NEBRASKA SANITARY AND IMPROVEMENT DISTRICT LEGISLATION

I. INTRODUCTION

Since its humble birth in 1949 the sanitary and improvement district (SID) has steadily evolved into a highly flexible and functional vehicle for community development. While basically a governmental subdivision (a “public corporation”) formed pursuant to statute for the purpose of allowing property owners within the district means for financing and implementing improvements, amendments of recent vintage have provided nearby cities with adequate power to control and demand the orderly development of the SID pursuant to their own master plans.

From the standpoint of a real estate developer the primary function of an SID is to provide a means of financing. As a public corporation the SID is vested with the power not only to contract for improvements, but also to issue bonds, tax, and levy assessments.


In as much as the current SIDs are predominantly formed under the Act of 1949, this article is restricted thereto.


2. An SID may be formed for the “purpose of installing electric service lines and conduits, a sewer system, a water system, a system of sidewalks, public roads, streets, and highways, to contract for water for fire protection and for resale to residents of the district, and to contract for gas and for electricity for street lighting to the public streets and highways within said proposed district, and to acquire, improve and operate public parks, playgrounds and recreational facilities.” Nebr. Rev. Stat. § 31-727 (Cum. Supp. 1969).

3. Nebr. Rev. Stat. § 31-739 (Cum. Supp. 1969): “The district may borrow money for corporate purposes and issue its general obligation bonds therefor, and shall annually levy a tax on the assessed value of all the taxable property in the district . . . .” Nebr. Rev. Stat. § 31-755 (Supp. 1971) provides in part: “For the purpose of paying the cost of the improvements herein provided for, the board of trustees, after such improvements have been completed and accepted, shall have the power to issue negotiable bonds . . . .”

4. See, e.g., Nebr. Rev. Stat. § 31-755 (Supp. 1971), which provides in part: “The board of trustees shall levy special assessments on all lots, parcels or pieces of real estate benefited by the improvement to the extent of the benefits to such property, which when collected, shall be set aside and constitute a sinking fund for the payment of interest and principal of said bonds. In addition to special assessments provided for in this section, there shall be levied annually a tax upon the assessed value of all the taxable property in said district except intangible property which, together with such sinking fund derived from special assessments, shall be sufficient to meet payments of interest and principal as the same become due.”

5. Id.
to pay therefor. Where the SID is within the zoning jurisdiction of a municipality (and thus assumedly will be subject to eventual annexation), the primary function of the SID from the standpoint of said municipality is to provide for orderly and complete expansion. This may be seen clearly when one focuses upon the nature of SID improvements: Streets, sewer lines and utilities are planned and installed; land may be set aside or developed for playgrounds, parks and recreational facilities. Absent the SID the city would often be faced with a costly state of affairs at the time of annexation: Dirt or gravel roads might have to be replaced, septic tanks converted to sewer systems, and utility lines installed. If the city decided to have recreational facilities, at a minimum the prices of land would have increased, and at a maximum the city would have to engage in costly condemnation proceedings to obtain land for public purposes. Under the 1971 amendments to the SID Act of 1949 the city has a “veto” power over all improvements made by a district when the SID is within the municipality’s zoning jurisdiction. As will be explored in detail below, this enables the city to ensure that the construction of roads, streets, sewers, and recreational facilities is in a manner consistent with its master plan and in conformity with its structural standards. More importantly, all this is accomplished without immediate cost to the city.

While laudatory in its concept, it should be immediately noticed that the SID has not escaped criticism — most recently a series of articles in the Omaha World-Herald pointed to abuses under the law. There have been allegations of irregularities in financing.


8. Dorr, Who pays in SIDs?, Omaha World-Herald, September 17-21, 1970. In this series of articles, Robert Dorr examined several of the SIDs within Douglas County, Nebraska. Some of the abuses pointed to may be summarized as follows:

No. 1. September 17, 1970: Focused upon the mill levy within SID No. 47 of Douglas County, Nebraska, which from 1963 to 1966 was taxed at one mill levy, in 1967 four mills, 15 mills in 1968, and 20 mills in 1969. In 1970 the mill levy skyrocketed to 50 mills.

No. 2. September 18, 1970: Attributed the increase in mill levy within SID No. 47 to the maturing of the district’s bonds and the inadequate mill levy from the standpoint of funding such indebtedness. Furthermore, it was alleged that special assessments were used to pay the annual interest on such bonds. The district through mid-1970 had collected a total of $394,454 in special assessments. “During that time, the interest on the debt amounted to $287,694. All of that interest was paid with special assessments money. The money left over paid construction costs.” P. 4, col. 1.

The article also discussed excessive profits made by district trustees through self dealing.

No. 3. September 19, 1970: Focused upon the construction of a clubhouse, complete with sauna baths, exercise equipment, fire place, color television, swimming pools and tennis courts, within the Camelot Village apartment project which
excessive interest rates, and irregularities in connection with the issuance of bonds. Criticism has also focused upon the nature of improvements made in the districts, excessive expenditures, inadequate assessments and mill levies, as well as excessive assumption of SID debts upon annexation. Throughout its analysis of the contemporary workings of an SID, this article will recognize and address itself to what has been accomplished to cure some of the defects heretofore existing, and will suggest solutions to possible abuses which still remain despite the active efforts of legislators to eradicate.

II. HISTORY

The history of SID legislation, particularly in the past twelve years reflects a continuous balancing of interests. Parties interested and affected by such legislation are diverse, and it has taken a series of amendments to develop a body of law responsive to the needs of the real estate developer, the city which will prospectively annex the district, and the taxpayers of both the SID and the city. The

was financed as a general obligation of the SID No. 166 of Douglas County, Nebraska.

No. 4. September 20, 1970: Pointed to the lack of control the prospectively annexing municipality had over the construction of parks, playgrounds and recreation facilities within the districts. By way of example, two narrow strips of land, one on each side of a creek, were purchased by a district and devoted to a "park". Swimming pools had been constructed in a manner inconsistent with what Omaha would have considered to be adequate standards and specifications.

