



FREQUENTLY ASKED QUESTIONS

About the 2009 State Raid of Redevelopment Funds and Litigation

(Questions about SERAF and payments begin on page 3)

ABOUT THE LAWSUIT

1. Why is the State taking redevelopment money if CRA was successful in last year's lawsuit challenging AB 1389?

CRA was successful in blocking a 2008 proposed shift of \$350 million in redevelopment funds in Sacramento Superior Court, and the State recently abandoned its appeal of the Superior Court ruling, meaning the 2008 raid is unconstitutional and agencies do not need to make the payment.

The State claims the 2009 budget legislation, ABX4-26, fixes the constitutional issues raised by the Superior Court by directing the redevelopment funds to schools with students within the boundaries of a redevelopment agency project area and students living in housing funded by redevelopment. The State claims that funding schools within a redevelopment project area "furthers" the purpose of redevelopment. CRA and its attorneys believe that ABX4-26 is also unconstitutional on the same grounds upon which AB 1389 was successfully challenged, and many additional grounds. Consequently, we've filed a lawsuit in Sacramento Superior Court to invalidate ABX4-26.

2. Does the new legislative language address the constitutional issues and Superior Court ruling?

No. ABX4-26 is unconstitutional because the unquestioned purpose of this budget bill is to help balance the State's budget, not to further the purpose of redevelopment. 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.

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.

3. On what grounds did CRA 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, the State and U.S. Constitutions prohibit the Legislature from enacting laws that impair the obligation of contract. Raiding \$2.05 billion in redevelopment funds could jeopardize bond covenants and other contractual obligations entered into by many redevelopment agencies creating an unconstitutional impairment of contract. (See question #20 below.) Finally, there are a number of other constitutional violations created by ABX4-26.

4. What is the latest on the appeal of last year’s Superior Court ruling.

In September, the State of California abandoned its appeal of the Superior Court ruling that found the 2008 raids were unconstitutional. As a result, the Superior Court decision is final and binding. The 2008 \$350 million raid is unconstitutional and agencies need not make that payment.

5. Who are the attorneys representing CRA in the lawsuit?

The same legal team that successfully represented CRA in the 2008 litigation has been retained. The two firms retained are McDonough Holland & Allen, and Nielsen, Merksamer, Parrinello, Mueller & Naylor.

6. In which court did CRA file the second lawsuit?

We filed in Sacramento Superior Court on October 20, 2009.

7. Instead of filing in Superior Court, why doesn't CRA file its lawsuit against the State directly with the Court of Appeal or the Supreme Court?

CRA's legal team has carefully evaluated where the case should be initially filed. Their judgment is that the case should be filed in Superior Court for the following reasons:

(1) Neither the Supreme Court nor the Court of Appeal is required to accept an original petition for writ of mandate. Most petitions for writ of mandate filed in appellate courts are denied without a ruling on the merits. This is the court's way of saying "start in a lower court." It could, however, take weeks or months for the appellate court to decide whether to accept the petition. If the court did not accept the petition and required it to be filed in a lower court, we would lose time critical to getting a decision before May 10 when payments from agencies are due.

(2) The ability to make a factual record in an appellate court is far more constrained than in the Superior Court. CRA's legal team believes that it will be especially important in this case to make a strong factual record. The best place for doing that is the Superior Court.

(3) As was the case with the AB 1389 litigation, CRA's objective is to obtain a ruling from the Superior Court that will apply to all agencies prior to May 10.

8. Who are the plaintiffs in the case?

The California Redevelopment Association, the Union City Redevelopment Agency and the Fountain Valley Redevelopment Agency are the plaintiffs, as well as John Shirey, CRA Executive Director, in his role as a California taxpayer and citizen.

9. Who are the defendants?

As in the 2008 litigation, the Director of the State of California Department of Finance will be the principal defendant in the lawsuit. For technical reasons, we have once again included county auditors as defendants, since auditors are the ones charged with the transfer of payments from redevelopment agencies into county Supplemental Educational Revenue Augmentation Funds (SERAF).

10. How is CRA going to pay for the lawsuit?

All CRA member agencies have been asked to pay a proportionate share of the costs of the lawsuit similar to what was done for the first lawsuit. CRA will seek an award of attorney fees if it is successful, as it has done in the AB 1389 litigation, but resolution of attorney fees issues likely will not occur until well after the lawsuit is finished.

11. Can my agency sue the State directly without joining the CRA lawsuit?

We strongly recommend that agencies *not* file separate litigation against the State. Multiple suits will lead to greater costs and possible delays in getting a decision from the court.

