

# Item No. 13

## “To Be Delivered” Material

For

### City of Sacramento

City Council

Financing Authority

Housing Authority

Redevelopment Agency

### Agenda Packet

**Submitted:** January 21, 2010

**For the Meeting of:** January 26, 2010

The attached materials were not available at the time the Agenda Packet was prepared.

**Title:** Report Back on FEMA issues and Building Division's issuance of 35 Natomas Central Building Permits

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# REPORT TO COUNCIL

## City of Sacramento

915 I Street, Sacramento, CA 95814-2604  
[www.CityofSacramento.org](http://www.CityofSacramento.org)

**Staff Report**  
**January 26, 2010**

**Honorable Mayor and  
Members of the City Council**

**Title: Report Back on FEMA issues and Building Division's issuance of 35 Natomas Central Building Permits**

**Location and Council District: City-Wide**

**Recommendation:** Receive and file report; direct the City Attorney and City Manager to finalize, organize, and transfer the investigation materials to the Audit Committee; and direct the Audit Committee to oversee the audit and, if necessary, any further investigation of the Building Division issues identified by the City Attorney's and City Manager's investigation and report back to Council on the audit and investigation by a date set by Council.

**Contact:** Sandra Talbott, Assistant City Attorney, 808-5346;  
John Dangberg, Assistant City Manager, 808-1222

**Presenter:** Sandra Talbott, Assistant City Attorney, 808-5346;  
John Dangberg, Assistant City Manager, 808-1222

**Department:** Office of the City Attorney; Office of the City Manager

**Division:** n/a

**Organization No:** 03001011

### **Description/Analysis**

**Issue:** On October 20, 2009 the City Council directed the City Attorney and Assistant City Manager John Dangberg to investigate the issuance of the 35 Natomas Central building permits after FEMA's December 8, 2008 flood zone remap of the Natomas Basin, and to identify any other issues discovered during the investigation. On November 24, 2009, City Attorney Eileen Teichert and Assistant City Manager John Dangberg presented an interim report to council providing a brief status of this investigation. This report provides the final report on the 35 Natomas Central building permits and a current status of the City's discussions with FEMA. This report also identifies broad categories of legal and management issues within the building division and recommendations for further handling.

**Policy Considerations:** This recommendation is consistent with the City Council's prior

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direction to investigate, report back and provide recommendations for further action.

**Environmental Considerations:**

**California Environmental Quality Act (CEQA):** CEQA does not apply where the matter before the Council does not constitute a CEQA "project." A report of this nature does not qualify as a CEQA project inasmuch as it can have no conceivable impact upon the environment.

**Sustainability Considerations:** There are no sustainability considerations associated with this report.

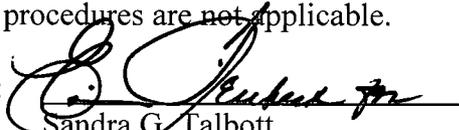
**Commission/Committee Action:** N/A

**Rationale for Recommendation:** The Audit Committee was formed by the City Council for the purpose of overseeing the conduct of audits and investigations at the direction of the City Council. It would be appropriate to transfer the additional issues identified in this report as meriting further audit or investigation to the Audit Committee for further handling.

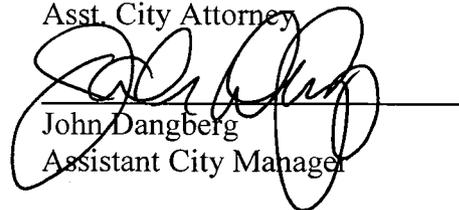
**Financial Considerations:** This report does not currently have a financial impact on the City's budget.

**Emerging Small Business Development (ESBD):** There is no discretionary expenditure involved in this report; consequently ESBD policies and procedures are not applicable.

