

Real Estate, Land Use & Environmental Law Blog

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Presented By **SheppardMullin**

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UPDATE ON REDEVELOPMENT LAW: LEGISLATIVE TWO STEP TO CUT REDEVELOPMENT AGENCY FUNDING GOES DOWN WITH GOVERNOR'S BUDGET VETO

This is the second in a series of blog entries monitoring the proposal to eliminate redevelopment agencies.

By [Michael Kiely](#)

Yesterday, after heated and reportedly almost violent debate, both houses of the California State Legislature voted to pass ABX1 26, which would eliminate California redevelopment agencies, called RDAs, effective October 1, 2011, and ABX1 27, which would exempt from elimination any RDA that agreed to make its share of a \$1.7 billion voluntary contribution of its revenues to other local government needs.

These bills, which are discussed in more detail below, were part of the overall budget package adopted yesterday. The 2011-2012 budget was passed by the Legislature by the statutory June 15 deadline for only the second time in 25 years, perhaps the result of Proposition 25, the 2010 ballot measure that lets the legislators approve the budget (other than a tax increase) by a simple majority vote, and withholds their pay if its not done on time. The entire budget package was sent to the Governor for signature.

Less than 24 hours later, the Governor vetoed the budget bill. He issued the [following statement](#):

"Unfortunately, the budget I have received is not a balanced solution It continues big deficits for years to come and adds billions of dollars of new debt. It also contains legally questionable maneuvers, costly borrowing and unrealistic savings. Finally, it is not financeable and therefore will not allow us to meet our obligations as they occur."

At this point, we understand the Governor will address the budget trailer bills, including the RDA bills, later today, although it has also been rumored that RDA bills have not yet been sent to the Governor. Some of our Sacramento sources predict that he will veto the RDA bills; others suggest that he will sign them. The two bills are linked together, so that if the Governor cannot try to end redevelopment altogether by signing the first bill ending RDAs but veto the second bill creating the voluntary payment and exemption. If he did that, neither bill would become effective.

The outcome for the fate RDAs remains unclear. Possible outcomes include:

- Governor Brown signs the two bills, notwithstanding that the budget process is not fully resolved. Many measures to reduce the overall budget deficit were adopted in March outside of the overall budget process. The benefit to the Governor's position would be that it locks in \$1.7 billion of revenues towards the 2011-2012 budget shortfall. In contrast, if the Governor insists on pursuing the complete elimination of RDAs, the State would be forced to chase the money. Such efforts may require litigation to try to unwind the cooperation agreements and other funding shield measures adopted by RDAs and cities since the Governor's initial RDA proposal in January.
- ABX1 26 and ABX1 27, or new bills similar to them, are resurrected as part of the ultimate compromise on a budget solution.
- A new bill similar to ABX1 26, eliminating redevelopment agencies but not requiring linkage to a bill providing for voluntary payment and exemption from elimination, could be adopted and by the Legislature and signed by the Governor. This would only occur as part of the ultimate compromise on the budget. Since initially raising the idea in December 2010, the Governor has not waived in his determination to completely end redevelopment. Complete elimination would yield substantially greater funds next year and following years to reduce State budgetary pressures. However, as noted above, the need to lock up the \$1.7 billion in the 2011-2012 fiscal year might lead the Governor to forgo this alternative.

It seems likely that any of these alternatives might be challenged as unconstitutional by the California Redevelopment Association, or CRA, and perhaps the California League of Cities. The bases for such a challenge are discussed below. If the voluntary payment and exemption from elimination bill becomes effective, then notwithstanding any such challenge, most, if not all, RDAs could be expected to make the voluntary payments called for under ABX1 27, subject to later recovery if the CRA challenge is successful.

BRIEF DESCRIPTION OF THE TWO STEP BILLS

RDA Elimination Bill: ABX1 26 is very similar to the earlier Governor-backed legislation to end RDAs.^{1[1]} Under ABX1 26, RDAs would cease to exist on October 1, 2011. Until then, RDAs are prohibited from taking any actions other than payment of existing indebtedness and performance of existing contractual obligations. On October 1, 2011, all RDA property and obligations, except for the assets of the low and moderate income housing fund, would be transferred to successor agencies and overseen by an oversight board, the county auditor-controller and the Department of Finance. Assets in the low and moderate income housing fund would be transferred to the auditor-controller for distribution to taxing agencies. Successor agencies will repay existing indebtedness, complete performance of existing contractual obligations and otherwise wind down operations and preserve agency assets for the benefit of taxing agencies.

