

STATE CANCELLATION OF REDEVELOPMENT AGENCIES MAY AFFECT YOU!

January 5, 2012 by *Michael Kiely and Phillip Tate*

On December 29, 2011, legislation to dissolve all redevelopment agencies became effective when the California Supreme Court released its opinion in *California Redevelopment Association v. Matosantos*, challenging the Legislature's adoption of AB 1X 26, providing for elimination of California redevelopment agencies (RDAs), and AB 1X 27, exempting from elimination any RDA that makes a voluntary contribution of its revenues. The Court has upheld the constitutionality of AB 1X 26 and struck down AB 1X 27.

The dissolution of redevelopment agencies in California may affect you if you have any of the following:

- Redevelopment Agency issues bonds or notes;
- Real property subject to an agreement with a redevelopment agency;
- A loan from a redevelopment agency;
- A lease with a redevelopment agency;
- A contract to acquire land from a redevelopment agency;
- Real property located in a redevelopment project area; or
- Any interest in acquiring redevelopment agency assets.

THE RDA DISSOLUTION LEGISLATION

AB 1X 26 and AB 1X 27 became effective on June 29, 2011, but were stayed by the California Supreme Court pending resolution of the challenge. The complex RDA dissolution legislation can be simply summarized as follows:

All redevelopment agency activity is now suspended except paying existing obligations;

All redevelopment agencies will be abolished on February 1, 2012 and "successor agencies" will be created to take over the assets and obligation of their former redevelopment agencies;

The successor agency is required to wrap up operations of the former redevelopment agency under the direction of an oversight board composed of 7 members, the majority of which are selected by the county board of supervisors or county superintendent of education;

Property tax increment formerly payable to redevelopment agencies will be distributed to taxing agencies after first paying amounts due on existing obligations under current payment schedules; and

Existing obligations, as defined in the legislation, will be honored; however, successor agencies are tasked with terminating contracts where savings could be created by termination payments.

POTENTIAL IMPACTS

1. **Agency Bonds or Notes.** Generally, scheduled amounts payable under Agency bonds or notes for which the Agency pledged tax increments will be honored under the RDA legislation. The successor agency will continue to receive tax increments for payments. However, to be payable any such obligations must be on the RDA's Recognized Obligation Payment Schedule, so holders should confirm their obligations are so scheduled. In addition, there may be disputes among the County Controller, the State Controller, the Department of Finance and the Successor Agency as to the characterization of such obligations, and whether they are appropriate to include on the Schedule at all.

2. **Other Agency Tax Increment Pledges – Other Agency Agreements.** Under many owner participation agreements between redevelopment agencies and property owners, a future pledge of tax increment is contemplated. For example, under some Owner Participation Agreements (OPAs) upon completion of the required project, the redevelopment agency is required to issue a tax increment-backed promissory note to the developer. In others, the redevelopment agency commits to issue tax allocation bonds upon completion of the required project or satisfaction of other conditions. In still others, redevelopment agencies set aside tax increment for payment upon certain milestones. Since the AB 1X 26 permits payment only on scheduled liabilities, it is unclear whether such commitments, which may not be certain with respect to timing or amounts, will be honored.

3. **Loan from an Agency.** Redevelopment agencies have frequently provided loans to developers, especially affordable housing developers, and non-profit organizations. Frequently, given the community development and planning goals of the redevelopment agencies, enforcement of such loans has not been strict. Since the successor agencies are charged with maximizing revenues for distribution to the taxing authorities, borrowers' assumptions regarding loan extensions, modifications, non-enforcement or conversions to grants should now be re-examined.

4. **Lease with a Redevelopment Agency.** Where the redevelopment agency is the landlord, no lease amendment will be possible until after formation of the successor agency. Successor agencies are obligated to sell all assets, so the agency's tenant should assume that all future dealings with the landlord under the lease will be undertaken in the context of landlord revenue maximization rather than redevelopment agency planning and community goals. The sale requirement may create an opportunity for the tenant to acquire the fee interest.

Where the redevelopment agency is the tenant, no lease amendment will be possible until after formation of the successor agency, if at all. Since the successor agencies are to receive only limited funding, landlords may expect successor agencies to default under, or at least try to renegotiate, lease obligations. However, there is nothing in AB 1X 26 to indicate that such leases would not be treated as an enforceable obligation. Landlords should consult their leases, since some leases with government agencies contain tenant termination rights.

5. **Agency Land Sale.** Generally, a redevelopment agency sells land pursuant to a Disposition and Development Agreement, with closing upon satisfaction of certain conditions, usually including obtaining financing for development of a defined project. Successor agencies are obligated to sell all assets, but in a way that maximizes yield. If the purchase price is below market value, then the successor agency could attempt to revoke such agreement, perhaps by invoking developer defaults or failed conditions.

If the RDA previously sold property to a developer with a right to repurchase if development did not proceed, then the successor agency may consider whether it should invoke such right. If the original purchase price was below market, and the debt level on the property is low enough, it might be prudent for a successor agency to consider exercising its option then selling the parcel for fair market value.

6. **Real Property Located in a Redevelopment Project Area.** If your real property is located in a redevelopment project area, then any anticipation of entering into a subsidy redevelopment deal involving redevelopment agency tax increment should be let go. Other subsidy sources should remain available, and there is contemplation in Sacramento of an expansion of the infrastructure financing district laws to make alternative financing more readily available.

There may also be land use implications. Some local jurisdictions include the redevelopment agency in their land use planning regulations. Examples include delegating authority to redevelopment agencies for design review, or permitting certain variances only for projects subject to redevelopment agency agreements. Some cities have already made alterations to their planning regulations regarding a transition of such powers to other agencies, such as planning commissions.

State land use planning laws may also be implicated. For example, the State Outdoor Advertising Act provides certain benefits for freeway-adjacent properties located in redevelopment project areas, the effects of AB 1X 26 on which are unclear.

7. **Sale of Redevelopment Agency Assets.** Under AB 1X 26, successor agencies are obligated to sell all former redevelopment agency assets in a way that maximizes yield. Some estimate that in Los Angeles County alone, there may be over 2,000 such sites. This suggests opportunities to acquire valuable sites without the baggage of typical redevelopment agency requirements (for example, no-flip provisions, development

covenant with deadlines, RDA design review, tenant mix approval, opening covenants, operating covenants, prevailing wage, living wage, or local hiring requirements). While AB 1X 26 requires successor agencies to conduct such sales “expeditiously and in a manner that maximizes value”, there is a possibility that successor agencies flooding the market may result in downward pressure on property values statewide.

WHAT TO DO NEXT

The intent of this message is to urge property owners and interest holders that may be affected to analyze the RDA dissolution legislation and determine their best course of action. The appropriate response may be to wait and see what the successor agency does with respect to your particular property or agreement. Another response would be to move aggressively either by negotiation or litigation with a successor agency in order to more clearly establish your rights.

The above summary of the RDA dissolution legislation is not intended as a complete summary and the description of potential risks as a result is not intended as this Firm's opinion as to the outcome of any dispute that may arise. Sheppard Mullin attorneys have deep and broad experience in redevelopment, and we stand ready to assist you. Please note more detailed analysis has been previously published relating to the RDA dissolution legislation in prior blog postings.