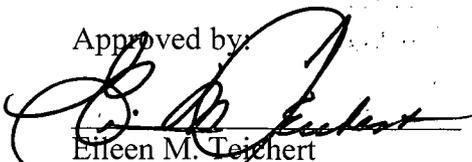
Respectfully submitted by:

  
Sandra G. Talbott  
Asst. City Attorney

Respectfully submitted by:

  
John Dangberg  
Assistant City Manager

Approved by:

  
Eileen M. Teichert  
City Attorney

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**BACKGROUND**

Effective December 8, 2008, the Flood Insurance Rate Map (FIRM) for the Natomas Basin was remapped by FEMA to an "AE" zone, instead of the prior Shaded "X" zone. The redesignation meant that all new residential construction had to meet a 33 foot base flood elevation (BFE) requirement. For example, if a house is proposed in an area that is 12 feet above sea level, the primary means of meeting the 33 foot BFE requirement is to construct the house on a 21 foot pad above the 12 feet above sea level grade. Due to the expense and impracticability of elevating a building to this height, the FEMA remap constituted a "de facto" building moratorium for the Natomas Basin.

The City received notice from FEMA in a letter dated June 6, 2008 that the remap of the Natomas Basin would be effective December 8, 2008. To prepare Community Development Department (CDD) Building Division staff for this event DOU Flood Plain Management staff conducted approximately monthly training for Building Division staff on this subject from June, 2008 to December, 2008. As part of the training DOU Flood Plain Management instructed Building Division staff that in order for a structure or a substantial improvement to a structure to be exempted from the new AE zone's 33 foot BFE requirement:

1. The building permit for such structure must have been issued prior to December 8, 2008; and
2. Start of construction on such structure must occur not later than 180 days after the permit issuance date. For residential structures, pouring of foundations is deemed the start of construction.

In late September, 2009, preparation of a routine report for FEMA by the DOU Flood Plain Management staff revealed that a number of new residential building permits for residential construction in the Natomas Basin had been issued September 22, 2009, by the building division of the CDD. At issue were 35 permits for single family residences in various stages of construction in K. Hovnanian's Natomas Central subdivision, that did not comply with the AE zone 33 foot BFE requirement. CDD was notified and their research into the matter was brought to the attention of the City Manager's Office (CMO) and the City Attorney's Office (CAO). DOU, CDD and CAO staff met with FEMA shortly thereafter to disclose discovery of these permits, and to address any FEMA concerns about these 35 permits. The CAO, in cooperation with the CMO and CDD, informed the City Council of this issue.

On October 14, 2009, when the City met with FEMA regarding the 35 permits, the City committed to putting immediate safeguards in place to ensure that no further permits would be issued in violation of City or FEMA regulations. Staff further committed to fully investigate City records to determine if other permits had been similarly issued in violation of regulations.

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FEMA's and the City's concerns with these 35 permits is that construction in violation of the City's floodplain management ordinance and FEMA regulations raises issues about life safety concerns, all City residents' access to the benefits of the National Flood Insurance Program, and the ability of federally regulated financial institutions to make, extend, or renew loans on structures in the City for which flood insurance is mandatory.

At the October 20, 2009, council meeting, Councilmember Fong requested an investigation into the issuance of these permits in the Natomas Basin. The City Council agreed and directed the CAO and the CMO to work together to develop a plan for investigating this matter.

At the October 27, 2009, council meeting, the CMO and CAO presented an oral report proposing a plan of action for an investigation and audit. Charts were presented to the City Council that graphically depict the allocation of responsibilities for the investigation and audit. Copies of those charts are attached to this report. The plan provided for the CAO to retain outside counsel to conduct the investigation of the 35 permits' issuance and related personnel issues, and for the CAO to work with FEMA to resolve the related flood plain management and flood insurance issues. The plan also provided for the Audit Committee to retain an outside consultant to audit the building division of CDD, regarding fee-related, processes and other issues. The council approved the plan for the investigation and audit, and directed staff to follow the evidence in the investigation to wherever it may lead. The Council further stressed the importance of moving swiftly to determine the cause of the problem and work with FEMA to resolve any issues that could affect funding or insurance rates. This process was to be as transparent as possible given that some areas would necessarily involve confidential personnel matters.

At the November 24, 2009, City Council meeting, the CAO and CMO gave an interim update on the investigation of the 35 permits' issuance and on related FEMA issues. Council was advised that the CAO had retained an outside law firm and that the investigation was well underway. No conclusions had been reached at that time as the investigation was on going. Council was advised that additional issues had arisen during the investigation, a number of which may be more appropriately handled by the Audit Committee. Concurrently, the Audit Committee was developing a scope of services for an RFP to be issued by the Audit Committee.

