OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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City Council Docket Date: July 23, 2012

Item Number: S-400, S-401, and S-402

AB 1484 True-Up Payment and Required Asset Transfers

OVERVIEW

As part of Governor Brown's plan for dissolving redevelopment agencies and distributing their funds to other local agencies, Assembly Bills (AB) 26 and AB 27 were passed by the California State Legislature and signed by Governor Brown in June 2011.[1] Despite a lawsuit challenging the constitutionality of each of these measures and a partial stay while the case was heard, the California Supreme Court issued its final opinion upholding AB 26 as constitutional and striking down AB 27 as unconstitutional. In January 2012, the City Council designated the City of San Diego to serve as the Redevelopment Agency's (RDA) Successor Agency for purposes of winding down its operations; making payments on enforceable obligations; and liquidating the agency's unencumbered assets for distribution to the county, school districts, and other local public agencies. The City also chose to serve as the Housing Successor Agency and retain the former RDA's affordable housing assets and assume related responsibilities.

California Redevelopment Agencies were dissolved on February 1, 2012, and their rights, powers, duties, and obligations were vested in the successor agencies. Since that time, successor agencies across the State have faced challenges and uncertainty, particularly since AB 26 did not provide specific direction for the administration of the dissolution and wind up activities. AB 1484 was passed as a trailer bill to the FY 2013 state budget on June 27, 2012. It was intended to make technical and substantive amendments to AB 26 based on experience at the state and local levels in implementing the legislation. AB 1484 took immediate effect and requires successor agencies and others involved in dissolution activities to learn and implement significant new rules of conduct. Further, AB 1484 moves up important deadlines for successor agencies and provides significant financial penalties for failing to meet these deadlines.

This report provides summary information and analysis of key redevelopment dissolution issues coming to Council in the next two weeks, including the need to retain reserves due to continuing

[1] AB 26 barred redevelopment agencies from engaging in new business and provided for their windup and dissolution by October 1, 2011. AB 27 provided an alternative allowing redevelopment agencies to continue operations if payments were made to other taxing entities, such as schools and special districts.

risks to the General Fund.

Fiscal/Policy Discussion

As shown in the table below, several important issues will be brought to Council today relating to redevelopment dissolution, some of which are related to provisions in AB 1484. It is important to maintain the distinction between the City itself and the City acting in its capacity either as the Successor Agency or the Successor Housing Agency.

Council Docket Date	Actions, Provisions, or Requirements	Related Deadline(s) and Potential Penalties
July 23, 2012 *Item S-400*	AB 1484 and True Up Payment: 1. Receive staff report summarizing key aspects of AB 1484 and its impacts on Successor Agency and Oversight board roles and responsibilities. 2. Ratify and authorize all actions taken by Mayor or signee to appropriate and expend uncommitted tax increment reserves funds of the Successor Agency to make the "true up" $89.6 million to the CAC on July 12, 2012 in compliance with statutory deadline in AB 1484.	Payment was due to CAC on July 12, 2012 Failure to make payment could have resulted in: • Separate penalties for the Successor Agency and the City of 10% of the amount owed plus 1.5% for each month that payments are not made. • The Successor Agency being prohibited from making any payment other than bond debt until the amount owed is paid to CAC. • The City will not receive a distribution of sales and use tax on July 18, 2012 or any subsequent distribution until the amount owed is paid.
July 23, 2012 *Item S-401*	Reversal of Asset Transfer: Authorize the execution and recording of conveyance instruments to accomplish the reversal of the transfer of real property assets and other assets that occurred between the former RDA and the City in March 2011.	State Controller's order dated April 20, 2012 called for the immediate reversal of transfers. Refusal to comply with the order may result in the Controller seeking a writ of mandate in Sacramento Superior Court to compel compliance.
July 23, 2012 *Item S-402*	Transfer of Affordable Housing Assets: *Successor Agency* 1. Authorize the execution and recording of conveyance instruments to accomplish the transfer of affordable housing assets from the Successor Agency to the Housing Successor Agency and to the Low and Moderate Income Housing Fund, following approval of list of housing assets by the Oversight Board and DOF. *Successor Housing Agency* 1. Authorize the execution and recording of conveyance instruments to accomplish the transfer of affordable housing assets from the Successor Agency to the Housing Successor Agency and to the Low and Moderate Income Housing Fund, following approval of list of housing assets by the Oversight Board and DOF. 2. Authorize City's Chief Financial Officer or designee to create Housing Asset Fund for purposes of depositing the affordable housing assets received from the Successor Agency and retaining any future funds generated from these assets.	A list of all housing assets must be provided to DOF by August 1, 2012. DOF has 30 days from the submission of the list to reject any item. Staff plans to seek approval from the Oversight Board in August 2012 to transfer housing assets to the City as Successor Housing Agency.

