

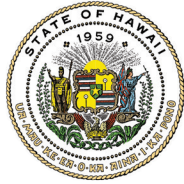
Audit of the Department of Education's Administration of School Impact Fees

A Report to the Governor
and the Legislature of
the State of Hawai'i

Report No. 19-13
September 2019



OFFICE OF THE AUDITOR
STATE OF HAWAI'I



OFFICE OF THE AUDITOR STATE OF HAWAII

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Foreword

Our audit of the Department of Education's Administration of School Impact Fees was conducted pursuant to Article VII, Section 10 of the Hawai'i State Constitution and Section 23-4, Hawai'i Revised Statutes, which authorizes the Auditor to conduct post-audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions.

We express our sincere appreciation to the staff of the Department of Education, in particular the department's Office of School Facilities and Support Services, the Facilities Development Branch, and Planning Section; the Board of Education; and other individuals whom we contacted during the course of our audit, for their cooperation and assistance.

Leslie H. Kondo
State Auditor



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ILLUSTRATION: DEPARTMENT OF EDUCATION

A Low-Impact Exercise: Audit of the Department of Education’s Administration of School Impact Fees

Introduction

LOCAL GOVERNMENTS COLLECT impact fees to offset the cost of new and expanded public facilities needed to serve new developments. Hawai‘i’s Department of Education (DOE) has been seeking land and cash contributions from developers for decades to help pay for additional public schools and classrooms to accommodate students moving into new residential projects. The practice was formalized in the late 1980s, when the DOE began negotiating “Fair Share agreements” with individual developers on a case-by-case basis. However, a perception that Fair Share agreements were inconsistent and unpredictable led the 2005 Legislature to establish a School Impact Fee Working Group (Working Group) to explore alternatives to address concerns of interested parties. The Working Group issued its report in March 2007.

The Working Group’s recommendations were incorporated into Act 245 (Session Laws of Hawai‘i (SLH) 2007), which requires the Board of Education (BOE) to designate “school impact districts” – geographic

We found the school impact fee law has been of questionable “impact.”

areas where anticipated residential growth may require new or expanded schools. The school impact fee law, codified as Sections 302A-1601 through 302A-1612, Hawai‘i Revised Statutes (HRS), further requires that all builders of new residential units within a designated impact district pay impact fees – individual home builders and large developers alike. The law sets forth formulas for calculating school impact fees, which include land for new schools (or fees in lieu of land) and a percentage of the estimated cost to build new schools.

We found the school impact fee law has been of questionable “impact.” In the 12-plus years since its enactment, the DOE has designated five school impact districts, one of which was suspended after a few months. As of December 31, 2018, the department had collected a total of \$5,342,886 in school impact fees across all impact fee districts. By contrast, the last elementary school built by the DOE, Ho‘okele Elementary School in Kapolei, cost \$55 million alone. The DOE estimates it would cost approximately \$80 million to build a single new elementary school today.

Our review showed the DOE has not made implementation and administration of the school impact fee law a priority. For instance, the DOE has largely delegated responsibility for establishing district boundaries and impact fees to a single employee, a Land Use Planner, who has not been provided administrative rules, written policies, or formal procedures for guidance. Yet the Land Use Planner has decided when and where to set up impact fee districts, has controlled the order and size of the districts designated by the board, and has been responsible for preparing the written analyses establishing the need for the designation of districts. Tracking and accounting for school impact fees have been minimal, and in some cases non-existent, and expenditures have yet to be made from any school impact fees collected.

This general lack of attention and prioritization has manifested itself in numerous ways. Most significantly, the DOE has been unable to meet all the requirements of its legislative mandate to implement the school impact fee law. We also question whether the impact fee districts the board has designated are appropriately sized to satisfy the constitutional requirement that there be a “nexus” – i.e., a reasonable connection – between the development of new residential units and the need for additional classroom capacity. Three of the four implemented impact fee districts include multiple school complexes; new residential development in one school complex, however, seems unlikely to cause the need for more classroom capacity in another complex.

The DOE has an important and broad mission – to serve our community by developing the academic achievement, character, and social-emotional well-being of our public school students to the fullest potential. We

recognize the DOE has many responsibilities and the money generated by the school impact fee program may be relatively small compared to the DOE’s facilities budget. Nevertheless, the department is required to administer the school impact fee law. The relatively small amount of money collected to date does not excuse the department from meeting this statutory mandate. However, the amount does call into question whether the law, as written, will generate enough fees to adequately mitigate the impact of new residential construction on DOE facilities.

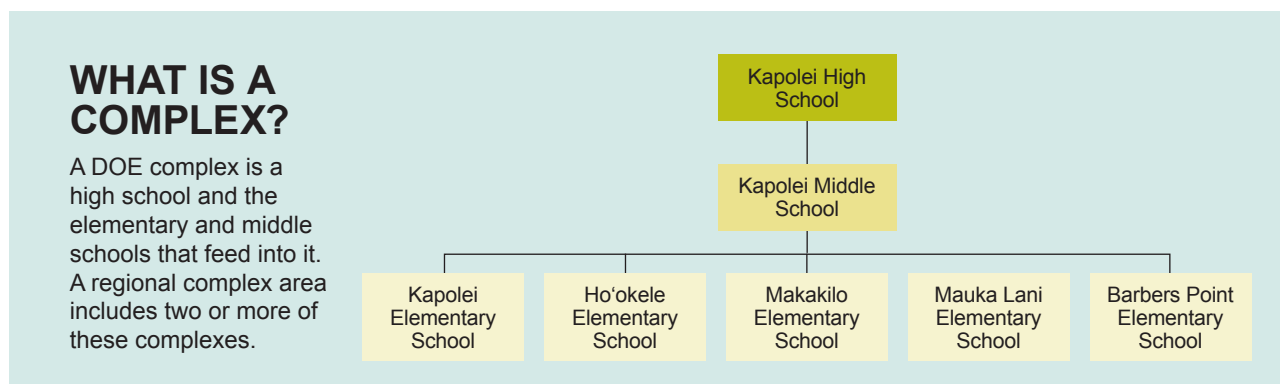
Background

Hawai‘i has the oldest public school system west of the Mississippi and the only statewide school district in the nation. Its 292 public schools are grouped into 41 “complexes,” each containing one high school and the elementary and middle schools that feed into it (see below). Two to four high school-led complexes are grouped into 15 regional complex areas. For example, the Campbell-Kapolei *complex area* consists of two *complexes*: Kapolei High School and its six feeder schools along with Campbell High School and its nine feeder schools. During the 2018-19 school year, 179,698 students were enrolled in public schools on seven islands – 168,152 students attended traditional schools and 11,546 attended charter schools. The public school system is funded primarily through the State’s general fund; for fiscal year 2020, the DOE has a \$2.1 billion operating budget and a \$565.9 million capital improvement project budget.

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Fair Share Agreements

When State Land Use Districts were established in 1962, the DOE was tasked with reviewing land classification petitions pending before the State Land Use Commission and commenting on the adequacy of existing



SOURCE: DEPARTMENT OF EDUCATION

“Flawed” statute delayed implementation from 2007 to 2010

ALTHOUGH THE SCHOOL impact fee law was enacted in 2007, designation of the first impact district did not occur until 2010. According to the DOE, this was largely due to drafting errors and problems with the statutory formula that required legislative action to correct. In 2010, the governor signed Act 188 (SLH 2010), in which the Legislature made several amendments to the school impact fee law. According to a legislative conference committee report, these changes were intended to improve “the accuracy and appropriateness of information used to determine school impact fees and create a more equitable assessment of school impact fees.”

Notably, Act 188 revised the formulas used to calculate land dedication and construction cost requirements to factor in student generation rates and the number of dwelling units in new residential developments, along with recent school construction cost estimates. Act 188 also added requirements to update the data used to establish school impact districts and calculate impact fees to reflect current conditions at three-year intervals as specified in Section 302A-1612, HRS.

public schools in those areas. When it was apparent the level of funding provided by the State for school facilities was falling short of fulfilling growth-related educational needs, the DOE began asking developers to contribute toward the construction of new schools and classrooms. By the late-1980s, these contributions were being negotiated on a case-by-case basis and were largely land-driven, reflecting a DOE preference that developers contribute land for school sites. These negotiations resulted in contracts which became known as “Fair Share agreements.”

In 2001, the department completed a *Fair-Share Contribution Study* to address State Land Use Commission and developer concerns, including a shared desire for more predictability in contributions required of developers. Using standards derived from the study, the DOE began asking developers for land contributions as well as 30 percent of the estimated construction-related costs. However, because the land dedication and construction fees were not required by statute, the DOE had to rely upon the State Land Use Commission’s willingness and cooperation to require developers’ Fair Share contributions as conditions of approval for changes in State Land Use District classifications.

According to the DOE, there are currently 68 Fair Share agreements and moneys collected under those agreements have been used to cover shortfalls in available funding for projects intended to increase school capacity. For example, Fair Share contributions have been used for funding shortfalls in Kapolei High School Phase 2, to complete Kamali‘i Elementary on Maui, and for five portable classrooms.

2005 School Impact Fee Working Group

The department’s *Fair-Share Contribution Study* resulted in general standards, but the DOE and the development community wanted more consistency and uniformity than individually negotiated Fair Share agreements offered. Act 246 (SLH 2005) established the School Impact Fee Working Group to study and recommend alternative ways of financing new school construction and the expansion of existing educational facilities.

The Working Group identified two types of districts that might warrant school impact fees: “greenfield” areas where large-scale planned residential developments on former agricultural lands will require new elementary, middle, and high schools; and “non-greenfield” areas where school complexes already exist and new residential development tends to occur on smaller, scattered sites. The key characteristic of non-greenfield areas is that the same schools will serve both existing and new housing. The Working Group offered recommendations for both types of districts.

2007 School Impact Fee Statute and Revisions

Working Group recommendations served as the basis for legislation passed by the 2007 Legislature and signed by the governor as Act 245 (SLH 2007). Among other things, Act 245 authorized the BOE to designate “school impact districts” in which land and funding could be collected to offset impacts on student enrollment caused by new residential development. After Act 245 was enacted, the DOE began collecting school impact fees from new residential projects that did not have existing Fair Share agreements. Since passage of Act 245, the school impact fee law has replaced the use of Fair Share agreements.

Act 245, codified in Chapter 302A, HRS, expressly requires everyone who builds a new residential unit within a designated school impact district to pay impact fees. More specifically, anyone requiring subdivision approval, a building permit, or condominium property regime for new residential construction in a designated school impact district must contribute toward the construction of new public schools or toward the expansion of existing school facilities. The requirement applies to individual home builders as well as large developers. Commercial projects, industrial projects, senior housing projects, and replacement homes or projects to enlarge existing homes are exempt from paying impact fees.

While the BOE designates school impact districts, the department must identify areas where high residential growth will require additional classroom capacity within 25 years, define the boundaries of the proposed school impact district, and prepare written analyses for the board’s review. The DOE also calculates the impact fees and must periodically update some of the factors that comprise the impact fee formulas detailed in the statute. There are separate formulas for the land dedication (or fee in lieu of land) and construction cost requirements.

According to the DOE, meaningful work toward the implementation of school impact fees could not take place until 2010, three years after the school impact fee law was enacted, because flaws in the original statute needed to be fixed. (See – “‘Flawed’ statute delayed implementation from 2007 to 2010 on page 4.”) The statute was amended again in 2016; as detailed in our later discussion of the Kalihi-Ala Moana (KAM) school impact district, many of those changes were tailored to the specific conditions presented by an urban district. For example, in urban Honolulu, i.e., the KAM district, the department can use school impact fees for maintenance, operational expenses, and administrative costs of existing schools.

Financial Information

To date, Fair Share and impact fee collections and expenditures have been minimal. Totals are noted below.

Fair Share Contribution Balance (As of December 31, 2018)		Impact Fee Balance (As of December 31, 2018)
\$8,585,795		\$5,342,886
Fair Share Contribution Expenditures and Transfers Out of Fair Share Trust Accounts		Impact Fee Expenditures
Prior to 2002	\$310,000	\$0
Lahainaluna Library	\$200,000	
Phase II of Kapolei H.S.	\$110,000	
Kamali'i Elementary	\$1,000,000	
In FY2005	\$993,955	
In FY2010	\$6,045	
Portables for 5 schools in FY2010)	\$1,909,856	
Mā'ili Elementary	\$58,208	

SOURCE: DEPARTMENT OF EDUCATION

PHOTO: ISTOCK.COM

Audit Objectives

1. Determine how the DOE assesses the need for additional classroom capacity within the next 25 years and decides to recommend the BOE designate a school impact district.
2. Describe the DOE's process to calculate and update school impact fees.
3. Evaluate the DOE's assessment and collection of school impact fees.
4. Assess whether the DOE is adequately accounting for money and land received from Fair Share agreements and school impact fees and providing the Legislature with complete and accurate reports regarding the Fair Share agreements and school impact fee law.
5. Make recommendations as appropriate.

Summary of Findings

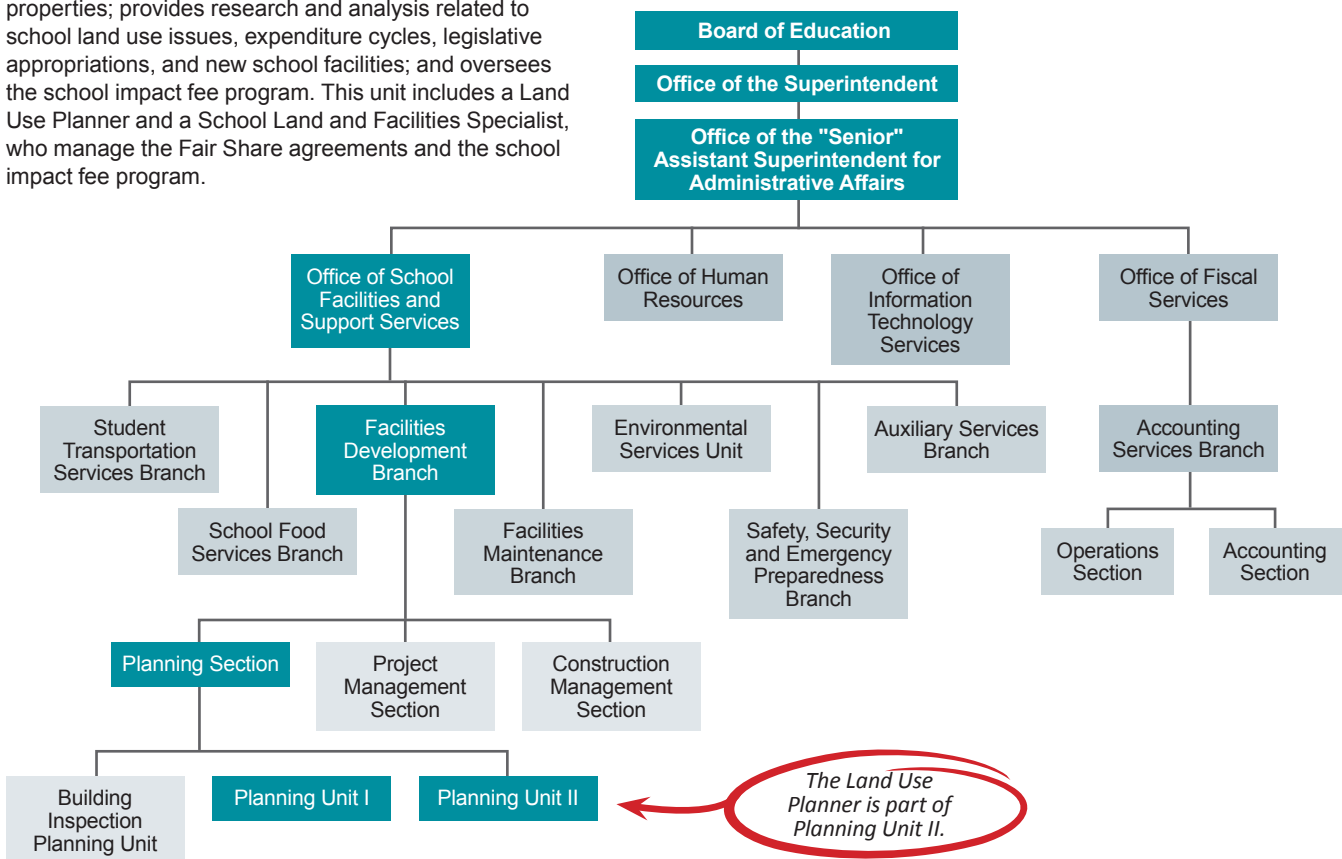
1. The DOE's designation of school impact districts lacks well-defined policies and procedures and the districts designated to date raise concerns as to whether constitutional "nexus" requirements have been adequately addressed;
2. The DOE's calculation of fees has been inconsistent and at times based on questionable assumptions, and updates to formula factors as well as other requirements of the school impact fee law have not been met;
3. "Gaps," i.e., delays, between designation of school impact districts and collection of fees have resulted in loss of fee revenue; and
4. The DOE cannot adequately account for Fair Share and school impact fee cash and land contributions.

