



City of
Santa Monica®

Office of the City Attorney
City Hall
1685 Main Street
PO Box 2200
Santa Monica, California 90407-2200

Marsha Jones Moutrie
City Attorney

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Via Federal Express and E-Mail

Pedro R. Reyes, Chief Deputy Director
Department of Finance
915 L Street, Floor 8
Sacramento, CA 95814

Mark Hill, Project Budget Management
Department of Finance
915 L Street, Floor 8
Sacramento, CA 95814

Jennifer K. Rockwell, Chief Counsel
Department of Finance
915 L Street, Floor 8
Sacramento, CA 95814

Wendy L. Watanabe, Auditor-Controller
County of Los Angeles, Department of
Auditor-Controller
500 West Temple Street, Room 525
Los Angeles, California 90012-3873

Re: ***Implementation of Health and Safety Code section 34183.5***

Dear Department of Finance Administrators and County Auditor-Controller:

Our office represents the City of Santa Monica ("City") in its capacity as the Successor Agency ("Successor Agency") to the former Santa Monica Redevelopment Agency ("RDA") in accordance with AB1x 26.

On or about June 27, 2012, the Governor signed Assembly Bill 1484 ("AB 1484"), which was passed as clean up legislation to AB1x 26. While the Successor Agency objects to numerous provisions of AB 1484, this letter specifically addresses our objection to the provision of AB 1484 that requires the Successor Agency to remit amounts allegedly due to affected taxing entities under Health and Safety Code section 34183.5. The Successor Agency made a payment to the County Auditor-Controller on July 12, 2012 under protest and is now following up its payment with a more detailed protest letter.

BACKGROUND

AB1x 26

AB1x 26, a portion of which is codified in part 1.85 of the Health and Safety Code ("HSC"), requires each county auditor-controller to deposit a certain amount of property taxes into a real property tax trust fund ("RPTTF") on behalf of each successor agency within the state. The property taxes deposited into the RPTTF are then subject to distribution according to a "waterfall" formula that benefits affected taxing entities (those entities that levy property taxes within a redevelopment project area)(also known as "ATEs"), once all authorized expenditures have been made from the RPTTF. AB1x 26, as originally enacted, required these taxes to be

deposited by county auditor-controllers into the RPTTF on January 16, 2012 for payments listed in each successor agency's recognized obligation payment schedule ("ROPS") for the six month fiscal period, beginning January 1, 2012.

AB1x 26 also changed the character of ad valorem property taxes allocated to the former redevelopment agencies. Before part 1.85 went into effect, ad valorem property taxes (referenced herein as "tax increment") were allocated to redevelopment agencies under Article XVI, section 16 of the California Constitution. After part 1.85 went into effect, ad valorem property taxes were allocated to the successor agencies under Article XII A, section 1 of the California Constitution (referenced herein as "property taxes"). The distinction is relevant because the allocation of tax increment is subject to certain constitutional restrictions that do not apply to property tax revenues.

Reformation of AB1x 26

After enactment of AB1x 26 in June 2011, the California Redevelopment Association challenged AB1x 26 directly with the California Supreme Court in the case named *California Redevelopment Association v. Matosantos et al.* (2011) 53 Cal.4th 231. Recognizing that the court's consideration of the issues resulted in the passage of certain statutory deadlines in AB1x 26 before a final decision was rendered, the court reformed the effective dates in part 1.85 arising before May 1, 2012, to take effect four months later.

AB1x 26 originally contemplated that redevelopment agencies would be supplanted by successor agencies on October 1, 2011, and county auditor-controllers would be collecting and distributing residual property taxes to the ATEs pursuant to HSC 34183(a) after October 1, 2011. The Supreme Court's ruling extended these dates so that redevelopment agencies would not be supplanted by successor agencies until February 1, 2012, and county auditor-controllers would not be distributing residual property taxes to the ATEs until after February 1, 2012.

AB 1484

AB 1484 was enacted as clean-up legislation to AB1x 26. Among other things, AB 1484 added Section 34183.5 to the Health and Safety Code, which requires successor agencies to make residual property tax payments to the affected taxing entities by July 12, 2012, based upon demand notices issued by county auditor-controllers on July 9, 2012.

