Then Governor Sebelius had formed a committee to interface with the military and the local communities. In addition, City officials made a trip to Washington, D.C. and met with congressional leaders, Pentagon and Army officials and the Secretary of Civilian Aid. Reportedly, the information shared in those meetings was consistent with information being shared by Fort Riley at that time.

However, as previously stated, the Army's troop movements evolve continually. Therefore, ideally, due diligence would be an ongoing process whereby troop movement information and detailed demographic information on the incoming soldiers and their dependents would be made available to the local communities and would be used in their planning activities.

It appears that Junction City officials did keep in contact with Fort Riley officials with regard to the number of troops and dependents anticipated. But City officials appear to have focused more on the final projected growth rather than the interim influx of military-related personnel to the community. Therefore, the aggressive Housing Program undertaken by Junction City was well entrenched by the time the housing demand slowdown began to emerge in the first six months of 2007. As a result, subdivision development sped past demand. We inquired of City officials why the Housing Program was not undertaken in a phased approach in which a certain number of housing units would be built and a stated absorption rate reached prior to additional development being approved. We were told that officials from Fort Riley indicated that the housing was needed as soon as possible and the fear was that if Junction City did not provide for the required 6,000 housing units quickly, the other surrounding communities would.

City officials were admittedly inexperienced with this magnitude of growth and perhaps focused more on the potential opportunity presented than the inherent risks of such an aggressive plan should troop movements not materialize as originally projected. Through our review of documentation and interviews of many City officials, representatives of the development community and members of the public, we found no evidence that any City official made a decision or pursued a growth strategy with malicious intent. However, given the lack of experience of City officials in this arena, prudence should have mandated the consideration of the use of the services of a City Planning Consultant at the outset of the Housing Program. Community planning activities should have taken a long-term view, but with short-term benchmarks to ensure that the development activity more closely adhered to the evolving housing demand.

Use of Development Agreements

Initially, Junction City utilized Special Benefit District financing in which approved infrastructure was contracted for by the City and assessed 90% against the Improvement District and 10% against the City at large over a 20-year term. This was the norm until spring of 2006 at which time City officials were looking to speed up the timeline to bring then needed infrastructure on line.

Traditionally, it took a number of months to move a development through the City's approval process to the point where the construction of infrastructure could commence. The extended length of time was due to the applicable legal requirements attached to a municipality. For example, the traditional process involved the City being responsible for the construction of the infrastructure. Once the petitions for infrastructure and related engineering costs submitted by the developer were approved, the City had to competitively bid the contract to construct the infrastructure. These requirements could take a number of weeks to complete.

As the Housing Program progressed, it was determined by City officials that more housing was needed quickly. Therefore, to shorten the time frame, the City investigated opportunities to "buy" infrastructure and suggested or accepted the use of Development Agreements. If the infrastructure was purchased, rather than built by the City, we were told by a representative of City's bond counsel, Gilmore & Bell, that a written agreement of some sort was required and that Gilmore & Bell suggested using Development Agreements. Reportedly, construction could begin after the Development Agreement was signed, but before the petition was formally approved. Furthermore, as the City was purchasing rather than building the infrastructure, there were no competitive bid requirements. Therefore, the construction of infrastructure could start earlier in the process.

Of the 39 developments we reviewed, Development Agreements[14] were used for:

- Eagle Landing - agreement dated June 20, 2006,
- Sutter Woods - agreement dated July 27, 2006; amended September 2, 2008,
- Falcon Ridge - agreement dated July 2006,
- Sutter Highlands - agreement dated August 30, 2006,
- Olivia Farms - agreement dated September 19, 2006, amended October 14, 2008
- Mann's Ranch Phase 1 - agreement dated September 20, 2006,
- Village at Freedom Place Phase 2 - agreement dated September 30, 2006, and
- A.C. Development - agreement dated June 2007.

The Development Agreements were reportedly negotiated between the developer, the then City Attorney and City staff. The individual commissioners indicated that the Commission was not involved in the negotiation process. However, the City Commission approved all Development Agreements.

There are many similarities among the Development Agreements. For instance, all agreements allow for the "Turnkey" construction of infrastructure in which the developer manages the design, construction and installation of infrastructure. The City purchases the infrastructure from the developer for the petitioned amount, plus the amount of any approved Change Orders.

Reimbursable items under the Development Agreements included:

- All fees and expenses paid by the developer for design of improvements and preparation of plans
- All verified costs paid by the developer to contractors and third parties for construction and installation of the improvement
- All fees paid by the developer for periodic inspection of the improvements on behalf of the City

[14]The copy of the Development Agreement reviewed by BKD for Falcon Ridge had not been executed by the developer. The copy of the Development Agreement reviewed by BKD for A.C. Development and Village at Freedom Place Phase 2 had not been executed by the developer or the City.

- All interest expense paid by the developer on construction period financing
- And, any miscellaneous bona fide and verified out-of-pocket expenses in the design, construction, installation and inspection of the improvements which the City would normally incur had they contracted directly for the performance of work

Land acquisition costs were not a reimbursable cost under the Development Agreements and no developers for subdivisions under our review were reimbursed for land acquisition costs according to information available for review.

Some developers requested and received additional incentives for their developments through their Development Agreements. For example, the City waived building permit fees and utility line connection or tap fees and provided water meters and pits, and connected the water service lines extending from the mains for free for Eagle Landing. Hook-up fees were also waived for Village at Freedom Place. Olivia Farms and A.C. Development were given water hook-up and sewer hook-up fees of $500 per lot per hook-up. These fees were not outlined in any other agreements.

The Development Agreements for Olivia Farms and A.C. Development both outline the ability to donate or specify areas to be designated as City owned public parks and public spaces. Upon acceptance of the plat for the subdivisions by the City, the maintenance of the areas would become the City's responsibility, and these areas would not be included in the allocation of the Special Assessments. However, the A.C. Development project did not ultimately offer public parks or public spaces to the City and the offered donations by Olivia Farms were rejected by the City Commission in September 2009.

In line with the City officials' desire to speed up the development process, most of the Development Agreements required the construction to be substantially completed within 270 days, or less, following the City's notification to the developer that it had approved and accepted the plans.

Significantly, as the purchase of infrastructure did not require a competitive bid process, it would appear that the City had no avenue to ensure that the infrastructure was being constructed in a cost-effective and efficient manner. A City official indicated that City officials realized that there would likely be a premium associated with the building of infrastructure in a short period of time. For instance, BKD was told by a representative of Big D that Big D paid a 7% premium to Larkin Excavating in order to meet a prescribed deadline to complete the infrastructure.

The City official further countered that the City Commission had signed off on a petition and associated engineer's costs for each development that utilized a Development Agreement and that all Development Agreements stated that the City would not be obligated for more than the petition amount plus any approved Change Orders. After appropriate adjustments[15], no subdivision under our review exceeded its petitioned amount. However, we found that the subdivisions of Falcon Ridge, Olivia Farms, Sutter Highlands and Sutter Woods petitioned the City after the Development Agreements were in place. In most instances, the City's files contained no documentation indicating that the Commissioners knew the estimated costs of the infrastructure for these subdivisions when agreeing to purchase them. Furthermore, actual construction began at some of these subdivisions prior to the petitions being approved by the City Commission.

[15]Eagle Landing general ledger payments exceeded the amended petition amount by $8,731.03. This was due to a $73,600 bill from J&K Contracting for water meter work completed as agreed upon in the Developers Agreement, which was not included in the petition amount. The costs for Village at Freedom Place exceeded the petitioned amount by $63,451.23 due to the cost of the dirt billed to the subdivision in contravention to the Development Agreement. Refer to page 27 of this report for a full discussion of this issue. Doc Hargreaves #1 exceeded the petition amount by $24,000. However, the petition contained a clerical error as it did not include the standard engineering soft costs, which were on the engineer estimate of costs.

Subdivision Development Policy Change

In the midst of the period in which the City was negotiating the majority of the Development Agreements, it was determined that the risk to the City of vacant lots with unpaid Special Assessments would grow as future development occurred. Therefore, to attempt to address that risk, as well as to preserve future City debt capacity for economic development, a number of revisions to the Subdivision Development Policy were considered in August 2006.

The then current subdivision regulations for the installation of improvements indicated that the City would pay 10% of the cost of streets, water, sewer, storm sewer, and sidewalks. The developer would be responsible for 90% of those costs. Generally, the developer would petition for this 90% to be passed onto homeowners through Special Assessments against the Improvement District, in the manner described in the "Special Benefit Districts" section in Appendix A[16]. The City's debt on the street portion of the improvement counts towards the City's general obligation debt limit, while water and sewer do not.

It was noted that the implementation of any policy revision would impact a number of developments. Therefore, a summit was scheduled for August 22, 2006 to invite public comments. The major issue discussed at the summit appears to have been the competitive advantage developers would have under the then current policy versus the proposed new policy. In August 2006, there were 20 subdivisions pending approval.

According to the August 29, 2006 City Commission minutes, the City staff recommended that the Subdivision Development Policy be changed effective October 1, 2006. On that date, the policy would require the developer to pay 100% of the cost of infrastructure. The developer could then petition the City to create a Special Benefit District. The City would continue using Special Assessments for water, sanitary sewer and storm sewer, but the cost of the streets would be the developer's responsibility. The developer would include the cost of the streets in the price of the lots. Beginning January 1, 2007, the developer would be required to pay for 50% of the street cost, with 50% assessed to the City. On January 1, 2008, that percentage would change to 75% of the street cost to the developer and 25% to the City. Finally, on January 1, 2009, 100% of the street costs would be paid for by the developer.

City staff further recommended the use of the Kansas Rural Housing Incentive Districts ("KRHID") to assist in the financing of infrastructure for subdivision developments of 100 lots or more. Subdivisions that would have been eligible at that time included Mann's Ranch, Sutter Woods, Sutter Highlands and Olivia Farms. The staff proposed using the then current 90/10 policy for pending subdivisions, inclusive of: Deer Creek Addition #2; Replat Michael's Run Addition, Oakwood Village Townhomes; Rivendell Addition; Doc Hargreaves Hilltop #5; Eagle Landing Addition; Indian Ridge Addition Unit #6; A.C. Development Unit #1; Village at Freedom Place Phase 2; Hidden Valley; Falcon Ridge; Russell J. Johnson Addition; and Deer Creek Unit #3.

The City staff considered the Subdivision Development Policy revisions and the use of KRHID for larger subdivisions to be as fair as they could be to current developments planned using the 90/10 policy, while retaining some debt capacity for the City for other major uses.

Action on this issue was tabled until the September 5, 2006 City Commission meeting. At that meeting, the City Commission unanimously voted to amend the Subdivision Development Policy to "start immediately with the 100% of the street improvements paid by the developer". There is no mention of any of the other suggestions from the August 29, 2006 meeting specifically being voted on. City staff could not find where the Commissioners updated the policy or passed a formal resolution updating the City codes. Therefore, it appears that none of the suggested changes officially took effect.

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[16] Refer to Appendix A – Funding Mechanisms for Housing Infrastructure for a discussion of the details of the various infrastructure financing mechanisms utilized or considered by Junction City for its Housing Program.

Financing of Junction City Housing Infrastructure

Special Benefit District Financing

All of the subdivisions within our scope ultimately utilized Special Benefit District financing and petitioned for Improvement Districts within which Special Assessments are assessed against homeowners to reimburse the City for the majority of the cost of the infrastructure within the Improvement District. Infrastructure costs eligible to be included in Special Assessments are detailed in Appendix A. We found that all infrastructure costs assessed against the subdivisions under our review were "eligible" costs. Special Assessments within subdivisions under our review are listed in ***Exhibit B***.

City Upgrades to Infrastructure

The City capitalized on the opportunity presented by the development boom and requested upgrades to the infrastructure in some subdivisions to provide for the future growth of the City. We found upgrades within ten of the developments under our review. Upgrades included, but were not limited to:

- Additional roads
- Paving of roads
- Lift stations
- Upgraded water mains
- Additional storm sewers

A City official indicated that City requested infrastructure upgrades would not be allocated to the Improvement District, and therefore not be included in the Special Assessments. We found, however, that the allocation of the cost of the upgrades was not consistently calculated. As an example, the infrastructure for both Deer Creek #1 and Deer Creek #2 included City upgrade costs in connection with the paving of Sandusky Drive. The additional paving cost for Deer Creek #1 was compared to the total construction cost. That additional percent was added to the 10% to be allocated to the City at large. In this case, the 13.56% additional cost was added to the standard 10% for a total of 23.56% of the cost allocated to the City at large.

When calculating the City at large percentage in Deer Creek #2, the amount of upgrade for paving was removed from total construction costs, and 10% of these remaining costs were calculated. Then, the cost of the upgrade for paving was added to the 10% City at large cost. This calculation gave the total cost to the City at large. This total was then divided by the entire cost of the improvement, which resulted in a 22.78% allocation to the City at large. Had Deer Creek #2 been calculated in the same manner as Deer Creek #1, the cost allocation to the City at large would have been 23.33%, a difference of 0.55%. We have not found any City policy or procedure that dictates the appropriate methodology by which City requested upgrade costs should be allocated to the City at large.