Overview: The DOE has not provided adequate resources and oversight needed to implement and administer the school impact fee law.

The DOE has no written policies and procedures for the selection of potential school impact districts, the factors that should be considered in determining the size of potential districts, or oversight and review of this process. Since school impact fees are primarily the responsibility of a single Land Use Planner within the DOE, it is this individual's discretion, rather than documented criteria and procedures, that determines the order and timing of school impact district designation, which affects when builders are obligated to begin paying fees. In

Departmental Organization Chart

Planning Unit II plans and coordinates the development of future school sites and improvements to existing properties; provides research and analysis related to school land use issues, expenditure cycles, legislative appropriations, and new school facilities; and oversees the school impact fee program. This unit includes a Land Use Planner and a School Land and Facilities Specialist, who manage the Fair Share agreements and the school impact fee program.



SOURCE: DEPARTMENT OF EDUCATION

setting the order for proposed district designations, the Land Use Planner considers information obtained via media reports, community plans, and developer feedback, and ultimately relies on intuition to decide whether residential development, much of which currently is still only a conceptual vision, will create a need for new schools or new classrooms in the next 25 years.

The DOE's lack of formal guidance documents also means the Land Use Planner's work cannot be easily replicated and the department's implementation of the school impact fee law cannot be meaningfully evaluated. According to the DOE Public Works Manager, writing procedures for such a small program is unnecessary. The manager believes that, if the current staff left the Planning Section or retired, their replacements could come to the same common-sense conclusions as they do.

We disagree. Written guidance helps ensure the efficiency of operations as well as agency implementation of the law, two areas the department has struggled with when designating school impact districts.

In addition, the BOE has not promulgated administrative rules to implement the law, although it is empowered by statute to do so. DOE personnel said they do not believe administrative rules are needed. According to the Public Works Manager, "the legislation was designed that way, it prescribes everything." This was echoed by the Land Use Planner, who said the "legislative intent of the impact fee law is that there be no administrative rules." When asked whether administrative rules or written policies and procedures would help Planning Unit II implement the impact fee law, the Land Use Planner replied, "No. We're talking about two people [who oversee and administer the entire program]."

Again, we disagree. While the department may believe the law was supposed to be so sufficiently detailed that administrative rules would not be needed, the statute, as enacted, contains few of the details necessary for the DOE to implement the law. Legislative acts often provide the general framework of a program, and agencies are required to "fill in the details" to implement the program through administrative rules, which are the agency's statements about how it interprets a statute, including the procedures the agency requires others to follow. As detailed below, the department has been inconsistent in its application of the school impact fee law, has been forced to rely on the cooperation of county building departments to enforce the school impact fee law, and has allowed school impact fees to go uncollected.

Rules Rule

ADMINISTRATIVE RULES

provide a check on an agency's discretionary power by requiring pre-established rules and standards that guide consistent agency behavior in its implementation of legislative directives.¹ Under Chapter 91, HRS, a rule is defined as, "each agency statement of general or particular applicability and future effect that implements, interprets, or prescribes law or policy, or describes the organization, procedure, or practice requirements of any agency." The Legislature empowers agencies to promulgate administrative rules that provide details on guidelines, limitations and parameters for implementing the policy in accordance with the statute. The Hawai'i Supreme Court has explained,

"[r]ule-making is an agency action governing the future conduct either of groups of persons or of a single individual; it is essentially legislative in nature, not only because it operates in the future but also because it is concerned largely with considerations of policy."²

¹ See *In re Terminal Transportation, Inc.*, 54 Haw. 134 (1972).

² *Pila'a 400, LLC v. Bd. of Land and Natural Resources*, 132 Hawai'i 247, 266 (2014) (quoting Note, 'Rule Making,' 'Adjudication' and Exceptions Under the Administrative Procedures Act, 95 U. Pa. L.Rev. 621 (1946-47)).

This laissez-faire approach is reflective of the DOE's overall attitude toward school impact fees. In this report, we highlight how the department appears to be inadequately considering and applying certain "core principles," which should be the foundation and framework for its implementation and administration of the school impact fee law.

Guidance Documents and Internal Controls

GOVERNMENT AGENCIES rely on guidance documents to clarify statutes or regulatory text and to inform the public about complex policy implementation topics.¹ Internal control – effected by an agency's oversight body and management – provides reasonable assurance an agency's objectives will be achieved.² Specifically, control activities are the policies, procedures, and techniques that ensure management's directives are carried out. Management objectives include the effectiveness and efficiency of operations; reliability of reporting for external or internal use; and compliance with applicable laws and regulations. Control activities are an integral part of an agency's planning, implementing, stewardship of government resources, and achieving effective results. Further, to improve accountability, agencies should clearly articulate their missions in the context of statutory objectives and develop implementation plans for the goals and objectives as well as measures of programs toward achieving them.³ Established time frames can also help ensure dedicated implementation of a program.

¹ *Regulatory Guidance Processes, Selected Departments Could Strengthen Internal Control and Dissemination Practices*, U.S. Government Accountability Office, April 2015.

² *Standards for Internal Control in the Federal Government*, U.S. Government Accountability Office, September 2014.

³ *Performance Measurement: An Important Tool in Managing For Results*, U.S. Government Accountability Office, May 1992.

The DOE based its estimates of future capacity need on O‘ahu on conceptual projections, raising questions about compliance with constitutional “nexus” requirements.

Core Principle The U.S. Constitution requires that impact fees meet “nexus” requirements.

What we found The DOE’s process for designating school impact districts, and the districts designated to date, present concerns as to whether “nexus” was given adequate consideration.

Prior to recommending the BOE designate a school impact district, the DOE prepares an analysis that verifies the need for new school facilities in the proposed area. Under the impact fee law, the analysis must include:

- Evidence that there will be need for a new school in the proposed district within 25 years based on state and county land use, demographics, growth, density, and other applicable historic projections and plans;
- The boundaries of the proposed district, including school enrollment in and around the proposed impact area;
- The student generation rates by dwelling type and the estimated number of students generated by new residential developments in the proposed impact district;
- The appropriate school land area or appropriate state lands and enrollment capacity, which may also include non-traditional facilities such as mid-rise or high-rise structures to accommodate school facility needs in high-growth areas within existing urban developments; and
- A statewide classroom use report, which includes the current maximum number of students per classroom per school, the current student enrollment per school, and the current number of classrooms not used for active teaching.

“Creating one district covering multiple neighborhoods and school complexes poses equity concerns that should be considered. The collection of fees in one school complex area (e.g., a high-growth neighborhood) are not required to be spent in the same complex where the rationale for the fee exists.”

**— Acting Director,
Department of Planning
and Permitting, City and
County of Honolulu, in
November 1, 2016, written
testimony on the proposed
designation of the Kalihi
to Ala Moana school
impact district.**

Once a district is designated, the DOE is required to complete a second analysis that considers the “advantages and disadvantages of potential changes to the statewide school site areas and design enrollment standards that may be appropriate for application in the particular school impact district.” Such considerations may include non-traditional facilities including vertical schools in existing urban areas. The DOE must also set the impact fees to be assessed in each school impact district.

The DOE designated O’ahu school impact districts and calculated school impact fees based in part on the number of residential units the City estimates will be built when the rail project is completed

There is no consistent process or documented framework for determining when a school impact district should be designated or when analysis should begin. As noted previously, the Land Use Planner is solely responsible for making these determinations. In interviews, however, the Land Use Planner could not describe the specific procedures used to perform the work and instead explained that designating districts is a matter of being “intuitive” or having a “feel” for the general development climate based on media reports and “keeping an ear to the ground.” The Public Works Manager described the process as using “professional judgment” and experience from years of working in the development area (rather than “feel”).

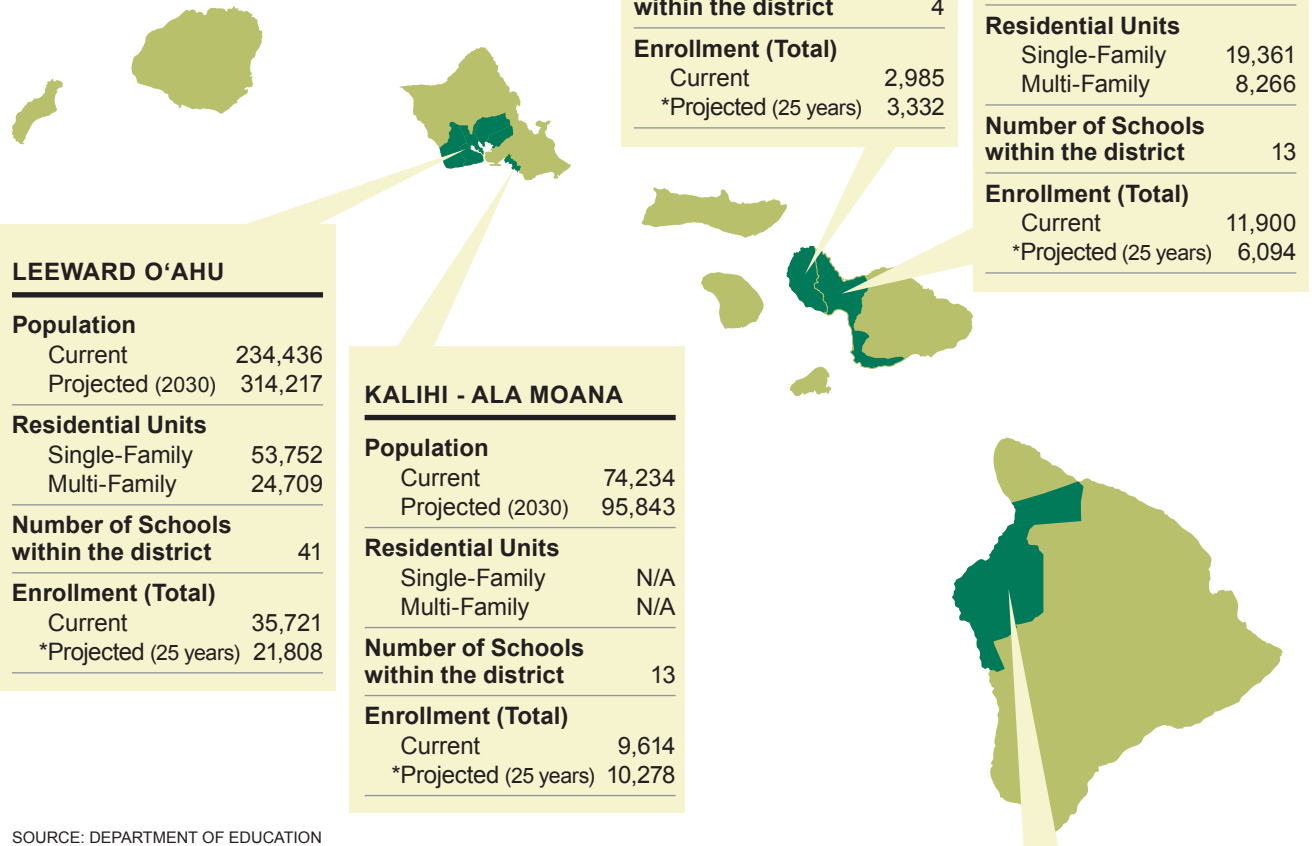
We do not believe implementing the school impact fee law based on “intuition” or even someone’s undefined “professional judgment” is appropriate. Neither the Land Use Planner nor the Public Works Manager could recreate the specific factors they considered in evaluating the need for new schools or additional classrooms, the timing of such reviews, or other material aspects of their analyses. Without documented policies and procedures (i.e., internal controls that set forth clear and consistent processes), we are unable to assess if the department is implementing the program consistently, fairly, and in accordance with the statute.

The school impact fee law directs the DOE to analyze whether new or expanded schools will be needed within the next 25 years, but anticipating new residential developments that are undefined and simply “envisioned” seems too speculative to reasonably support the assessment of impact fees on current projects. To illustrate, the BOE designated the KAM school impact district based primarily on the department’s projection of a substantial number of public school students moving into the residential transit-oriented development

EXHIBIT 1 District Demographic Comparisons

The Board of Education has designated five school impact fee districts in geographic areas where student enrollment is projected to exceed current school capacity within 25 years based on anticipated residential development.

* Additional students projected within 25 years.



SOURCE: DEPARTMENT OF EDUCATION

(TOD) projects the City and County of Honolulu (City or Honolulu) envisions being built around the rail transit route (See “Tomorrowland: Transit-Oriented Development” on page 20). Nevertheless, anyone who builds a new residential dwelling within this impact district must pay a school impact fee even though TOD projects may not be completed for decades, if at all, and many of the schools within the designated school impact districts are currently under-enrolled. We note the School Impact Fee Working Group recommended that the DOE look ahead 10 years when forecasting capacity needs, rather than 25 years.



The U.S. Constitution Requires Nexus

THE CONCEPT OF NEXUS and rough proportionality is grounded in the U.S. Constitution, and has been developed through court cases; we include a brief discussion of two of the leading cases here. Broadly speaking, there must be a sufficient relationship, or “nexus,” between the fee and the government’s interest in regulation, and “rough proportionality” between the amount of the fee and the projected impacts. We question, for example, whether the impact of someone building a new residence in ‘Ewa Beach creates a “ripple effect” that spreads all the way to ‘Aiea, which is part of the same designated school impact district. We find it difficult to see how the “ripple” of additional school capacity needs caused by the ‘Ewa Beach builder would spread beyond the schools in that complex. Yet the fee paid by the ‘Ewa Beach builder can be spent anywhere in the district, including as far away as ‘Aiea.