Item S-400 – AB 1484 and "True-Up" Payment

AB 1484 contains provisions to ensure that FY 2012 pass-through payments are made to taxing entities and any residual amounts of funds have been distributed. If AB 26 had gone into effect on October 1, 2011 as originally intended, the CAC would have made the first distribution from the RPTTF on December 16, 2011 for the period January 1-July 30, 2012. Because of the California Supreme Court stay, the funds that would have been available for deposit into the RPTTF for the December distribution were dispersed to RDAs in late 2011 and used by most successor agencies to pay enforceable obligations on the Recognized Obligation Payment Schedule (ROPS) 1.

Essentially, if local taxing entities did not receive the full amount of their allocated share of property taxes for the periods January 1-June 30, 2012 (ROPS 1) and July 1-December 30, 2012 (ROPS 2), the CAC was required to determine the amount owed by the Successor Agency and send a demand for payment by July 9, 2012.[2] AB 1484 did not explain how this amount should be determined (since there was no distribution from RPTTF for this period). However, the DOF provided a prescribed methodology on its website for calculating the residual balanced payment—called the July true-up process. The City received a demand letter from the CAC on July 9, 2012 for the payment of $89.6 million so that it could be distributed pro rata to the taxing entities. The CAC's method for calculating that payment is shown in the table below.

Method	Amount *(Millions)*	IBA Comments
Total tax increment received by former RDA	$ 93.0	Amount received through January 31, 2012 and was transferred to the City as the Successor Agency's reserves and used to pay enforceable obligations for ROPS 1.
Minus pass through payments made in which were applicable in FY 2012	-	Although the former RDA made $26.0 million in pass-through payments in early 2012, these were attributable to FY 2011 per delayed payment procedures set up in the applicable tax-sharing agreements, so these cannot be deducted.
Minus amount of RPTTF used for ROPS 1	3.3	Total ROPS 1 enforceable obligations equaled about $207.0 million. About $203.7 million was paid from other available revenues including reserves.
Equals amount the City must pay	$ 89.6	The CAC allocated this amount pro rata among taxing entities. The City received about 17% or $18.7 million which has fallen to General Fund reserves.

Failure to make payment could have resulted in significant financial penalties for both the City as Successor Agency and the City itself. As addressed in Staff Report 12-096, the Successor Agency made the payment to the CAC on July 12th from its reserves under protest. Although staff did not have time to bring this item to Council prior to the payment being made without incurring a financial late penalty, two prior resolutions adopted by Council delegated authority to the Mayor or his designee to take action in accordance with State law relating to redevelopment wind down.

[2] If the demand for payment is not made, CAC is subject to penalties of 10% of the amount owed plus1.5% for each month that the payments are not made.

The payment of $89.6 million is not expected to cause any cash flow problems or compel the City as Successor Agency to breach any enforceable obligations or tap into any bond proceeds or affordable housing funds during the ROPS 2 period ending December 31, 2012. Further, as part of the new procedures for reviewing the available cash assets of the former RDA, discussed in the next section of this report, the City as Successor Agency will ultimately be required to transfer all unobligated cash reserves to the CAC. The City received its pro rata share of the CAC's distribution of about 17% or $18.7 million which has fallen to General Fund reserves.

Item 401 - State Controller Order Requiring Reversal of Asset Transfers

Item 401 relates to the State Controller's April 20, 2012 order requiring that any asset transfers not allowed by AB 26 immediately be reversed and all applicable assets returned to the Successor Agency. AB 26 does not allow asset transfers that occurred from RDAs to the City or County that created them after January 1, 2011.[3] The former RDA for the City of San Diego made a transfer of assets to the City in March 2011 which is now being reversed to comply with this order. This transfer was intended to facilitate the City's ability to appropriately complete redevelopment projects and related activities and to pay debts previously incurred between the RDA and the City. The transfer included:

1. About 100 properties and related controls and obligations. A list of these properties is included as Attachment A to Staff Report 12-097.
2. Recorded Deeds of Trust in the City's favor against about 10 real estate assets for the purpose of securing debt owed by the former RDA to the City. These properties are included as Attachment 2 to the same staff report.
3. An advance of $289.4 million from the former RDA to the City to implement redevelopment projects included on the Cooperation Agreement approved by Council on February 28, 2011.