Additionally, during our analysis, we found that the City did not recalculate the assessment percentage for City requested infrastructure upgrades of $600,636.99 and $91,369.34 for Sutter Woods and Sutter Highlands, respectively. These upgrades respectively represent approximately 11.3% and 1.8% of the construction costs for those two subdivisions. As these amounts were not separated in the calculation of the percent assessed to the City at large, it appears that 90% of the City requested upgrade costs are included in the Special Assessments for lots in those subdivisions.

Recommendations

- We recommend the Commission formalize a consistent methodology to be used to calculate the City at large percentage for City requested infrastructure upgrades.
- We recommend the Special Assessments for Sutter Woods and Sutter Highlands be reviewed for accuracy with regard to the City requested infrastructure upgrades and amended accordingly.

Unsuccessful Attempts for KRHID Funding

As previously discussed, the City sought to use KRHID[17] to assist in the financing of infrastructure for subdivisions of 100 lots or more. In the spring of 2006, the City received the approval of the State of Kansas for the creation of a KRHID. On November 6, 2006, the City Commission approved the establishment of a KRHID for Olivia Farms for the construction of streets. On January 2, 2007, the City Commission approved the inclusion of Mann's Ranch, Sutter Woods and Sutter Highlands in the KRHID. Ultimately, only Olivia Farms, Sutter Woods and Sutter Highlands were included in plans to utilize KRHID.

KRHID was hoped to be used to reimburse the City for street related infrastructure paid for by the City and the developers for certain qualifying expenses not reimbursed by the City. Under KRHID, the City would receive the captured incremental property taxes instead of Special Assessments against the property to pay for the portion of street, curb, gutter and sidewalks assumed by the City. The City proposed that KRHID would be used to make the Special Assessments for Olivia Farms, Sutter Woods and Sutter Highlands more in line with Special Assessments on other developments, thus making lots in those three subdivisions more salable. However, some saw KRHID as an advantage being offered to the developers of those subdivisions that was not made available to other developers, thus creating an unfair financial advantage for those developers.

In 2007, although the specific KRHID plans for the three subdivisions had not been formally submitted to any taxing authority for approval, the School Board and the County Commission formally considered the creation of the KHRID. The School Board approved the KRHID. However, in December 2007, the County Commission voted against the creation of a KRHID. Reportedly, the majority of the County Commissioners felt that the City did not discuss the use of KRHID with them and took for granted that they would approve the districts. A City official offered that the City had in fact not formally communicated with the County Commission regarding KRHID and may have assumed their eventual approval based on their previous approval of the KRHID for The Bluffs project. However, efforts at educating the public and providing adequate information to the County Commission were made in early 2008. In July 2008, the City formally notified the Board of County Commissioners that the City was considering the approval of a KRHID for Sutter Woods, Sutter Highlands and Olivia Farms.

The plan for each subdivision was that the City would assume an "at large" portion of the costs of street infrastructure improvements. The portion of the street infrastructure costs not assumed by the City would be paid by Special Assessments. The real property taxes attributable to the increased values of properties after the 2008 "base year" would be "captured" and used in the following order of priority:

[17]Refer to Appendix A – Funding Mechanisms for Housing Infrastructure for a discussion of the detail of the various infrastructure financing mechanisms utilized or considered by Junction City for its Housing Program.

1. First, to reimburse the City for its "at large" share of the costs of street infrastructure improvements and related financing costs. The plan was for the following amount of street related infrastructure costs to be allocated to the City at large.

	% of Street Costs	Not to Exceed
Olivia Farms	54%	$ 2,592,494.00
Sutter Woods	74%	3,599,849.23
Sutter Highlands	49%	2,980,484.75

2. Second, to reimburse the developers for certain costs which were eligible for reimbursement under KRHID and had not been reimbursed to developers by the City under the Special Benefit District financing. The additional costs reimbursable to the developers were capped as follows:

	Not to Exceed
Olivia Farms	$ 1,120,392.16
Sutter Woods	574,825.00
Sutter Highlands	674,580.00

The additional reimbursement sought for Olivia Farms was to reimburse the developer for hard and soft costs, specifically, interior streets, sidewalks, street trees and street landscaping, irrigation for street ways, street signs, monument signs at entryways, supervision and overhead, erosion control, seeding, compaction tests, drainage way and retention pond, fence that borders the project and street lights that serve the development, and costs to extend gas, electricity, cable and telephone service connections. The additional reimbursement sought for Sutter Woods and Sutter Highlands was to reimburse the developer for underground utility trenching and conduits within the public right-of-way.

The incremental property taxes from the three taxing authorities, the City, the School District and Geary County, were to be captured for 15 years, beginning in 2009, except that the capture period for Geary County taxes would have been limited to 10 years. The property taxes based upon the 2008 base year would not have been captured, and would have continued to go to the taxing jurisdictions. Conventional Special Benefit District financing would have been used to pay for water, sewer and storm sewer improvements

On November 10, 2008, the County Commission again voted not to approve the use of KRHID funding for Sutter Woods and Sutter Highlands. On November 12, 2008, Fort Development withdrew its pending application for KRHID financing for Olivia Farms. On January 13, 2009, all three subdivisions' petitions were amended to allow for 90% of the infrastructure costs for streets, water, sewer and storm sewers to be assessed against the Improvement District and 10% to be paid for by the City at large.

Review of Housing Developments Subject to Analysis

Preliminary research was conducted on each development listed in ***Exhibit A***, which included, but was not limited to:

- Identifying owners and investors of the development, where possible
- Kansas Secretary of State information on the development company
- Kansas Secretary of State registered agent information and related companies
- Internet searches of developer and owners

For each development, we collected and analyzed information from the City's individual subdivision files, the City Engineer's files and bond issuance documentation, if available. This included, but was not limited to:

- Development petitions
- Development Agreements (for certain developments)
- Amended development petitions
- Engineer Cost Estimates submitted with development petitions
- Board Resolutions
- Commission meeting minutes
- Bids for construction
- Pay estimates
- Change Orders
- Engineering agreements
- General ledger information
- Bonded cost information
- Development plats

With this information, we were able to perform a number of analyses, which are described in more detail in the following section:

- Analysis of bid submissions for developments without Development Agreements
- Analysis of Change Orders on construction costs
- Pay estimate documentation
- General ledger records for the developments
- Bond financing cost analysis of selected developments

Analysis of Bid Submissions for Developments without Development Agreements

All developments that did not utilize a Development Agreement utilized a competitive bidding process to hire the contractor to build the infrastructure. There were 31 developments under our review that used a competitive bidding process. KVE served as the design engineer for the developments and performed many of the duties of the City Engineer at various points in the Housing Program. Through interviews with KVE and City staff, we learned that KVE would typically disclose to inquiring contractors a general figure for the engineering estimate for the development(s). Contractors would then submit sealed bids. The bid openings were reportedly held at meetings that were open to all bidders and representatives of the City. It was standard for KVE to recommend to the City the lowest "reasonable bidder" for each job. A contractor may not have been considered a "reasonable bidder" if KVE was not familiar with the contractor or did not know their work history.

Our analysis of the bids on all competitive bid developments indicated that the cost of the winning bid averaged 84.9% of the engineering estimate for the job. It was noted that J&K Contractors won 72% of their bid submissions, a significantly higher percentage than any other contractor. We inquired as to whether there were any significant relationships, business or otherwise, between any bidders and City officials or representatives of KVE. We were told that, outside of normal social relationships that would be expected for a city the size of Junction City, there were none. According to a representative of KVE, J&K Contractors made a business decision to aggressively price their bids to gain the work. See ***Exhibit C*** for the detailed results of the bids. A summary of the bid analysis is presented below:

	Number of		%
	Bids	**Wins**	**Wins**
J&K Contractors	25	18	72%
Middlecreek Corp	25	2	8%
Nowak Construction	22	1	5%
Midlands Contracting	17	6	35%
Smokey Hill, LLC	10	0	0%
Emerson Construction	6	1	17%
Ebert Construction	5	2	40%
Meadows Construction	5	0	0%
Bazin Excavating	3	0	0%
Larkin Excavating	3	0	0%
Boyd Excavating	2	0	0%
Wildcat Construction	2	0	0%
Carlson Utility, LLC	1	0	0%
Cheney Construction	1	0	0%
Deep Creek Const.	1	0	0%
Hi-Plains Sand, Inc.	1	0	0%
Joshua Excavating	1	0	0%
Walters-Morgan Const.	1	0	0%

Analysis of Change Orders in Construction Costs

After reviewing the competitive bidding process and the winning bids, we considered the possibility that Change Orders could have caused the bid to be awarded to other than the actual low bidder.

Throughout the construction process, Change Orders of over $1 million dollars were added to the approved petition amounts for developments under our review. Change Orders were brought before the City Commission, typically with a recommendation from the City Engineer, and were approved or denied. For the developments under review, 42 Change Orders were made on 19 different developments. The largest Change Orders were in the developments of Olivia Farms totaling $352,000, and Prairie Ridge #1 totaling $336,930.65.

Olivia Farms operated under a Development Agreement. Therefore, neither City officials nor City staff reviewed or approved the Change Order requests. Olivia Farms Change Order #1 involved a $195,000 increase "related to excess rock generated by street, sewer, storm and waterline excavation", which was approved by Fort Development LLC. Change Order #2 was for $157,000 "to cover the additional site grading that was due to excess rock and the additional hauling to place compactable fill", approved by Fort Development LLC.

The two Change Orders in Prairie Ridge #1 included Change Order #1 for $325,486.65 for site changes from single family to multi-family, which required different sanitary and water sewer lines and Change Order #3 for ($11,444) for the deletions of gas conduits due to the use of electric power in all future buildings. All Change Orders for Prairie Ridge #1 were approved by the City Commission.

Below is the summary of the Change Orders per contractor.

Contractor	Number of Developments	Number of Change Orders	Total of Change Orders
J&K Contractors	9	21	$ 157,614
Midlands Contracting	3	7	356,891
Middlecreek Corp	2	6	73,811
DFC Company of Lawrence	1	2	352,000
Ebert Construction	1	2	13,523
Emerson Construction	2	2	23,316
Nowak Construction	1	2	25,819
	19	42	$ 1,002,974

From the information contained in the City's files, it does not appear that any Change Orders were inappropriate. Upon inquiry to the City Engineer, we were told that the larger Change Orders approved by the City, such as those described above for Prairie Ridge #1, would have been made by any contractor due to changes in the underlying project. Therefore, it does not appear that any Change Order for a competitively bid project would have resulted in another contractor being the low bidder.

Pay Estimate Documentation

Non-Development Agreement Developments

Payments for construction on the non-Development Agreement developments exceeded $25 million. During our review of the pay estimate documentation, we noted that the contractor submitted an "Estimate for Payment" form which indicated the amount of the contract price, units completed and the value of work completed. The form provided a signature area for the job engineer, City Engineer, City Manager and the contractor. It also had an area to record the date the pay estimate was approved by the City Commission.

We inquired as to what additional documentation was provided for construction pay estimates. Interviewing City staff, we learned that the City felt the "Estimate for Payment" form submitted was sufficient, and required no other documentation. Per City staff, payments were compared to the contract price from the bid, and over runs were reviewed on a line-by-line basis. The City Engineer would question any significant line cost overrun.

We had expected to see, at a minimum, documentation such as subcontractor contracts, a summary of hours worked, invoices from subcontractors, and invoices or receipts for materials. With no additional documentation required by the City for payment, there can be no assurance that the City paid the actual costs for the development or that all materials charged to the project are actually for that project.

The pay estimate documentation in the City's subdivision files and the City Engineer's files was voluminous, but incomplete. For all 39 developments which had multiple pay estimates (typically 4-8 each), we were not able to find complete pay estimate documentation on all requests. Other pay estimates in the files were at various stages of approval.

Recommendations

- We recommend the Commission evaluate the policy of the required documentation for pay estimates, and consider requiring more support for payments.
- We recommend an internal review be conducted of each subdivision file to ensure the information is complete and includes appropriate documentation for each pay request.

General Ledger Records for the Developments

The City recorded payments for the developments in its general ledger in Fund 88 (Buildings & General Improvements) in separate job codes. It was the intention of the City to have a separate job code for each development. The general ledger shows detailed information such as the check number, check date, payee, amount, and usually a general description of the payment.

We reviewed a "History Detail Listing" general ledger report for each development and analyzed the costs that had accumulated. Costs were typically broken down into sub-accounts, including engineering services, contractor's agreements, other services, and interest.

There were multiple instances where the costs for a development were included in the general ledger detail of another development, or the general ledger showed costs that belonged to a project outside of the scope of our review. Discussions with City staff revealed that early on there were some issues with coding and human error mistakes were made along the way. City staff also mentioned that some job codes were re-used, and a job code may contain costs for more than one project.

City staff indicated that they chose not to make journal entries in the general ledger to correct the mis-postings they identified, as a journal entry does not contain the same level of detail (check date, check number, etc.). Therefore, City staff decided to leave the entries where they were, and work to make sure when these costs were bonded, they ended up in the right development. (See the "Bond Financing Cost Analysis" section below for our review of the bonded costs.)