## **SCOPE OF REPORT**

This report addresses only the FEMA issues and the 35 permits investigation. This report does not discuss the status or outcome of the personnel investigations. This report also briefly discusses additional issues identified in the Building Division of CDD that merit further audit or investigation and makes recommendations for further handling.

## **INVESTIGATION**

Three days after receiving Council authorization of the plan, the CAO and CMO completed interviews of prospective law firms and retained the law firm Renne, Sloan, Holtzman, Sakai on October 29, 2009 to conduct the investigation. The CAO and CMO provided the law firm with the

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scope of investigation and background documentation on the 35 permits. The law firm's scope of services did not include calculating or determining the accuracy of any fees associated with these permits. The law firm was provided with read-only access to the Building Division's building permit database. The CAO established a tip-line for five weeks to allow witnesses to provide relevant information with anonymity. The law firm conducted interviews of more than two dozen witnesses obtained additional documents from witnesses and reviewed voluminous documents and relevant electronic building permit database information. The law firm summarized and organized the evidence and made findings based upon the evidence regarding personnel matters.

The law firm's interviews led to identification of additional potential legal issues within the Building Division. The CAO and CMO reviewed witness-provided documents, Accela database electronic records and other documents in order to determine whether the issues merited further audit or investigation.

**INVESTIGATION SUMMARY (EXCLUDING PERSONNEL ISSUES)**

Based upon the evidence known to date, the following summarizes the non-personnel facts regarding the issuance of and the fees associated with the 35 new lot permits.

*Issuance of Permits*

In early March 2009, a K. Hovnanian Homes representative requested CDD staff "transfer" or "switch" 35 building permits, from 35 "original lots" to 35 "new" lots all in the Natomas Central subdivision. The building permits for the original lots previously had been issued between December 12, 2006 to December 5, 2008, and authorized construction of cottage or duplex residential structures. K Hovnanian's representative explained the request was due to the absence of a market for the housing "product" for which the 35 original lot permits were issued, and K. Hovnanian desired to build instead more marketable single family residential structures on 35 new lots that could accommodate these larger residences.

CDD staff agreed to help K. Hovnanian and had K. Hovnanian complete applications for permits for the new lots. In April, 2009, K. Hovnanian's representative made periodic requests that City staff prepare the necessary documents so that construction could commence on specific lots. City staff prepared Tyvek© (waterproof) inspection envelopes for each of those lots. These inspection envelopes are posted outside at construction sites so that City inspectors can place their inspection reports inside the envelopes. Each inspection envelope was labeled with a different 2009 permit number, i.e. RES 09-01101, etc. Staff overrode the FEMA warning that appeared in the Accela database and proceeded to create 35 new electronic permit records showing each of the permits were in "applied", but not "issued" status. Therefore, staff did not issue the permits at that time.

K. Hovnanian began pouring foundations on all of the new lots and constructing homes on some of the new lots. As work progressed on the new lots, K. Hovnanian would request City inspections of work being performed. At least twice a City inspector questioned K. Hovnanian

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construction workers why construction was occurring under 2009 permit numbers and expressed concerns that this violated FEMA regulations. Each time, K. Hovnanian complained about this inspector to CDD supervisors. The inspector was told that FEMA had approved it and that he should perform the inspections. K. Hovnanian completed pouring the foundations on the 35 new lots from approximately May 6, 2009 to June 1, 2009.

While staff should have recognized that permits issued December 8, 2008, and thereafter would require compliance with the AE zone 33 foot BFE requirement, no intentional violations of the City flood plain management ordinance and FEMA regulations were found. It does not appear that CDD management had actual knowledge about this permit activity. There were no findings of criminal conduct.

Fees

Staff allowed construction to occur on the new lots prior to issuance of the new permits and prior to payment of additional fees. K. Hovnanian was advised that the permits for the new lots could not be issued until additional fees were paid, and that it would take time to calculate these fees. The additional fees were ostensibly to address the differences between the valuations for the original lots and valuations for the new lots. Staff also charged K. Hovnanian either \$280.00 or \$420.00 per permit for staff time to process these new permits, transfer old fees and calculate new fees.