To coerce the successor agencies and their host cities into making these residual property tax payments, Section 34183.5 imposes a civil penalty on both a successor agency and its host city in the amount of 10 percent of the amount allegedly owed to affected taxing entities, and requires the withholding of the city's share of sales and use tax scheduled for distribution on July 18, 2012, or any subsequent payment, until the residual property tax payment is made (referenced hereinafter as "the off-set").

Unlike other provisions of AB 1484, which offer a successor agency the ability to dispute remittance amounts before any penalties or off-sets are imposed, Section 34183.5 requires full payment within three (3) days and no opportunity for administrative appeal before a civil penalty or the off-set is imposed.

AB 1484 also modified the definition of "administrative cost allowance". Section 34177(b) originally defined "administrative cost allowance" as "5 percent of the property tax allocated to the successor agency for the 2011-12 fiscal year". AB 1484 modified this definition to provide that the "administrative cost allowance" is "5 percent of the property tax allocated to the successor agency on the *Recognized Obligation Payment Schedule covering the period January 1, 2012 through June 30, 2012*". The difference is that the amount of property tax allocated on the Recognized Obligation Payment Schedule ("ROPS") for January - June 2012 was significantly less than the amount allocated to the successor agency for the 2011-12 fiscal year. While the AB1x 26 definition of "administrative cost allowance" applied at the time that the DOF reviewed the January – June 2012 ROPS, the DOF ignored this definition and applied the formula that is now codified in AB 1484.

DOF review of the January – June 2012 ROPS

Before part 1.85 went into effect, the Redevelopment Agency of the City of Santa Monica ("RDA") received tax increment remittances from the Los Angeles County Auditor-Controller for property taxes collected and distributed to the RDA during the period of November 2011 – January 2012. The County Auditor-Controller did not deposit these remittance amounts into the RPTTF because part 1.85 of the Health and Safety Code was not in effect when these taxes were collected and distributed to the RDA. Similarly, the RDA did not have any obligation under AB1x 26 to make residual payments to the affected taxing entities from the tax increment distributed to the RDA during the November 2011 – January 2012 period because HSC section 34183(a)(4) was not in effect until after February 1, 2012. Accordingly, the RDA made payments pursuant to the Enforceable Obligation Payment Schedule ("EOPS") that was in effect during this period, per HSC section 34169.

After part 1.85 went into effect, the property taxes collected by the County for the period February – May 2012 were deposited into the Santa Monica Successor Agency's RPTTF and then distributed by the County Auditor-Controller in the June 1, 2012 distribution. The County Auditor-Controller withheld statutory pass through and made residual payments from the amounts deposited into the RPTTF, as required by HSC section 34183(a).

In accordance with part 1.85, the Successor Agency submitted the ROPS for February – June 2012 to the Oversight Board and DOF for approval in April 2012. The Successor Agency omitted the January payments from the ROPS because the EOPS was still in effect in January 2012 and the Successor Agency was not in existence until February 1, 2012 per the Supreme Court's reformation of AB1x 26. After its review, the DOF issued correspondence to the Successor Agency, stating that the ROPS for the entire period would be denied until the

Successor Agency resubmitted the ROPS with January 2012 payments. The Successor Agency complied with this demand under protest. The DOF then denied a January \$4,065,000 payment on the ROPS that the DOF failed to disapprove through the EOPS process per AB1x 26, which payment had already been made to the Santa Monica-Malibu School District ("School District") by the time the Successor Agency submitted its ROPS to the DOF for approval in April 2012. The DOF also applied the "administrative cost allowance" of 5 percent of property taxes allocated to the Successor Agency on the ROPS, instead of the property taxes allocated to the Successor Agency in fiscal year 2011-12, as provided in the version of HSC section 34171 that was in effect at the time of DOF's review. The DOF's misapplication of the "administrative cost allowance" definition decreased the amount of property taxes allocated to the Successor Agency by \$847,973, despite the fact that this amount represented administrative costs incurred by the former RDA prior to February 1, 2012.

County Auditor Controller Remittance per AB 1484

In accordance with AB 1484 (HSC section 34183.5), on July 9, 2012, the County Auditor-Controller issued a remittance to the Successor Agency for a residual property tax payment to the affected taxing entities in the amount of \$12,645,547.72 ("Residual Payment"). The Residual Payment was calculated by deducting the amounts approved for payment by the DOF on the January – June 2012 ROPS from the gross tax increment collected by the County Auditor-Controller and remitted to the RDA in November 2011 – January 2012, before part 1.85 was in effect. The Residual Payment thus includes the payment amounts on the January – June 2012 ROPS that were disapproved by the DOF, including the \$4,065,000 payment that was already paid to the School District in January 2012 and the \$847,973 that was already expensed by the RDA during November 2011 – January 2012.