BKD found over $6.3 million of costs that were incorrectly coded for general ledger purposes. (See ***Exhibit D*** for the detail of these amounts.) Over $4.5 million of these mis-posted costs related to projects that were not in the scope of our analysis, and therefore we did not review the supporting documentation for these expenditures. We found no indication that any reconciliation was preformed between the authorized development expenditures and the costs that accumulated in the general ledger system.

Recommendations

- We recommend the Commission consider hiring a chief financial officer to oversee the accounting function for the City.
- We recommend the procedures on coding costs to the general ledger system be reviewed. Personnel making accounting entries should be appropriately trained, and a second level of review of expense coding should be performed.
- We recommend a periodic review of the developments costs in comparison with authorized amounts for each subdivision be conducted. This may identify any costs that are inadvertently mis-posted.
- We recommend when mis-postings are identified, a corrective journal entry be made to move the cost into the correct account. This will allow the general ledger to properly reflect the cost in each development at any given time.
- We do not recommend the reuse of job codes. The general ledger system should be robust enough so that reusing codes is unnecessary.

Bond Financing Cost Analysis on Selected Developments

While reconciling the general ledger payments, we noted that some developments had more mis-postings than others. Based on the degree of mis-postings in the general ledger and other concerns arising during our investigation, BKD selected 12 developments on which to perform an initial analysis of bonded financing costs. The developments selected were:

- Doc Hargreaves #2
- Doc Hargreaves #3
- Ehlers Hilltop
- Ehlers Addition
- Olivia Farms
- Prairie Ridge #1
- Prairie Ridge #2
- Spring Valley #1
- Spring Valley #2
- Sutter Highlands
- Sutter Woods
- Wheatland Hills #4

We were provided worksheets that showed the build-up of costs for these developments. (See the "Olivia Farms", "Sutter Highlands" and "Sutter Woods" sections later in this report for further analysis of the costs included in the financing for those developments. The remaining nine developments are included in the analysis in this section)

We compared the worksheets to the general ledger detailed costs listings. This was a laborious and time consuming process, as the general ledger had significant mis-postings of costs as described previously.

We found:

- Costs that were in the general ledger and not included on the bond worksheet, and
- Costs on the bond worksheet that were not included in the general ledger.

Working with City staff, we determined the following (see ***Exhibit E*** for a detailed listing):

- $14,393 of cost was excluded from the issued bonds,
- $224,883 was included in the wrong project in the bonds issued, and
- $4,457 of cost was bonded in two projects, duplicating the cost.

The City staff person who is primarily responsible for the general ledger function of the City originally performed the reconciliation of the general ledger to the bonded costs. This individual indicated that the noted errors involved mis-coding, mis-keying and other mistakes. The individual told BKD that the City relied on its financial advisors to verify the amounts to be bonded prior to preparing the bond documentation. However, based on our analysis, it does not appear that detailed reconciliations are performed.

With findings of this significance, the City should consider expanding this analysis to the remaining 27 developments. Without reviewing the remaining developments, we cannot make a determination on the accuracy of the issued bonded costs for the City. Therefore, we make no determination of the accuracy of the Special Assessments against the lots in the subdivisions that were not reconciled.

Recommendations

- We recommend that reconciliation between bonded costs and the general ledger cost for the remaining 27 developments be performed, preferably by someone outside of the general ledger function.
- We recommend that future bond issuances have a multi-level review of bonded costs submitted for each subdivision or project. City staff should not rely on the City's financial advisors to catch errors in the accumulated costs.

Sutter Woods and Sutter Highlands

Sutter Woods and Sutter Highlands were developed by Big D, which was based out of Lawrence, Kansas. We looked specifically at Sutter Woods and Sutter Highlands during our investigation as a result of interviews with various developers and citizenry and the concerns they raised.

Sutter Woods

The original Sutter Woods Development Agreement between Big D and the City was dated July 27, 2006. As previously described in the section on "Use of Development Agreements", the Development Agreement was a turnkey agreement which obligated the City to purchase the infrastructure from the developer at an amount not to exceed the petitioned amounts, plus the amount of any approved Change Orders. Also as was the norm, there was no competitive bid requirement for the construction of the infrastructure.

According to a representative of Big D, infrastructure construction began in August of 2006 and builders began constructing single-family homes in September 2006[18]. Based on documentation made available to BKD, it appears that construction commenced prior to the City Commission's approval of the final costs the City would be obligated to pay.

The Engineer's Cost Estimates for water, sewer and storm sewer and for streets were dated January 24, 2007. However, we saw no documentation indicating that the City Commission had been presented those costs until the approval date of the petitions. The original petitions for water, sewer and storm sewer and for streets were not approved by the Commission until May 1, 2007. The petitions were amended in 2007 to revise the method of allocating the petitioned costs among lots. The petitions were amended a second time, after the failure of the KRHID for Sutter Woods in November 2008, to change the allocation of Special Assessments from 100% against the Improvement District to 90% against the Improvement District and 10% against the City at large. The petitions and amendments are detailed below.

	Petition Approval Date	Amount	Allocation Per Lot	Assessment to Improvement District
Water, Sewer and Storm Sewer	May 1, 2007	$4,234,014.58	% of total area	100%
	September 18, 2007	4,234,014.58	Equally	100%
	January 20, 2009	4,234,014.58	Equally	90%
Streets	May 1, 2007	3,024,009.58	% of total area	100%
	September 18, 2007	3,024,009.58	Equally	100%
	January 20, 2009	3,024,009.58	Equally	90%

A representative of Gilmore & Bell, the City's bond counsel, indicated that it would be permissible for construction on the infrastructure to begin prior to the approval of the cost by the City Commission as the City was acquiring the infrastructure rather than building it. A July 10, 2007 letter to the City from KVE, who was hired by the City to provide construction inspection services, indicated that "Sutter Woods meets the full project complete status" aside from a few listed exceptions. Therefore, it appears that significant construction costs were likely incurred prior to the City Commission's approval of those costs.

Recommendation

- We recommend that, in the future, all required approvals be in place prior to the construction of any infrastructure to be paid for by the City, as a risk management control.

[18] "Talking Points for February 18, 2008 Town Hall Meeting", Brennan Fagan.

Big D Construction Administration/Inspection Fees

We noted that the January 24, 2007 Engineer's Cost Estimates included an estimated $300,000 for "Construction Administration/Inspection" fees for the water, sewer and storm sewer petition and for the street petition, for a total of $600,000. However, on September 12, 2006, the City had contracted with KVE for the provision of construction supervision and inspection services. The City paid KVE approximately $134,000 for those services.

Pay Estimate #1 from Land Plan Engineering included this same $600,000 as "Construction Supervision". An amount of $95,000 was requested against this line item and was paid by the City. Documentation supporting this amount were invoices from Big D for "Superintendent Fees". Pay Estimate #1 totaling $6,165,233.64 was paid by the City on June 22, 2007.

A pay estimate from Land Plan was submitted in July 2007 for a total of $685,035.96, which was not approved or paid. This request for payment included the additional $505,000 of "Construction Supervision" fees. In August 2007, the City Engineer notified the City Manager and Assistant City Manager that the inspection cost for Sutter Woods had been billed. When the City Engineer reviewed the charge, it was noticed that this same line item in the budget was being drawn against by Big D. The City Engineer recommended that the City not pay the supervision fees to Big D, as the fees "were for construction administration and inspection. Which would be the inspection" which was being provided by KVE. The City Attorney and the City's Bond Counsel further reviewed the request for payment of "Construction Supervision" by Big D and both found that the City was not obligated to pay the request.

Pay Estimate #2 for $145,900.83 was paid on May 7, 2008. In the payment request, the $95,000 of supervision fees paid with Pay Estimate #1 was reversed, reducing the reimbursement to Big D. Therefore, ultimately Big D was not compensated for its "Construction Administration/Inspection" fees.

Costs Bonded for Sutter Woods

The total cost for Sutter Woods was as follows:

Payments to Big D	$ 6,311,134.47
Inspection paid to KVE	134,248.20
Water meters	60,500.00
City usage fees	11,470.00
Publications	2,570.05
Cost of issuance	266,660.29
Interest	515,436.45
Total infrastructure costs bonded	$ 7,302,019.46

Total costs for infrastructure construction, engineering design and financing costs payable to Big D under the petitions totaled $6,477,842.80. The actual payments to Big D for these expenses of $6,311,134.47 were within the amount approved by the City Commission. The total infrastructure costs bonded of $7,302,019.46 exceeded petitioned costs due to the inclusion cost of issuance incurred by the City in excess of estimated amounts.

Sutter Highlands

The original Sutter Highlands Development Agreement between Big D and the City was dated August 30, 2006. The Development Agreement was very similar to the Sutter Woods Development Agreement previously discussed.

According to a representative of Big D, infrastructure construction began in August of 2006 and builders began constructing single family homes in September 2006[19]. Based on documentation made available to BKD, it appears that the construction commenced prior to the City Commission's approval of the final costs the City would be obligated to pay.

The Engineer's Cost Estimate for water, sewer and storm sewer in the amount of $3,817,674.38 was dated January 24, 2007. The Engineer's Cost Estimate for streets in the amount of $3,336,436.94 was dated May 31, 2007. However, we saw no documentation indicating that the City Commission had been presented those costs until the approval date of the petitions. The original petitions for water, sewer and storm sewer and for streets were not approved by the Commission until May 1, 2007. The petitions were amended in 2007 to revise the method of allocating the petitioned costs among lots. The petitions were amended a second time, after the failure of the KRHID for Sutter Highlands in November 2008, to change the allocation of Special Assessments from 100% against the Improvement District to 90% against the Improvement District and 10% against the City at large. The petitions and amendments are detailed below.

	Petition Approval Date	Amount	Allocation Per Lot	Assessment to Improvement District
Water, Sewer and Storm Sewer	May 1, 2007	$3,817,674.38	% of total area	100%
	September 18, 2007	3,817,674.38	Equally	100%
	January 20, 2009	3,817,674.38	Equally	90%
Streets	May 1, 2007	3,336,436.94	% of total area	100%
	September 18, 2007	3,336,436.94	Equally	100%
	January 20, 2009	3,336,436.94	Equally	90%

As was the case with Sutter Woods, it appears that significant construction costs were likely incurred prior to the City Commission's approval of those costs.

Recommendation

- We recommend that in the future, all required approvals be in place prior to the construction of any infrastructure to be paid for by the City, as a risk management control.

Big D Construction Administration/Inspection Fees

We noted that the January 24, 2007 and May 1, 2007 engineering estimates included an estimated $310,000 for "Construction Administration/Inspection" fees for the water, sewer and storm sewer petition and for the street petition, for a total of $620,000. However, the City contracted with KVE for the provision of construction supervision and inspection services. The City paid KVE approximately $145,000 for those services.

[19] "Talking Points for February 18, 2008 Town Hall Meeting", Brennan Fagan.

Pay Estimate #1 from Land Plan Engineering included this same $620,000 as "Construction Supervision". An amount of $185,000 was requested against this line item and was paid. Documentation supporting this amount were invoices from Bid D for "Superintendent Fees". A total of $5,892,929.38 was paid in on June 22, 2007.

A pay estimate from Land Plan was submitted in July 2007 totaling of $501,783.29, which was not approved or paid. It included the payment for the remaining $435,000 of "Construction Supervision" fees. In August 2007, the City Engineer notified the City Manager and Assistant City Manager that the inspection cost for Sutter Highlands had been billed. When the City Engineer reviewed the charge, it was noticed that this same line item in the budget was being drawn against by Big D. The City Engineer recommended that the City not pay the supervision fees to Big D, as the fees "were for construction administration and inspection. Which would be the inspection" which was being provided by KVE. The City Attorney and the City's Bond Counsel further reviewed the request for payment of "Construction Supervision" by Big D and both found that the City was not obligated to pay the request.

Pay Estimate #2 was for $456,097.03 and paid on May 7, 2008. In the payment request, the $185,000 of supervision fees paid with Pay Estimate #1 was reversed, reducing the reimbursement to Big D. Therefore, ultimately Big D was not compensated for its "Construction Supervision" fees.

Costs Bonded for Sutter Highlands

The total cost for Sutter Highlands was as follows:

Payments to Big D	$ 6,349,026.41
Inspection paid to KVE	144,657.31
Water meters	74,000.00
City usage fees	13,360.00
Publications	2,592.00
Cost of issuance	268,187.12
Interest	514,459.77
Total infrastructure costs bonded	$ 7,366,282.61

Total costs for infrastructure construction, engineering design and financing costs payable to Big D under the petitions totaled $6,507,391.32. The actual payments to Big D for these expenses of $6,349,026.41 were within the amount approved by or incurred at the request of the City Commission. The total infrastructure costs bonded of $7,366,282.61 exceeded petitioned costs due to the inclusion cost of issuance incurred by the City in excess of estimated amounts.