The requested action is for the Successor Agency to authorize the execution and conveyance instruments to accomplish the reversal. The City as the Successor Agency will become the holder of the assets until these are audited as required by AB 1484.

S-402 –Transferring Affordable Housing Assets to the Housing Successor Agency

A list of all housing assets previously transferred to the Successor Housing Agency must be submitted to the DOF by August 1, 2012. When the City assumed the duties of Successor Agency and Successor Housing Agency, it did not separate out the affordable housing assets. Therefore, Successor Agency staff have developed a list of these assets, included as Attachments A-D in Staff Report 12-098. The requested action for Item S-402 is for the Successor Agency to authorize the execution and recording of conveyance instruments to accomplish the transfer of affordable housing assets from the Successor Agency to the Housing Successor Agency and to the Low and Moderate Income Housing Fund (LMIHF), following approval of the list of housing assets by the Oversight Board and DOF.

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[3] Such transfers are allowed only if the City, County, or RDA contractually committed to a third party for an expenditure or encumbrance of a specific asset prior to June 28, 2011.

In addition, the requested action for the Successor Housing Agency is to authorize the execution and recording of conveyance instruments to accomplish the transfer of affordable housing assets from the Successor Agency to the Housing Successor Agency and to the LMIHF, following approval of the list of housing assets by the Oversight Board and DOF. In addition, the Successor Housing Agency is requested to authorize City's Chief Financial Officer or designee to create Housing Asset Fund for purposes of depositing the affordable housing assets received from the Successor Agency and retaining any future funds generated from these assets.

Establishing an approved list of housing assets is a first step for the provision in AB 1484 which requires successor agencies to retain the services of a licensed accountant to review unobligated reserve balances of both LMIHF and all other funds. Due to upcoming deadlines, related items will likely be coming to Council in October 2012.

Preserving Funds for Impact of Redevelopment Dissolution

While the full fiscal impact to the City's General Fund still is not fully known, there continues to be several significant factors that pose a risk. These factors include increased scrutiny and potential dispute of enforceable obligations by the Successor Agency Oversight Board and DOF, loss of unobligated reserves of the former RDA for paying enforceable obligations when Redevelopment Property Tax Trust Fund (RPTTF)[4] is not sufficient, potential clawback of assets per the State Controller's order, and potentially less than anticipated distributions of RPPTF due to the CAC's method of allocating monies. As shown in the table below, the City has set aside about $40.4 million to address the potential impact to the General Fund. We concur with the Mayor's Office and the City Attorney's Office that it is important to preserve these funds given the ongoing high level of risk.

Millions of Dollars

Amount	Source
$ 5.0	Portion of FY 2012 revenue surplus retained in reserves (FY 2012 Year-End Budget Monitoring Report) for unforeseen circumstances or to mitigate impacts of dissolution
10.7	Transient Occupancy Tax (TOT) fund balance from FY 2012 (FY 29013 May Revise)
3.7	Appropriated reserve (FY 29013 May Revise)
2.4	City's allocation of residual funds from CAC's June 1, 2012 RPTTF distribution[a]
18.6	City's allocation of July True-Up Payment
$ 40.4	**Total**

[a]About $1.2 million of this amount is being used to advance the FY 2013 Budget of Civic San Diego to ensure adequate cash flow.

CONCLUSION/RECOMMENDATION

The City as Successor Agency has made notable progress moving forward with redevelopment dissolution and wind up activities despite significant challenges, including the non-specific and sometime contradictory provisions in AB 26, varying interpretations on methodologies for allocating RPTTF, related uncertainties, and the sheer volume of the task at hand. Despite

[4] This includes the Successor Agency's share of tax increment that is distributed by the County Auditor and Controller (CAC) on June 1st and December 16th of each year.

receiving less than anticipated RPTTF, the Successor Agency has been able to rely on the reserves of the former RDA to pay enforceable obligations thus far. However, the required reversal of the asset transfer per the State Controller's order and new provisions in AB 1484 for remittance of unobligated funds for distribution to taxing entities may provide future challenges for paying enforceable obligations. In addition, enforceable obligations on ROPS 3 are likely to face increased scrutiny by the Oversight Board and DOF with some obligations potentially being disallowed. The City currently has set aside about $40.4 million to mitigate these and other unforeseen risks to the General Fund from the dissolution and unwinding of the RDA. We believe that it is important to both preserve these funds for this purpose and to consider setting aside addition property taxes received from the City's residual distribution of RPTTF given the ongoing high level of risk.

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