On November 1, 2016, the City and County of Honolulu’s Department of Planning and Permitting (DPP) submitted written testimony opposing the proposed Kalihi to Ala Moana (KAM) school impact district, which expressed similar nexus concerns. In the letter, DPP, which had been planning for Transit-Oriented Development (TOD) around future rail stations for more than a decade, expressed its concerns that the DOE’s “current proposal runs contrary to the objectives of TOD.” For example, regarding the size of the KAM district, DPP pointed out that:

Creating one district covering multiple neighborhoods and school complexes poses equity concerns that should be considered. The collection of fees in one school complex area (e.g., a high-growth neighborhood) are not required to be spent in the same complex where the rationale for the fee exists.

We agree.

The Hawai‘i School Impact Fee Working Group Report, issued in 2007, included a review of the legal framework for development extraction and impact fees. The following is a summary of the legal research included in the report:

In *Nollan v. California Coastal Commission (Nollan)*, the U.S. Supreme Court invalidated a decision of the California Coastal Commission requiring permit applicants, the Nollans, to dedicate a trail across their beachfront property as a pre-condition to their building permit to demolish a single-family dwelling and replace it with another, larger single-family dwelling. The Court rejected the commission’s argument that there was an essential nexus between visual access to the ocean and a permit condition requiring lateral public access along the Nollans’ beachfront property.

The *Dolan v. City of Tigard* case arose when Florence Dolan applied for a building permit to expand an existing hardware and plumbing supply store from 9,000 square feet to 17,000 square feet and to pave a 39-car parking lot. While the project conformed with existing zoning, the City of Tigard imposed, as a condition of Dolan’s building permit, a requirement that Dolan dedicate land to the city for use as a floodway, a greenway, and a bike path. The Supreme Court applied the test it announced in *Nollan* and found an essential nexus between the City of Tigard’s requirement that Dolan dedicate land to the city for use as a floodway, a greenway, and a bike path and the city’s legitimate state interest in preventing flooding and reducing traffic congestion (caused by Dolan’s expanded paved parking lot and store size).

However, in rejecting the City of Tigard’s permit conditions on Dolan’s property, the Court announced that, in addition to an essential nexus, there must also be a “rough proportionality” between the impact of a proposed development and the burden of the exaction imposed on it. The Court explained that this second part of its analysis requires a determination of whether the degree of the exactions demanded by the city’s permit conditions bears the required relationship to the projected impact of the proposed development. Though “no precise mathematical calculation is required” to determine proportionality, the Court held that the government must make some sort of individualized determination that the required dedication is related both in nature and extent to the impact of the proposed development.

Constitutional requirements not thoroughly considered by the department

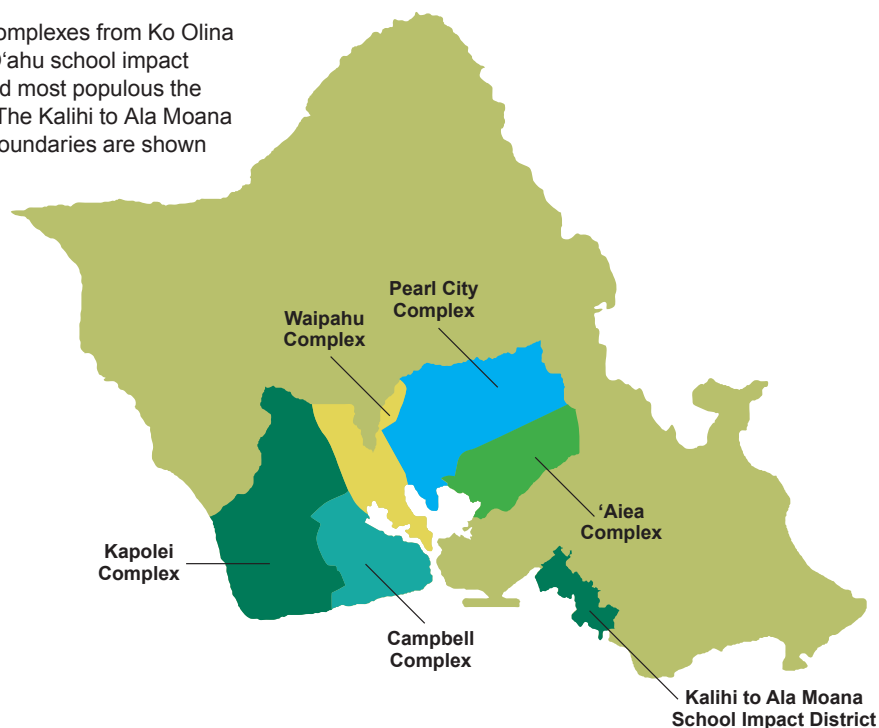
The U.S. Supreme Court has made clear that impact fees, such as those required under the school impact fee law, must satisfy certain constitutional requirements. For school impact fees, there must be a substantial relationship, or a “nexus,” between the new residential development and the need for new schools and classrooms to serve that development.

Our review of the DOE’s implementation of the school impact fee law, however, raises questions as to whether the impact fee districts designated by the board to date – some of which involve expansive areas spanning several school complexes – meet that requirement. Allowing KAM district fees to be used for maintenance, operational expenses, and administrative costs of existing schools in urban Honolulu raises further nexus questions; fees collected in the other school impact districts are limited to capacity-building projects.

For example, the Leeward O’ahu School Impact District (Leeward District) includes *five* school complexes: the Kapolei complex, the Campbell complex, the Waipahu complex, the Pearl City complex, and the ‘Aiea complex (see Exhibit 2). Any new residential construction in the Leeward

EXHIBIT 2 Leeward O’ahu School Impact District is Comprised of Five School Complexes

Spanning five school complexes from Ko Olina to ‘Aiea, the Leeward O’ahu school impact district is the largest and most populous the BOE has designated. The Kalihi to Ala Moana school impact district boundaries are shown for comparison.



SOURCE: DEPARTMENT OF EDUCATION

district – from a single home to a large residential subdivision – must pay a school impact fee that can be used anywhere in the Leeward impact fee district to build additional classroom capacity. That means that fees collected from new residential construction in Kapolei can be used to build or expand classrooms in Pearl City, far away from the development's "impact."

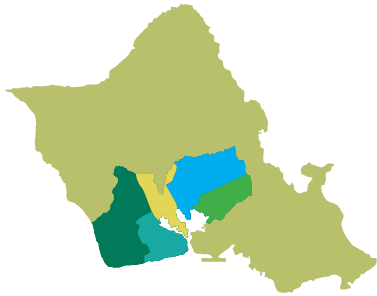
A detailed examination of O'ahu's Leeward and KAM districts highlights our concerns about the sufficiency of the nexus required as well as other concerns we noted during our work on this audit. The Leeward district covers a large geographic region; the KAM district covers a wide range of property values and land needs.

The Leeward district: A tale of two complexes

The most populous of the DOE's school impact fee districts is the Leeward O'ahu School Impact District, stretching from Ko Olina on the Leeward Coast to 'Aiea on the edge of Honolulu's urban core. In 2010, the district's 234,000 residents accounted for more than a quarter of the island's overall population. Its 35,721 public school students (2011-12 school year) – more than the student populations of the other four districts combined – attended 41 schools in 5 different school complexes.

According to the DOE's "Analysis of the Leeward O'ahu School Impact District," the identification of the Leeward district was based on growth experienced over the past 25 to 30 years and growth expected over the next 25 to 30 years. The DOE analysis compared the Leeward district's population to that of the City and County of Honolulu from 1990 to 2010. It also included population projections (2010 to 2035) for Honolulu county, the Leeward school impact district, and the rest of O'ahu (excluding the Leeward district). The analysis concluded that Leeward district experienced a substantial rate of growth over the past two decades. In addition, it projected that in the 25-year period from 2010 to 2035, the Leeward district's population will increase by 41 percent.

However, a review of the analysis' data on historical and projected enrollment for schools in the district's five complexes provides a much more nuanced view of the district's growth. Specifically, from the perspective of student generation, the Leeward district's historic, recent, and projected growth was, is, and will be primarily driven by two school complexes: Campbell and Kapolei. For example, from the 1980-81 school year to the 2011-12 school year, the Campbell complex experienced a net gain of 4,601 students. The nearby Kapolei complex had similar growth, gaining 4,905 students. Moving eastward toward Honolulu, the Waipahu complex experienced a moderate increase of

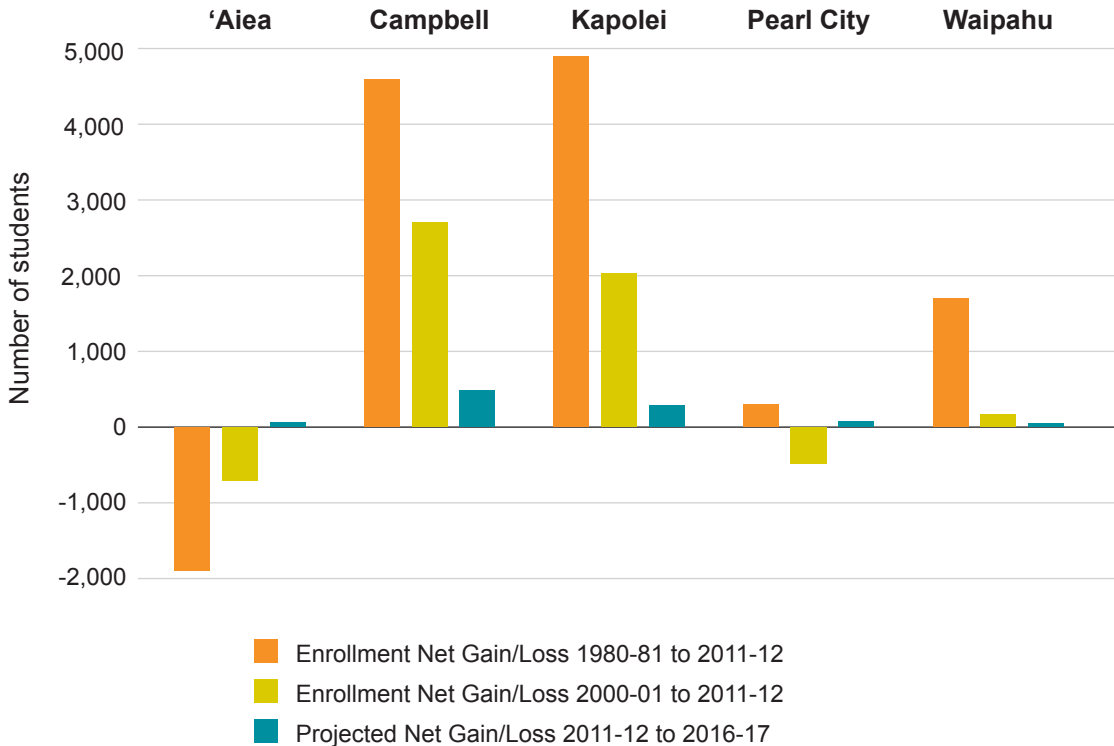


When we asked the Land Use Planner why the Leeward district was so large, she described a "general feeling" that the demographics in the area were similar. "It just made sense," she said.

EXHIBIT 3

Current Enrollment and Projected Net Gain/Loss 1981–2017

Projected growth in the Leeward O’ahu School Impact District is primarily driven by Campbell and Kapolei complexes.



SOURCE: DEPARTMENT OF EDUCATION

1,704 students, while the Pearl City complex saw even fewer at 299. Meanwhile, during the same 32-year period, the ‘Aiea complex saw enrollment decrease by 1,902 students.

More recent student population statistics show similar differences from one end of the district to the other. For example, from the 2000-01 to the 2011-12 school year, the Campbell and Kapolei complexes saw their enrollment numbers increase by 2,711 and 2,028, respectively. In contrast, Waipahu’s enrollment increased by just 159 students, while Pearl City was down 486 and ‘Aiea lost 708 students.

In addition, the analysis’ projections of near-term student enrollment gain or loss told the same story, with the Campbell and Kapolei complexes leading the way with projected student growth of 484 and 289, respectively, while the other three complexes had much smaller projections (‘Aiea – 53, Pearl City – 75, and Waipahu – 40).

Leeward district created to “catch the small guys”

The DOE’s analysis of the Leeward district forecasts 55,613 residential units will be built in the coming decades. Many of these units are within projects covered under Fair Share agreements which, among other things, identify specific types and numbers of residential units to be built. The DOE’s analysis also includes residential projections based on the City’s proposals of higher-density zoning changes for TOD projects. (See “Tomorrowland: Transit-Oriented Development” on page 20.) The department estimates these possible TOD projects could eventually yield 9,380 residential units, all of which the DOE assumes will be multi-family units. We note that TOD estimates are based on zoning changes that allow residential development, not actual planned projects, so these estimates are much more speculative than those under Fair Share agreements.

When we asked the DOE planners why ‘Aiea and Pearl City were included in the same district as the high-growth Campbell and Kapolei complexes, the School Land and Facilities Specialist responded that TOD projects were expected to generate 4,000 to 5,000 new residential units in the Pearlridge area, which would result in student growth the ‘Aiea complex could not accommodate. When we pointed out the developmental timelines of the various areas are vastly different (‘Ewa and Kapolei are currently undergoing significant development, while TOD projects are perhaps decades away), the Public Works Manager described additional TOD-related proposals being worked on, but did not address our question.

The Land Use Planner said designation of the Leeward O‘ahu School Impact District was a “little bit after the fact,” since many of the large developers had already signed Fair Share agreements with the DOE and had received land use approvals. We note that the DOE has either secured land through Fair Share commitments or has identified and discussed school sites with developers for 15 elementary, 4 middle, and 3 high school sites. When we asked why the department thought it necessary to designate Leeward O‘ahu as a school impact district when land had been secured and much of the area’s future capacity needs had been accounted for through Fair Share agreements, the Land Use Planner remarked that there was a strong desire by the development community to pass the school impact fee law “to catch the small guys.”



Kalihi and Kaka‘ako: Another comparison

The KAM district, a four-mile corridor following the eastern-most path of the Honolulu Authority for Rapid Transportation railway, is home to roughly 70,000 to 80,000 people, according to the DOE’s written analysis. Unlike the DOE’s previous districts, which were based on

proposed suburban plans for vacant, former agricultural lands, the KAM district was a departure from this suburban model as there were few residential projects already announced by area landlords. Instead, the district was proposed entirely on the basis of TOD plans being made by the City, the Hawai'i Community Development Authority, and Hawai'i Public Housing Authority. And, according to the *State Strategic Plan for Transit-Oriented Development*, Kalihi could see as many as 7,500 new housing units over the next 50-plus years, with neighboring Iwilei and Downtown Honolulu adding as many as 9,300 units, and Kaka'ako another 17,970.

The KAM district is bounded not by school complexes encompassing several schools, but by smaller elementary school "service areas" along the rail route. Therefore, by following the planned rail line, the KAM district includes only portions of the Farrington and McKinley complexes, which means builders of units in the same complex may or may not have to pay the impact fee even though they create the same high school capacity demand. For instance, builders in the Kalihi Waena Elementary School service area would be subject to the school impact fee, but those building homes in the Kalihi Elementary School service area less than two miles away would not, although both elementary schools feed into Farrington High School. Therefore, a portion of the impact fee used to add capacity for additional Farrington High School students may go to serve new developments outside the school impact district, for example the Kalihi Elementary School service area.