No. 5. September 21, 1970: After stating the general advantages of the districts, the author suggested four "steps" to tighten the law:
1. A requirement that the districts levy sufficient tax to pay both the district's operating expenses and the interest on debt.
2. Give the prospectively annexing municipality control over the construction of recreational facilities within the districts. (See Laws of Nebraska L.B. 188 (1971) in which such municipality was given a virtual veto power over the construction of parks, playgrounds and recreational facilities within the district.)
3. Require disclosure of information to the prospective purchasers of the SID property.
4. Modify the method of electing district trustees to give greater power to the home owners within the districts and less to the owners of undeveloped property.

9. See In re Sanitary and Improvement District No. 194 of Douglas County, Nebraska, Docket 594, No. 160, in the District Court of Douglas County, Nebraska. In a motion to vacate the district court's bond validation decree the plaintiff alleged excessive bond issue, that such bonds were issued with a double coupon for the sole purpose of compensating the district's fiscal agent, and that the bonds were issued at an excessive interest rate. The motion was denied, the court holding that the interest rates were not excessive in as much as the City of Omaha had recently issued bonds at a higher effective rate, and that there was no proof offered as to the other allegations.

For other district court litigations, see Ed Pedersen v. Westroads, Inc., a Nebraska Corporation; the City of Omaha, a Municipal Corporation; and Sanitary and Improvement District No. 130 of Douglas County, Nebraska, Docket 618, No. 145, in the District Court of Douglas County, Nebraska.
current law is in general an equitable compromise between the conflicting interests.

Initially SID legislation was quite limited in scope, providing only for the installation of sewer systems, electrical facilities, and contracting for water for fire protection. In 1961 significant expansion of SID purposes took place, with new provisions for the installation of public roads, public parks, playgrounds, and recreational facilities. Existing SIDs were empowered to amend their articles of incorporation to take advantage of the new permissible powers. Discussion of the 1961 amendments in committee hearings foreshadowed the important role the SIDs were eventually to assume.

The new powers were subjected to certain checks and balances in 1965, when it was provided that the SID gain approval for proposed sewer and electrical installations from any municipality within the same county as the SID. This presented the first step in the evolution of the control mechanism through which a city or village was to be insured that SID construction would be consistent with its standards. Significantly, the 1965 amendment changed the provisions for the maturing of SID bonds, requiring that they mature serially, with the first series due no more than three years after issue.

The 1967 amendments redefined the requirements for approval of sewer and electrical installations, providing that such approval would be from the public works department of a municipality, and would be required only where the SID was within the zoning jurisdiction thereof. The approval was to relate to conformity with the

10. See Laws of Nebraska ch. 78, p. 194 (1949), which provides in part that certain landowners "may form a sanitary and improvement district for the purpose of installing a sewer system, to contract for water for fire protection, and to contract for electricity for street lighting for the public streets and highways within said district."


12. Id. The articles of association set forth the purpose for which the SID is formed. However, where all the permissive powers are not set forth, the articles may be amended. Such amendments may be proposed by the majority of the board of trustees, and after notice by publication may be adopted, unless opposed by a petition signed by the property owners representing a majority of the front footage of real estate within the district. In the latter case the amendment must be submitted to and receive the approval of the district court. The decision is governed by focus upon whether the amendment is conducive to the public health, convenience, or welfare. See Neb. Rev. Stat. § 31-740.01 (Reissue 1968).

13. See, e.g., Hearings on L.B. 610 before the Committee on Urban Affairs (1961). Reported comments of Mr. Ben Wall, Assistant City Attorney from Omaha: "[T]he City of Omaha, operating under a time budget, has not had the funds to obtain the niceties of life. He said the City of Omaha spends its money on sewers, police and fire protection, etc., and they have not been able to go out and obtain park sites, etc." Reported comments of Mr. Richard E. Croker, representing Omaha Home Builders Association: "Cities generally do not have the money to set up these necessary parks and if this can be accomplished, we will have a facility which the people need and which could not be provided in any other manner."


15. Id. In its pre-amendment form the statute provided that such bonds were payable in terms not to exceed thirty years.
construction standards and specifications of such municipality (where no such standards existed, no approval was required). In order to limit the allocation of improvement costs to property owners throughout the district, it was provided that property within the SID be specially assessed to the extent benefited by improvements. Where the SID was within the zoning jurisdiction of a municipality, such municipality was made a party to the special assessment hearing.

The 1969 amendments included provisions that prohibited a district from owning more than ten acres of land, unless it was actually used for public purposes within three years of acquisition. Committee discussions reveal that the motive of this restriction was to prohibit the SID from being used as a vehicle for the avoidance of county property taxes. Other amendments provided for an increase

16. Laws of Nebraska chs. 188, 189, pp. 514, 517 (1967). The procedure wherein the SID is required to gain the approval of a municipality in whose zoning jurisdiction they lie is discussed in more detail below, see text at notes 43 to 47 infra. In reference to the provisions requiring the approval of the public works department, and the need therefor, it was stated:

[B]ut I realize that particularly on sanitary and improvement districts you almost have to have some control. Otherwise a bunch of people get together and try to do a job with the least possible cost perhaps, and you can't blame them for that, but we had testimony that one SID had plastic water lines. Maybe plastic is better, I don't know. But maybe it isn't. And the point is that if the city does not have some control then these people could put in anything they want. And that's alright if that's the way they want to live, but these houses were sold. Other people come in and they don't know about these underground lines and so forth. So I think there is an element here of protecting them.

17. Laws of Nebraska chs. 191, 192, pp. 526, 527 (1967). In committee hearings it was stated:

The law as it is now written had not been completely clear as to what part of the taxes should be assessed against the individual property and what goes into general obligation bonds. This becomes significant, when for example the city of Omaha annexes. If a Board of Trustees can put most of the obligation of this district under the general obligation of the district, when the City of Omaha annexes it is also the law that the city has to pay off those bonds. You can see if everything could be dumped into the general obligation bonds the home owner would get all these utilities and things put in for nothing. Now, that is not being generally done. I think — generally speaking — the districts have been quite fair about this. But you can see that the present law leaves it open. Three of these bills tie this down and say that you can assess these improvements, you have to assess them to the extent that the property is benefited thereby.