12. Section 10 of ABX4-26 states that, if a court finds a remittance is not legally permissible for a particular redevelopment agency, such determination has no effect on all other agencies. Does that mean that all agencies must join the lawsuit as plaintiffs in order to block the SERAF transfers?

Since CRA is challenging the constitutionality of ABX4-26, a favorable finding by the court should invalidate the statute in total so that the ruling would benefit all redevelopment agencies as did the AB 1389 ruling.

Given the unusual language in section 10 of ABX4-26, the litigation was filed as a plaintiffs' class action, with the two named redevelopment agencies representing a class of all redevelopment agencies required to make the SERAF payment. This class action is intended to eliminate the need for all individual agencies to join the suit.

ABOUT THE NEW SERAF

13. What is the difference between past ERAF takes and ABX4-26's "SERAF" take?

The structure for the redevelopment fund shift is similar to last year's budget trailer bill, AB 1389. The primary difference is that, in an effort to get around CRA's successful lawsuit, the Legislature created a new county "Supplemental" ERAF (SERAF). Under this new SERAF, redevelopment funds are to be distributed to a K-12 school district(s) or county office of education located partially or entirely within any project area of the agency.

14. How does the new SERAF work?

The funds deposited into the new county SERAF must be distributed to a K-12 school district or county office of education located partially or entirely within any project area of the agency.

- The funds distributed to schools or county offices of education from the SERAF must be used to serve pupils living in the project area or in housing supported by redevelopment funds. *(It is unclear how an agency is supposed to determine how many students are in housing supported by redevelopment funds).*
- The total amount of SERAF funds received by a school district is deemed to be local property taxes and will reduce dollar-for-dollar the State's Prop 98 obligations to fund education.

15. How and when is each Agency's SERAF payment calculated?

The Department of Finance will determine each agency's SERAF payment by November 15 of each year. The formula for calculating the amount each agency must pay is based half on net tax increment (net of pass-throughs to local property taxing entities) and half on gross tax increment. The legislation states that the calculations for FY 2009-10 and FY 2010-11 will be based on State Controller's Office Tax Increment data from FY 2006-07.

On November 12, 2009, Governor Schwarzenegger signed SB 68 (Steinberg) which contains another provision regarding the calculation of SERAF payments. If property within a redevelopment project area was deleted prior to August 1, 2009 and this deletion is not accounted for in the FY 2006-07 State Controller's data, the Department of Finance, in calculating the SERAF payment, must adjust an agency's tax increment revenue to account for the subsequent deletion of the property. The new law allows this adjustment to be made for FY 2009-10 and FY 2010-11 SERAF payments.

CRA has posted an *estimate* of each agency's payment for each fiscal year and a total on its website at www.calredevelop.org. It's important to note that these figures are just estimates based on the implementing legislation. The Department of Finance will produce the official SERAF amount owed by each agency for FY 2009-10 by November 15, 2009.

16. Why does ABX4-26 require the Director of Finance to use 2006-07 data from the State Controller to calculate SERAF payments when 2007-08 data is available?

We do not know if this is intentional or an oversight, but differences in payments are significant depending on which year's State Controller data is used by the Department of Finance.

17. When does my agency have to pay its share of the take?

Payments are due by May 10 of the applicable fiscal year. The legislative body of the redevelopment agency must report to the county auditor by March 1 how it intends to fund the payment.

18. Should I pay my SERAF early?

No. Because of the pending litigation, CRA recommends not making any payments until further notice. CRA will regularly inform its members of the progress of the lawsuit.

19. What funds can I use to make the SERAF payment?

The agency can use any legally available funds to make the SERAF payment. For FY 2009-10, the agency may “suspend” all or part of the required 20% allocation or set aside to its Low- and Moderate-Income Housing Fund (Housing Fund) in order to make the payment.

On November 12, 2009, Governor Schwarzenegger signed SB 68 (Steinberg) which amends ABX4-26 to also allow agencies to use accumulated funds in their Housing Funds to make payments. Important Note: Agencies may use accumulated housing funds for SERAF payments for the FY 2009-10 year only. They 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 by 5 percentage points (to 25% for most project areas) for as long as the project area continues to receive tax increment.

The local legislative body (City Council or County Board of Supervisors) may also lend the SERAF payment to the agency and, in that case, the agency is authorized to repay the legislative body from tax increment.

- The legislative body may make the payment on behalf of the agency.
- The provisions of existing law that permit a joint powers authority (i.e. CSCDA or California Communities) to sell bonds and loan the proceeds to redevelopment agencies in order to make ERAF payments are also available for the 2009-10 and 2010-11 payments.