Cost Concerns for Sutter Woods and Sutter Highlands

Concerns over the cost of these developments arose throughout our investigation. Based on the costs that were bonded, we have calculated the assessment per lot below:

	Sutter Highlands	Sutter Woods
Bonded cost	$7,366,282.61	$ 7,302,019.46
Percent to special assessment	90%	90%
Percent paid by City-at large	10%	10%
Special assessments (90%)	6,629,654.34	6,571,817.51
Number of lots	295	243
Assessment per lot	$ 22,473.40	$ 27,044.52

The Special Assessments per lot for Sutter Woods and Sutter Highlands are on the higher end of the range of Special Assessments for the subdivisions under our review. We found the following may have contributed to the level of the Special Assessments per lot:

- The use of a Development Agreement and turnkey development eliminated a public competitive bid process, which may have resulted in increased construction cost
- Big D was using a design/build method while planning to use KRHID financing for the costs which resulted in the expenditure of funds for certain improvements that absent KRHID, might not have been incurred or incurred at the price point actually paid
- Big D paid a 7% premium to Larkin Excavating due to the urgency for construction
- The contractors encountered more rock than they had expected. The method used for cutting the rock may have not been the most cost efficient (dynamite versus rock saw)
- Land Plan Engineers used different engineering models than KVE, and planned for larger water mains, more sewer infrastructure, more man holes, etc.
- As previously discussed, the petitions to the City did not include City requested upsizing in the amount of $600,636.99 for Sutter Woods and $91,369.32 for Sutter Highlands. However, these amounts were included in the bonded costs which were allocated 90% to the subdivision and 10% to the City at large

Olivia Farms

Olivia Farms is being developed by Fort Development, LLC ("Fort Development"), based out of Lawrence, Kansas. We looked specifically at Olivia Farms during our investigation as a result of interviews with various developers and citizenry and the concerns they raised.

The City entered into a Development Agreement with Fort Development on September 19, 2006. As a Development Agreement was used, there was no competitive bid process for the construction of the infrastructure. The contractor used for the construction of the infrastructure was DFC Company of Lawrence, L.C., a related party of the developer[20].

As previously discussed in the "Use of Development Agreement" section, the Development Agreement allowed for turnkey construction and obligated the City to purchase the infrastructure from the developer for the petitioned amount, plus the amount of any approved Change Orders.

An exhibit to the Development Agreement dated December 19, 2006 gave an estimated cost for the project of $16,493,579.80. This figure included significant amounts related to items that were requested for payment under KRHID, that were ultimately not reimbursed by the City. However, the Engineer's Estimates of Probable Construction Costs were dated March 8, 2007. The cost estimate for water, sewer and storm sewer was $4,553,748.74 and for streets was $5,159,560.51[21]. Petitions in those amounts were approved by the City Commission on September 4, 2007. The cost of the infrastructure was to be assessed equally per lot with 100% assessed against the Improvement District and 0% against the City at large.

[20]The Company's registered agent shares the address of Fort Development, and the same last name as the principal member of the developer.
[21]As revised on August 30, 2007.

There is six months between the signing of the Development Agreement which obligated the City to purchase the infrastructure at its cost to complete and the submission of the Engineer's estimates of those costs. Furthermore, there is nearly a year between the signing of the Development Agreement and the submission/approval of the petitions. Documentation in the City's files includes engineering fees dating back to September 2006, and inspection fees dating back to March 2007. This indicates that the construction of the infrastructure was well underway by the petition date. As previously mentioned, a representative of Gilmore & Bell indicated that there is no requirement that the petition be approved prior to construction commencing for infrastructure that is purchased by the City. However, by the date the City Commission approved the petitions, the developer had already incurred significant construction costs. The first pay estimate request, submitted by the developer on October 2, 2007, was in the amount of $7.8 million, or approximately 83% of the final construction costs.

Recommendation

- We recommend that in the future, all required approvals be in place prior to the construction of any infrastructure to be paid for by the City, as a risk management control.

Amended petitions were approved by the City Commission on September 2, 2008. The petition for water, sewer, and storm sewer amended the allocation of the Special Assessments from equally per lot to percentages per lot based on the type of housing to be built (single-family, multi-family or duplex). The petition for street costs made the allocation change, but also increased the petition amount from $5,159,560.51 to $7,389,846.79, an increase of $2,230,286.28. The City Commission minutes indicated that the increase was due to additional interest expense and bond and legal costs incurred by the developer due to the increased length of debt carry. The petitioned amount also increased due to the inclusion of a $561,000 escrow for sidewalks.

After the developer withdrew the KRHID application for Olivia Farms, as previously discussed, the street and water, sewer and storm sewer petitions were amended a second time and approved by the City Commission at a special board meeting on January 13, 2009. The cost of the street petition was reduced from $7,389,846.79 to $6,093,140.07. The water, sewer and storm sewer petition was increased from $4,553,748.74 to $4,990,961.99. Therefore, the final amount of petitioned costs for Olivia Farms was $11,084,102.06. The petitions amended the allocation to 90% to the Improvement District and 10% to the City at large. However, a notable aspect of these amendments is that they increased the size of the Improvement District by including a large tract of undeveloped land and allocating 16.5971% of the costs assessed against the Improvement District to that tract as described later in this report.

Costs Bonded for Olivia Farms

The total cost for the construction and engineering for Olivia Farms is detailed below.

Payments to developer	$ 9,418,271
Escrow for sidewalks	560,999
Water meters	98,000
City usage fees	10,140
Publications	2,038
Cost of issuance	416,352
Interest	623,313
Total infrastructure cost to be bonded as of September 2009	$ 11,129,113

The total costs to be bonded as of September 2009 of $11,129,113 exceeded the final petition amounts of $11,084,102.06 due to interest incurred in excess of the amounts estimated in the petitions.

Cost Concerns

The Special Assessments for Olivia Farms vary per lot based on the type of housing planned for each lot (single-family, multi-family or duplex). The majority of the lots have Special Assessments of between $24,000 (single-family) and $37,000 (duplex) per lot.

It appears that the Special Assessments may be higher in this development than others in the community due to a number of reasons:

- Representatives of the developer explained that they built Olivia Farms in the same manner and to the same level with regard to amenities and aesthetics they build all of their subdivisions. Olivia Farms was modeled after Hutton Farms, a subdivision City officials toured in Lawrence, Kansas
- The use of a Development Agreement and turnkey development eliminated a public competitive bid process, which may have caused an increase in construction cost
- Land Plan Engineers used different engineering models than KVE, and planned for larger water mains, more sewer infrastructure, and more man holes
- Fort Road was designated as a "collector" road by the City, and was therefore built with a roadway width of 41 feet. A representative of the developer indicated that per state law, a collector road is only required to have a roadway width of 31 feet. Furthermore, the representative of the developer indicated that the developer questioned the City's desire for a collector road when the subdivision does not collect traffic, and the topographic area will not allow the neighborhood to be expanded where it sits
- The concrete on the collector road was much deeper that the standard 6 inches. A representative of the developer estimated it is approximately 10 inches deep
- Additional financing costs were incurred by the developer due to the lengthened period of debt carry
- The terrain was covered with trees and hilly. Therefore, there was a higher cost for clearing and grading
- Fort Development was an out-of-town developer, and the development included mobilization cost of $80,000

Block 12, Lot 31

As previously discussed, on November 12, 2008, the developer withdrew the KRHID application for Olivia Farms as the applications for Sutter Woods and Sutter Highlands had recently been vetoed by the County Commission. However, the developer and the City Commission found a way to lower the Special Assessments for Olivia Farms by expanding the Improvement District to include a large undeveloped tract of land that was being held by the developer for future use. The City Commission approved second amended petitions for Olivia Farms at a special board meeting on January 13, 2009 which changed the petitioned amounts, as previously discussed, and the apportionment of Special Assessments between lots. The amended petitions allocated 16.5971% of the 90% of costs to be assessed against the Improvement District, estimated to approximate $1.7 million, to "Block 12, Lot 31", which originally was not part of the Improvement District and therefore had no allocation. An email from a representative of the developer to City staff indicated that this lot is zoned multi-family, and was initially going to be developed with the current Olivia Farms. However, it was subsequently determined that it would be better to develop this tract when the parcel to the east of the current Olivia Farms is developed.

Some citizenry have described this lot to BKD as "an eight acre ravine which appears to be waste land". If the description is accurate and this land is determined to be too difficult to build on in the future, there is a risk that the property could be abandoned by the developer. This could cause the taxpayers to absorb the cost of the $1.7 million of Special Assessments against this lot. Additionally, it appears that this lot may have been added to the Improvement District solely to reduce specials on the remaining lots as the City and the developer were not able to use KHRID to accomplish that goal.

Recommendation

- We recommend that consideration be given to conducting further investigation into the propriety of the expansion of the Improvement District to include Block 12, Lot 31.

Related Matters of Interest

Village at Freedom Place

The developer for Village at Freedom Place purchased land on Grant Avenue for the development of townhomes and apartments. The land was considered less than desirable by some as it was located in a flood plain. The developer met with City officials regarding the proposed development of Phase 1 and learned that there were back taxes due on the property. Reportedly, in a meeting with a City official in September 2005, the City official offered to refund the back taxes to the developer if the developer would pay them upfront. The City official also offered free dirt to be excavated and hauled to the development at the City's expense to resolve the flood plain issue and waived tap related hook-up fees for Village at Freedom Place. The City official told BKD that these offers were discussed when negotiating the Development Agreement, but that other than the waiving of hook-up fees, the incentives were never formalized in the agreement. The City official indicated that the rationale behind the offers was to assist the developer in getting the development "vertical" by the end of the year.

By check dated October 27, 2005, the City refunded $63,598.98 for the back taxes to the developer through check #97590. The City official indicated that the back taxes were refunded because they were long delinquent and the bonds on the original development in that location were retired. The payment was approved by the City Commission through their approval of the Appropriations Ordinance at their November 15, 2005 meeting. The Appropriations Ordinance is part of the Consent Agenda, thus there was no discussion of the content of the Appropriations Ordinance at the City Commission meeting. Therefore, BKD was unable to determine if the City Commissioners truly knew what the expense was for when approving it.

The dirt was donated from the Ehler's Addition subdivision and the City paid $87,656.50 to the dirt contractor for excavation and hauling of 18,454 cubic yards of dirt on December 1, 2005 through check #98089. The developer indicated that he had been told the City would cover the cost of the dirt excavation and hauling. However, our analysis indicates that the $87,656.50 was charged to the general ledger account for the Village at Freedom Place Phase 2 development. The general ledger total for the project agrees with the "project costs" in the "Statement of Final Costs" in the bond covering the cost of this development. This indicates that this amount is included in the Special Assessments for the development.

The Development Agreement for Village at Freedom Place Phase 2 indicates that "In accordance with the initial agreements regarding the VFP, the Developer and or Builder shall continue to be exempt from tap related fees at point of permitting."

The City official indicated that the City Commissioners were aware of these incentives through weekly reports. However, BKD could find no written documentation of any communication to that end.

Furthermore, these incentives were originally offered in conjunction with Phase 1 of Village at Freedom Place which was financed by the developer and that Phase did not utilize Special Assessments, but did utilize the Neighborhood Revitalization Program with a 95% tax abatement. Therefore, the developer stated that the Special Assessments for Village at Freedom Place, Phase 2 are incorrectly calculated and are too high.

Recommendation

- We recommend the City Attorney review the inclusion of the cost of the dirt for Phase 1 in Special Assessments for Phase 2 to determine if this represents a violation of any law, statute or ordinance.

Debt Management Policy

The City's Debt Management Policy details debt affordability limits for the City. These benchmarks are:

1. Total City debt is not to exceed $500 per capita
2. Total annual debt service as a percent of net expenditures shall not exceed 15% of the total governmental expenditures
3. Annual general obligation debt service as a percentage of assessed value of real property is limited to 3%
4. Total general obligation bond principle outstanding is limited to 75% of the statutory debt limit

The City's Comprehensive Annual Financial Reports include many of these calculations. The most recent report available from the City's website is for the year ending December 31, 2008. This report indicates that the City is not in compliance with some of the requirements of the Debt Management Policy.

The City has exceeded their maximum debt per capita for all years under our review.

	Net Bonded Debt Per Capita[22]
2005	1,034.74
2006	1,143.02
2007	2,009.39
2008	2,579.76

Furthermore, the $34,280,000 bond issued on May 15, 2009[23], and the bonds under consideration for issue as of February 2010, will substantially raise debt per capita, as the calculation for 2008 is based on a net bonded debt of $53,326,183.

The City works closely with bond counsel to ensure that it does not exceed its statutory debt limit. In the State of Kansas, a city is limited on the amount of bonded debt (General Obligation debt) they can have. This statutory debt limit for cities is 30% of their total assessed value. City staff testified in front of the Kansas House Governmental Organization and Elections Committee in February 2006, that Junction City needed an additional 9,000 housing units in the area over the next three years. The Committee voted in favor of allowing Junction City to have a 40% statutory debt limit for a period of five years, rather than the 30% then in place. The bill took effect after publication in the statute book in mid-2006.