20. Hearings on L.B. 1386 before the Committee on Urban Affairs, May 7, 1969. SID land is exempt from county taxes. See NEB. CONST. art. VIII, § 2. The problem, as stated in support of the amendment, was that in some cases there were several hundred acres owned by SIDs which were being farmed. Thus, the SID was being used as a "tax shelter" for land which was appreciating rapidly. See Hearings on L.B. 1386 before the Committee on Urban Affairs, May 7, 1969 (comments of Senator Keyes and Mr. D. Trumble, who represented the Sarpy County Taxpayers Association).
in the maximum interest payable on warrants and bonds, prohibited the SID from levying special assessments after annexation, and authorized the district to contract for gas, street lighting, and the installation of sidewalks.

The 1971 amendments bring us up to date, and of significance were provisions requiring the districts to gain approval for the construction of playgrounds, parks and recreational facilities from the governing body of a municipality, again if the SID was within the zoning jurisdiction of such municipality.

After briefly noting the procedure for forming a sanitary and improvement district, this article will explore the law as it relates to three prime areas: (1) Scope and nature of SID improvements; (2) financing for SID obligations, and (3) annexation. Attention will be placed upon the procedural checks and balances, their strengths and weaknesses, from the viewpoint of the various parties affected by SID activities.

III. FORMATION

A majority of the owners having an interest in the real property of a proposed district must file articles of association and a petition praying that the district be declared a sanitary and improvement district with the district court for the county in which the SID is located. Prior to a hearing on the petition the district court must issue a summons, which is served as in civil cases, to all property owners of the proposed district who have not signed the articles of association. Such owners of real estate may object to the formation of the district by filing their written objections stating why the proposed district should not be declared an SID, and why their land would not be benefited by SID improvements. If the court deter-

24. Laws of Nebraska L.B. 188 (1971). Other amendments in 1971 included: (1) Require that elections be conducted at a place or location within the SID. (2) Prohibiting the SID from constructing clubhouses and similar facilities for the giving of private parties. (3) Provisions for mandatory levy and collection of special assessments.

There were three legislative bills passed in the 1972 session of the legislature — L.B. 1317, 1442, and 1387. L.B. 1317 and 1442, passed within four days of each other in an attempt to amend Neb. Rev. Stat. § 31-753 (Supp. 1971), by inconsistent amendments and repeal of the same section have muddied the waters even further. Assumedly, one will be repealed. L.B. 1387 amended Neb. Rev. Stat. §§ 31-715 and 31-740 (Supp. 1971) in an effort to provide consistent auditing requirements for both those SIDs formed under the Act of 1947 and those under the Act of 1949. Basically, § 31-740 now contains the reporting and auditing requirements heretofore found only in § 31-715.

mines that the formation of the district is conducive to the public health, convenience, or welfare, then the SID is declared a public corporation of the state. The court has the power to exclude the property of objecting landowners when it appears that such real estate would not be benefited by the proposed district. The SID is administered by a board of trustees who are initially appointed, subsequently elected, and who must post bond.

IV. SCOPE AND NATURE OF IMPROVEMENTS

The scope of permissible SID improvements has gradually expanded through the years. Under the Act of 1949, an SID could be formed for the purpose of installing sewer systems, to contract for water for fire protection, and to contract for electricity for street lighting. In 1961 the SIDs were authorized to acquire, improve and develop public parks, playgrounds, and recreational facilities, and to contract with public utility companies for the extension of their water mains in order to serve the areas within the districts.

The pertinent statutory provisions in their latest form are as follows:

Section 31-727: (An SID may be formed) for the purpose of installing electric service lines and conduits, a sewer system, a water system, a system of sidewalks, public roads, streets, and highways, to contract for water for fire protection and for resale to residents of the district, and to contract for gas and for electricity for street lighting for the public streets and highways within said proposed district, and to acquire, improve and operate public parks, playgrounds and recreational facilities.

Section 31-740: The board of trustees of any district organized under sections 31-727 to 31-762 shall have power to provide for establishing, maintaining, and constructing electric service

29. Id.
30. Trustees are initially appointed upon the formation of the district: "The articles shall propose the names of five or more trustees, who shall be owners of real estate located in the proposed district, to serve as a board of trustees until their successors are elected and qualified, should said district be organized." Neb. Rev. Stat § 31-727(3) (Cum. Supp. 1969).
31. After formation the SID is required to conduct elections: "At such time as the board of trustees shall designate, which time shall be not more than twelve months after the judgment of the district court creating said district, and each two years thereafter, the board of trustees shall cause an election to be held, at which election a board of trustees of five in number shall be elected. . . . Any person may cast one vote for each trustee, for each acre of unplatted land or fraction thereof and one vote for each platted lot which he may own in the district." Neb. Rev. Stat § 31-735 (Supp. 1971).
33. Laws of Nebraska ch. 78, p. 194 (1949). reprinted in part at note 10 supra.
34. Laws of Nebraska ch. 142, p. 408 (1961).
lines and conduits, water mains, sewers, and disposal plants, and dispersing of drainage, waste, and sewage of such district in a satisfactory manner; for establishing, maintaining, and constructing sidewalks, public roads, streets, and highways, including the grading, changing grade, paving, repaving, graveling, regaveling, widening or narrowing roads, resurfacing or relaying existing pavement, or otherwise improving any road, street, or highway within the district; and may contract for electricity for street lighting for the public streets and highways within the district, and shall have power to provide for acquisition, improvement, maintenance and operation of public parks, playgrounds and recreational facilities.

Utilization of the above powers enables an SID to become a virtual extension of a city or village, complete with all improvements characteristic of a developed municipality.

The procedure by which the SID approves and contracts for the construction of specific improvements is governed by detailed statutory provisions. In general, after notice of the time and place for a hearing on a proposed resolution, the trustees may pass such resolution if it is not opposed by a petition signed by the owners of a majority of the foot frontage of the land to be assessed for the proposed improvement. At the hearing, all property owners whose land could be subject to assessment may appear and object to the resolution. Upon passage of the resolution the trustees may enter into a contract for the construction of improvements, subject to a requirement of bidding where the cost thereof is in excess of $500. Upon completion, the engineer is required to file with the clerk of the district a certificate of acceptance approved by the trustee. Thereafter, the engineer prepares a complete statement of all costs of improvements, a plat of the property in the district, and a schedule of the amount proposed to be assessed against each separate piece of property, and files same with the clerk for the district. When the SID is located within the zoning jurisdiction, the procedure for the approval of proposed improvements is subject to the following statutory provisions:

Section 31-740: Prior to the installation of any of the improve-

42. Id.
ments provided for in this section, the plans for such improvements, other than for public parks, playgrounds and recreational facilities, shall be approved by the public works department of any municipality when such improvements or any part thereof are within the area of the zoning jurisdiction of such municipality, and plans and exact costs for public parks, playgrounds and recreational facilities shall be approved by resolution of the governing body of such municipality. Such approval shall relate to conformity with the master plan and the construction specifications and standards theretofore established by such municipality . . . ."