ABX1 26 does contain some differences from the earlier version, including:

- Tax increments taken from RDAs in 2011-12 fiscal year would be treated the same as other property tax revenues. The new bill eliminates the direct payment of these amounts to the State. Presumably, this change was to address concerns raised by the Legislative Counsel Bureau that payments of tax increment to reimburse the State would be unconstitutional.^{2[2]}
 - The definition of "approved development project" and authorization for successor agencies to continue to pursue such projects has been deleted. These deletions may be intended to address concerns that the limitations tying which obligations could be treated as enforceable based on the state and timing of the project would illegally impair the contracts of RDA contracting parties relating to projects that did not fit the definition of "approved development project."
 - ABX1 26 provides that the successor agency will not have liability beyond its tax increment and other agency receipts. This seems to have been added to address concerns that cities acting as successor agencies would place their general fund at risk.
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Voluntary Pay/Exemption Bill: ABX1 27 provides that, notwithstanding ABX1 26, an RDA may continue its existence, operation and function if its local government, e.g., the city, enacts an ordinance by November 1, 2011 committing to make annual payments into a Special District Allocation Fund and Educational Revenue Augmentation Fund established for each county and administered by the county auditor-controller.

The amount of the payment for each city or county is initially based on its RDA's share of all redevelopment property tax increment, less amounts necessary to pay bonded indebtedness (but not other indebtedness) multiplied by \$1.7 billion. For subsequent years, the formula changes to an amount equal to approximately 23.53% of the 2011-2012 payment, adjusted based on the increase or decrease in property tax increments, PLUS 80% of the share of tax increment that would have been received by schools in the absence of redevelopment, less pass-through payments to schools.

Various commentators have stated that such payment can be expected to total between 25% and 35% of the total revenues for each RDA.

BASIS FOR CRA CONSTITUTIONAL CHALLENGE

Based on an email to CRA Members sent by John Shirey, the head of the CRA on June 15, 2011, the proposed two step arrangement resulting in a loss of funding for the RDAs would violate the following provisions of the California Constitution:

1. Article XIII A, section 25.5, which prohibits city or county property tax from being used for schools.
2. Article XIII A, section 1, which prohibits the transfer of property tax to transit districts.
3. Article XIII, section 24, which prohibits the Legislature from restricting the use of taxes imposed by local governments for their local purposes.
4. Article XIII A, section 25.5, which prohibits indirect allocation of tax increment to schools, transit districts and fire protection districts.
5. Article XVI, section 6, which prohibits the transfer of city or county revenues to schools and transit districts and fire protection districts which is an unlawful gift of public funds.

6. Article XIII B, which prohibits the use of property tax to fund state mandates.
7. Article XVI, section 16, which requires all tax increment to be used to repay indebtedness incurred by the redevelopment agency to carry out the redevelopment project.
8. Article XIII A, section 25.5, which prohibits city and county property tax from being transferred to special districts without a 2/3 vote.

CONCLUSION

Property owners, developers, borrowers, bond holders and others that may be affected by the elimination of RDAs as contemplated by ABX1 26 should continue to follow legislative developments it to determine their best course of action. The Governor's veto should not be seen as a sign that RDAs are safe. Based on recent developments, the likelihood seems very great that, at a minimum, RDAs will lose some of their funding, and the outright elimination of RDAs remains a strong possibility.

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[3\[1\]](#) AB 101 and SB 77 failed to pass in March by less than one vote in each house. The mechanics of this very complex legislation, and the problems it would present for property owners, developers, lenders and others were discussed in more detail in [California Redevelopment Update: No News is ...No News, May 5, 1011](#).

[4\[2\]](#) Letter from Legislative Counsel Bureau to Hon. Diane Harkey dated April 28, 2011, regarding Community Redevelopment: Property Tax: Public Health And Safety Fund -

#1115418, which concluded that "the requirement [in AB 101] that, for the 2011-12 fiscal year, property tax revenues in a Redevelopment Property Tax Trust Fund that are . . . use[d] solely to reimburse the state for costs of providing health care or trial court services in that county, would violate Section 1 of Article XIII A of the California Constitution."