Staff agreed to credit the various fees collected by the City for the 35 original lots permits (including 15 expired permits) against the fees owing for the new lots permits. Staff calculated those additional fees, credited the various fees from the original lots to the new lots, added the staff time charges, and determined approximately \$61,000 in additional fees were owed by K. Hovnanian.

K. Hovnanian paid those additional fees in late June 2009. At CDD supervisors' direction, these additional fees were not deposited in June 2009 as CDD had a surplus in their FY 2009 budget, and preferred the additional fees be deposited after July 1 and be applied to the FY 2010 budget. The additional fees were deposited September 22, 2009, at which time the 35 permits were changed to "issued" status in Accela.

During the investigation, CDD staff reviewed the fee calculations for the new lot permits to determine their accuracy. CDD staff identified at least two problems with the calculation of the fees for these permits. The problems identified are: 1) failure to charge the fee types and the higher fee amounts in effect on the dates fee payments were triggered in 2009, but rather charged the lower fees in effect from Dec. 2006 through Dec. 2008; and 2) unauthorized transfer of fees from 15 expired permits.

Approximately 19 fees apply to each of these permits with differing fee calculation dates applicable to each type of fee. Generally, City Code and otherwise applicable law, requires the City to charge permit applicants the fee types and fee amounts that are in effect on the dates when the

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various fees are due and payable. The following are a few examples of fee types and triggering fee payment events.

| <u>Fee Type</u> | <u>Triggering Fee Payment Event</u> |
|-----------------|-------------------------------------|
| Building permit | Permit issuance                     |
| Plan check      | Plan submittal                      |
| SAFCA DIF       | Permit issuance                     |

After the law firm completed the interviews, CDD staff performed a review and recalculation of the fees charged for the 35 new lot permits. For simplicity of recalculating the fees, CDD utilized the fee types and fee amounts that were in effect as of June 2009. Based upon CDD's recalculation of fees it has been preliminarily determined that at least \$300,000 in fees were undercharged and undercollected.

The City Code provides that building permits expire 180 days after their issuance date, unless the permittee applies and shows good cause for an extension of that date. Fifteen of the original permits were well beyond their 180 day expiration date and therefore had expired before K. Hovnanian requested transfer of fees from those permits. K. Hovnanian also did not request extensions of any of those permits. Some of the fees credited to K. Hovnanian were non-refundable and others (development impact fees) were refundable or creditable under limited circumstances. Calculations are still underway to determine the amount of fees improperly credited to K. Hovnanian from the expired permits.

**FEMA**

Staff has swiftly and actively fulfilled the City's commitments made to FEMA during their October 14, 2009 meeting on the 35 permits. These commitments include: putting immediate safeguards in place to ensure that no further permits are issued in violation of City or FEMA regulations; and a full investigation of City records to determine if other permits had been similarly issued in violation of regulations.

Since the last update to City Council on FEMA, the following additional actions have occurred. On December 15, 2009, the CAO wrote to FEMA outlining CDD and Floodplain Management measures for enhanced permit control, including additional safeguards for the computerized permit system to ensure compliance with floodplain development standards and to prohibit unauthorized override of FEMA warnings in the system. The December 15, 2009, letter from the CAO to FEMA also outlined a City proposal for allowing homes under the 35 permits to be completed, sold, and occupied, and be eligible for Shaded X Zone rating NFIP insurance. As of the date of writing this report, the CAO has not received a written response from FEMA. FEMA has requested and staff has provided additional data regarding permits issued during the past several years in the City's Special Flood Hazard Areas.

The investigation indicated that the only new residential permits issued after December 8, 2008 resulting in new home construction in the Natomas Basin were the 35 permits for K.

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Hovnanian Homes in the Natomas Central subdivision.