The significance of the 1971 amendment, italicized above, cannot be overemphasized, for not only does it directly focus on an area of past abuse,43 but it also resolves the problem by giving the prospectively annexing municipality virtual veto power over the construction of recreational facilities. Prior to this amendment, as noted in reference to the 1967 amendments,44 the SID was required to gain the approval of the municipality public works department before the installation of other types of improvements,45 and such approval related only to construction specifications and standards. The new provisions are not a mere extension of the above procedure to parks, playgrounds and recreational facilities — approval is required of the governing body of the municipality, not just the public works department. Furthermore, in addition to the construction standards and specifications, the district must submit the "exact costs" for approval.

The City of Omaha has taken full advantage of the 1971 amendments by initiating a detailed procedure by which proposed recreational improvements are reviewed and studied by the public works department, the parks advisory board, and the city planning board before presentment for approval to the city council. The threshold decision centers on whether the proposed recreational facility is consistent with the master plan of the city, and whether, in light of the projected residential developments within the area, the proposed facility is desirable. Once it is decided that a recreational facility of the type proposed is needed in the area, it is necessary to review the location, construction standards and specifications, as

44. The term "abuse" is used from the standpoint of a municipality which prior to the 1971 amendments was required upon annexation to assume the cost of recreational facilities that were built to plans, specifications and standards set by the board of trustees.
45. See text at notes 15 to 18 supra.
46. In general, public works department approval was required before the district could make any improvements related to streets, roads and highways, water mains, or the acquisition of electricity. For detailed itemization of the types of improvements for which the district must seek the approval of the public works department, see Neb. Rev. Stat. § 31-740 (Supp. 1971).
well as the exact cost, as all must be approved by the city council.

The very nature of the city's power, total veto, is conducive to informal discussions between the city and developers. In view of the fact that upon annexation the city will assume the obligations of the district attributed to the construction of the recreational facilities, it is understandable that the city be given control over the cost and construction of such improvements.

The 1971 amendments also contain the following prohibition: "Provided, that power to construct clubhouses and similar facilities for the giving of private parties within the zoning jurisdiction of any city or village is not included in the powers herein granted." This amendment upon release from the Committee on Urban Affairs was much broader in scope, providing that no SID "has the power to construct race tracks, club houses, golf courses, skating rinks, auditoriums, stadiums, field houses, theaters, dance halls and bowling alleys." In opposition to the broader amendment it was argued that not only would it be ineffective, as it would allow a myriad of other types of improvements, e.g., a cocktail lounge, but also that it was unnecessary, because municipality approval before any recreational facility could be built provided ample statutory protection.

In favor of denying the SIDs power to make certain types of improvements it was argued further that since upon annexation the cost thereof would burden the entire city, it was unfair to those taxpayers of the annexing city who did not have access to similar facilities in their part of town. Nevertheless, the essence of SID leg-

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47. Upon annexation the municipality assumes the general obligations of the district, NEB. REV. STAT. § 31-763 (Cum. Supp. 1969). The cost of parks, playgrounds and recreational facilities is not specially assessed against the property owners within the district.
49. Hearings on L.B. 188 before the Committee on Urban Affairs, May 4, 1971.
50. Id. See, e.g., comments of Senator Proud.
51. See, e.g., Hearings on L.B. 188 before the Committee on Urban Affairs. Senator Simpson: "The people in the older sections of the city should have the same opportunity to set up their little area districts within the city and put in everything they wanted and then ask the people of the whole city to pay for them." Senator Morgan: "All we are trying to do is stop the golf courses, club houses. I feel that this is used by a very few people. Yet all of the people are paying for it." (Hearings on May 4th, 1971). Senator Morgan: "I added that amendment to this bill to prohibit the building of golf courses, club houses, etc. And I'm the last person that wants to see development stopped in our city. I can tell you as a developer, that there have been abuses of this and one abuse might be a 2 million dollar golf course that was just built in our city and I think it's unfair that the people in east Omaha and other areas of our city are paying for golf courses and this is in west Omaha when they don't even have paved streets. The rest of his amendment is fine, but I just want to prohibit this and I also have a letter from the president of the Omaha City Council here on April 15 who advises me that there has (sic) been abuses and that the existing laws allow too much leniency. He wants to see my amendment stay on and I would hope that we would adopt his amendments except for the one section that provides for the building of golf courses and club houses, etc." (Hearings on April 30, 1971).
islation is to provide for a means of financing complete developments, and to advocate that a new development should be curtailed to anything less than optimal because of deficiencies in the developments of older parts of the city is to argue for the compounding of deficiency. To deny districts the powers in the rejected amendment would be dysfunctional: One of the primary advantages of the SID to an annexing city is that it allows for such improvements.

V. FINANCING OBLIGATION

As has been alluded to, the SID is a means of financing the cost of improvements. This is accomplished generally as follows: In payment for obligations the SID issues warrants, which upon presentation for payment draw interest. The holder thereof may retain the warrants or sell them outright, normally to the fiscal agent, who is contractually obligated to make such purchases. Eventually the SID may issue negotiable bonds which can be used to retire warrants or to pay directly for the cost of improvements.

