



Redevelopment Agencies File Second Lawsuit to Block Unconstitutional Raids of Redevelopment Funds

In April 2009, a Sacramento County Superior Court ruled that State raids of redevelopment funds are unconstitutional, invalidating a 2008 state budget bill to take \$350 million in redevelopment funds. Despite the clear unconstitutionality, just three months later legislators and the Governor approved budget bill ABX4-26 as part of the 2009 State budget which authorizes a devastating \$2.05 billion raid of local redevelopment funds, including \$1.7 billion in FY 2009-10 and another \$350 million in FY 2010-11. The California Redevelopment Association and two of its member agencies filed a lawsuit on October 20, 2009, to challenge the constitutionality of State raids of redevelopment funds.

The courts ruled it was unconstitutional in April 2009. Raiding voter-approved redevelopment funds is STILL unconstitutional today.

- Article XVI, Section 16 of the California Constitution states that redevelopment tax increment funds can only be used for specified redevelopment activities, specifically *“to finance or refinance ... the redevelopment project.”* Taking redevelopment funds to balance the State’s budget, the unquestioned purpose of ABX4-26, does not qualify as a constitutionally permitted use of redevelopment funds.
- That’s why in April 2009, a Sacramento Superior Court invalidated a 2008 State raid of redevelopment funds, finding that it *“violates the intent of Section 16 (of the State Constitution), to allocate the tax increment to the financing of redevelopment projects.”*
- While legislative staff and lawyers changed the wording of the 2009 legislation in an attempt to get around the State Constitution and Superior Court Ruling, this raid is still unconstitutional. The clear purpose of ABX4-26 is to redirect redevelopment funds to school districts to reduce the State’s obligation to fund education. In other words, ABX4-26 is intended to reduce the State’s budget obligations – not to further redevelopment – which is a violation of the Constitution.

State raids of redevelopment funds unconstitutionally impair bonds and other contracts.

- State and Federal Constitutions prohibit the Legislature from enacting laws that impair the obligation of contract. Raiding \$2.05 billion in redevelopment funds will jeopardize bond covenants and other contractual obligations entered into by many redevelopment agencies creating an unconstitutional impairment of contract. Under Article XVI, Section 16 of the State Constitution, redevelopment agencies irrevocably pledge tax increment to pay bond debt service and other obligations that raise capital for the redevelopment project. By redirecting funds that are pledged to pay back bonds and other creditors, ABX4-26 impairs the contractual pledge of revenues on which redevelopment financing is based.

(more)

Raiding \$2.05 billion in redevelopment funds will kill tens of thousands of jobs, damage our economic recovery and harm local communities.

- The magnitude of this redevelopment raid will force many agencies to stop work on important redevelopment projects, stalling or killing vital economic revitalization, affordable housing, infrastructure and other projects that are critical in a down economy.
- According to an economic analysis prepared for CRA, \$2.05 billion in redevelopment revenues could support 198,000 full- and part-time jobs in the construction and related industries. At a time when California unemployment is more than 12%, these raids are job killers that will further stall our economic recovery.

(Timeline and FAQ on Following Pages)

Timeline of State Raids of Redevelopment Funds and Litigation

September 30, 2008 – State Legislature passes and Governor signs AB 1389, a state budget trailer bill raiding \$350 million of redevelopment funds for state purposes in FY 2008-2009.

December 4, 2008 – California Redevelopment Association (CRA) files lawsuit in Sacramento Superior Court, alleging AB 1389 and redevelopment raids are unconstitutional.

April 30, 2009 – Superior Court rules in favor of CRA, invalidates AB 1389 and says the redevelopment raid, “*violates the intent of section 16 [of the State Constitution], to allocate the tax increment to the financing of redevelopment projects.*” State of California announces it will appeal the decision.

June 15, 2009 – A month-and-a-half after the Superior Court ruled redevelopment raids for state purposes are unconstitutional, the legislative Budget Conference Committee votes to include a \$1.05 billion raid of redevelopment funds in a budget trailer bill (\$350 million/yr for 3 years).