However, the investigation did uncover some additional permits issued after December 8, 2008, that were problematic. There were five permits issued for new construction of two-story commercial buildings, but as no construction had taken place at the time of discovery during the investigation, the City Manager's Office revoked those permits. There remain eight additional permits pending further review and action by CDD and DOU staff. The eight permits are: a storage shed with electrical, a stand-alone garage, the rebuild of a house which burned down, a condominium remodel, the repair of a house damaged by a falling tree, the repair of another house damaged by fire, and the placement of an underground propane tank, and an above ground propane tank. These need to be resolved through floodplain management procedures.

**ISSUES MERITING FURTHER AUDIT OR INVESTIGATION**

There are a number of issues that were independently raised by staff or brought to light through the investigation that merit further review. The categories of these issues meriting further review are:

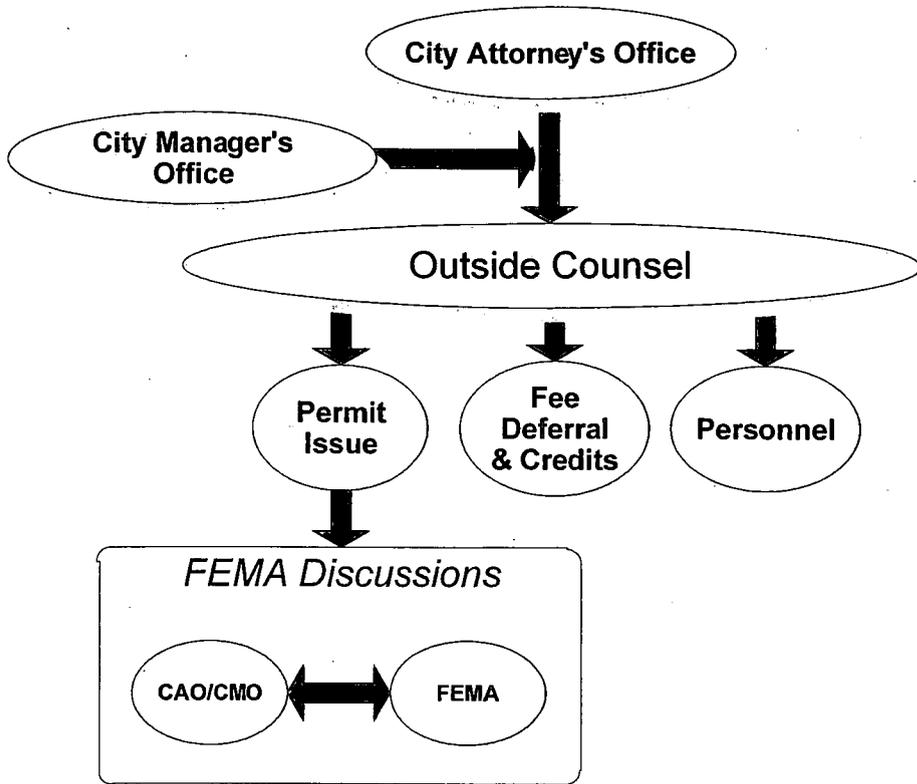
- Conflicting messages arising out of departmental culture
- Deferral, waiver, non-collection and underassessment of fees
- Non-compliance with Fee-Deferral Program
- Construction prior to plan, fee payment or permits issuance
- Permit transfers between property owners
- Grading permits without HCP fee payment
- Non-compliance with City's planning requirements
- Mischaracterization of project or permit and related fee impacts
- Demolition without CEQA review
- Potential quid pro quo

It is recommended that further handling of these issues be under the oversight of the Audit Committee. The Audit Committee may choose to have certain issues audited by the new Auditor after the Auditor is appointed, or by an outside consultant. The Audit Committee would report back to the full Council on dates specified by the Council. It is also recommended that additional personnel investigations arising out of these issues be conducted by the Labor Relations Department under the oversight of the City Manager.

City Manager and CDD staff will continue to proactively investigate these matters and implement measures to address them. Where corrective actions are taken, staff will keep records of program and process changes for later review during the audit process.

The City Attorney's Office will conduct an orderly transition of the records and information associated with these issues to either the Audit Committee or Labor Relations Department, and will provide legal advice and counsel as needed regarding the audit and investigations.

**Investigation Natomas Central Permits  
and Related Issues**



# ***Program Audit***