A warrant is a non-negotiable instrument drawn by the SID authorizing the county treasurer, who acts as treasurer for all the SIDs, to make payment. Since there are generally no immediate funds available with which to make payment, the warrant is reg-

For the purpose of paying the cost of the improvements herein provided for, the board of trustees, after such improvements have been completed and accepted, shall have the power to issue negotiable bonds of any such district, to be called sanitary and improvement district bonds, payable in not to exceed thirty years and such bonds shall be payable serially with the first maturity not later than five years from date of issue and bearing interest payable semi-annually. Such bonds may either be sold by the district or delivered to the contractor in payment for the work, but in either case for not less than their par value. For the purpose of making partial payments as the work progresses, warrants may be issued by the board of trustees upon certificates of the engineer in charge showing the amount of work completed and materials necessarily purchased and delivered for the orderly and proper continuation of the project, in a sum not to exceed eighty-five per cent of the cost thereof. Such warrants shall draw interest at such rate as fixed by the board of trustees and endorsed on the warrants, from the date of presentation for payment and shall be redeemed and paid from the proceeds of special assessments or from the sale of the bonds issued and sold as aforesaid or from any other funds available for that purpose. The board of trustees shall levy special assessments on all lots, parcels or pieces of real estate benefited by the improvement to the extent of the benefits to such property, which when collected, shall be set aside and constitute a sinking fund for the payment of the interest and principal of said bonds. In addition to the special assessments provided for in this section, there shall be levied annually a tax upon the assessed value of all the taxable property in said district except intangible property which, together with such sinking fund derived from special assessments, shall be sufficient to meet payments of interest and principal as the same become due. Such tax shall be known as the sanitary and improvement district tax and shall be payable annually in money.

53. Id.

istered and thenceforth earns interest. In the past the interest rate payable on warrants was subject to a statutory maximum, initially at 6%, then in 1969 raised to 8%. Both warrants and bonds were subject to the same interest limitation until the 1969 amendments, which set the interest rate on bonds at 7%. Supportive of the 1969 amendment allowing the 1% differential was the argument that the holders of warrants were subject to a higher degree of risk than were the holders of bonds. The risk was attributable to the fact that warrants are issued at a time when the SID has no real tax base. In addition, warrants are designed as a means of interim financing, and without the increased interest rate SID financing would be seriously impaired.

In 1971 all interest rate limitations were removed and the trustees were empowered to set the interest rates on both bonds and warrants at their discretion.

Notwithstanding the fact that warrants may be designed for interim financing, such is not the law, for there is no statutory requirement that they be of definite duration. This feature, as will be shown, when combined with the mode of measuring SID mill levy, can operate to the detriment of the taxpayers of both the SID and the municipality.

SID bonds may be issued after the completion and acceptance of improvements. The trustees, or holders of such bonds, are re-

56. See Laws of Nebraska ch. 171, p. 518 (1947).
58. See Laws of Nebraska ch. 171, p. 518 (1947).
59. Hearings on L.B. 1185 before the Committee on Urban Affairs, April 9, 1969.
60. Laws of Nebraska L.B. 1 (1971). L.B. 1 was placed on the General File without a committee hearing.
61. See text at notes 83 to 91 infra.
quired to petition the district court in the county in which the SID is located, praying in effect that the court examine, approve, and confirm the legality and validity of the proceedings leading up to the issue. Notice of the pendency of the hearing is by publication, and persons interested in the issuance of the bonds or in the organization of the district have standing to answer or move for a dismissal of the petition. The scope of the district court's inquiry may be comprehensive, as it has the power and jurisdiction to examine the legality and validity of, and approve and confirm, or disapprove and disaffirm each and all of the proceedings from and including the organization of the district, and all other proceedings which may affect the legality or validity of the bonds. After the district court enters a decree finding that the proceedings of the SID were valid and legal, the trustee must present a written record of such proceedings with the decree of the district court to the Auditor of Public Accounts of the State of Nebraska. The auditor, upon satisfaction that the bonds have been issued pursuant to law, so certifies, and registers the bonds at his office. No bonds shall be issued or be valid unless certified and registered.

SID bonds must be payable in not to exceed thirty years, serially due, with first maturity not later than five years from the date of issuance. The bonds may be sold by the district or delivered to the contractors in payment for work — in either case at not less than par value.

If there exist defects running to the "validity" of SID bonds the remedies available to a taxpayer of the district, or a taxpayer of an annexing municipality, are quite limited after the bonds have been issued. A vigilant taxpayer may oppose the issuance of SID bonds at the validation proceeding by answering or moving to dismiss the petition of the district. Failure to enter as a party to the bond validation proceeding may result in the taxpayer being barred from subsequently attacking the validity of such bonds. The Supreme Court of Nebraska has not addressed the question of whether the bond validation decree is final and not subject to collateral attack. However, if the bond validation proceeding is to have any

68. Id.
69. "Defects" as used here refers to the multiplicity of situations where, but for the rules of law concerning the innocent purchaser for value, as codified in the Uniform Commercial Code Art. 8, the bonds would be unenforceable.
71. This would entail a determination of whether such bond validation proceedings are, as a matter of law, final on the question of bond validity.
meaning, it would appear that it at least stands for the proposition that there has been substantial compliance with the legal requirements governing the issue, or that the SID has the power to issue bonds for the purpose stated. In either case, U.C.C. section 8-202 may operate to validate the bonds in favor of a purchaser for value without notice, or transferee thereof. The SID and the municipality, after annexation, would be denied the benefit of such defects, with the bonds enforceable as a matter of law.72

After defective bonds have been issued the only apparent remedy available to a taxpayer of the SID would be an action against the parties responsible therefor. In this regard it should be noted that after annexation the liability of trustees is limited by the extremely short statute of limitations,73 and the bonding requirements for

72. UCC § 8-202(2) provides:
(2) (a) A security other than one issued by a government or governmental agency or unit even though issued with a defect going to its validity is valid in the hands of a purchaser for value and without notice of the particular defect unless the defect involves a violation of constitutional provisions in which case the security is valid in the hands of a subsequent purchaser for value and without notice of the defect.
(b) The rule of subparagraph (a) applies to an issuer which is a government or governmental agency or unit only if either there has been substantial compliance with the legal requirements governing the issue or the issuer has received a substantial consideration for the issue as a whole or for the particular security and a stated purpose of the issue is one for which the issuer has power to borrow money or issue the security. (Emphasis added).

This section of the Code treats separately governmental and nongovernmental securities. In the case of the latter, they are valid in the hands of a purchaser for the value without notice of the particular defect, unless the defect is constitutional, in which case the security is valid in the hands of a subsequent purchaser. The identical rule applies to governmental bodies only if either:
(1) There has been substantial compliance with the legal requirements governing the issue, or
(2) (a) the issuer has received a substantial consideration for the issue, and
(b) a stated purpose of the issue is one for which the issuer has the power to borrow money or issue the security.