While population growth over the next 25 years is expected throughout the district, the types of housing units projected to be developed and the value of the land on which they will be built vary widely from Kalihi to Kaka'ako. For example, public housing projects in the urban core are expected to generate far more students per unit than luxury apartments in the district. And, DOE appraisals of properties in the district found that parcels in the Ala Moana area were more than twice the value of comparably sized properties in Kalihi. Instead of designating separate impact fee districts for these widely disparate areas, department planners lumped them together and created separate metrics for luxury residential units and public housing projects. They also "blended," or averaged, property valuations from Ala Moana and Kalihi to determine district-wide property values. The end result is a fee that is less likely to reflect or address the projected impact.

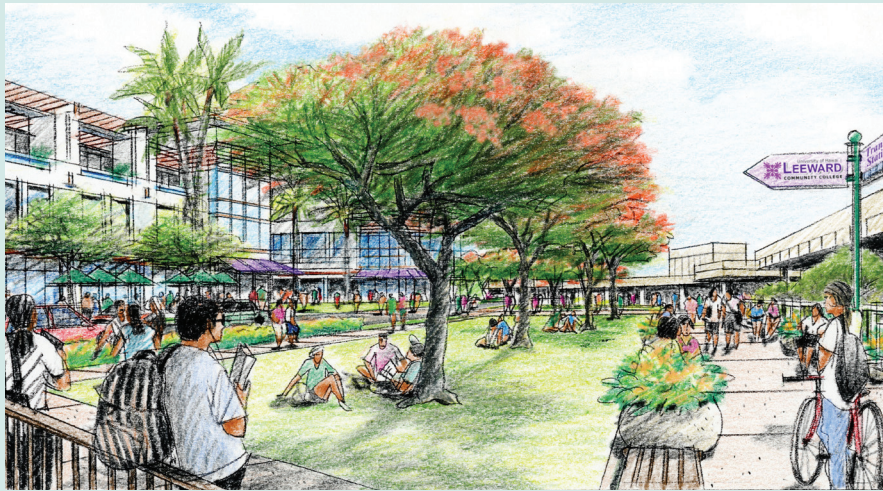


PHOTO: 'AIEA-PEARL CITY NEIGHBORHOOD TOD PLAN

Tomorrowland: Transit-Oriented Development

TRANSIT-ORIENTED DEVELOPMENT typically refers to development or redevelopment that is within easy walking distance (between ¼ to ½ miles) of a major transit stop that both capitalizes on and supports transit ridership. Transit stops may be rail stations, major bus stops, or other well-used transit hubs. For Honolulu, these hubs of activity are the rail stations along the Honolulu Authority for Rapid Transportation's (HART) 20-mile railway, which will eventually stretch from East Kapolei to Ala Moana Center.

For the past ten years, the City and County of Honolulu's Department of Planning and Permitting has been working with communities, landowners, and state agencies to develop TOD plans that integrate land use and transportation planning around HART's planned rail stations and their surrounding neighborhoods. For example, the Kalihi Neighborhood Transit-Oriented Development Plan includes everything from assessments of existing properties and zoning regulations to community vision statements and detailed projections and descriptions of potential new developments, which "reflect the level of development that can be absorbed from TOD, based on the assessment of market data and real estate conditions." To date, the City has completed plans for 8 of the 19 station areas under its jurisdiction: 'Aiea – Pearl City, Airport, Ala Moana, Downtown, East Kapolei, Hālawa, Kalihi, and Waipahu.¹ Four of the plans ('Aiea –

Pearl City, Downtown, Kalihi, and Waipahu) have been adopted by the City Council.

Some of the neighborhood plans contain specific unit estimates of potential residential development. For instance, the Kalihi Neighborhood TOD Plan projects development around three of the area's planned rail stations could include as many as 6,000 new housing units; however, the plan does not reference specific developments or developers to support these estimates. Meanwhile, the 'Aiea – Pearl City TOD Neighborhood Plan envisions a development of 820 townhouses and apartments located on a 27.3-acre overflow parking lot on the Leeward Community College campus. Again, no mention of a possible developer, actual development plans, or potential start or completion dates, but the plan states: "Tremendous potential exists for new transit-oriented development due to the large surface parking lot that currently serves all students and faculty."

We realize that TOD planning is a long-term exercise that entails beyond-the-horizon visioning, however, when we reviewed the school impact district analysis for the Leeward O'ahu School Impact District, we found that the DOE had integrated these speculative and unsupported residential growth estimates into its impact fee calculations. While the City's TOD plan may be the appropriate vehicle to showcase the potential of visionary projects developed around the railway, we believe it is inappropriate to use projected numbers associated with these virtual developments to calculate real school impact fees.

¹ Two station areas – Kaka'ako and the Civic Center – are under the jurisdiction of the Hawai'i Community Development Authority.

The DOE uses numerous assumptions and variable data to project district growth and does not update factors as required by law.

Core Principle: The DOE must apply and update the formulas for calculating land and construction components in compliance with the school impact fee law.

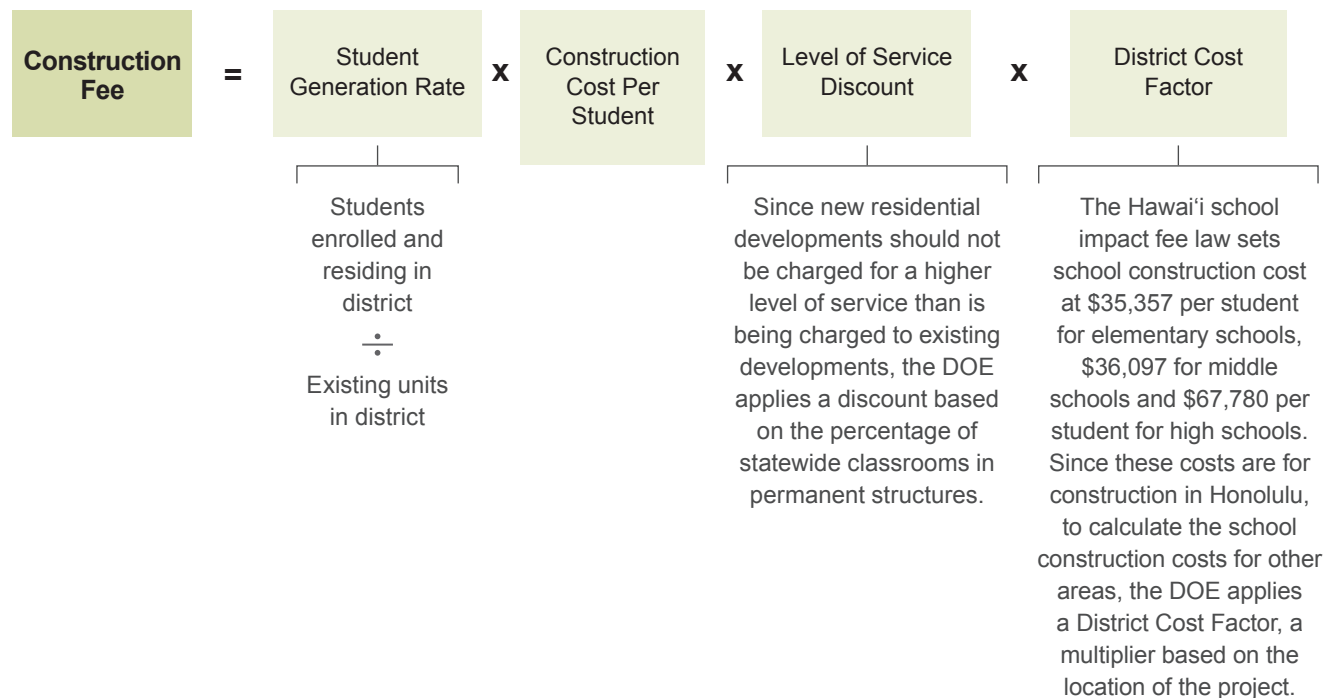
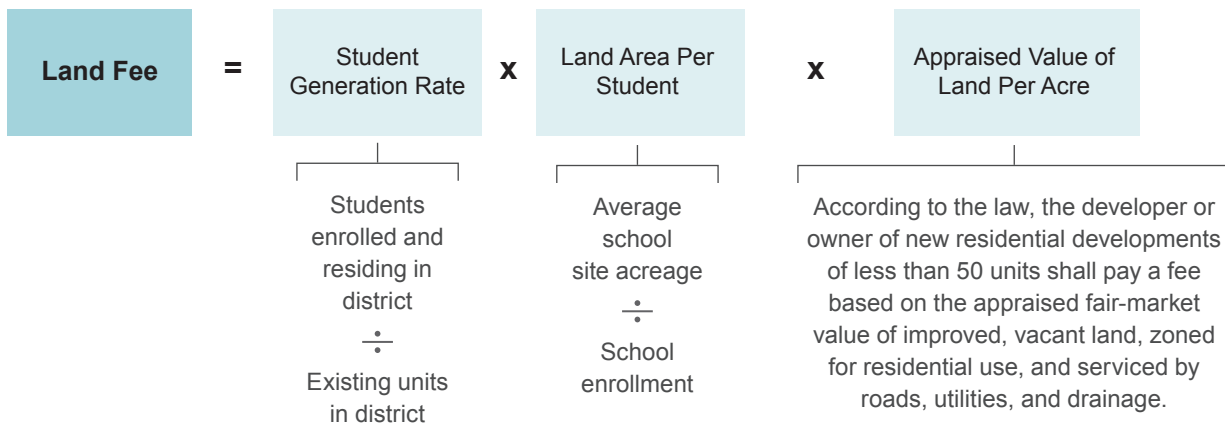
What we found: The DOE has not complied with many of the requirements contained in the school impact fee law, and the formulas are not as straightforward as they seem.

When the BOE designates a school impact district, new residential developments in the district are obligated to satisfy two contribution requirements: the *land requirement*, which is either a proportionate share of the actual acreage needed for new schools (unless land is not required in the school impact district) or a fee in lieu of land; and the *construction requirement*, which is either the actual construction of new schools or an in-lieu fee.

Much of the school impact fee formula and its component factors have been carried over from the department's land-focused and individually negotiated Fair Share agreements. We reviewed the DOE's application of the statutory impact fee formulas and found, when broken down, some of the individual factors that make up these seemingly straightforward math-based formulas have been adjusted to yield certain results. Nowhere is this more evident than in the urban core – the KAM district. The initially proposed impact fee was over \$9,000; after several meetings and changes in policies and factors, the fee finally imposed was about \$3,800. The fees imposed to date, and some of the key factors that make up the fee formulas, are summarized on the next page.

EXHIBIT 4
How the Impact Fee Works

$$\begin{array}{r}
 \text{Land Fee} \\
 + \text{Construction Fee} \\
 \hline
 \text{Impact Fee}
 \end{array}$$



SOURCE: HAWAII REVISED STATUTES

Land Factors

Student Generation Rate

The student generation rate (SGR) is the number of public school students, on average, per residential unit within a district and is the only factor used in both the land fee and the construction fee. The initial step in calculating an SGR is determining the composition of the housing units within a district. To do this, the department uses data from the U.S. Census for the total number and types of housing units within the district and determines the “residential unit mix,” or a breakdown of single-family and multi-family residences.

Next, the DOE uses its own data on the number of students who both resided and attended public schools in the district and applies the residential unit percentages to get a breakdown of the number of students coming from single-family and multi-family housing. DOE then divides the number of public school students living in single-family and multi-family units by the respective number of units to determine the SGR or the number of students a district can expect for every 100 new single-family or multi-family units built. For example, a 0.5 SGR for a place or project would mean, on average, there would be 50 students per 100 units. According to the DOE, these estimates try to capture the student rate when a project or area has reached a maturation point where the population stabilizes.

Land Area Per Student

Land area per student is the area of land required per student for a school site based on new elementary, middle, and high schools constructed between 1997 and 2007. Basically, $\text{Average School Site Acreage} \div \text{School Enrollment} = \text{Land Area Per Student}$.

Appraised Value of Land Per Acre

According to the law, the developer or owner of new residential developments of less than 50 units shall pay a fee based on the appraised fair-market value of improved, vacant land, zoned for residential use, and serviced by roads, utilities, and drainage. In addition, the developer must retain a licensed appraiser to determine the value (per acre) of the land identified for a new school facility in the district. Developers of 50 or more units can either pay the fee in lieu or convey the appropriate acreage of land.

Construction Factors

Construction Cost Per Student

The Hawai'i school impact fee law sets school construction costs per student at \$35,357 per student for elementary schools, \$36,097 per student for middle schools, and \$64,780 per student for high schools. Since these costs are for construction in Honolulu, to calculate the school construction costs for other areas, the DOE applies a district cost factor, a multiplier based on the location of the project. The impact fee law identifies 26 different district cost factors throughout the state.

Level of Service Discount

A school's level of service is the percentage of classrooms located in permanent structures, not including classrooms located in portable buildings. Since new residential developments should not be charged for a higher level of service than is being charged to existing developments, the DOE applies a discount based on the percentage of statewide classrooms in permanent structures.

New Math: The calculation of the KAM district's SGR deviates from previous practices

THE STUDENT GENERATION RATE (SGR) is arguably the most important metric in the school impact fee formula, used to calculate the number of prospective students as well as a district's land fee and construction fee. It is also one of the most transparent and easily understandable of the formulas' metrics, hard data calculated with simple math, except in the KAM district.

Before the KAM district, the department used recent demographic data to calculate the district's SGR, which was relatively straightforward: the number of students in the district enrolled in public schools and living in single- and multi-family units divided by the respective single-family and multi-family units currently in the district. The data was sourced from the DOE's own databases and the U.S. Census – actual people and actual places.

In its "Analysis of the Kalihi to Ala Moana School Impact District," the DOE explains that the KAM district was a departure from the department's previous designation efforts. The first four districts were based largely on developer-proposed projects but, according to the DOE, area landowners had announced very few residential projects in the KAM district.

As a result, the department based its SGR on the possible number of units to be built, unlike previous districts' SGRs that reflected the current demographics of their respective areas. But how DOE planners calculated this rate is unclear, since the KAM analysis provides no data or calculations to support its proposed SGR. Instead, the DOE simply states: "For the purpose of calculating school impact fee amounts, the DOE proposes an initial total (kindergarten to 12th grade) SGR of 0.12 for the units to be built in the Kalihi to Ala Moana school impact fee district."

The DOE does explain it proposed just a single, multi-family SGR for the KAM district because it anticipates new housing in the urban district will be located almost exclusively in high-density, high-rise buildings. It also acknowledges that the public housing projects proposed by the Hawai'i Public Housing Authority (HPHA) will

produce more students than the TOD-projected units, so the department proposed a separate and significantly higher SGR of 1.5 (150 students for every 100 units) for public housing. Again, the analysis did not provide any support of this proposed rate.

We reviewed subsequent calculations in the KAM analysis and found the multi-family SGR and the public housing SGR were unevenly applied. For instance, the DOE used both SGRs to estimate the number of students generated by the respective project types: 34,870 TOD units x 0.12 SGR = 4,184 students and 4,063 public housing units x 1.5 SGR = 6,094 students. However, in

its calculations of both land and construction cost components, the DOE used only the SGR for TOD-proposed units (0.12), which significantly lowered the resulting numbers for each.

According to the Land Use Planner, the DOE decided not to apply the "very generous" SGR after learning at a public meeting that much of HPHA's proposed residential units would be affordable housing, not public housing as earlier projected. We note that this explanation is not included in the "Analysis of the Kalihi to Ala Moana School Impact District."