[22]City of Junction City, Kansas Comprehensive Annual Financial Report for the Fiscal Year Ended December 31, 2008, page 73.
[23]Junction City Statement of Indebtedness, 2010.

Although the increase allowed for over $14 million more in debt in 2007, the City's debt affordably provisions indicate that the City should stay within 75% of their statutory debt limit. Therefore, the City is limited is 75% of the 40% statutory limit, or approximately 30% of their assessed value. The City has exceeded this limit. At December 31, 2008, the City's financial advisor calculated that the City was at 35.46%[24] of its statutory debt limit. The City is in compliance with the state statute; however, this level exceeds the limitation placed on the City under its Debt Management Policy. City staff has confirmed that they have not updated their Debt Management Policy for several years, dating back to the year 2000.

Recommendation

As the City is not in compliance with its own debt affordability limits, we recommend that the Commission amend the policy, or take steps to come into compliance with the existing policy.

Purchasing Policy

The City's written Purchasing Policy requires that all purchases in excess of $10,000 be competitively bid and awarded to the "lowest responsible bidder". Furthermore, purchases over $10,000 are to be awarded (approved) by the City Commission prior to their execution. Purchases below $10,000 may require a competitive bid and are awarded by the City Manager, or by the Purchasing Agent if below $300. Non-competitive negotiations can be used only when (1) the use of competitive negotiations is not feasible, such as only one supplier, (2) there is some public emergency or (3) the results of the competitive negotiation are inadequate.

When reviewing the bond amount for Village at Freedom Place, Phase 2, we noted that the $87,656.50 payment for the excavation and hauling of dirt, as previously discussed, did not appear to have been competitively bid or pre-approved by the City Commission.

The City Manager indicated that the hauling was not competitively bid as it was provided by the contractor for the Ehler's Addition where the dirt was taken from during construction. However, there is no indication that such a circumstance would be an exclusion from the competitive bid requirement.

The City Manager indicated that he had received approval for this payment by email from the members of the City Commission. However, our questioning of the City Commissioners on the Commission at the time of the payment indicated that none of them recalled such an email exchange. Furthermore, they stated that it would be highly unusual for them to be asked to approve payments by email. The City Manager indicated he had not retained copies of his email exchanges. However, he disagreed with the individual Commissioners' recollection of the event. It appears that this is an instance of non-compliance with the accounting policies of the City.

City Commission Approval of Checks

The City Commission receives Appropriations Ordinances in their meeting packets prior to the City Commission meeting. Typically, the Appropriations Ordinances will have attached check listings printed from the general ledger system that show a listing of the checks to be approved, what fund the check is being applied to, check number, payee, amount, and a short description of the purpose of the check.

In researching the previously discussed payment for the dirt for Village at Freedom Place, we searched the meeting packets preceding and subsequent to the issuance of the $87,656.50 payment, and found that the detailed check listings for the Appropriation Ordinances were not located in the City's files.

[24] City of Junction City, Kansas Comprehensive Annual Financial Report for the Fiscal Year Ended December 31, 2008, page 72.

We then searched for the detail supporting the Appropriations Ordinances where the City refunded $63,598.98 in back taxes, as previously discussed. Again, there was no detailed check listing in the City's files for the City Commission meeting.

Although the Appropriations Ordinances are passed at City Commissioner meetings, we have not been able to verify that the Commissioners are consistently provided information on the expenditures they are approving.

Recommendations

- We recommend that the City Commissioners not approve Appropriations Ordinances if they have not been provided the detail of the expenditures prior to the City Commission meeting.
- We further recommend that the Commissioners review the detailed expenditures in a manner as to fulfill their fiduciary duties as elected officials of the City.

Kaw Valley Engineering

KVE benefited financially from the Housing Program due to their involvement as a service provider in the development process. A representative of KVE indicated that KVE was involved in 98% of the subdivisions in the past five years. Their primary involvement was in the areas of surveys, plats, rezoning, annexing and de-annexing, and preparing infrastructure designs and cost estimates. KVE also provided construction observation and inspection services for the City for many of the developments. In that capacity, KVE was responsible for signing off on pay estimates, submitted by developers to the City, to verify that the work for which reimbursement was being sought had been completed. Of the 39 subdivisions under review, KVE performed various of these services for 38 of them.

KVE's fee for Engineering Cost Estimates was based on a percentage of their original cost estimate. However, we noted that on average, the actual construction bids were only 84.9% of the original cost estimated by KVE. Therefore, KVE was reimbursed based on a higher than actual cost number in some cases. The representative of KVE indicated that KVE tracks local costs in the area and builds in up to a 10% cushion to avoid having the costs come in too low due to price changes and the usual unforeseen circumstances.

On August 29, 2006, the City awarded a Construction Inspection Engineering contract to KVE. Four proposals were received by the City and two oral presentations were given. Thus, KVE was hired to act as the City Engineer to monitor projects. KVE provided construction monitoring and inspection services for Sutter Woods and Sutter Highlands; however, it did not design the infrastructure for those developments. The only development within our scope that KVE did not provide services for was Olivia Farms.

A representative of KVE that appeared to be significantly involved on behalf of KVE in the provision of the described services was also a member of the developer community through his partial ownership in Western Frontier Developers, LLC. It was suggested to BKD by one of the other developers that this individual used his influence in the development process to delay one phase of their development while ushering through a project in which he was involved. BKD could not verify that the reportedly delayed project was delayed inappropriately. However, having a member of the developer community involved in the administration of the Housing Program creates at least the appearance of impropriety and can be considered to be a conflict of interest.

A conflict of interest occurs when an individual or organization has an interest that might compromise their objectivity and reliability. A conflict of interest exists *even* if no improper acts result from it, and can create an appearance of impropriety that can undermine confidence in the conflicted individual or organization. Potential conflicts of interest should be carefully considered and managed by City officials to ensure the legitimacy of transactions and to avoid perceptions of possible self-dealing or mismanagement.

Recommendations

- The City Commission should consider amending its practice of paying engineering related fees equal to a percentage of the original Engineering Cost Estimate to a percentage of the actual costs. This would avoid the possibility of the inflation of the amount of the Engineering Cost Estimate for the sole purpose of a higher fee.
- Commissioners and City staff should be mindful of the appearance of conflicts of interest. Potential conflicts of interest should be carefully considered and managed to ensure the legitimacy of transactions and to avoid perceptions of possible self-dealing or mismanagement.

Reportedly Unfulfilled Commitments by City Staff

During our investigation of the Housing Program, some reportedly unfulfilled commitments made by City staff to developers were brought to our attention and are detailed below. In most instances it is difficult to determine whether commitments were actually made as the written record is open to interpretation or these commitments were reportedly made in conversations. However, statements made by City officials and City staff can be interpreted as commitments by the City on which others rely.

KRHID for Olivia Farms

The Development Agreement for Olivia Farms indicated that the City shall pursue the use of KRHID to provide a means of financing some of the proposed infrastructure. However, a representative of the developer indicated to BKD that City staff and City officials verbally assured them that the passage of the KRHID for Olivia Farms was “a done deal”. The representative speculated that the developer may not have undertaken the project if they had known that KRHID was not guaranteed.

Olivia Farms Donation of Public Spaces

The Development Agreement for Olivia Farms provided for the developer to designate and donate to the City areas within Olivia Farms designated as public parks or public spaces for which the City would be responsible for the upkeep and maintenance. The developer would file for a charitable contribution deduction for tax purposes. In the City’s files, we found a power point presentation by Fort Development entitled “Olivia Farms; Proposal for Special Benefit District Financing”. Based on the content of the presentation, it appears it was presented in December 2008. The presentation quotes the Development Agreement Section 1.6 regarding the donation of public parks or public spaces to the City. There is also a “Summary of Dedicated Properties” slide with arrows pointing to the lift station, the clubhouse, the swimming pool and the pond and outlet. Furthermore, BKD was told by various Commissioners that a City official had been actively supporting the donation of these amenities, particularly the swimming pool, throughout the development process for Olivia Farms.

Representatives of the developer indicated to us that they were verbally told by City staff that the City was going to take the lift station, clubhouse, swimming pool, pond and pond outlet. However, the Commission voted to notify Olivia Farms that the City was not interested in trading land or accepting as a donation the storm water retention pond and walking trail at the September 15, 2009 City Commission meeting.

Donation of Dirt for Village at Freedom Place

As previously discussed, the developer for Village at Freedom Place indicated that a City official had offered dirt to raise the property out of the flood plain free of charge. However, in reality, the cost of hauling the dirt is included in the Special Assessments allocated to the Improvement District. Therefore, the developer believes that the City reneged on the offer of “free” dirt and that the Special Assessment for Village at Freedom Place are too high.

The City official verified to BKD that the dirt for Village at Freedom Place was offered free of charge.

Access Road for Doc Hargreaves #5

The developer indicated that KVE designed the infrastructure for Doc Hargreaves #5, on behalf of the City, with access to Highway 77 through Nicole Lane. Therefore, the developer contends that there was a commitment by the City in 2006 to provide direct access to the subdivision from Highway 77 through Nicole Lane. To facilitate this access, the land for the right-of-way for Nicole Lane was donated to the City.

Subsequent to the commencement of construction, the developer was informed by KVE that contrary to previous indications, the Kansas Department of Transportation would not allow access to Highway 77 through Nicole Lane. However, by a letter dated July 15, 2007 and signed by the City Manager, the developer was informed that a frontage road would be built from Rucker Road to Nicole Lane to provide an additional access point to the subdivision. The letter indicated that the road would potentially be complete in 2009. To date, the frontage road has not been built.

The developer indicated that currently the only entry to Doc Hargreaves #5 is through an adjacent apartment complex and that this has resulted in lost lot and home sales. The City Manager indicated that the City does intend to build the frontage road between Rucker Road and Nicole Lane, but does not currently have the funds to do so.

C.L. Hoover Opera House

Background and Entities

The Opera House was a significant area of interest and speculation on the part of many citizens who spoke with BKD during our investigation. Questions raised related to ownership, solicitation efforts during fundraising, the total cost of the renovation and what entity ultimately paid these costs.

The Junction City Opera House was donated to the City in the 1980's for use as a convention center. However, the cost of renovating the building was prohibitive, and it sat unused for several years. In 1986, the citizens of Junction City voted against a bond issue which would have funded the building's renovation. However, as part of a generalized effort to revitalize Junction City's downtown, concerned citizen's formed the Opera House Foundation to raise funds for the repair and renovation of the Opera House as a convention and performing arts venue.

In the 2001 timeframe, the Opera House Foundation determined that they would not be able to raise the necessary funds to renovate the Opera House. City staff stated that the City then created a Capital Campaign Task Force (the "Task Force"), which was comprised of five people from the non-profit group who had been leasing the Opera House, five people from the Little Theater group, and five people from the City.

The Task Force decided to hire an architect to do a feasibility study to determine what the Opera House could be used for. The firm Bowman Bowman Novick, Inc. was hired, and the cost of the feasibility study was paid by the City. The City Commissioners decided in 2003 that the Opera House would be a performing arts center.

The Opera House was placed on the Kansas State Historic Register in November of 2003. Its status as a historic building made possible the use of Historic Tax Credits to assist in funding the renovations. In order to qualify for the various tax credits, a series of non-profit entities (the "Opera House Entities") were established. The Opera House Entities and the planned flow of funds between the Opera House Entities are detailed in ***Exhibit F***.

In September 2003, the City entered into a contract with Chris Keeshan Associates for professional fundraising services. (See the section "Fundraising" below for further discussion regarding Chris Keeshan Associates.) In 2005, the City hired Pioneer Group as the developer and for historic preservation guidance. The Pioneer Group has been paid approximately $260,000 for their development services. In September 2007, the Pioneer Group facilitated an agreement with NGM Insurance Company to sponsor 2008 Federal Historic Tax Credits of $1.29 million.

Renovation Cost and Funding

The expected cost of the renovation, and who ultimately paid these costs, has been a concern that was voiced to us repeatedly during our investigation. During our analysis of the cost, we found multiple sources which gave differing amounts:

- In March 2005, development costs had been anticipated to be $5.1 million[25]
- In November 2006, the winning construction bid was for $4.7 million[26], while the contract price on the first pay estimate in April 2007 was $5.2 million[27]
- In August 2007, the City arranged for $5.5 million of Taxable Industrial Revenue Bonds to fund the construction of the Opera House[28]
- In January 2008, information provided at a City Neighborhood meeting indicated that the Opera House is a "$5.5 million renovation project"[29]
- In April 2009, the Topeka Capital Journal reported that the Opera House was a $5.8 million renovation[30]
- Hired fundraisers, Chris Keeshan Associates, Inc. states on their website that the total campaign goal was $6.7 million[31]
- The website for the Opera House states that the building underwent at $7 million renovation[32]

There was less documentation to be found regarding what entity was to pay for the renovation. City staff stated that it was the intention of the Task Force to minimize the amount of renovation cost to the taxpayers. The fundraising goal was $1.8 million[33] and they had hoped to receive $3.8 million in Federal and State historic tax credits.[34] These hoped for sources of funds together would have generated $5.6 million. However, City staff told BKD that City staff had made it known all along that any shortfall in renovation funds, due to lower than anticipated donations or the inability to secure historic tax credits, would be funded directly by the City.