It should be noted that such validity is vis-a-vis the issuer only. "Issuer", defined in UCC § 8-201, would include the municipality upon annexation (with respect to obligations on or defenses to a security "issuer includes a person who... becomes responsible for or in place of any other person"). Here "person" can be interpreted to include governmental subdivisions.

The transferee of a purchaser for value without notice is protected by the provisions of UCC § 8-202 by virtue of § 8-301 shelter provisions: "Upon delivery of a security the purchaser acquires the rights in the security which his transferee had or had actual authority to convey...."

73. NEB. REV. STAT. § 31-764 (Cum. Supp. 1969) provides in part:
The trustee shall within thirty days of the effective date of the merger submit to the city a written accounting of all assets and liabilities, contingent or fixed, of the district. Unless the city or village within thirty days thereafter brings an action against the trustees of the district for an accounting or for damages for breach of duty, the trustees shall be discharged of all further duties and liabilities and their bonds exonerated.... The city or village shall represent the district and all parties who might be interested in such an action.
trustees are minimal. Of course the ultimate weapon, non-annexation, remains a possibility as a result of defective bonds.

In light of the limited remedies available after defective SID bonds have been issued, the importance and function of the bond validation proceeding becomes apparent. It is an interim step taken before the rights of innocent purchasers are involved, designed to protect the rights of those who will become obligated to pay for the bonds. The shortcoming of the present bond validation procedure, if any, lies in the fact that it is not necessarily adversary, for unless "any person interested" moves to dismiss or answers the petition the district court must examine the SID without the benefit derived from a challenge.5

The two primary sources of district revenue are special assessments and an annual tax.7 Although perhaps this classification does not seem of significance, it in fact can operate to allocate the cost of improvements between the property owners of the district and the taxpayers of the municipality upon annexation. Regardless of whether the costs thereof have been specifically assessed, the improvements are financed through the issuance of warrants or bonds. The debt instruments of the district, when viewed from the standpoint of the parties who bear the burden thereof, represent two separate sources of funding. In general it may be stated that to the extent that the funds derived from special assessments are insufficient to pay the interest and principal on district obligations, there must be levied a tax. Special assessments survive annexation, hence to the degree that such assessments are insufficient to fund the interest and principal when due the municipality bears the burden. From the standpoint of such a municipality it is thus of critical importance that special assessments be adequate, and that the proceeds be applied to such indebtedness.

74. Nebr. Rev. Stat. § 31-734 (Reissue 1968) requires SID trustees to execute and file a bond running to the State of Nebraska in the penal sum of five hundred dollars. By contrast, Nebr. Rev. Stat. § 31-706 (Reissue 1968) requires such bonds of trustees in the penal sum of five thousand dollars. Hence under the more limited SID Act of 1947 (Nebr. Rev. Stat. §§ 31-701 to 31-726), which has no provisions for the construction of parks, playgrounds, and recreational facilities, the bonding requirement is ten times as great as that required under the Act of 1949.

75. Nebr. Rev. Stat. §§ 31-756 to 31-758 (Reissue 1968). In particular, see Nebr. Rev. Stat. § 31-758 (Reissue 1968), which provides in part:

Any person interested in the district, or in the issuance or sale of the bonds, may move to dismiss the petition, or file an answer thereto.

Prior to the 1967 amendments it was possible for the SIDs to allocate without restriction almost all improvement costs to the general obligations of the district without appropriate special assessments. Such an allocation would operate to the benefit of the district landowners, as a great proportion of the district obligations would be assumed by the annexing city or village.

The amount of special assessments today is determined by the board of trustees after a hearing in which the owners of property subject to assessment are given an opportunity to be heard. The 1967 amendments provide that special assessments of property must be to the extent of the benefit, that a municipality has standing to appear at the special assessment hearing when the SID is located within its zoning jurisdiction, and that the municipality if not satisfied with adequacy of assessments may appeal to district court, which is directed to "hear and determine such appeal in a summary manner as in a case in equity . . . and shall increase or reduce the assessments as the same may be required to provide that the assessments shall be to the full extent of special benefits . . . ." The provisions operate hand in hand with those considered earlier relating to a municipality's veto power over the construction of parks, playgrounds, and recreational facilities, to give the potentially annexing municipality a significant degree of control over the amount of obligations they will assume. Standing to contest the adequacy of special assessments militates against the SID allocating the cost of special benefits to general financing. The veto power over the construction of recreational facilities makes the municipality a party at the planning stage as to those improvements that will be allocated to general financing.

The second major source of SID revenue is provided by an annual tax, levied pursuant to section 31-755, which provides in part:

In addition to special assessments provided for in this section, there shall be levied annually a tax upon the assessed value of all the taxable property in said district . . . which, together with such sinking fund derived from special assessments, shall be

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77. See Laws of Nebraska chs. 191, 192, pp. 526, 527 (1967), and Hearings on L.B. 121, 125, 126, 127 before the Committee on Urban Affairs, January 25, 1967, as discussed in footnote 17 supra.
79. The property owners' constitutional right to be heard at the special assessment hearing was not clarified until the 1971 amendments, when it was provided that the owners of property subject to assessment were to be given notice and opportunity to be heard. See Neb. Rev. Stat. § 31-749 (Supp. 1971). However, pre-1971 law allowed such property owners to object in writing, with a right to appeal to the district court. See Laws of Nebraska ch. 250, p. 909 (1969).
81. Laws of Nebraska ch. 190, p. 524 (1967).
82. Id. at 526.
sufficient to meet payments of interest and principal as the same become due. It is also provided that the district must levy a tax for the purpose of creating a sinking fund for the maintenance and repairing of district improvements. In this regard it should be noted that warrants are of indefinite duration, by their terms interest and principal are never "due" within the meaning of the above quoted statute. The result is somewhat anomalous, for notwithstanding the fact that district obligations are in the form of both warrants and bonds, the mill levy is determined without reference to the former. Indeed under the present law warrants may remain outstanding, at a relatively high interest rate, completely at the discretion of the board of trustees. The effect of maintaining district indebtedness in the form of warrants is fourfold: (1) It allows an unrealistic current mill levy; (2) it may operate to postpone payment of district indebtedness until extinguished by annexation; (3) it tends to mislead prospective district property purchasers as to the amount of district indebtedness (since interest accrual is not reflected as to amount on county records); (4) in the long run, warrants tend to lower the net cost of financing. The following chart derived from the Douglas County Court House records serves to dramatically elucidate both the length of time that warrants can be left outstanding, and the considerable sums involved:

<table>
<thead>
<tr>
<th>S.I.D. Identification</th>
<th>Registry date of Outstanding Warrants</th>
<th>Amount of Warrants Registered</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>1-27-61 to 6-12-69</td>
<td>$228,803</td>
</tr>
<tr>
<td>B</td>
<td>11-26-63 to 4-7-65</td>
<td>13,731</td>
</tr>
<tr>
<td>C</td>
<td>10-15-63 to 9-9-69</td>
<td>544,538</td>
</tr>
<tr>
<td>D</td>
<td>1-7-63 to 7-27-66</td>
<td>323,678</td>
</tr>
<tr>
<td>E</td>
<td>8-17-64 to 9-8-69</td>
<td>528,811</td>
</tr>
<tr>
<td>F</td>
<td>10-2-63 to 8-11-65</td>
<td>161,557</td>
</tr>
<tr>
<td>G</td>
<td>11-3-64 to 12-15-67</td>
<td>289,856</td>
</tr>
<tr>
<td>H</td>
<td>1-27-65 to 9-12-67</td>
<td>98,708</td>
</tr>
<tr>
<td>I</td>
<td>4-7-65 to 7-16-71</td>
<td>253,465</td>
</tr>
<tr>
<td>J</td>
<td>6-16-65 to 6-27-69</td>
<td>1,254,862</td>
</tr>
<tr>
<td>K</td>
<td>5-25-65 to 9-15-70</td>
<td>259,773</td>
</tr>
</tbody>
</table>

   The district . . . shall annually levy a tax . . . sufficient to pay the interest and principal on the bonds and for the purpose of creating a sinking fund for the maintenance and repairing (of SID improvements).
85. There is no requirement that the district levy a tax sufficient to fund interest and principal on warrants. For all tax purposes warrants may be ignored.
86. Interest payable on warrants accrues but does not compound. Hence, depending upon the relative interest rates of warrants and bonds, and the length of time the warrants have been outstanding, it may be less costly to forego conversion to bonds.
87. The figures reported herein are the courtesy of Mr. E. J. Hewitt, Finance
In the above example, some of the older outstanding warrants would have up to 60% interest accrual applying, and many would be in the 42-48% range.

Even if the district has no outstanding bonds, the property owners within the district must still pay special assessments and a tax for the maintenance and repair of district improvements. Such special assessments are paid into a sinking fund and may be used to retire warrants.

Where in addition to warrants the district has issued bonds, the quagmire grows. The statutes require that the interest and principal on bonds be paid when due. If for that purpose a tax was imposed, there would be no problem. However, there is no statutory mandate that the proceeds of special assessments be utilized only for the retirement of district debt, and in fact accusations have been made to the effect that in many instances the proceeds have been diverted to other uses.

The application of special assessments to the payment of interest on bonds, or to any other purpose, in lieu of the retirement of the related district obligation, is certainly an unsound financial practice. It allows the district to circumvent a realistic mill levy on the short term. In the long run the district taxpayers may be faced with either of the following: If the district indebtedness is in the form of bonds, principal on such bonds will become due serially, with the first series due five years from the date of issue. If the district obligations are in the form of warrants, with high interest accrual, and the funds from past special assessments are depleted, the neighboring municipality may refuse to annex simply because the district debt ratio is too high. In either case the district taxpayers will be faced with an immediate skyrocketing of property tax. Actually, if annexation is refused because of the district's high debt ratio, it makes little difference whether the debt is in the form of warrants or bonds. If in bonds the district must increase mill levies in order to meet payment of principal. If the district debt is in the form of warrants, as a condition to annexation the municipality may insist that a certain proportion of warrants be retired; again the mill levy would have to be raised.

In summary, the lack of regulation on the application of special assessments and the mode of measuring SID taxation, combined with
provisions which allow warrants of indefinite duration, enable a district to maintain a high proportion of its debt in the form of warrants. From the standpoint of the prospectively annexing municipality such a procedure operates to postpone payment on general obligations until annexation. Thereafter, the cost is shared by the taxpayers of such municipality. It could be argued with merit that such postponement is unfair and that the district should be required to apply special assessments to the retirement of warrants, or to deposit such assessments in a separate sinking fund reserved for the payment of principal on bonds when it becomes due. This would require that the SID levy a tax sufficient to meet interest on bonds.

The bifurcation of district debt into warrants and bonds is necessary. At the initial stages of development the district is devoid of a tax basis — here warrants serve the important function of interim financing. However, as it stands today, the "interim" can be indefinite. A solution might require that special assessments be paid into a separate sinking fund, to be dispursed quarterly to retire warrants. In the event such warrants were converted into district bonds the sinking fund should remain inviolate, strictly reserved for the payment of principal on bonds. The district could be required to levy an annual tax sufficient to pay the interest on such bonds. The flexibility of the present system, whereby mill levy need not be sufficient to pay the interest accumulating on warrants, may be a very desirable feature. Where the district has constructed parks, playgrounds and recreational facilities, pursuant to specifications and standards over which the neighboring municipality has a veto power, it may be unreasonable to demand that district taxpayers bear the burden of financing, particularly where such improvements by their nature are of benefit to the entire city or village. If this is a countervailing consideration, it could be recognized as such, with provisions for a separate class of warrants issued solely in payment for parks, playgrounds and recreational facilities. Such warrants could be made exempt from mandatory conversion provisions applicable to other warrants.