Without a clear understanding of how DOE planners calculated the KAM district's SGR and why they applied the rate in the manner that they did, it is difficult to conclude that the resultant school impact fee is reflective of the KAM district's potential growth.

Without a clear understanding of how DOE planners calculated the KAM district's SGR and why they applied the rate in the manner that they did, it is difficult to conclude that the resultant school impact fee is reflective of the KAM district's potential growth.

DOE's land valuation process: Statutory procedures have not been followed

Section 302A-1606(d), HRS, states, "In determining the value per acre for any new residential development, the fee simple value of **the land identified for the new or expanded school facility** shall be based on the appraised fair market value of improved, vacant land, zoned for residential use, and serviced by roads, utilities, and drainage." However, we found the department "blends," or applies, a weighted average of the appraised values of multiple properties in the area to calculate per acre land values in the Leeward O'ahu and KAM school impact school districts. Also, according to the law, the appraiser must be selected and paid for by the developer. We found the DOE selected and paid for the appraisals.

We understand that these statutory requirements may be remnants of the Fair Share program, in which agreements were negotiated for greenfield developments on a case-by-case basis. At the same time, the DOE's school impact fees are calculated for and applied to an entire district rather than a

EXHIBIT 5 Fee Formula by District

SINGLE-FAMILY UNIT	WEST HAWAII*	WEST MAUI	CENTRAL MAUI**: WAILUKU, MAKAWAO	LEEWARD O'AHU
Student Generation Rate	0.35	0.50	0.49	0.46
Acres per Student	0.006592	0.009648	0.009388	0.00907
Construction Fee	\$1,609	\$2,508	Wailuku \$2,153 Makawao \$2,340	\$2,141
Fee in lieu of acreage		\$3,270	\$3,220	\$3,363
Total School Impact Fee		\$5,778	Wailuku \$5,373 Makawao \$5,560	\$5,504

The factors used to calculate school impact fees vary by district. The KAM district's drastically different results are discussed in "New Math" on the opposite page.

MULTI-FAMILY UNIT	WEST HAWAII*	WEST MAUI	CENTRAL MAUI**: WAILUKU, MAKAWAO	LEEWARD O'AHU	KALIHI TO ALA MOANA***
Student Generation Rate	0.22	0.18	0.22	0.37	0.12
Acres per Student	0.003952	0.003374	0.003998	0.00709	0.00050
Construction Fee	\$971	\$877	Wailuku \$913 Makawao \$993	\$1,683	\$584
Fee in lieu of acreage		\$1,178	\$1,458	\$2,651	\$3,280
Total School Impact Fee		\$2,055	Wailuku \$2,371 Makawao \$2,451	\$4,334	\$3,864

* West Hawaii fees were never collected, following the suspension of implementation of the district.

** Central Maui calculated separate construction fees for Wailuku and Makawao.

*** The KAM district made no distinction between amounts paid for Single-Family or Multi-Family Homes.

SOURCE: DEPARTMENT OF EDUCATION

Lessening the Impact: The Evolution of the KAM District School Impact Fee

APRIL 19, 2016

The Office of School Facilities and Support Services (OSFSS) Assistant Superintendent explains to the BOE's Finance and Infrastructure Committee that as many as 31,000 additional residential units could be built in the KAM district in the coming years, which would possibly require the DOE to build 6 new elementary schools, 1.5 middle schools, and 1.5 high schools. The department has calculated a fee of \$9,374 per residential unit for the KAM district. The impact fee for the Leeward district is \$4,334, Central Maui is \$5,373, and West Maui is \$5,378.

FEBRUARY 21, 2017

The DOE proposes a preliminary plan to the committee that would lower the fee from **\$9,374** to **\$5,858** per residential unit by building new facilities on existing school campuses instead of newly acquired land and reducing urban campus sizes. The new strategy could reduce the KAM impact fee by as much as 40 percent.

MAY 23, 2017

The BOE votes to designate the KAM district but agrees to take up the issue of impact fee rates at a later date. Two months earlier, the board had met with its Deputy Attorneys General in executive session to clarify its authority over the department's fee calculations.¹

¹ According to a board member we interviewed, when he and two other board members questioned their Deputy Attorneys General about this authority in executive session, they were met with blank stares. "And they went back [and read the law] and said, 'Oh, you guys are right, we're not supposed to do that,'" he said.

specific residential development and a school site, which complicates program implementation. However, at minimum, the DOE should take steps to clarify its role in this regard so it can calculate and administer a relevant and equitable fee and, if needed, pursue any amendments of the statute that may be needed.

Other issues of note:

- The Leeward O'ahu and KAM school impact districts' blended valuations were calculated by DOE staff, not a licensed real estate appraiser as required in the school impact fee law.
- For the KAM district, the estimated values for hypothetical elementary school sites were determined by a real estate salesperson retained by the DOE, not a real estate appraiser. In addition, the hypothetical school sites were valued as though zoned for mixed-use, which permits residential uses. Section 302A-1616(d), HRS says the appraisal instead should be based on "improved, vacant land, **zoned for residential use**, and serviced by roads, utilities, and drainage."
- For Central Maui, the appraisals of the two elementary school sites selected by the DOE – one in Kihei and the other in Kahului – were concluded to have the same values. In fact, these values were identical to those of the Lahaina elementary school site that was assessed (by the same appraiser) for the West Maui impact fee analysis.

KAM district fee deliberations raise concerns

In the introduction to "Fee Analysis for the Kalihi to Ala Moana School Impact Fee District," the DOE explained that its current method of building schools is based on a suburban (or greenfield) model: large residential developers providing vacant land for schools for their planned communities. But in the KAM district, located squarely in Honolulu's urban core, there are no such greenfields; parcels of land large enough to build conventional-size school campuses just do not exist. If they did, their price would far exceed the price of any other land the DOE has ever considered purchasing.

To help account for the differences between the KAM district's urban realities and the impact fee law's suburban roots, the department applied several "urban exceptions" to their fee factors and formulas. The following are some notable allowances the DOE made for the KAM district during its school impact fee deliberations:

Urban Exception No. 1: Suburban vs. Urban

According to the DOE Public Works Manager, department planners anticipated difficulties in adapting the school impact fee’s suburban model to the KAM district’s urban setting: “The impact fee law is the derivative of Fair Share. Principally, it was always [about] getting a site for a school...,” the manager said. “When we first did the numbers between Kalihi to Ala Moana, [we found that] developers would have had to give us 214 [283] acres, I believe. So instantly you go, ‘Well, that’s not going to work [because] it’s a greenfield type of thing....’”

Initially, the Public Works Manager recommended the department go back to the Legislature or task force to provide more guidance on what to do in an urban setting; however, at the urging of DOE leadership to establish a fee, planners used a provision in the school impact fee law that allows for an “urban exception,” allowances and adjustment to the fee factors and formulas that take into account the KAM district’s urban environment. (See Appendix C “Creating Communities of Learners” on page 49.) For example, to determine the amount of land necessary to build new schools in the district, the law requires the department to apply “school site area averages” to the fee formula based on the acreages of the department’s newest schools built statewide. Instead, planners used the acreages of the KAM district’s 13 existing schools and a “conservative” SGR to calculate an adjusted land area requirement for new schools in urban Honolulu.

The differences in the required acreages were significant. The KAM district school land requirements totaled 63.5 acres instead of the 283 acres that suburban schools would require; compared to suburban schools, the average acreage per student at urban schools is 39 percent less at the elementary level, 15 percent less for middle schools, and 38 percent less for high schools. Department planners also decided to eliminate a single-family unit SGR from its calculations. (See Exhibit 4 “How the Impact Fee Works” on page 22.) Despite these adjustments, the resulting school impact fee for the KAM district was \$9,374 per unit, more than twice the Leeward district’s multi-family unit fee of \$4,334, and significantly higher than the multi-family unit fees imposed in West Maui and both of Central Maui’s cost districts: \$2,055 (West Maui), \$2,371 (Wailuku Cost District) and \$2,451 (Makawao Cost District).

Urban Exception No. 2: Build on Existing Campuses

Responding to requests from both inside and outside the department to reduce the required school site size and the resultant school impact fee, the Public Works Manager assigned a department engineer to

Previously, according to one board member, the board had approved fees for the respective districts, but the board would later acknowledge that school impact fee rates are solely the responsibility of the department, and it had no authority to approve them.

OCTOBER 17, 2017

The OSFSS Assistant Superintendent presents two additional KAM impact fee options to the Finance and Infrastructure Committee. One option is to amend a BOE policy to allow smaller school campus sizes in the urban area and allow higher student enrollment in those schools. Another option is to pursue legislative changes that remove the “land-specific contribution” for urban development. The Assistant Superintendent points out that school land requirements for new residential developments in the current law are based on recent school site averages. This is problematic because the department does not have any current urban models. However, the Assistant Superintendent says the department is currently working on plans for a vertical school, which could serve as a model.

JANUARY 18, 2018

The Assistant Superintendent informs the Finance and Infrastructure Committee the department is working on a new draft fee analysis for the KAM district, which is dependent on proposed amendments to Board Policy 301-2, “Creating Communities of Learners.” The Assistant Superintendent states the department reviewed different methods to understand campus sizes for urban areas and referenced a research study driving the department’s decision-making, emphasizing the department is not making decisions in a vacuum.

The committee votes unanimously to recommend amending Board Policy 301-2.

FEBRUARY 15, 2018

The BOE approves the committee's recommendation to amend Board Policy 301-2. The amendment establishes new enrollment guidelines for new schools built in existing urban areas, where the availability of land is limited. Acreages for schools are reduced dramatically; however, enrollment numbers for these new urban schools remain the same.

MARCH 13, 2018

The DOE provides the revised "Fee Analysis for the Kalihi to Ala Moana District" to the committee. The DOE Public Works Manager provides an overview of the analysis, explaining the department used the "urban exception" from Board Policy 301-2 to recalculate a new fee in lieu of land for the KAM district. The result: the impact fee for the KAM district is reduced from **\$9,374** to **\$3,864** per residential unit. The Assistant Superintendent informs the committee that the department intends to initiate the impact fee for the KAM district on July 1, 2018.

OCTOBER 18, 2018

The Assistant Superintendent reports to the committee that the department began implementing school impact fees of **\$3,864** per unit for the KAM district on October 1, 2018.

determine if there is available space on the KAM district's current school campuses to construct new school facilities. On February 21, 2017, the Public Works Manager presented the study to the BOE Finance and Infrastructure Committee. The study concluded that roughly 30 to 40 percent of new facilities could be built on existing school campuses – reducing the estimated impact fee from \$9,374 per unit to **\$5,858 per unit**. The board deferred taking action on this fee proposal.

Urban Exception No. 3: Build Vertically

One year later, at a February 2018 board meeting, the department proposed that BOE Policy 301-2, "Creating Communities of Learners," be amended to adjust for the urban environment. (See Appendix C "Creating Communities of Learners" on page 49.) The policy, which was first approved by the BOE in 1997 and had not been revised since 2008, establishes design and enrollment guidelines for new elementary, middle, and high schools statewide; however, it contained acreages that are not available in urban Honolulu, such as 45 to 55 usable acres for a high school. At a previous meeting, the department had explained that it is currently planning a vertical school in the KAM district, which will sit on a much smaller footprint than other DOE campuses.

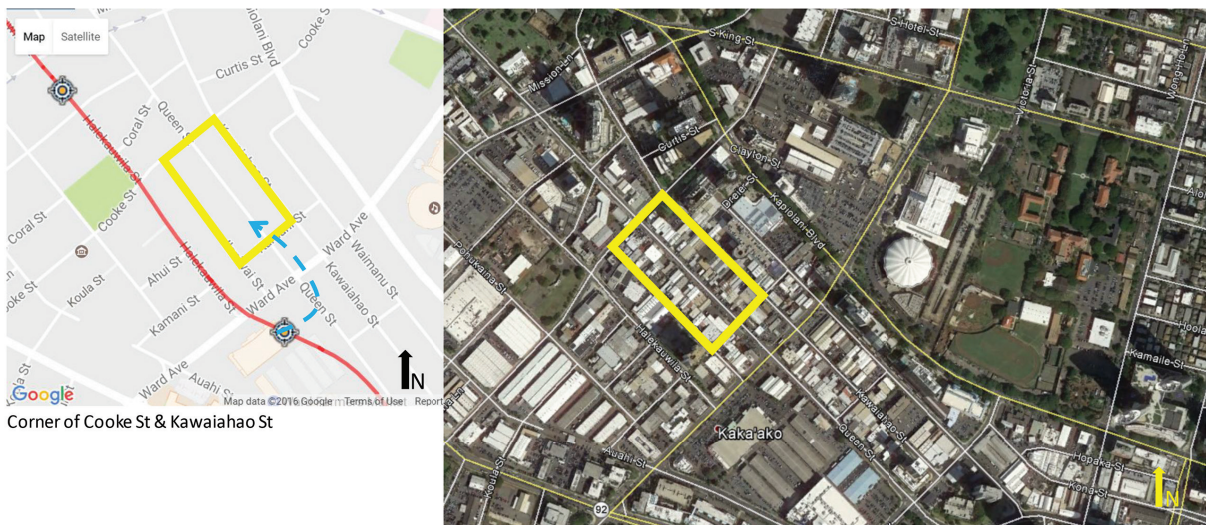
According to the Public Works Manager, the Policy 301-2 changes were based on three different studies. For high school acreages, the department had a school design consultant review the viability of building a high school in an urban setting on parcels of ten acres and less. The consultant was also asked to identify other schools around the country built on small parcels of land. The resulting study, "Defining Appropriate Site Area for a Vertical High School," published on January 12, 2017, contained three vertical prototype schools with an enrollment of 1,600 students in approximately 300,000 square feet of building space, located on a theoretical urban block(s) near a planned rail stop: Approach A sat on 9.92 acres on two city blocks, Approach B on 2.64 acres, and Approach C on 1.32 acres. The study found only Approach A met the DOE's athletics and parking requirements. However, since the typical urban city block is not wide enough to accommodate a competition track and football field, the department would have to secure a city street and acquire the properties on either side of the street.

EXHIBIT 6

Theoretical Urban Site Location

Downtown Honolulu with Easy Rail Stop Access

There are no viable site options that are wide enough to host the minimum track width. The DOE would instead need to absorb a city street and acquire properties on either side of the street.



SOURCE: "Defining Appropriate Site Area for a Vertical High School," by Fielding Nair for DOE

To determine size requirements for urban middle schools, the department used size requirements for school spaces from the Association for Learning Environments' Guide for Educational Facility Planning. For elementary schools, the Public Works Manager said studies conducted by the DOE School Design personnel for Pohukaina Elementary School in Kaka'ako were used. The school is planned to be the DOE's first vertical school and will use 100,000 square feet of space in a four-story structure located on a half-acre parcel of land.

The Public Works Manager said the studies were used to calculate the minimum amount of land needed to build an elementary school. However, the manager recalled complying with a department leadership request for even lower minimums. On February 15, 2018, the BOE approved the amendments to Board Policy 301-2, which included new acreage requirements for urban schools with the lower minimums.

The amended policy provided drastically reduced acreage requirements for urban schools, which in turn yielded a corresponding reduction in the school impact fee amount.