I.

The County's and/or DOF's implementation of Section 34183.5 conflicts with the California Supreme Court reformation of AB1x 26.

As noted earlier in this letter, the California Supreme Court reformed several deadlines for performance of obligations in part 1.85 of the Health and Safety Code, as follows:

Accordingly, we exercise our power of reformation and revise each effective date or deadline for performance of an obligation in part 1.85 of division 24 of the Health and Safety Code (§§ 34170-34191) arising before May 1, 2012 to take effect four months later....

Where a provision imposes obligations in both this and subsequent fiscal years, we reform the provision only as it relates to obligations arising before May 1, 2012. Thus, for example, section 34183 requires certain calculations from county auditor-controllers by January 16, 2012 and June 1, 2012, for this fiscal year, and

on January 16 and June 1 in subsequent years. (§ 34183, subd. (a).) *We reform the January 16, 2012 deadline by extending it to May 16, 2012, and leave the remaining deadlines unchanged. (Emphasis added.)*

California Redevelopment Association v. Matosantos (2011) 53 Cal.4th 231.

Because the California Supreme Court postponed the redevelopment agency dissolution date from October 1, 2011 to February 1, 2012, redevelopment agencies throughout the state continued to operate using tax increment collected and distributed by the county auditor-controllers before February 1, 2012. Similarly, many of the operative provisions of part 1.85, including the definitions of “enforceable obligation” and “administrative cost allowance” in HSC section 34171 were not applicable until February 1, 2012.

Health and Safety Code section 34183.5, which was added by AB 1484, purports to apply the Section 34183(a) waterfall distribution to tax increment collected by the county auditor-controllers and distributed to redevelopment agencies before February 1, 2012. It also purports to impose the HSC section 34171 definition of “administrative cost allowance” to limit the RDA’s operating costs, before that definition became effective on February 1, 2012.

Legislation that purports to undo a final judgment constitutes a violation of Article III, Section 3 of the California Constitution (separation of powers clause). *See, e.g., Mandel v. Myers*, 29 Cal.3d 531, 547 (1981). After giving full consideration to the future implementation of AB1x 26, the Supreme Court extended all statutory deadlines contained in part 1.85 and arising before May 1, 2012. *Matosantos* at 274-276. The Supreme Court’s decision was deemed as final by the court “forthwith”. *Id.* at 276. The aforementioned provisions of AB 1484 retroactively impose part 1.85 obligations on the former RDA and thus conflict with the Supreme Court’s reformation AB1x26. *Id.* These provisions thus violate Article III, Section 3 of the California Constitution.

II.

The County’s and/or DOF’s implementation of Section 34183.5 constitutes an unlawful attempt to implement AB 1484 retroactively.

The California Supreme Court recently ruled that legislative enlargement of a limitations period does not revive lapsed claims in the absence of express language of revival. *Quarry et. al. v. Doe I*, 53 Cal. 4th 945 (2012). In so holding, the court applied the rule that in construing statutes there is a presumption against retroactive application unless the Legislature has plainly directed otherwise by means of express language of retroactivity or other sources that provide a clear and unavoidable intent that the Legislature intended retroactive application. *Quarry* at 957. The court further stated that such express language must be unmistakable, rather than merely suggestive or implied. *Quarry* at 958.

As discussed, above, AB 1484 unlawfully purports to apply certain provisions of AB 1484 retroactively. AB 1484 modified the definition of "administrative cost allowance" in HSC section 34171(b) to limit the amount of administrative costs that could be claimed by a Successor Agency on the ROPS. There is no language in this section or in any other part of AB 1484 that suggests an intent to apply this limitation before the Successor Agency became a legal entity. Consequently, there is no express language in that section which unmistakably evidences any legislative intent to apply this definition to property revenues distributed to the RDA before part 1.85 became effective. Moreover, by its express terms, the definition of "administrative cost allowance" applies to the *successor agency's* administrative expenditures rather than the former *redevelopment agency's* administrative expenditures, thus contradicting any assertion that the Legislature intended to apply this definition to tax increment distributed to the RDA before part 1.85 was in effect.