City staff stated that the Task Force and the City Commission meetings were all public meetings and that no there was no attempt to hide the possibility of the City's financial involvement in the Opera House. However, the seemingly contradicting cost figures, and the passive communication by the City and the Task Force to the public did not ease any confusion and speculation.

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[25]From the "Junction City Opera House Development Agreement by Pioneer Group, Inc. for Junction City Opera House Foundation."
[26]Bid by First Management Inc./ First Construction LLC submitted to Junction City Opera House, LP on November 7, 2006.
[27]Opera House Pay Estimate No #1, dated April 25, 2007 for $129,665.30.
[28]Engagement letter with Gilmore & Bell dated August 31, 2007, address to Mr. Mike Rhodes, Mayor; Junction City, Kansas.
[29]From City of Junction City Neighborhood Meeting on January 22, 2008, presented by Mr. Ken Talley.
[30]http://cjonline.com/news/state/2009-04-05/opera_house_gets_new_life.
[31]http://www.chriskeeshan.com/CKA%2520Website/junctioncityoperahousecka.htm.
[32]http://www.jcoperahouse.org/History.htm.
[33]From letter from Chris Keeshan to Mr. Rod Barnes dated January 24, 2002.
[34]From City of Junction City Neighborhood Meeting on January 22, 2008, presented by Mr. Ken Talley.

Fundraising

A "Contract for Fundraising and Development Services" was entered into on September 1, 2003 with "Chris Keeshan Associates" for fundraising services for one year, signed by the then City Mayor. Compensation for the fundraising services was $65,000 annually plus a $2,500 bonus per each $100,000 payable upon receipt of cash, signed pledge cards/commitment letter. The cost for fundraising services totaled the following:[35]

2003	$ 32,166.82
2004	60,723.30
2005	100,508.71
2006	8,700.00
2007	34,496.00
2008	5,088.00
	$ 241,682.83

A fundraising campaign was initiated, and pledges were made beginning in 2004. Solicitors for funds included the professional fundraisers, City staff and members of the community.

As of the most recent report provided by the City, the fundraising campaign had accumulated pledges of $2.4 million, and had collected just under $1.7 million in cash donations. This included a naming gift of $500,000 from the Hoover-Koken Foundation, Inc. for the naming rights of the Opera House. See the following chart for pledges and payments by year, if the date was provided.

	Pledges	Payments
No date*	$ 451,945	$ 351,445
2004	124,710	56,838
2005	194,725	140,029
2006	640,686	357,770
2007	473,917	142,885
2008	517,164	595,243
2009	500	49,250
	$ 2,403,647	$ 1,693,460

*No date listed with pledge or payment on report.

In addition, there were non-cash contributions of the Opera House itself, an additional building, and in-kind donations that totaled approximately $1.2 million.

As the housing development started gaining momentum in Junction City, the number of pledges from out-of-town developers also increased. City staff stated that out-of-town developers would inquire how they could get involved in and show their support of the community. A City official indicated that the developers were provided various opportunities to do so, which included donating to the annual Sundown Salute, the Opera House, and other community activities. We found documentation on the following pledges made by individuals involved in the 39 developments in the scope of our review.

[35]Taken from the monthly payment logs located in the Opera House binders kept for tax credits.

	Date Pledged	Amount Pledged	Amount Paid
Greg & Deborah Hargreaves	12/1/2005	$ 5,000	$ 3,000
David & Linda Alexander	1/9/2006	1,000	1,000
David Freeman*	3/6/2006	25,000	25,000
Gery Schoenrock*	7/11/2006	15,000	6,000
JCTD Properties	12/18/2006	5,000	5,000
American Communities*	2/8/2007	250,000	—
George Marcus	3/20/2007	500	500
Big D Development	8/1/2007	25,000	—
JCTD Properties	8/1/2007	5,000	—
Fort Development	8/1/2007	30,000	30,000
Jason Rothwell*	9/25/2007	2,500	—
Kathie Johnson/Russell Johnson	12/21/2006	250,000	83,333
Leon & Lisa Osbourn	not dated	5,000	5,000
		$ 619,000	$ 158,833

*Indicates review of the signed pledge document.

Other familiar names were on the fundraising report. The following is a listing of other parties that we have learned about during the course of our investigation.

	Date Pledged	Amount Pledged	Amount Paid
David Christie, Inc. *(developer of "The Bluffs")*	1/1/2005	$ 15,000	$ 15,000
Bowman Bowman Novick Inc. *(Opera House architect firm)*	1/4/2005	10,000	10,000
Kaw Valley Engineers *(primary engineer on developments)*	1/4/2005	10,000	10,000
Hunters Ridge Apartments *(subdivision outside of our scope)*	2/2/2005	5,000	5,000
Roger Morningstar *(developer involved with early developments)*	1/6/2006	25,000	—
Doug Compton/First Management *(construction contractor for the Opera House)*	11/16/2006	100,000	50,000
Tim J. Malone *(developer on subdivisions outside of our scope)*	12/7/2006	25,000	2,000
Pioneer Group *(firm hired for historic preservation guidance)*	not dated	50,000	50,000
		$ 240,000	$ 142,000

We inquired of every developer we interviewed if they were asked to donate to the Opera House in exchange for preferential treatment in the development process or any item or service of value. No developer indicated that they had been promised or offered anything in exchange for their pledge. However, many individuals related anecdotal conversations with regard to Mr. Russell Johnson's pledge. Therefore, we specifically reviewed that pledge.

Russell Johnson Pledge

The City Manager's Update for "The Opera House Project"[36] stated that the City Manager asked Mr. Russell Johnson for a $250,000 pledge. This Update asserts that after he met with his advisors, including his attorney, accountant and with a developer, Mr. Russell Johnson came up with a plan as follows: "If the City would help develop the East Ash Street extension and get his land ready for development, he would use proceeds from the dirt and land sale to make a contribution to the Opera House. Russ saw this as a win/win for everybody and the City Commission certainly was pleased to have both projects moving forward."[37]

The East Ash Street Extension Development Agreement was dated August 18, 2005, and was between Russell M. Johnson; The City of Junction City, Kansas; Briggs Auto Group, Inc.; Bottiger's Marine, Inc.; and Rotherwell Property Management, LLC for the construction, extension and installation of the improvement. The road would become a four-lane, two-way paved street. The agreement states that none of the cost of these improvements would be assessed or charged against the land.

Mr. Johnson's obligation included the conveyance of land called the "Borrow Area", for which he reserved and retained the right to receive compensation from the City's contractor(s) for all soil and fill material removed from the Borrow Area at the rate of $4.00 per cubic yard of material removed.

The City's obligation included the grading of the Borrow Area and the creation of a public recreational pond, additional draining, fill and grading work to the adjoining land, removal of I-70 screening, drainage ditch and river channel work.

A representative from KVE recalled that there were approximately 111,000 cubic yards of dirt removed for the pond and 20,000-25,000 cubic yards removed from a rail road crossing on Russell Johnson's land. The representative of KVE stated that the market cost of dirt was $1 per cubic yard. A total of approximately 135,000 per cubic yards of dirt was removed, for which the Development Agreement stated Mr. Johnson would be paid $4 per cubic yard. Therefore, the payment to Mr. Johnson would have approximated $544,000. However, if the market price for dirt, as indicated by the representative of KVE, was approximately $1 per cubic yard, the profit to Mr. Russell Johnson in this transaction was over $400,000.

A check was written on April 17, 2006 for $520,292 to the "Estate of Russell M. Johnson, Deceased", fulfilling the obligation for the dirt. The amount of the check (divided by the contract price of $4.00 per cubic yard) indicates that 130,073 cubic yards of dirt was borrowed from the Borrow Area. The contractor charged the City $7.20 per cubic yard for this borrowing. The final pay estimate shows that a total of 130,073 cubic yards was borrowed from the pond excavation for at total of $936,545.60. The contractor also borrowed an additional 41,468 cubic yards at $7.20 per cubic yard for an additional $298,569.60, which appears to be excluded from the calculation of dirt from the Borrow Area. As Contractors are in the business of making a profit, it is likely that they recovered the cost of the payment to Russell Johnson from the City during the construction of this project.

We were told that the $520,292 check in payment to Mr. Johnson was sent to KVE, and was then picked up by the City Manager rather than being sent directly to the representative of Russell Johnson's Estate. It has been suggested by many that this action was to ensure the fulfillment of the $250,000 pledge. However, Mr. Johnson's attorney picked up the check from the City to deposit it in the bank. The check was deposited on April 28, 2006, eleven days after it was written.

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[36]http://www.jcks.com/rodupdates/archives/2008/0115_1.html.

[37]Ibid.

There was no written documentation regarding the pledge by Russell Johnson until a pledge card was signed by Mrs. Kathie E. Johnson on October 17, 2006. The pledge card is typed, indicating that three annual gifts of $83,333.33 would be made for a total of $250,000. The pledge card shows the signature of Mrs. Johnson. The first gift of $83,333.33 was recorded in the fundraising report as having been received on December 21, 2006. No other payments on the pledge were made.

It is clear that this particular situation was a topic of interest to many in the community. Opinions varied from Russell Johnson being strong-armed by the City to donate to the Opera House, to the City suggesting a "quid pro quo transaction." However, it appears likely that Russell Johnson made a business deal, the proceeds from which he planned to use to make the donation to the Opera House and still make a profit from the sale of the dirt.

Construction/Rehabilitation of the Opera House

The construction/rehabilitation of the Opera House was competitively bid through the solicitation of sealed bids through the project architect, Bowman Bowman Novick, Inc. The following bids were received:

	Bid Amount	Price for "Alternatives"	Total
Kansas Building Systems, Inc.	$ 6,469,797	$ 225,761	$ 6,695,558
McPherson Contractors, Inc.	5,712,000	150,700	5,862,700
First Management, Inc./First Construction LLC	4,700,000	255,001	4,955,001

The Architect, along with the Task Force reviewed the bids, and selected the low bid from First Management, Inc./First Construction LLC. City staff explained that subsequent to the time of the bid selection in November 2006, discussions with the architects lead to various changes in the plans, and alternatives were exercised. City staff have record of a different bid submitted by First Management, Inc./ First Construction LLC dated December 8, 2006 for a total of $5.39 million. It is unclear if the rest of the bidders were given the opportunity to submit a second bid for the Opera House. This amount was reduced through architect changes for a final contract price of construction was $5.2 million. Even at the higher price submitted on December 8, 2006, First Management, Inc./First Construction LLC remained the lowest bidder.

Between the two bid dates, First Management pledged $100,000 to the Opera House. We did not see that any of the other bidders made pledges to the Opera House. As of the date of the latest fundraising report, First Management has paid $50,000 on their pledge, though the Opera House is now completed.

In September 2007, the City entered into an agreement with the Spirit of '76, Inc. ("Spirit") in which Spirit became the lessee of the Opera House and the City issued $5.5 million in Industrial Revenue Bonds ("IRB's") to fund the construction/rehabilitation of the Opera House. Central National Bank bought the IRB's and made a loan to Spirit in the same amount for the construction cost of the renovation. Further, upon completion of the Opera House, the City made an economic development grant to Spirit to meet the debt service on the bonds loan.

Previous to establishing a loan account with Central National Bank, the payments for construction were made by both the City and the Opera House Foundation. Once the IRB was purchased, payments for the construction were made against the loan account. When the $5.5 million was fully drawn against, the City paid the remaining bills for construction.

Final Renovation Cost

The Opera House Entities flow chart (***Exhibit F***) highlights the number of entities involved with the renovation process for the Opera House. Payments from a number of these entities were made for various costs. Documentation for the tax credits is complete, but the "soft costs" for items such as fundraising, consulting, maintenance, financing interest, and other such expenses that did not qualify for the tax credits are not as well documented in the City's files. Therefore, we were unable to quantify the actual total cost of the renovation, but only to give an approximate cost from the information we have been provided.

Based upon information made available to BKD, the funding sources for the renovation include the following:

Donations	$ 1,693,459
City loan payment	2,400,000
Other city payments	1,087,579
Kansas tax credit	338,815
Kansas tax credit	1,178,777
Federal tax credit	1,349,842
	$ 8,048,472

Per the general ledger records, the City has paid $3,487,579.

Costs from 2002 through 2009 are approximately $7.5 million. The other sources of funds from donations and the tax credits allowed for an approximate $500,000 surplus. This surplus is not directly controlled by the City, and is likely used for maintenance and operating cost for the Opera House.

Appendix A - Funding Mechanisms for Housing Infrastructure

Without incentives to assist with development costs, a developer finances the purchase of the land and the infrastructure construction cost until such time the lots in the subdivision are sold. These costs are included in the price of the lot to the purchaser. In order to entice developers to create infrastructure to meet the new housing demand, Junction City offered incentives in the form of funding mechanisms to lessen the developer's financial burden and risk. The City had intended to use:

- The creation of Special Benefit Districts or Improvement Districts, with funding through Special Assessments
- The Kansas Rural Housing Incentive District, with funding through tax increment financing

Both of these incentives benefit the developer by the City paying for certain infrastructure costs. This significantly reduces the financial risk to the Developer, who may not otherwise have developed the land due to the fear that lots would not sell. The City is then reimbursed for a portion of its costs through either Special Assessments against the Improvement District or the capture of incremental property taxes from the benefited area, as described below.