In contrast, the previous policy, and the acreages, are still applicable to non-urban schools:

School Type	Non-urban Schools	Urban Schools
Elementary (preK-5)	8 to 15 useable acres	2.5 to 3 useable acres
Middle (6-8)	15 to 20 useable acres	5 to 6 useable acres
High (9-12)	45 to 55 useable acres	8 to 10 useable acres

The Public Works Manager believed department planners put in their best efforts, but he was not convinced the policy could stand without further study. The Manager suggested the formation of a task force, which would give the department the opportunity to go back and “nail every one of these doors shut until we figure out what makes sense of the entire thing.”

EXHIBIT 7

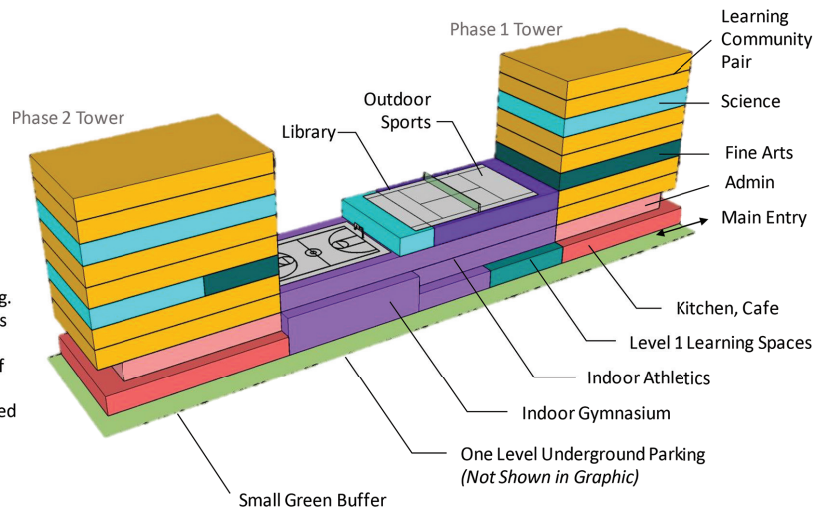
Approach (C): 1600 Student School without outdoor athletics or surface parking

Spaces for Level 1

- Learning Spaces
- Heart of the School
- Active Learning

Spaces for Level 2

- Central Support/Admin
- Central Library
- Fine Arts Wing
- Science Wing
- Learning Community



Design Features:

- Key learning spaces arranged into two towers of 800 students.
- Second tower located on the site for easy phasing.
- Connection between the towers happens indoors on levels 1-4 or outdoors on level 5.
- Building shape intentional for minimizing the # of windowless rooms
- Each tower is organized into 3 pairs of 2 connected levels of learning spaces separated by levels of science of fine arts.
- Tower 1: 10 stories total
- Tower 2: 8 stories total
- Up to 1 level of underground parking = 186 stalls

SOURCE: “Defining Appropriate Site Area for a Vertical High School,” by Fielding Nair for DOE

DOE has not updated fee factors as required by law

The school impact fee law has two update schedules for various formula factors the DOE must follow: (1) three-year updates starting in 2010 that must occur, irrespective of any district designation analysis in the interim; and (2) three-year updates to any district designation (starting from the date of designation).

The DOE Planning Section said it has only updated cost factors for purposes of determining the impact fee for new school impact districts but has not updated the cost factors for the current roster of districts already designated. The Public Works Manager stated their office intends to update the cost factors for all the districts.

According to the Public Works Manager, the updated cost factors could be used to reanalyze school impact districts to determine whether the area still merits designation and whether any of the land or construction fee rates need to be adjusted. The Land Use Planner noted updates have not been conducted in the past because the office was focused on designating new impact fee districts instead. In addition, the Land Use Planner and the Public Works Manager noted that limited resources also impacted their ability to comply with the cost factor update requirements.

However, we note that all the components the DOE must update under Section 302A-1612, HRS, are required for the calculation of either the land requirement or the construction requirement for impact fees in new districts that are designated by the board. Thus, at a minimum, the school site acreage averages, costs per student, and the statewide level of service data the DOE must update when preparing a written analysis for a potential district are also used to calculate impact fee amounts when the new impact fee district is designated. For example, while the DOE did not apply updated school site acreage averages to adjust the school impact fee in Central and West Maui, the DOE used updated data when it prepared the written analysis for the Leeward O‘ahu school impact district.

However, Section 302A-1612, HRS, suggests the update requirements are intended to ensure that data reflects “recent conditions.” The Land Use Planner acknowledges the DOE has an obligation to revisit prior district calculations but explained its work has been driven by the urgency to establish new districts rather than update existing districts. School site area averages, costs per student, district cost factors, and student generation rate data have not been updated since the West Maui, Central Maui, and Leeward school impact districts were designated. As a result, the land requirement and construction requirement calculations performed in 2010 for the West and Central Maui impact fee districts

and 2012 for the Leeward impact fee district are no longer based on “recent conditions,” as described in the law.

For instance, the Central and West Maui school impact districts were designated on November 18, 2010. Pursuant to the plain language of the school impact fee law, the DOE should have updated its data (and calculations) on November 18, 2013, for both Maui districts. According to Maui County Planning Department data, the DOE approved 685 building permit applications in the Central and West Maui school impact districts between November 18, 2013 and June 30, 2018, all of which were charged school impact fees that had not been updated since 2010.

The DOE is not updating prior impact fee calculations (by either increasing or decreasing the fee amount) to reflect current conditions. Changes in student generation rates, school site area averages, and construction costs per student directly affect the calculation of both the land and construction contribution requirements under the impact fee law formulas. According to the Land Use Planner, the reason DOE has not done the required updates is “lack of manpower, lack of time.”

We note, if the DOE was held to the time schedule stated in law, it would need to update multiple cost factors every year. Expecting the DOE to use the updated cost factors to reanalyze each affected designated district would arguably require a commitment of additional resources by the department. Based on the time schedule as currently written in state law, the DOE would need to conduct at least two new district and cost fee analyses reports nearly every year.

“Gaps” between designation and collection of impact fees, and in one case, no collection at all, resulted in potential loss of revenue.

Core Principle: The impact fee law provides that the obligation to pay impact fees occurs upon the designation of a school impact district.

What we found: The DOE has not been collecting fees upon designation. It has been collecting fees only after a collection system has been set up with cooperation from county permitting departments.

The school impact fee law requires builders of new residential units in a designated school impact district to pay school impact fees. To facilitate implementation of the school impact fee requirement, counties are required to receive written confirmation from the DOE that the school fee requirements have been met by the permit applicant before issuing building permits for new residential developments in a designated school district:

*School impact districts; new building permit requirements.
No new residential development in a designated school impact district under chapter 302A shall be issued a residential building permit or condominium property regime building permit until the department of education provides written confirmation that the permit applicant has fulfilled its school impact fee requirements. This section shall only apply to new dwelling units.*

Notwithstanding the plain language of the school impact fee law, in practice, the DOE has not required payment until it has established a system with the county permitting departments to identify the projects subject to the school impact fee and to collect the fee from developers. In addition, the DOE has not promulgated administrative rules to proscribe the process it intends the counties to follow before issuing building permits for new residential construction in an impact fee district. There was no Memoranda of Understanding between DOE and the Honolulu planning department for the KAM district. The Deputy Director of the DPP for the City and County of Honolulu said it has simply been “accommodating” DOE’s request to help implement the school impact fee law without any formal agreement. Moreover, it appears the DOE has sought, but failed to receive, any legal options from the Department of the Attorney General about Hawai‘i county’s statutory obligation to issue building permits for new residential construction in impact fee districts

Honolulu DPP Reporting Issues

IN JANUARY 2019, roughly three months after fee collections for the KAM district began, the DOE wrote to Honolulu's Department of Planning and Permitting (DPP) about a problem with the notification system. The letter stated that DPP's system had not notified the DOE about a building permit application for a mixed-use commercial property in the KAM district even though the project included hundreds of residential units that may have been subject to the school impact fees. The department sent a second letter to DPP about the matter in February 2019, reporting that hundreds of thousands of dollars could be lost if the DOE is not informed about residential units within planned mixed-use commercial projects in the Leeward O'ahu and KAM districts.

In April 2019, we brought the letters to the attention of the DPP Deputy Director who said he was unaware of the problem. After exploring the issue, the DPP Deputy Director found that building permit applications for commercial mixed-use projects were being reviewed by commercial reviewers who were not required to input the number of planned residential units for each project, which is why the system did not forward these applications to the department. In April 2019, DPP said it had changed its procedures to remedy that.

In addition, the DPP Deputy Director informed our office that he reviewed all building permits issued for mixed-use commercial projects in the KAM district after fee collections began in October 2018 and did not find any other permit applications that should have been forwarded to the DOE. However, he added that his review did not cover the period from when the KAM district was designated in May 2017 to when collections began in October 2018.

only after the DOE has confirmed payment by the person seeking the building permit.

In April 2010, the BOE designated the State's first school impact district in West Hawai'i. The then-Mayor of Hawai'i opposed the imposition of school impact fees, citing negative impacts on affordable housing and an ailing construction industry. Roughly two months after the board's decision, he informed the then-OSFSS Assistant Superintendent that Hawai'i County would not help the department with fee collection. The then-OSFSS Assistant Superintendent said a Deputy Attorney General provided no response and took no action after being informed that building permits were being issued in West Hawai'i and no school impact fees were being paid. The DOE reported in July 2010 it had suspended implementation of the West Hawai'i district. As of June 30, 2019, the area remained a designated school impact district but no fees had been collected. The former OSFSS Assistant Superintendent said the DOE has asked a Deputy Attorney General for guidance but did not seem to have "a good plan of attack on the situation" and was not certain what legal options were available for the department. As a result, no school impact fees have been collected from new residential construction in the West Hawai'i impact fee district notwithstanding the BOE's designation of the district in 2010.

Collection in the West Maui and Central Maui impact areas began roughly six weeks after the districts were designated, but it took well over a year for the DOE to begin collecting fees in its two O'ahu school impact districts (Leeward and Kalihi-Ala Moana). Both the former OSFSS Assistant Superintendent and the Public Works Manager acknowledged the DOE does not collect fees in designated districts until a collection process is in place, which we found has resulted in millions of dollars in potential fee revenue left uncollected. The lack of statutory timetables, compounded by the DOE's lack of administrative rules, policies, and procedures to guide the post-designation process, raises questions about whether the department is administering the program efficiently, maximizing the fee revenue by ensuring all legally owed school impact fees are being paid, and meeting the intent of the law.

The resultant "gap" between designation and collection is not merely theoretical; the delay in collection has resulted in foregone revenue from developments that fell within the gap. For example, in the Kalihi to Ala Moana district, a number of large multi-family projects were not subjected to impact fees prior to October 1, 2018, when the implementation became effective. To determine the duration of these non-collection periods, we calculated the time that elapsed between the district designation and when fee collections officially started for

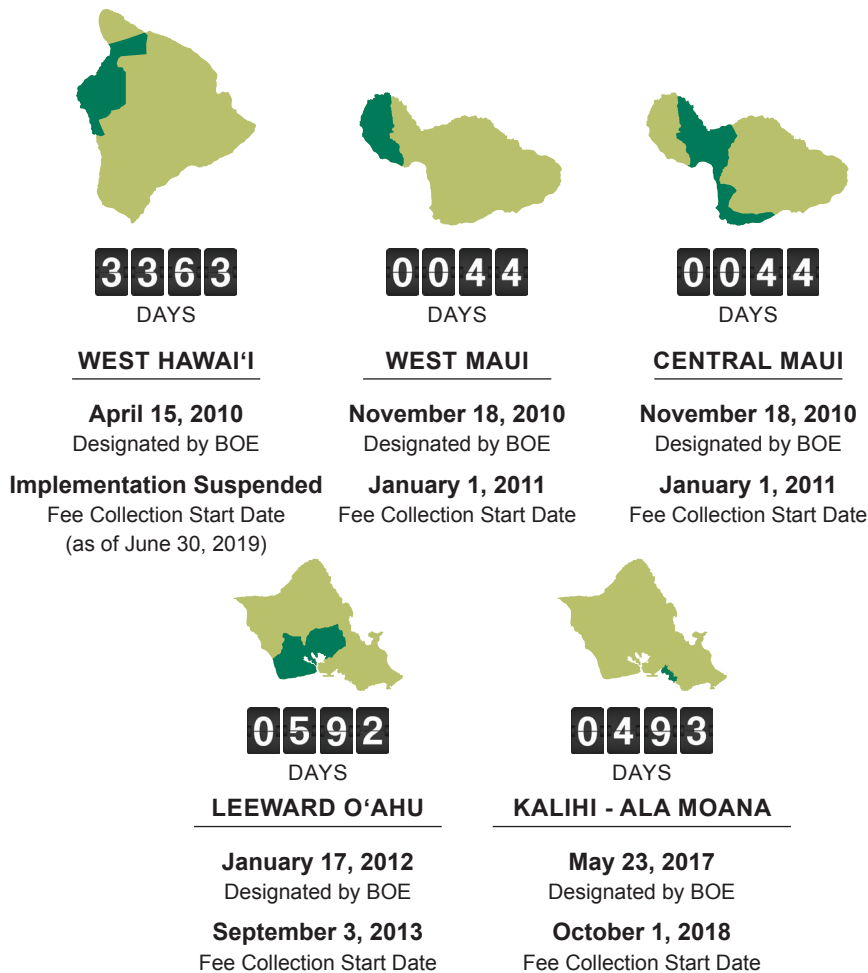
each area. We estimate the potential lost revenue to be approximately \$10.7 million (see “Mind the Gap” on page 36). The fee revenue estimate is based on the assumption that these building permits will all be approved by DPP and there are no project cancellations.

No timelines or deadlines for fees

The law also requires the department to prepare an impact fee analysis once the board designates a school impact district, but it does not establish when the fee analysis must be completed or when fee collections must subsequently begin. The former Assistant Superintendent for OSFSS said internal written procedures would help ensure compliance with the law and provide guidance for future administrators of the program. We agree.

**EXHIBIT 8
Elapsed Time Between Designation and Collection Start Dates**

With no set timeframes or deadlines, "gaps" between designation and collection have varied.



SOURCE: OFFICE OF THE AUDITOR

County Cooperation

THE PURPOSES of administrative rulemaking are to implement legislation and to establish operating procedures for state agencies. Generally, a legislative act will provide the superstructure for a program and agencies are required to “fill in the details” and implement the program on a day-to-day basis. Without administrative rules, the DOE is highly dependent on the cooperation and willingness of the county planning divisions to provide information to the department about building permit applications. Every day, the Maui County Planning Department sends the DOE’s Planning Unit II a list of all permit applications, while the City and County of Honolulu’s Department of Planning and Permitting (DPP) sends a list of all applications filed for the previous day. Either the School Land and Facilities Specialist or Land Use Planner must sort through DPP’s list to identify the permits that are for new residential construction in an impact fee district.

Once the list is sorted and the applications subject to a fee are determined, either the School Land and Facilities Specialist or the Land Use Planner logs into the counties’ respective systems and enters information into the system if a fee is required. A letter is then generated to inform the applicant that a fee is required before a building permit is issued. When the fees are received, DOE employees note the impact fee has been paid in the respective county’s database. In accordance with state law, the county may issue a residential building permit for projects in designated school impact districts once it receives written confirmation from the DOE that the applicant has fulfilled its school fee impact requirements.