Specifically in the area of warrants and financing it thus can be seen that the current law is not responsive to the interests of either the municipality or the taxpayers of the district. A complete solution is not readily apparent, and it involves questions of policy far beyond the scope of this article. In 1969 the Committee on Urban Affairs rejected an amendment that would have provided that "warrants issued for the payment of any contract shall be converted to negotiable bonds and placed on the tax roll of the district, not later than one year after the completion date of the improvement project."90 The arguments in opposition to the amendment made it clear

90. See Hearings on L.B. 1185 before the Committee on Urban Affairs, April 9, 1969 (comments of Senator Bloom).
that mandatory conversion alone is not the solution — difficulties in forced sale and lack of an adequate tax base were but two of the many arguments raised against mandatory conversion.91

VI. ANNEXATION

Annexation may be initiated by petition of either the SID or the municipality, while it remains at the discretion of the latter.92 The city's decision-making will in large part be governed by financial criteria. If the general obligations of the SID are too great, the debt limitations of the city may bar annexation. Also to be considered is the amount of taxable property within the district in comparison to the obligations to be assumed. Where the general obligations of the district are vastly in excess of its ability to pay therefor, annexation may be delayed until such time as the SID's debt ratio is reduced.

The city initiates the formal annexation process by ordinance. Thirty days after the effective date of the ordinance the city merges with the SID,93 succeeding to all its interests, rights and obligations.94 If the validity of the annexing ordinance is challenged by a

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91. Id. In opposition to the amendment it was argued:
(1) That it would require 15 to 20 bond issues per district at a cost in excess of $1,000.00 each.
(2) That it would force the bonds on the market at the wrong time.
(3) That in terms of ascertaining the obligations of an SID, warrants are registered with the county treasurer, and therefore may be determined by prospective purchasers of SID property.
(4) That many warrants are paid off by special assessments and that mandatory issuance of bonds would force the SID to pay 5 years interest thereon.
(5) That provisions for mandatory levy of special assessments within a specified time period would adequately protect the parties involved.

Hearings on L.B. 1185 before the Committee on Urban Affairs, April 9, 1969 (comments of John Delehant). This argument is certainly strong when measured against the proposed amendment; however, it does not militate against the adoption of an amendment that would require the retirement of warrants upon the payment of special assessments.

92. There are no statutory provisions for compulsory annexation of an SID. However, in the interest of SID taxpayers who seek relief from the burden of paying the principal on SID bonds when same become due, compulsory annexation has been discussed. Such provisions should not be too objectionable from the standpoint of the annexing municipality under the law as amended in 1971. Compulsory annexation prior to 1971 would have entailed such municipality assuming the cost of parks, playgrounds, and recreational facilities, where there was no control over costs, standards and specifications. Prior to 1967 compulsory annexation could have entailed assuming the cost of improvements for which there had been levied inadequate assessments. Today, with the municipality a party to the special assessment hearing, and with a veto power over the construction of parks, playgrounds, and recreational facilities, the interest of SID taxpayers seems to outweigh any objection, excepting debt limitations, that such municipality may set forth. Such objections would have merit as to existing SIDs whose improvements and special assessments were not subject to the new safeguards.

94. NEB. REV. STAT. § 31-763 (Cum. Supp. 1969) provides in part:
[T]he district shall merge with the city or village and the city or village shall succeed to all the property and property rights of every kind, contracts,
proceeding in a court of competent jurisdiction, the effective date of the merger is thirty days after final determination of the validity of the ordinance.95

After the effective date of the annexation the trustees are divested of their powers and cannot thereafter levy special assessments,86 authorize improvements,97 or levy tax.98 The annexing city may levy the special assessments which the district was authorized to have made at the time of merger.99 However, the city is bound by the trustees' prior decisions as to the extent of special benefits and the amount of special assessments.100 Within thirty days of the effective date of the merger the trustees are required to submit to the city a written accounting, and unless the city within thirty days brings an action against the trustees, they are discharged from all further duties and liabilities.101

VII. CONCLUSION

The SID has played an important role in the development of the City of Omaha — it is estimated that some 90% of new residential development outside the city limits are through this vehicle. Opportunities for abuse have existed in the past, but abuse has been by no means prevalent, and in the main the districts are being used to the advantage of all parties concerned.

The 1971 amendments are meritorious, particularly in reference to the provisions relating to recreational facilities; with a "veto power" the city is in a position to protect its interest to a degree not heretofore possible.

As has been discussed, there remains an area of significant conflict over the indefinite duration of warrants, the application of special assessments, and the mill levy within the district. At base this conflict may be reduced to the proposition that the districts should be required, at least to some degree, to pay the finance charges accruing on district obligations. From the standpoint of the municipality costs will be minimized if the districts, to the extent not funded by special assessments, are required to levy a tax sufficient

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97. See In re Sanitary & Improvement District No. 75, 182 Neb. 63, 152 N.W.2d 111 (1967).
100. Id.
to pay the interest and principal on bonds, as well as the interest accumulating on warrants. From the standpoint of the SID there are several countervailing considerations which militate against the adoption of such a rigid approach. First of all, such a requirement would seriously impair the district's ability to finance improvements since initially the district has no ability to meet such a mill levy. Secondly, a strong argument may be made that the district should not be required to bear the burden of paying the finance charges attributable to the costs of parks, playgrounds, and recreational facilities, where these improvements inure to the benefit of the entire community. Thirdly, the cost of improvements is often substantially increased by the requirements of the neighboring municipality. The standards and specifications to which the district must conform are often dictated by the long range plans of the city and bear no relationship to the actual needs of the district. For example, districts have been required to install larger sewer lines, wider streets, cloverleafs, and overpasses for benefit of the municipality. The district should not be required to levy taxes to fund the interest attributable to these improvements.

As a suggested approach to compromise, it could be provided that the districts reserve special assessments for the payment of principal on district indebtedness, and be required to levy a tax sufficient to pay the interest on bonds. Districts may be required to bear a greater proportion of the cost of financing without interfering unnecessarily with warrants by providing that, in addition to the mill levy for bonds, the district maintain a minimum mill levy whenever warrants are outstanding. Such minimum should be framed in terms of a specific levy of perhaps "15 mills or in an amount sufficient to fund the interest accumulation on warrants, whichever is the less," and not in terms of "sufficient to fund the interest accumulating on warrants," since the latter could require a tax in excess of the district's ability to pay.

The above suggestion is predicated strictly upon academic considerations and it is realized that an equitable solution will demand the insight of individuals with an understanding of the conflicting interests, and the ability to evaluate a solution in terms of the day to day operations of the districts.

John C. Minahan, Jr. — '73