Lastly, a separate, but overlapping, section of ABX4-26 permits an agency to borrow the amount required to be allocated to the Housing Fund in order to make the SERAF payment.

- This provision apparently applies to fiscal years 2009-10 and 2010-11.
- It requires a finding that there are insufficient non Housing funds to make the SERAF payment. (There is no parallel requirement to make findings for the “suspension” in FY 2009-10.)
- Amounts “borrowed” from the current year allocation to the Housing Fund under this section must also be repaid by June 30, 2015 or June 30, 2016, as applicable.

20. Is the obligation to make the SERAF payment subordinate to obligations to repay bonds and other indebtedness?

Yes. An agency may pay less than the amount required if it finds that it is necessary to make payments on existing obligations required to be committed, set-aside, or reserved by the agency during the applicable fiscal year. An agency that intends to pay less than the required amount in order to pay existing obligations must adopt a resolution prior to December 31, 2009, listing the existing indebtedness and the payments required to be made during the applicable fiscal year.

However, it is important to note that agencies that fail to make their SERAF payments are subject to the “Death Penalty” or “Suspension Penalty” described below.

21. What happens if an agency fails to make its SERAF payment?

An agency failing to timely make its SERAF payment – even if it must do so to pay existing obligations – is subject to the “Death Penalty” as follows:

- An agency may not adopt a new redevelopment plan, amend an existing plan to add territory, issue bonds, further encumber funds, or expend any moneys derived from any source except to pay pre-existing indebtedness, contractual obligations, and 75% of the amount expended on agency administration for the preceding fiscal year.
- This penalty would last until the required SERAF payments have been made.

In addition to suffering the Death Penalty, the agency must increase its housing set-aside by 5 percentage points on July 1, 2010 or July 1, 2011, whichever is applicable, for the remainder of the time the agency receives tax increment.

22. What happens if my agency does not/cannot repay the Housing Fund loan by the required June 2015 or June 2016 deadline?

If the agency fails to repay the Housing Fund, the required allocation of tax increment to the Housing Fund is increased by 5 percentage points (to 25% for most project areas) for as long as the project area continues to receive tax increment.

23. Do I have to pay interest on the use of our current year housing set-aside funds to make the SERAF payment?

No.

24. Can I borrow from the accumulated balance in the Housing Fund to make the SERAF payment?

Yes. When ABX4-26 was passed, its provisions only allowed the agency to borrow from its current year’s allocation to the Housing Fund. However, SB 68, which was signed into law November 12, also allows agencies to borrow from the accumulated funds in their Housing Fund to the extent this reduction in funds does not impair executed contracts. Important Note: Agencies may use accumulated housing funds for SERAF payments for the FY 2009-10 year only. They cannot do the same for the second year, FY 2010-11.

25. Can SERAF payments be made with bond proceeds?

Agencies in all cases should first consult with their bond counsel. But the general rule is if the bonds are tax-exempt, you may not make SERAF payments with bond proceeds. If the bonds are taxable, you likely can use proceeds to make your SERAF payment. Again, each agency must consult with bond counsel to make a final determination.

26. What happens to redevelopment funds being accumulated in order to finance a longer-term project?

Under ABX4-26, an agency must make its full required SERAF payments using any available funds, and that includes funds being accumulated in order to fund a project.

27. If my agency pays on time, does the legislation authorize a one-year extension of our project area plan?

Yes. If an agency makes its full payment on time for the current fiscal year, FY 2009-2010, time limits on plans can be extended by one year. Extensions cannot be enacted until after the required payment has been made. This one-year extension does not apply to the second year payment in FY 2010-11.

28. Do funds paid to SERAF count against my project area dollar cap?

Yes. Unlike previous ERAF shifts, ABX4-26 makes no provision for excluding payments from the limit on receipt of tax increment.

29. Should I include the SERAF payment in my annual Statement of Indebtedness?

While ABX4-26 does not go into effect until October 23, 2009 and payments are technically not an indebtedness of the agency until that date, we are advising agencies to include the required SERAF payment in their next SOI.

30. I am currently updating the Five-Year Implementation Plan. Given the pending litigation, how do I write the plan not knowing whether the SERAF payments will have to be made?

There is no one answer to this question and opinions will vary. CRA suggests that your agency develop its implementation plan based on the assumption that there will be no SERAF and then include a paragraph at the end stating that programs may have to be curtailed if and to the extent a SERAF take is imposed by the State.