“During the period we reviewed, we found 32 building permit applications were submitted to DPP, representing a total of 2,806 planned residential units. Based on an all-cash fee of \$3,864 per unit for the KAM district, we estimate more than \$10.7 million in potential fee revenue was not collected....”

Mind the Gap

THE DEPARTMENT OF PLANNING AND PERMITTING provided us with data on building permit applications for new residential units and mixed-use commercial units in the KAM district that were submitted between May 23, 2017 – when the KAM district was designated – and September 30, 2018 – the day before collection was implemented. Our office also judgmentally selected and reviewed development projects in the KAM district that applied for building permits during the same period to calculate how many residential units may have been subject to the school impact fee and how much revenue they may have generated based on the current KAM district fee rate.

During the period we reviewed, we found 32 building permit applications were submitted to DPP, representing a total of 2,806 planned residential units. Based on an all-cash fee of \$3,864 per unit for the KAM district, we estimate more than \$10.7 million in potential fee revenue was not collected, assuming the building permits were approved and no projects were canceled.

According to the Public Works Manager, the DOE's standard practice is to notify the public 30 to 60 days before school impact fee collection begins. We found six of the nine building permit applications for mixed-use commercial projects were submitted the month before the department began to collect the fees for the KAM district, which is arguably within the 30- to 60-day public notification window. We have no evidence to support that submission of those six commercial building permit applications was prompted by the DOE's notification in an effort to avoid paying the impact fees. However, we found the plans for the six mixed-use commercial projects include 1,590 residential units which represent an estimated \$6.1 million in lost potential fee revenue.

The DOE's ability to plan for future capacity demands is hampered by inadequate monitoring and accounting for school impact fee assets and expenditures.

Core Principle: DOE should have an accurate and complete accounting of all land and cash contributions intended to meet increased capacity needs.

What we found: DOE does not have an adequate framework to account for, monitor, make use of, and report fair share and school impact fee land and cash contributions.

Our review of the DOE's records, processes, and practices related to Fair Share agreements and the school impact fee law raised several concerns about the monitoring and accounting of builders' contributions of money and land. Collectively, these shortcomings obscure the big picture and inhibit the DOE's ability to plan for capacity demands created by future residential development. For instance, the DOE does not maintain an inventory of lands it has received or is expecting through developer contributions, nor can it easily determine how much money is available for capacity projects by school or by district.

Information is available, but not easily accessible

The School Land and Facilities Specialist, the Land Use Planner, and a Clerk/Typist receive regular emails about new building permit applications from Honolulu and Maui counties. These individuals are also able to access Honolulu's and Maui's permit application systems to notify the counties when the DOE has been paid and the county can issue the building permit. In addition, the School Land and Facilities Specialist maintains OSFSS's Tracker Excel spreadsheets that contain impact fee collection data. The spreadsheet has fields for the date the notification letter was sent, the date the payment was received, the amount paid, and the current status.

However, we found the DOE does not track impact fees for large, ongoing developments, which means, for a given project, the DOE does not have available records to show how many homes have been built and sold and how many units have impact fees still forthcoming. This is a concern, for example, when large developments have an agreement

that the impact fee can be remitted to the DOE at closing. The DOE does not account for a receivable that would be created in a case described above. Tracking ends once the check has been processed.

The DOE also does not maintain an inventory of all land contributed through Fair Share agreements. As a result, the DOE is unable to readily identify existing school sites built on such land, as well as the land that has been promised under the terms and conditions of the agreements, but not yet conveyed to the State. Without a complete inventory of both land contributions that have been used for school sites and those that have been contractually promised, there is no formal record of the land the DOE is entitled to when planning future school facilities.

In addition to the inventory, the department's documentation should include the summary of a project, its developer, the number of units, Fair Share or impact fee agreement terms and conditions, milestones, land area, or fees in lieu of land. But according to the Public Works Manager and Land Use Planner, there are no unusual terms and conditions the DOE would need to track more closely; otherwise, project files could be referenced or the Land Use Planner would reach out to the developers for updates. The Land Use Planner does not believe maintaining an inventory or tracking agreement terms and conditions is necessary.

However, certain requirements within the statute would be difficult to monitor without a listing of lands. For example, state law requires refunds or recommitment of all in-lieu and construction cost impact fees that have not been spent within 20 years of the date of collection. Separately, in Section 302A-1610, HRS, the owner of a development who dedicates more land for school facilities than required is entitled to receive credit for the excess land that can either be applied to future developments or by partial or full reimbursement from fees collected from other developers within the same school impact district. The reimbursement cannot exceed the available balance in the school impact district account.

Accounting for cash contributions treated as an afterthought

There is no separate special fund established by the school impact fee law specifically to hold Fair Share contributions or school impact fees. Section 37-62, HRS, defines a special fund as one that is "dedicated or set aside by law for a specified object or purpose, but excluding revolving funds and trust funds." According to the State's Accounting Manual, special funds are used to account for revenues earmarked for particular purposes and from which expenditures are made for those purposes. Instead, the Fair Share contributions and school impact fees

are held in a DOE account labeled “T-902: Donations & Gifts,” where they are identified by the individual fair share projects and school impact fee cash and construction balances. In addition, these accounts should be earning interest. However, we found a total of 15 Fair Share project accounts were not earning interest. The total balance as of the end of FY2018 in these accounts was \$542,294; some of these funds could have been earning interest since 2005.

We found impact fee accounts have not been distributed any interest since collection began in April 2011. After reviewing the details of these accounts, the DOE’s Accounting Section calculated \$110,649 in interest for the period from April 2011 through June 2018 should be distributed to the accounts.

Conclusion

When the school impact fee law was first passed in 2007, it was with good intentions. The law was meant to provide a means for “implementing a new method for financing, in part, new or expanding existing department of education educational facilities in partnership with developers of new residential developments.”

We found the path to implementation has not been easy. As detailed above, the DOE has struggled with the law. Since 2007, only \$5.3 million in school impact fees, for both in lieu of land and for construction costs, have been collected – a fraction of the \$80 million to \$100 million the DOE estimates it needs to build a single school. We raised serious questions regarding DOE’s process for selecting location and boundaries for impact districts; application of fee formulas and statutory procedures; collection of fees and securing county assistance in collection efforts; and the monitoring of fees and lands given to DOE for school impact purposes.

It is difficult to pinpoint whether these problems are the result of a lack of resources, lack of planning, or inherent flaws in the law that need to be identified and addressed. Most likely, it is a combination of these. The lack of written policies and procedures and the low priority status of school impact fees within the broad duties of the DOE made it more challenging for us to assess implementation. However, we make several recommendations that will hopefully bring some focus and clarity to DOE’s efforts to meet its obligations under the law.

Finally, as well-intentioned as it may have been, we question whether the school impact fee law can be effective enough to make the “impact” we believe lawmakers were hoping to make. We are not alone in raising this question. According to one Board member:

The department...simply does not have the expertise at all. And in fairness to them, it’s not their job. Their job – with tremendous issues and problems with school facilities – their job is to process contracts, deal with efficiency... And this statute should never have been passed without the Legislature creating a position – allocating money – to properly administer it. It is unfair to the department to expect them – with all they have to do with limited resources – to correctly implement a statute that, even for a lawyer, is very confusing.

The Board member continued:

Do you really want to do this properly? And if you do, it's going to require substantial amount of time and resources and do that knowing the ultimate amount of revenue achieved – in relative terms – is not that much.

Whether the law needs to be revisited is a matter beyond the scope of this report. Until that happens, however, the DOE is still tasked with implementing the law correctly and effectively.

Recommendations

The Department of Education should:

1. Undertake a comprehensive evaluation of its implementation and administration of the school impact fee law, including an assessment of the appropriate staffing and other resources necessary to implement and administer the law.
2. Create written policies and procedures to guide and direct staff's and management's implementation and administration of the school impact fee law. Documented policies and procedures are some of the controls necessary for the DOE to ensure effective and efficient implementation and administration of the law in accordance with the statute, legislative intent, and constitutional requirements. At minimum, policies and procedures should address:
 - a. The stage in the development process at which a proposed new residential project should be included in the DOE's consideration of classroom capacity requirements. We found the decision to recommend designation of a school impact district (and its boundaries) was left to the discretion of a land use planner who relied heavily on the City and County of Honolulu's vision of transit-oriented residential development projects that were purely conceptual, without specific developers, development plans, or even land commitments for those projects. The policies and procedures should include criteria and other objective factors to be considered in evaluating when designation of a school impact district is appropriate.
 - b. The factors that determine the size and composition of a proposed impact fee district. Without a consistent process or documented framework, some of the department's district designations appear questionable or even arbitrary: For instance, the expansive and diverse Leeward O'ahu district encompasses five school complexes (41 schools) with varying rates of past and projected student enrollment growth. Meanwhile, the KAM district boundaries are based on smaller elementary school service areas; as a result, the impact fee district includes only 10 of the 15 elementary schools in the Farrington and McKinley complexes.
 - c. The collection, tracking, and accounting of lands dedicated to or that will be dedicated to the DOE under the school impact fee law, fees in lieu of land dedication, and construction component fees.

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- d. The tracking and accounting of transfers and expenditures of lands and moneys paid under Fair Share agreements and the school impact fee law.
 - e. The use of moneys received by the DOE under Fair Share agreements and the school impact fee law. Under the school impact fee law, fees collected within an impact fee district can be spent only within the same district. We found that, with only one exception, the impact fee districts designated by the Board of Education encompass multiple school complexes. We raised concerns about whether the DOE can use school impact fees from a specific development in a school complex within the same impact fee district that is unaffected by the additional public school students created by the development.
 - f. The use and updating of cost factors (including “recent conditions”) in school impact fee calculations.
 - g. Management’s responsibilities in overseeing and approving staff’s implementation and administration of the school impact fee law.
3. Obtain written legal guidance from the Department of the Attorney General as to the constitutional restrictions associated with impact fees, including nexus and rough proportionality requirements. The legal guidance should specifically consider whether impact fee districts encompassing multiple school complexes satisfy constitutional requirements, considering Section 302A-1608(a), HRS, allows the department to use school impact fees anywhere within the impact fee district and does not restrict the department’s use of school impact fees collected from a residential developer to the school complex in which the development is situated.
 4. Work with the Department of the Attorney General to establish the legal basis and the resultant policies for the collection of school impact fees from builders of new residential construction effective upon designation of the impact fee district.
 5. Assess whether certain provisions in the school impact fee law, for example the land valuation procedures, are applicable to the constraints and requirements of district designation and district-wide fee setting, particularly in the urban setting. If needed, pursue amendment of the statute.

6. Assess whether the “urban exceptions” made for the KAM district ensure fees collected for urban schools are relevant to that district and equitable to those collected for suburban schools. If needed, pursue amendment of the statute.
7. Develop an expenditure plan for existing funds, including documented policies and procedures for ensuring that expenditures are made in accordance with existing Fair Share Agreements and the school impact fee law.
8. Ensure proper maintenance of records of land contributions for Fair Share and the school impact fee program. Records should be regularly updated and accessible to both management and the public. Promulgate administrative rules necessary to provide direction to developers, county permitting agencies, and the public as to how the DOE interprets and intends to implement the school impact fee law. At minimum, the administrative rules should address:
 - a. The specific information the DOE expects the county permitting offices to provide to the department regarding the applicants for county subdivision approvals and county building permits, including the form of the information, the timing of delivery of the information, and the method by which the counties should transmit the information.
 - b. When and how applicants must pay the school impact fees, including the process and procedure by which the department or the county building departments intend to collect the fees.
 - c. If the department intends to allow developers to pay all or portions of the school impact fee subsequent to the issuance of county subdivision approval or county building permits, and the process by which payment shall be made, including the timing of the payment.
 - d. The process and procedures by which a developer can contest or appeal the imposition of school impact fees on the developer’s project.
 - e. The process and procedures by which the DOE will inform the county building departments that a developer has satisfied the school impact fee requirement.

The Board of Education should:

1. Require the department to submit a written report that provides a comprehensive evaluation of its implementation and administration of the school impact fee law. This report should include the department's findings and conclusions, specific actions that the department intends to implement to address our recommendations, other changes the department intends to make, and copies of policies and procedures. The report should also include a timeframe for implementation and note any additional resources the department feels may be necessary for successful implementation.
2. Direct the DOE to implement the recommendations necessary to address and correct the audit findings.
3. Direct the DOE to report at least quarterly on the status of its implementation of the recommendations necessary to address and correct the audit findings.
4. For each school impact district considered by the board, obtain the Department of the Attorney General's opinion, in writing, that the school impact district satisfies constitutional requirements, including nexus and proportionality requirements, prior to designation of the district.

Appendix A

Impetus, Scope, and Methodology

We conducted this audit pursuant to Article VII, Section 10 of the Hawai‘i State Constitution and Section 23-4, HRS, which authorizes the Auditor to conduct post-audits of the transactions, accounts, programs, and performance of all departments, offices, and agencies of the State and its political subdivisions.

We focused on the Department of Education’s (DOE) designation of school impact fee districts and the related processes. We reviewed information since the school impact fee law was passed in 2007 through fiscal year 2018, and any relevant prior or subsequent events. We interviewed personnel within DOE’s Office of School Facilities and Support Services, previous employees, legislators, DOE administration, board members, and personnel from the City & County of Honolulu’s Department of Planning and Permitting. We have made recommendations as appropriate. We also assessed the sufficiency of DOE’s applicable internal controls relating to implementation of school impact fees.

We reference the *Hawai‘i School Impact Fee Study* which served as basis for legislation creating the school impact fee law. That working group was administratively attached to our office. We determined that there are no independence issues with respect to our work with the school impact fee audit.

Our audit was performed from February 2019 to June 2019 and conducted according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for the findings and conclusions based on our objectives.

This is our first audit of the DOE’s administration of school impact fees. However, we have conducted numerous audits of specific DOE programs in the past, most recently, the *Management Audit of the Department of Education’s School Bus Transportation Services*, Report No. 12-07.

Appendix B

Organization

Board of Education

The Board of Education (BOE) oversees Hawai'i's public school system and the Hawai'i State Public Library System. The BOE formulates policy and is responsible for, among other things, conducting short- and long-term strategic planning and reviewing budgets for the BOE, the DOE, and the public library system.

With regard to school impact fees, the BOE is responsible for *“designat(ing) a school impact district for school impact fees only after holding at least one public hearing in the area proposed for the school impact district.”* The BOE does not approve the fees but reviews the components and calculations and members have stated that these components should be brought to them for review.

Organizational Structure of DOE Office of School Facilities and Support Services

The Office of School Facilities and Support Services (OSFSS) oversees the business, construction, repair, and maintenance of school facilities. OSFSS is also responsible for food services, heat abatement, and transportation support. The unit within OSFSS given primary responsibility for implementation of school impact fees is Planning Unit II.

The Facilities Development Branch, headed by a Public Works Administrator, oversees a variety of engineering and architectural services, including land acquisition, planning, designing, project management, construction inspection, design and construction quality control, contracting, construction management, and equipping facilities and improvements for the DOE among several other duties.

The Planning Section, headed by a Public Works Manager, is responsible for the administration and direction of planning activities for schools and other facilities. Its major responsibilities include providing land acquisition coordination and planning services, formulating and implementing capital improvement project and repair and maintenance requests, and conducting other requested studies.