June 2009 – CRA warns legislators and Administration that, despite altered language, budget bills still violate Constitution and proposed redevelopment raids are illegal.

July 24-29, 2009 – Legislature passes and Governor signs ABX4-26 as part of budget package, a devastating \$2.05 billion raid of redevelopment funds this year and next.

September 28, 2009 – State of California drops appeal of 2008 lawsuit, making the April 30 Superior Court decision final and binding.

October 20, 2009 – California Redevelopment Association files second lawsuit in Sacramento Superior Court. Lawsuit challenges constitutionality of ABX4-26 included as part of the 2009 State budget.

FREQUENTLY ASKED QUESTIONS

1) Why is CRA filing this lawsuit?

We are seeking to invalidate ABX4-26 and block the unconstitutional transfer of \$2.05 billion in local redevelopment funds to county Supplemental Educational Revenue Augmentation Funds (SERAF).

In addition to the unconstitutionality of these raids, they will hurt California's economic recovery. Raiding \$2+ billion in redevelopment funds will result in the loss of tens of thousands of jobs and kill needed economic revitalization, affordable housing, and other projects that communities desperately need in this down economy.

2) On what grounds will you sue to invalidate ABX4-26?

Article XVI, Section 16 of the California Constitution states that redevelopment tax increment funds can only be used for specified redevelopment activities, specifically *"to finance or refinance ... the redevelopment project."* Taking redevelopment funds to balance the State's budget – the real purpose of ABX4-26 – does not qualify as a constitutionally permitted use of redevelopment funds and is therefore unconstitutional.

Additionally, raiding \$2.05 billion in redevelopment funds constitutes an unconstitutional impairment of contracts. Under Article XVI, Section 16 of the State Constitution, redevelopment agencies irrevocably pledge redevelopment (tax increment) revenues to pay back bonds and other obligations that raise the capital to fund the redevelopment project. By raiding funds that are pledged to pay back bonds and other creditors, ABX4-26 impairs the contractual pledge of revenues on which redevelopment financing is based.

3) When do you expect a ruling?

We are asking the court for a ruling before May 2010, the date redevelopment agencies must make their 2009-10 payment to the State. While there is no way to predict how long a court proceeding will take, given the magnitude of the raid and the impact it will have on redevelopment agencies, we are hopeful the court will rule sometime in early 2010.

4) Didn't a Superior Court rule that 2008 raids of redevelopment funds are illegal? What has changed?

In April 2009, a Sacramento Superior Court invalidated a proposed 2008 State raid of \$350 million of redevelopment funds, finding that the State raid of redevelopment funds *"violates the intent of section 16 [of the State Constitution], to allocate the tax increment to the financing of redevelopment projects."*

In September 2009, the State of California dropped its appeal of the Superior Court ruling, making that ruling final and binding.

Nothing has changed since that ruling in April. ABX4-26 is likewise unconstitutional because it redirects redevelopment tax increment funds to finance the State's obligation to fund education.

While legislative staff and lawyers changed the wording of the 2009 legislation in an attempt to get around the State Constitution and Superior Court ruling, this raid is *still* unconstitutional. The Legislature cannot change the wording or meaning of the Constitution by statute.

5) The Legislature, Administration and staff say they have written ABX4-26 to address the Superior Court ruling and that the 2009 State Budget raid is legal because funds will only go to schools and students within a redevelopment project area, which furthers the purpose of redevelopment.

We disagree.

In the 2008 lawsuit, the State also claimed the intent was to benefit schools, which purportedly furthers the purpose of redevelopment. The Superior Court judge rejected that argument and found the 2008 raid unconstitutional.

ABX4-26 is also unconstitutional because the purpose of this budget bill is to help balance the State's budget – which does not qualify as a constitutionally-permitted use of redevelopment funds. Under ABX4-26, schools won't receive one dime more than already guaranteed from the State. ABX4-26 simply shifts the obligation from the State to redevelopment agencies.