Special Benefit Districts

The City has pursued a policy of utilizing Special Benefit Districts[38], to pay the cost of certain improvement projects that directly benefit the underlying property. Kansas statutes allow for the creation of Special Benefit Districts to pay for the cost of a variety of improvements, including street construction, storm water drains, sanitary sewer system improvements, street lighting, water system improvements, recreational facilities, flood control projects, bridges and parking facilities. The City has typically utilized Special Benefit Districts to pay for the costs associated with constructing certain street, sewer and water improvements within the subdivisions of the Housing Program.

The creation of Special Benefit Districts, the determination of property benefited, and the method of allocating the costs of the improvement is at the discretion of the City. Property owners have the ability to suggest improvements to be made through a petition process and to comment on the final amounts of their assessments. The City may or may not be included as part of the Special Benefit District. All property owners have the option to pay their portion of the improvement cost with a one-time payment during a 30-day assessment prepayment period or in annual installments with interest over 20 years.

Upon completion of the Special Benefit District improvement projects and the 30-day prepayment period, the City issues General Obligation Bonds to provide for permanent project financing. The payment of the principal of and interest on the bonds is paid from the Special Assessments levied annually on the benefited property owners. The final amount of the Special Assessment on the Improvement District includes:

- Engineering costs for the development
- Construction cost of the infrastructure
- City water fees
- City issuance fees
- Cost for legal notices
- Bond interest

[38]In accordance with the Kansas General Improvement and Assessment Law, K.S.A. 2005 Supp.12-6a01 et seq.

Special Assessments are paid at the same time and in the same manner as ad valorem property taxes. If at any time the Special Assessments received from the property owners are insufficient to provide for the payment of the principal of and interest on the bonds, the City is obligated to provide for the balance of such payments through its ability to levy unlimited ad valorem property taxes.

All subdivision under review utilized Special Benefit District financing.

Kansas Rural Housing Incentive District

The Kansas Rural Housing Incentive District program ("KRHID") was developed by the State of Kansas to assist developers in the financing of public improvements. KRHID captures 100% of the incremental increase in real property taxes in City, County and School District property taxes for up to 15 years to pay for the infrastructure. To determine the increase in value, a "base year" is used for the property assessed value. When comparing the base year to the assessed value after the improvement, the resulting increase in property taxes is calculated. Property taxes of the "base year" amount continue to be paid to the taxing authorities to be used in their traditional manner. The incremental property taxes would be used to reimburse the City for its funding of the cost of infrastructure within the KRHID. Notably, the City would benefit from incremental property taxes that otherwise would be paid to the County and School District.

Cities can issue Special Obligation Revenue Bonds to finance these costs, and temporary notes for interim financing. Permitted costs that are allowed to be reimbursed to the developers by a city include:

- Acquisition of property
- Payment of relocation assistance
- Site preparation
- Sanitary and storm sewers and lift stations
- Drainage conduits, channels and levees
- Street grading, paving, curbs and gutters
- Street lighting
- Underground public or private utilities
- Sidewalks
- Water mains and extensions

There is a multi-step approval process to successfully use financing through KRHID which includes, but is not limited to:

- Approval by the Secretary of Commerce of the housing shortage findings from a Housing Needs Analysis that is prepared
- Various public hearings
- Notices delivered to the Planning Commission, School District, County and the City
- Published Notices
- 30 day protest period
- Approval by the City, County, and School District

Ultimately, the use of KRHID was not approved by all taxing authorities, thus no subdivision under review utilized KRHID.

Exhibits

Exhibit A
Listing of Subdivisions Reviewed

Exhibit A

Subdivisions Reviewed for this Report

- AC Development
- Deer Creek #1-3
- Deer Trail
- Doc Hargreaves #1-5
- Eagle Landing (Tackwell Addition)
- Ehlers Addition
- Ehlers Hilltop
- Faith Tabernacle
- Falcon Ridge
- Hickory Hill
- Hickory Hill Replat
- Hidden Valley
- Indian Ridge #6
- Mann's Ranch #1-2
- Michael's Run
- Oakwood Village
- Olivia Farms
- Peterson Addition
- Prairie Ridge #1-2
- Rivendell
- Round House
- Russell J. Johnson Addition
- Spring Valley #1-2
- Sutter Highlands
- Sutter Woods
- Turkey Hollow
- Turkey Ridge
- Village at Freedom Place
- Westwood Triangle
- Wheatland Hills #4

Exhibit B
Range of Special Assessments

Subdivision	# of Lots	Total Project Costs	% Improvement District/City	Per Lot Assessment against Improvement District	City at large Amount	
AC Development	89	$2,029,311.74	90/10	$20,521.13	$202,931.17	
Deer Creek #1	122	2,337,720.46	76.44/23.56	14,647.16	550,766.94	
Deer Creek #2	1	295,648.93	77.22/22.78	228,300.10	67,348.83	
	50	1,241,067.08	77.22/22.78	19,167.04	282,715.08	
	45	1,419,773.31	77.22/22.78	24,363.31	323,424.36	
		2,956,489.32			673,488.27	
Deer Creek #3	93	2,227,903.87	90/10	21,560.36	222,790.39	
Deer Trail	61	1,156,046.24	90/10	17,056.42	115,604.62	
Doc Hargreaves #1	14	348,756.18	90/10	22,420.04	34,875.62	
Doc Hargreaves #2	59	1,161,563.16	90/10	17,718.76	116,156.32	
Doc Hargreaves #3	32	652,136.89	90/10	18,341.35	72,387.19	
Doc Hargreaves #4	7	160,015.88	90/10	20,573.47	16,001.59	
Doc Hargreaves #5	105	2,575,148.33	90/10	22,072.70	257,514.83	Under Review by City
Eagle Landing (Tackwell Addition)	1	460,461.83	31.2/68.8	143,664.09	316,797.74	
Ehler's Addition	14	336,445.04	90/10	21,628.61	33,644.50	
Ehler's Hilltop	49	1,032,575.24	80.382/19.618	16,938.87	202,570.61	
Faith Tabernacle	1	429,495.93	46.4/53.6	199,286.11	230,209.82	
Falcon Ridge	8	206,027.02	90/10	23,178.04	20,602.70	
Hickory Hill	50	792,346.67	90/10	14,262.24	79,234.67	
	2	369,339.89		166,202.95	36,933.99	
	1	214,393.28		192,953.95	21,439.33	
		1,376,079.83			137,607.98	

Subdivision	# of Lots	Total Project Costs	% Improvement District/City	Per Lot Assessment against Improvement District	City at large Amount
Hickory Hill Replat	38	883,692.53	90/10	20,929.56	88,369.25
Hidden Valley	32	622,476.16	100/0	19,452.38	0.00
	6	70,158.00	100/0	11,693.00	0.00
		692,634.16			0.00
Indian Ridge #6	19	466,575.61	90/10	22,100.95	46,657.56
Mann's Ranch # 1	91	2,404,605.84	100/0	26,424.24	0.00
Mann's Ranch #2	82	1,953,950.94	100/0	23,828.67	
Michael's Run Replat	33	959,855.45	83.66/16.34	24,333.79	156,840.38
	1	203,605.70	83.66/16.34	170,336.53	33,269.17
		1,163,461.15			190,109.55
Oakwood Village	90	2,071,705.00	90/10	20,717.05	207,170.50
Olivia Farms	120	3,273,497.33	90/10	24,551.23	327,349.73
	1	74,700.30	90/10	67,230.27	7,470.03
	71	2,960,086.24	90/10	37,522.22	296,008.62
Clubhouse, Pool and Pond	3	0.00	0/0	0.00	0.00
	1	381,941.74	90/10	343,747.57	38,194.17
	2	709,328.58	90/10	319,197.86	70,932.86
	1	300,098.24	90/10	270,088.42	30,009.82
	2	545,641.58	90/10	245,538.71	54,564.16
	1	409,219.20	90/10	368,297.28	40,921.92
	1	1,847,114.00	90/10	1,662,402.60	184,711.40
	1	245,531.40	90/10	220,978.26	24,553.14
	2	381,954.56	90/10	171,879.55	38,195.46
		11,129,113.18			1,112,911.32
Peterson Addition	1	86,408.31	81.7/18.3	70,595.59	15,812.72
	1	60,866.23	81.7/18.3	49,727.71	11,138.52
	1	111,443.18	81.7/18.3	91,049.08	20,394.10
	1	103,581.29	81.7/18.3	84,625.91	18,955.38
		362,299.01			66,300.72

Subdivision	# of Lots	Total Project Costs	% Improvement District/City	Per Lot Assessment against Improvement District	City at large Amount	
Prairie Ridge #1	258	2,056,920.88	82.79334/17.20666	6,600.75	425,083.27	
Prairie Ridge #2	36	1,407,956.40	90/10	35,198.91	140,795.64	
	20	586,648.44	90/10	26,399.18	58,664.84	
	3	58,664.83	90/10	17,599.45	5,866.48	
	1	723,633.06	90/10	651,269.75	72,363.31	
		2,776,902.73			277,690.27	
Rivendell	27	656,406.00	90/10	21,880.20	65,640.60	
Round House	18	407,756.20	90/10	20,387.81	40,775.62	
Russell J. Johnson Addition	17	387,554.86	90/10	20,517.61	38,755.49	Under review by City
Spring Valley #1	75	1,675,600.31	80/20	17,873.07	335,120.06	
Spring Valley #2	123	1,886,988.10	90/10	13,807.23	188,698.81	
Sutter Highlands	295	7,366,281.11	90/10	22,473.40	736,628.11	
Sutter Woods	243	7,302,020.40	90/10	27,044.52	730,202.04	
Turkey Hollow	1	59,860.01	90/10	53,874.01	5,986.00	
	1	618,553.56	90/10	556,698.20	61,855.36	
	11	271,745.59	90/10	22,233.73	27,174.56	
		950,159.16			95,015.92	
Turkey Ridge	1	70,795.08	90/10	63,715.57	7,079.51	
	1	401,172.13	90/10	361,054.92	40,117.21	
		471,967.21			47,196.72	
Village at Freedom Place Phase 2	145	1,492,497.89	90/10	9,263.78	149,249.79	
Westwood Triangle	8	65,717.24	90/10	7,393.19	6,571.72	
Wheatland Hills #4	34	507,071.84	90/10	13,422.49	50,707.18	

Note: These figures were taken from Junction City City Commission Minutes dated March 6, 2007, February 17, 2009 and February 16, 2010 and the associated agenda items.
Slight differences in total project costs and City at large costs per project from published amounts are due to their calculation based on published Special Assessments per lot and number of lots.

Exhibit C
Bid Analysis

City of Junction City, Kansas
Investigation of Housing Program
Bid Analysis

	Number of Bids	Number of Wins	% Wins	Westwood Triangle	Wheatland Hills#4	Spring Valley #1	DOC Hargrvs #1	Peterson Addit.	Ehlers Addition	Round House	Ehlers Hilltop
Date of Comparison				5/12/2005	6/2/2005	8/11/2005	8/11/2005	9/9/2005	9/15/2005	10/28/2005	11/17/2005
No. of Bidders				1	2	4	3	2	2	3	5
Engineer Estimate				36,468	362,183	742,631	288,024	301,726	234,038	305,469	989,015
J&K Contractors	25	18	72%	$\boxed{42,663}$		809,511	$\boxed{271,404}$	$\boxed{265,742}$	$\boxed{189,508}$	257,354	$\boxed{782,339}$
Middlecreek Corp	25	2	8%			894,365	312,214	274,919	230,301	$\boxed{242,079}$	956,569
Nowak Construction	22	1	5%			936,268					1,034,387
Midlands Contracting	17	6	35%		$\boxed{360,427}$	$\boxed{803,739}$				280,744	857,647
Smokey Hill, LLC	10	0	0%								1,080,098
Emerson Construction	6	1	17%								
Ebert Construction	5	2	40%								
Meadows Construction	5	0	0%								
Bazin Excavating	3	0	0%								
Larkin Excavating	3	0	0%								
Boyd Excavating	2	0	0%		393,819						
Wildcat Construction	2	0	0%								
Carlson Utility, LLC	1	0	0%								
Cheney Construction	1	0	0%								
Deep Creek Const.	1	0	0%				330,713				
Hi-Plains Sand, Inc.	1	0	0%								
Joshua Excavating	1	0	0%								
Walters-Morgan Const.	1	0	0%								