Planning Unit I consists of one engineer and two planners who each handle a key performance indicator (capacity, instructional space, and program support) and a related allotment for their project area. They are responsible for coordinating funding for projects based on available funding and departmental priorities. The unit has used Fair Share contributions to cover budget shortfalls for capacity-building projects.

DOE Accounting Section: This section handles two major activities related to Fair Share and school impact fees: the processing of cash receipts and creation of journal vouchers for investment pool distribution. For both, accounting provides administrative support via the receipt and recording of transactions.

Appendix C

POLICY 301-2

CREATING COMMUNITIES OF LEARNERS

The Department of Education shall design school facilities that create smaller communities of learners. For existing schools with high enrollments, the state office and school staff shall analyze their school performance indicators to determine if the school size is negatively affecting student achievement. If student achievement is found to be negatively affected, school staff and community members shall identify and implement educational programs that create smaller communities of learners.

To foster greater personalization established through educational programming and smaller communities of learners while providing flexibility when planning schools for new communities, design enrollment guidelines for new schools shall be:

Elementary (preK-5)	400 to 750 students	8 to 15 usable acres
Middle (6-8)	500 to 1,000 students	15 to 20 usable acres
High (9-12)	800 to 1,600 students	45 to 55 usable acres

In existing urban areas where the availability of land is limited to infill sites and where new housing developments require the construction of new school facilities, design enrollment guidelines for new schools shall be:

Elementary (preK-5)	400 to 750 students	2.5 to 3 usable acres
Middle (6-8)	500 to 1,000 students	5 to 6 usable acres
High (9-12)	800 to 1,600 students	8 to 10 usable acres

The Department shall make every effort to ensure that all educational needs are met when designing and siting new urban-based school facilities. Where possible, the Department should seek design solutions that create environments conducive to creating communities of learners in urban areas.

The Department shall make the final determination as to whether land is usable based on an evaluation of the specific property taken in the context of the development as a whole. Usable is generally defined as land free of encumbrances determined to be unnecessary by the Department, slope of five percent or less, and with no ravines or streambeds. Usable land for the construction of new school facilities with usable acres or enrollment other than established in these design enrollment guidelines shall be subject to the approval of the Board of Education.

Rationale: Research studies show that a larger student enrollment may depersonalize the school environment, thereby negatively affecting student attitude, behavior, and academic achievement.

[Approved: 02/17/2015 (as Board Policy 301.2); amended: 06/21/2016 (renumbered as Board Policy 301-2), 02/15/2018]

Former policy 6701 history: approved: 03/20/1997; revised: 04/18/2002, 12/2007, 06/2008

SOURCE: DEPARTMENT OF EDUCATION

Office of the Auditor's Comments on the Department of Education's Response to the Audit Findings

WE PROVIDED A DRAFT OF THIS REPORT to the Department of Education (DOE) on August 23, 2019, and met with the Interim Assistant Superintendent, Office of Facilities and Operations; Public Works Administrator; Public Works Manager; Director, Internal Audit; and an Internal Audit Specialist on September 9, 2019, to discuss our findings. The DOE offered its written response to the draft report on September 13, 2019, which is included in its entirety as Attachment 1.

The DOE did not materially disagree with or dispute any of the audit findings, stating that the audit was “helpful in determining the strength and weaknesses of our administrative process, such that improvement may be made.” We did make one correction to our report, adding Barbers Point Elementary School to the graphic of the elementary and middle schools in the Kapolei High School complex on page 3 of the report.

The DOE took issue with our overall assessment that the school impact fee law has had a questionable impact. In its response, the department paraphrased language from the school impact fee law regarding its basic components and intended impact. But, the bottom line is that after 12-plus years, the DOE has collected a total of \$5.3 million in school impact fees. Meanwhile, the department estimates that it would cost approximately \$80 million to build a single new elementary school today.

Regarding our review of the DOE district designation efforts, we continue to disagree with the department regarding certain fundamental responsibilities and practices. For instance, the department asserts that it is dependent on the counties to initiate and implement the fee collection process. This has resulted in failure to collect upon district designation, and, in the case of West Hawai‘i, not collecting any impact fees at all. Instead of relying on the cooperation and accommodation of the counties, the DOE needs to promulgate administrative rules to proscribe the process it intends the counties to follow before issuing building permits for new residential construction in an impact fee district.

The department also took issue with our critique of its use of the City's transit-oriented development (TOD) plan as a basis for the KAM district's school impact fee. In its response, DOE pointed out that it uses the same data that the City uses, which reinforces rather than contradicts our point. As we stated in our report, while TOD plans may be a suitable vehicle to showcase the potential development around the railway stations, it is not appropriate to use the projected numbers associated with these virtual developments to calculate real school impact fees. Importantly, the DOE's broad application of these speculative development estimates does not consider the need for additional infrastructure that the City has deemed necessary to support future development. For instance, for just the Iwilei-Kapalama area alone, the City estimates total infrastructure investment needs of \$760 to \$910 million, roughly a third of which is funded or programmed by the City. Until the City has a clear, defined plan to fund and construct the needed infrastructure, we are concerned that the projected TOD projects are too speculative to support the need for new schools and additional classroom capacity.

Regarding identified gaps between the designation and collection of impact fees and our estimate that nearly \$11 million in potential fee revenues was not collected during these gaps, the department claims that our calculations do not take into account the process of "fee analysis," which occurs after the designation of an impact fee district. While this may be the DOE's position today, this is a mischaracterization of the department's practice at the time of our audit. For the KAM district and every school impact fee district before it, the department's proposed district designation and fee analysis were submitted to the Board of Education in a singular report for approval. In fact, it was not until the lengthy deliberations over the KAM district's designation and fee that the board and department realized that previous fee setting had been improperly handled. According to the statute, the authority to approve the district impact fee lies with the department and not the Board.

The school impact fee law is clear that, with certain limited exceptions, anyone obtaining a building permit for new residential construction in a designated impact fee district owes an impact fee. If the Board determines there is a need for an impact fee district, it is the department's responsibility to ensure that an appropriate fee is collected upon designation to help offset the costs of meeting school capacity demands caused by the new developments. That means having a formal, documented process for fee collection and building permit approval in place at the time of district designation. The process' policies and procedures should clearly define and designate the roles of the respective stakeholders.

The DOE also objected to our general assessment that tracking and accounting of its Fair Share and impact fee lands and fees has been minimal, and in some cases non-existent. In its response, the department pointed out that it provided us with “financial materials” that show a full accounting of funds received. However, these financial materials largely consist of a series of Excel spreadsheets that planning staff use to log fee payments as they are received. While it is true that financial information exists in various locations in department-wide logs and rosters, it is difficult to access and compile this data for basic tracking and planning purposes. For instance, when asked for a listing of Fair Share agreements the DOE had on file, planning staff admitted that they did not have one and that to create such a list required a manual review of physical project files.

As we stated in the report, the department also does not maintain an inventory of all the land contributed through Fair Share agreements. In addition, since the department does not have the ability to consolidate its data, it cannot track the progress of large, ongoing residential developments: how many homes have been built and sold and how many units have impact fees still forthcoming. Instead, according to the DOE, its “tracking” ends when the fee for the last unit in a development is collected. Without adequate recordkeeping, it is unclear how the DOE makes this determination. In our view, failure to have the relevant information compiled and readily available to those who need it to implement school impact fees is a shortcoming that needs to be addressed.

Finally, we also found that a total of 15 Fair Share project accounts were not earning interest. The DOE responded that its cash status report now shows that all Fair Share accounts are earning interest as part of the DOE investment pool. The DOE neglects to mention necessary corrections were made only after the issue was brought to their attention.

In sum, the department’s comments do not substantively change our report or our audit findings. We believe the points raised by the department do not address the crux of the issues we identified. While we appreciate the department’s feedback and expressed intent to address the issues raised in our report, we remain convinced that there are areas that the DOE must address, many of which are more substantive and significant than those raised in the department’s response, to properly implement the school impact fee law.

DAVID Y. IGE
GOVERNOR




DR. CHRISTINA M. KISHIMOTO
SUPERINTENDENT

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OFFICE OF THE SUPERINTENDENT

September 13, 2019

To: The Honorable Leslie H. Kondo
State Auditor, Office of the Auditor

FROM: Dr. Christina M. Kishimoto 
Superintendent

SUBJECT: **Response to the Audit of the Department of Education's School Impact Fees and Fair Share Contributions**

The Department of Education (DOE) appreciates the opportunity to respond to the draft copy of *A Low-Impact Exercise: Audit of the Department of Education's Administration of School Impact Fees*, Report No. 19-13/August 2019.

We would like to thank the State Auditor's Office for their time and effort in conducting this audit. We would also like to thank the State Legislature for their continued support and leadership. The DOE values the service of the impact fee law, in providing new school sites and revenue to build new school capacity. Since the year 2000 the DOE has garnered more than \$14 million in funds and 90 acres of land through the school fair-share program and the school impact fee law, (Act 245 SLH 2007). The continued application of the impact fee law is an important aspect of school facilities funding.

The questions raised by the audit provide valuable insight into the impact fee law and the DOE's efforts to administer this program. This exercise was helpful in determining the strengths and weaknesses of our administrative process, such that improvements may be made. To that end, the DOE would like to offer its comments in the hopes of providing greater clarity, and to ensure the veracity of information presented.

1. Page 1 – the audit states: **“We found the school impact fee law has questionable impact.”**

Response: The DOE disagrees that the school impact fee law has questionable impact. Impact fee law plays a vital role in the development of new schools by providing 100 percent of school land and ten (10) percent of the construction cost for new school facilities, required to accommodate new residential development. New, and projected, development in West Oahu and urban Honolulu will significantly impact school capacity in the near future. It is this significant impact that drives the need for accessibility to schools and free, quality, education for the state.

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2. Page 2 – the audit states: **“Tracking and accounting for school impact fees have been minimal, and in some cases non-existent....”**

Response: The auditors were provided tracking information and accounting data, which we believe is counter to this assessment. It would be helpful to know what criteria was used to make this judgement.

3. Page 3 – audit graphic: **“What is a Complex?”** does not show Barber’s Point Elementary School as part of the Kapolei Complex.

4. Page 7 – the audit states: **“The DOE cannot adequately account for Fair Share and school impact fee cash and land contributions.”**

Response: The auditors were provided with financial materials showing a full accounting of funds received.

5. Page 9 – the audit states: **“the department has been inconsistent in its application of the school impact fee law, has been forced to rely on the cooperation of county building department to enforce the school impact fee law, and has allowed school impact fees to go uncollected.”**

Response:

- We are unaware of any inconsistencies in our application of the law;
- The counties hold sole authority to issue building permits. We are dependent on the counties’ permitting process; and
- Once the impact fee district is engaged with the county’s permitting system, the county will not issue a building permit until the impact fee has been collected.

As identified by the audit, in areas where impact fee districts were not supported by the local Building Permit Office, fees could not be collected.

6. Page 19 – the audit questions: why the KAM District boundary was set by elementary school service areas, rather than whole complex areas, **“by following the planned rail line, the KAM district includes only portions of the Farrington and McKinley complexes, which mean builders of units in the same complex may or may not have to pay the impact fee even though they create same high school capacity demand.”**

Response: The law defines school impact district areas as ranging “from one school, to one or more high school complexes”. The DOE’s responsibility is to identify only high growth areas where additional enrollment will require new or enlarged schools. The analysis of the KAM district determined that the elementary school service areas best encapsulated the high growth areas. In the KAM district, future growth will be highly condensed. The fee amounts are based on the impact of each unit on all levels of schools.

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7. Page 20 – the audit found: **“While the City’s TOD plan may be the appropriate vehicle to showcase the potential of visionary projects developed around the railway, we believe it is inappropriate to use projected numbers associated with these virtual developments to calculate real school impact fees.”**

Response: The DOE uses the same available data that the City & County of Honolulu’s Department of Planning and Permitting, and the State of Hawaii’s Office of Planning, use to address projected future growth for planning purposes.

8. Page 36 – the audit states: **“we estimate more than \$10.7 million in potential fee revenue was not collected....”**

Response: These calculations do not take into account the process of “fee analysis,” which occurs after the “designation” of an impact fee district. As stated in the audit sidebar, page 26, May 23, 2017 – “The BOE votes to designate the KAM District but agrees to take up the issue of impacted fee rates at a later date.” Once an impact fee district is established the law directs the administrator to do a fee analysis. The fee must be established before collection can occur. In the case of the KAM District, the district was designated by the BOE on May 23, 2017, while the fee was not fully established until March 13, 2018.

9. Page 37 – the audit states: **“The DOE’s ability to plan for future capacity demands is hampered by inadequate monitoring and accounting for school impact fee assets and expenditures.”**

Response: The DOE reports on impact fee assets on a quarterly basis. Planning for capacity demands is not hampered by the monitoring or accounting of these funds.

10. Page 37 – the audit states: DOE can’t easily determine **“how much money is available for capacity projects by school or by district.”**

Response: The DOE’s accounting system can provide cash balances for any trust account, for any district, at any time.

11. Page 37 – the audit states: **“we found the DOE does not track impact fees for large, ongoing developments, which means, for a given project, the DOE does not have available records to show how many homes have been built and sold and how many units have impact fees still forthcoming.”**

Response: The Fair Share Tracker accounts for monies received from projects. There is a separate page for each project. Information per page includes the total number of developed units, number of units for which payments have been received, dates when payments were deposited into accounts, and whether all fees have been collected. An Impact Fee Tracker has also been established with the same information.

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Per our discussions with the State Auditor’s Office, the audit team has acknowledged that adequate tracking information and records are being kept by the DOE. Their concern is about access to, and organization of, the information.

12. Page 38 – the audit states: the DOE **“does not maintain an inventory of all land contributed”**

Response: The DOE maintains a land inventory on a data base. The data base was made available to the Audit staff.

13. Page 38 – the audit states: the DOE should be documenting **“the summary of a project, its developer, the number of units, Fair Share or impact fee agreement terms and conditions, milestones, land area, or fees in lieu of land.”**

Response: This information is contained in the written Education Contribution Agreements, executed between the DOE and the developer for any project of more than 50 units. The Audit staff reviewed all Educational Contribution Agreements.

Per our discussions with the Auditor’s Office, the audit team has acknowledged that the DOE does maintain all the information listed, (i.e. developer, number of units, conditions, milestones, land area, and fees in lieu of land). Their concern is about access to, and organization of, the information.

14. Page 38 – the audit states: a lack of an inventory would keep the DOE from complying with a requirement that land or fees be returned if not **“spent within 20 years of the date of collection.”**

Response: The DOE maintains an impact fee log that will permit us to return unspent fees to the person who paid the fees. The DOE does not receive the transfer of land until it’s ready to build on these site. Once we have built a facility on the property, there is no provision for return.

15. Page 39 – the audit states: **“we found a total of 15 Fair Share project accounts were not earning interest.”**

Response: The cash status report, generated from the DOE’s Financial Reporting System, shows that all Fair Share accounts are earning interest as part of the DOE investment pool.

In closing, should you or your audit team have additional questions or need additional information, please feel to contact our subject matter expert, Heidi Meeker, Planner with the Facilities Development Branch, Planning Section, at 784-5080 or by email at heidi.meeker@k12.hi.us.

CMK:hm

c: The Honorable Kenneth Uemura, Chairperson, Finance and Infrastructure Committee
Denise Yoshida, Internal Audit Office