Further, it is not enough that tax increment be spent within a redevelopment project area. The constitutional requirement is that tax increment be spent to repay indebtedness incurred to finance the redevelopment project. ABX4-26's redirection of tax increment to SERAF fails the constitutional requirement because the revenues diverted are not related or proportional to the cost of any direct benefit to the redevelopment project.

6) Who are the plaintiffs in the case?

The California Redevelopment Association is the main plaintiff along with two local redevelopment agencies, the Union City Redevelopment Agency and the Fountain Valley Redevelopment Agency. John Shirey, Executive Director of CRA, is also a plaintiff as a California taxpayer.

7) Who are the defendants?

The State of California Department of Finance will be the principal defendant in the lawsuit. For technical reasons, we have included county auditors as defendants, since auditors are the officials charged with the transfer of payments from the redevelopment agencies into County Supplemental Educational Revenue Augmentation Funds (SERAF).

8) If you're victorious, won't you blow a \$2 billion hole in our already deficit-ridden budget?

It is the responsibility of state lawmakers to pass a responsible budget that does not rely on gimmicks or illegal raids of funds just as local governments have had to do. We have repeatedly informed the Legislature and Administration that any proposal to shift redevelopment funds to SERAF is unconstitutional and will be challenged.

Given the recent Superior Court ruling in the 2008 lawsuit, legislators and the Administration are fully aware of the constitutional issues surrounding the redirection of redevelopment funds.

The Governor himself is on record agreeing that raiding redevelopment funds is unconstitutional. In 2004, Governor Schwarzenegger signed ballot arguments in the voter information guide in support of Proposition 1A (local government revenue protection). The voter information guide, which was sent to millions of California voters, read: *"Redevelopment agency tax increment revenues are already protected by the State Constitution."*

9) Given the enormity of the State's budget deficit, shouldn't redevelopment be asked to pitch in to solve the crisis?

The irony is that if redevelopment funds were left to be invested in communities, construction workers would be put back to work, suppliers would receive more orders, and small businesses would be assisted. That economic activity would also generate more taxes. Thus, redevelopment investments could be providing much-needed economic stimulus. Instead, the State's action serves to further slow the economy.

Local governments are already facing severe financial hardships due to the down economy and have made difficult decisions locally to balance their own budgets, including laying off staff, eliminating community projects and cutting services. The State must balance its budget without illegally raiding local government funds.

10) Will this impact redevelopment bond and/or credit ratings?

The impairment issue is of great concern to bondholders and redevelopment agencies alike. If the State can alter the finances of an agency after these agencies have entered into covenants/agreements with bondholders, it will have a negative impact on all future bonding.

In fact, a July 2009 analysis by Moody's says "the proposed \$1.7 billion shift from redevelopment agencies ... is of a substantially greater magnitude than might have been anticipated, and it could have a material impact on some redevelopment agencies' overall credit quality."

What's more, by illegally impairing bond contracts, State lawmakers are jeopardizing the integrity of all California state and municipal bonds. After all, bond holders are going to be much less willing to buy California bonds if the Legislature repeatedly jeopardizes repayment of these bonds.

11) How will this impact funds for affordable housing?

For FY 2009-2010, a redevelopment agency may suspend all or part of the required 20% allocation to its low- and moderate-income housing fund in order to make the required payments. If needed, the agency may also borrow accumulated funds from its Housing fund for the FY 2009-10 year only. It cannot do the same for the second year, FY 2010-11.

The Housing Fund must be repaid by June 30, 2015. If the agency fails to repay the Housing Fund, the required allocation of tax increment to the Housing Fund is increased to 25% for most agencies for as long as the project area continues to receive tax increment.

Many agencies will have no alternative but to borrow at least a portion of the SERAF payment from its Housing Fund. This will result in the delay or elimination of many affordable housing projects where redevelopment funding is a key component of the financing, leveraging other State and Federal financing sources.

12) Will schools lose money if you are successful?

No. Schools are constitutionally guaranteed a minimum funding level. ABX4-26 simply (and illegally) shifts the burden for funding schools from the State to redevelopment agencies. If we're successful, the State will have to provide funding to the schools.