City of Junction City, Kansas
Investigation of Housing Program
Bid Analysis

				Faith Tabernacle	DOC Hargrvs #2	Deer Trail Addition	Hickory Hill	Prairie Ridge #1	Deer Creek #1	Spring Valley #2
Date of Comparison				11/21/2005	2/2/2006	2/3/2006	3/2/2006	3/21/2006	3/22/2006	4/12/2006
No. of Bidders				5	4	5	4	2	2	4
Engineer Estimate				400,222	1,119,093	1,369,418	1,255,470	1,598,467	2,102,337	1,767,119
	Number of Bids	Number of Wins	% Wins							
J&K Contractors	25	18	72%	328,923	928,316	1,066,971	1,060,146			1,536,658
Middlecreek Corp	25	2	8%	380,881	1,003,526	1,034,584	1,066,569	1,746,424	1,881,461	1,881,866
Nowak Construction	22	1	5%	395,831	976,913	1,126,092	1,050,335		2,302,675	1,717,606
Midlands Contracting	17	6	35%	435,987	1,004,584	946,260	1,070,469	1,428,921		
Smokey Hill, LLC	10	0	0%							1,791,351
Emerson Construction	6	1	17%							
Ebert Construction	5	2	40%			880,590				
Meadows Construction	5	0	0%							
Bazin Excavating	3	0	0%							
Larkin Excavating	3	0	0%							
Boyd Excavating	2	0	0%							
Wildcat Construction	2	0	0%							
Carlson Utility, LLC	1	0	0%							
Cheney Construction	1	0	0%							
Deep Creek Const.	1	0	0%							
Hi-Plains Sand, Inc.	1	0	0%							
Joshua Excavating	1	0	0%							
Walters-Morgan Const.	1	0	0%	507,359						

City of Junction City, Kansas
Investigation of Housing Program
Bid Analysis

	Number of Bids	Number of Wins	% Wins	DOC Hargrvs #3	DOC Hargrvs #4	Prairie Ridge #2	Deer Creek #2	DOC Hargrvs #5	Russell J. Johnson
Date of Comparison				4/20/2006	5/31/2006	6/14/2006	7/26/2006	8/23/2006	8/23/2006
No. of Bidders				4	2	4	5	4	4
Engineer Estimate				531,061	122,184	2,015,703	2,244,808	2,294,575	299,492
J&K Contractors	25	18	72%	526,107	105,449	1,646,933	2,358,079	1,970,335	240,596
Middlecreek Corp	25	2	8%	636,445		2,165,476	2,263,212	2,239,207	282,415
Nowak Construction	22	1	5%	670,734		2,091,891	2,285,417	2,393,358	318,351
Midlands Contracting	17	6	35%			1,883,638	1,990,364		
Smokey Hill, LLC	10	0	0%	535,906			2,228,305	2,133,952	292,591
Emerson Construction	6	1	17%						
Ebert Construction	5	2	40%						
Meadows Construction	5	0	0%						
Bazin Excavating	3	0	0%						
Larkin Excavating	3	0	0%						
Boyd Excavating	2	0	0%		109,999				
Wildcat Construction	2	0	0%						
Carlson Utility, LLC	1	0	0%						
Cheney Construction	1	0	0%						
Deep Creek Const.	1	0	0%						
Hi-Plains Sand, Inc.	1	0	0%						
Joshua Excavating	1	0	0%						
Walters-Morgan Const.	1	0	0%						

City of Junction City, Kansas
Investigation of Housing Program
Bid Analysis

				Hidden Valley	Indian Ridge #6	Rivendell	Oakwood Village	Hickory Hill Replat	Deer Creek #3	Michael's Run	Turkey Hollow	Turkey Ridge
Date of Comparison				9/13/2006	9/26/2006	10/11/2006	10/12/2006	1/9/2007	2/27/2007	4/17/2007	8/17/2007	8/17/2007
No. of Bidders				7	6	5	4	7	10	6	6	7
Engineer Estimate				1,190,242	370,816	459,662	1,697,196	780,421	1,957,860	955,682	743,172	432,353
	Number of Bids	Number of Wins	% Wins									
J&K Contractors	25	18	72%		338,275	447,193		621,906	1,622,335	857,796	604,228	315,694
Middlecreek Corp	25	2	8%	1,069,191	492,321	523,588	1,629,411	777,646	1,530,607	961,897		
Nowak Construction	22	1	5%	1,320,692	495,589	598,954	1,737,606	788,107	1,743,006	1,066,606	617,165	370,015
Midlands Contracting	17	6	35%	988,761				667,774	1,482,551	1,156,574	739,130	415,668
Smokey Hill, LLC	10	0	0%	1,020,071	416,018			694,308	1,700,773			
Emerson Construction	6	1	17%				1,500,368	719,955	2,060,997	976,675	914,746	503,722
Ebert Construction	5	2	40%	1,074,014			1,602,087	573,735	1,580,485			
Meadows Construction	5	0	0%	1,296,543	648,212	581,492				1,303,719		520,248
Bazin Excavating	3	0	0%					805,494			835,346	466,724
Larkin Excavating	3	0	0%					828,399			758,057	464,688
Boyd Excavating	2	0	0%									
Wildcat Construction	2	0	0%	1,337,303	555,333							
Carlson Utility, LLC	1	0	0%						1,596,322			
Cheney Construction	1	0	0%					987,117				
Deep Creek Const.	1	0	0%									
Hi-Plains Sand, Inc.	1	0	0%			704,034						
Joshua Excavating	1	0	0%						2,032,696			
Walters-Morgan Const.	1	0	0%									

Exhibit D
General Ledger Analysis Findings

Exhibit D

City of Junction City, Kansas
General Ledger Mis-Postings

	Project Incurring Cost		Charged To Project	Amount	Type of Cost
	Doc. Hargreaves #2		Doc. Hargreaves #3	$ 149,448.82	Contractor Cost
	Ehlers Hilltop		Ehlers Addition	194,307.87	Contractor Cost
1	Buffalo Soldier Park		Ehlers Addition	74,577.01	Westar Energy (Utilities)
	Ehlers Addition		Ehlers Hilltop	22,049.24	Engineering Costs
	Doc. Hargreaves #2		Ehlers Hilltop	16,980.00	Engineering Costs
	Spring Valley #1		Peterson Addition	8,180.20	Engineering Costs
	Ehlers Hilltop		Peterson Addition	250,718.90	Contractor Cost
	Spring Valley #1		Doc. Hargreaves #3	215,085.49	Contractor Cost
	Spring Valley #1	1	Tom Neal Industrial Park	158,393.14	Contractor Cost
	Spring Valley #1		Doc. Hargreaves #3	151,523.84	Contractor Cost
	Spring Valley #1		Spring Valley #2	343,241.18	Contractor Cost
	Spring Valley #1		Ehlers Addition	13,114.00	Engineering Costs
	Spring Valley #2	1	Strauss Add/Spring Valley	73,800.00	Engineering Costs
	Wheatland Hills #4		Doc. Hargreaves #3	395,456.60	Contractor Cost
1	Spring Valley Utilities		Doc. Hargreaves #3	661,509.05	Spring Valley Grading & Utilities
1	Ash Street Extension		Spring Valley #2	2,121,401.11	Ash Street Extension
1	*Old Agreement*		Prarie Ridge #1	1,360,000.00	Payments to DJ Christie
1	Spring Valley Utilities		Spring Valley #1	46,343.87	Engineering Costs
	Ehlers Addition		Deer Creek #1	55,000.00	Engineering Costs
	Ehlers Addition	1	Strauss Addition	4,350.80	Engineering Costs
	Wheatland Hills #4	1	Gateway Buisness Park	5,123.40	Engineering Costs
	Wheatland Hills #4		Advertising Expenses	16.00	Engineering Costs
	Wheatland Hills #4		Other Services Expense	2,500.00	Engineering Costs
				$ 6,323,120.52	

1 Projects outside of the scope of our analysis. Total= $ 4,505,498.38

Exhibit E
Bond Financing Cost Analysis Findings

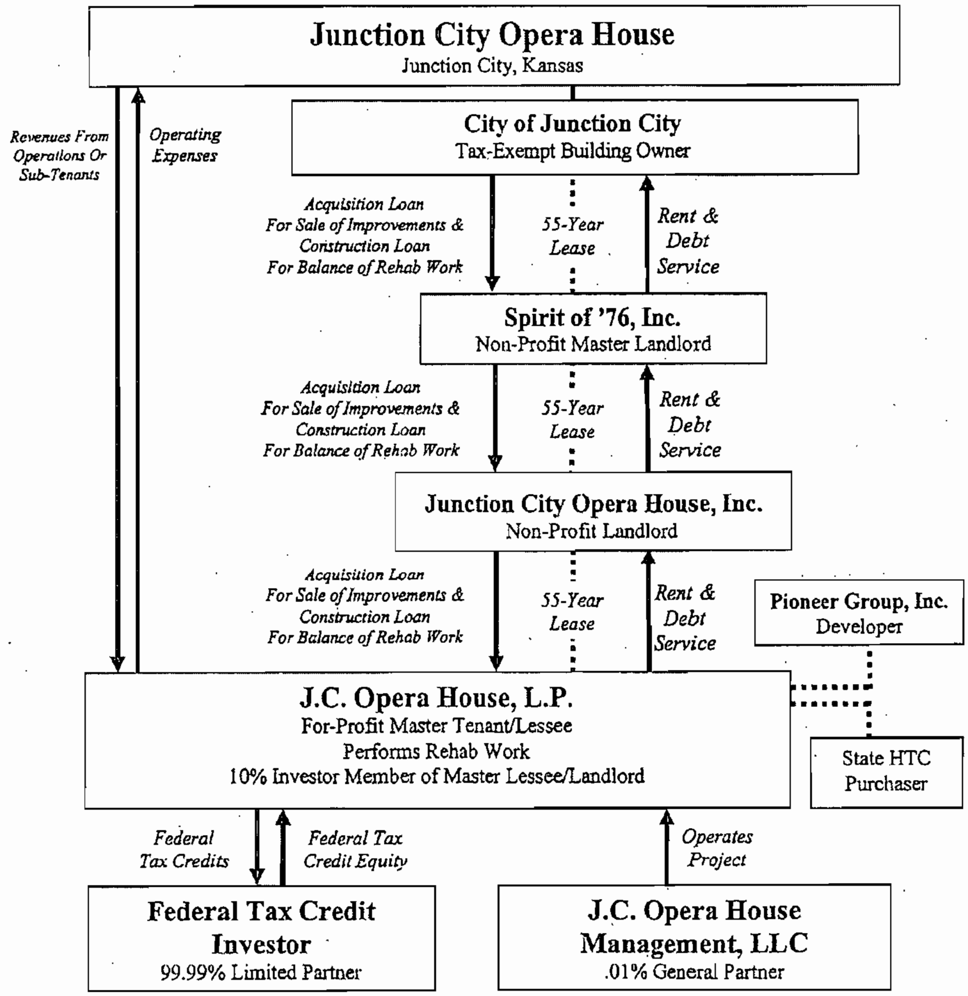
Exhibit E

City of Junction City, Kansas
Findings from Limited Bond Cost Analysis

Project Incurring Cost	Project Showing Cost in G/L	Cost included in Bond Amount	Cost Type	Excluded from Bonds	Bonded to Wrong Project	Bonded in Two Projects
Doc Hargreaves #2	Doc Hargreaves #2	*(not included)*	Engineering Costs	6,492.80		
Convention Center	Prairie Ridge #1	Doc Hargreaves #3	Engineering Costs		1,779.75	
McCluskey's Addition #4	Doc Hargreaves #3	Doc Hargreaves #3	Engineering Costs		1,188.00	
Southwind Drive	Doc Hargreaves #3	Doc Hargreaves #3	Engineering Costs		395.20	
Wheatland Hills #3	Doc Hargreaves #3	Doc Hargreaves #3	Engineering Costs		4,457.00	4,457.00
Southwind Drive	Wheatland Hills #4	Wheatland Hills #4	Engineering Costs		431.05	
Strauss Addition	Strauss Add/Spring Valley	Spring Valley #1	Contractors Cost		189,815.71	
Tom Neal Industrial Park	Tom Neal Industrial Park	Spring Valley #1	Engineering Costs		9,980.00	
Spring Valley Utilities	Spring Valley #1	Spring Valley #1	Engineering		1,186.00	
Tom Neal Industrial Park	Tom Neal Industrial Park	Spring Valley #1	Engineering		4,672.60	
Spring Valley/Rucker Road	Spring Valley #1	Spring Valley #1	Engineering		10,978.00	
Spring Valley Utilities	Spring Valley #2	Spring Valley Utilities	Engineering	(600.00)		
Spring Valley Utilities	Spring Valley #2	Spring Valley Utilities	Engineering	8,500.00		
				14,392.80	224,883.31	4,457.00

Exhibit F
Opera House Entities

Opera House Entities



Per a September 1, 2007 agreement, the City leased the Opera House to Spirit, which subleased to Junction City Opera House, Inc., a Kansas not-for-profit corporation which received public contributions to partially fund the Opera House. The project was further subleased to J.C. Opera House, L.P., a Kansas limited partnership, which sold federal historic tax credits to partially fund the project.

The City issued IRB's to fund the project which were purchased by Central National Bank. Central National Bank made a construction loan in the amount of the IRBs to pay the construction costs.