Similarly, the tax increment revenues collected by the county auditor-controller during November 2011 – January 2012 were distributed to the former RDA without the limitations imposed by part 1.85. Nothing in AB 1484 evidences any intent to retroactively apply part 1.85, including the residual distribution of property tax revenues required by Section 34183(a), to tax increment revenues received by the RDA before part 1.85 became effective. As such, neither the definition of "administrative cost allowance" nor the residual distribution under HSC section 34183(a) should have any application to tax increment revenue distributed to the RDA before February 1, 2012.

The Residual Payment should have excluded any revenues distributed to the former RDA in November 2011 – January 2012. But even if any portion of the Residual Payment is determined to be valid, the Successor Agency should receive a credit for the administrative expenses incurred by the former RDA before February 1, 2012 and for the payment made to the School District in January under the EOPS in effect during that time.

III.

The off-set provision in Section 34183.5 constitutes a violation of article 13, section 25.5 of the California Constitution.

Proposition 1A

Proposition 1A was a California ballot proposition that was approved by voters on November 2, 2004.

The passage of Proposition 1A added Article 13, Section 25.5 to the California Constitution. It provides, in pertinent part, that on or after November 3, 2004, the Legislature shall not enact a statute that either modifies the way in which ad valorem property tax revenues are allocated to local agencies (including cities), based upon November 3, 2004 allocations, *or* changes the method of distributing Bradley-Burns sales and use taxes to cities and counties, *or*

changes the pro rata shares in which property tax revenues are allocated among local agencies, except by a two-thirds vote in each house.

According to the voter's pamphlet, this proposition intended to prevent revenues collected by local governments (cities, counties, and special districts) from being transferred to the state for statewide use.

Section 34183.5 mandates that *the City's* share of sales taxes distributed on July 18, 2012 be withheld if the *Successor Agency* fails to make the Residual Payment. The mandate alters the manner in which sales taxes are distributed to the City, and thus constitutes a violation of Proposition 1A.

Proposition 22

Proposition 22, the Local Taxpayer, Public Safety, and Transportation Protection Act, was approved by the voters on November 2, 2010. The passage of Proposition 22 amended Article 13, Section 25.5 of the California Constitution by preventing the legislature from requiring the transfer of property taxes allocated to a redevelopment agency under Article XVI, Section 16 of the California Constitution to either the state or other local taxing entities. The stated goal of Proposition 22 was to protect existing funds that are allocated to local government, public safety, and transportation, including redevelopment agencies.

AB1x 26 (HSC section 34182(c)(1) effectively deemed all ad valorem tax revenues received by the Successor Agency as property tax revenues within the meaning of subdivision (a) of Section 1 of Article XIII A of the California Constitution *upon dissolution of the RDA*. As discussed above, the RDA was not dissolved until February 1, 2012. Consequently, the Legislature's attempt to require the Successor Agency to pay to the ATEs tax increment allocated to the RDA before part 1.85 went into effect constitutes a violation of Proposition 22.

AB1x 26 (HSC section 34182(c)(3) also authorizes the withholding of civil penalties from the City's share of property taxes under HSC section 34183(a)(4) and authorizes the redistribution of such penalties to the other ATEs, without due process, and in violation of Proposition 22.

IV.

The off-set provision in Section 34183.5 improperly interferes with the City's conduct of its municipal affairs.

As described above, in order to coerce successor agencies and cities into making the residual waterfall payments under HSC section 34183.5 by July 9, 2012, AB 1484 imposes concurrent civil penalties on both successor agencies *and cities*, and additionally authorizes the DOF to direct the State Board of Equalization to withhold cities' share of sales taxes until the

remittances are made. Given the current reduction in general fund revenues and increasing general fund obligations, the off-set threatens the City's ability to run its municipal affairs. To the extent that the off-set is merely a threat, such threat reduces the City's perceived credit worthiness (as most recently evidenced by Moody's statewide bond rating downgrades), which, in turn, interferes with the City's ability to issue bond funds or, alternatively, reduces the amount of bonds that can be issued for municipal improvements. To the extent that the off-set is applied, it reduces general fund revenue previously budgeted and would leave the City with the Hobson's choice of either reducing its services (including police and fire) or failing to pay its third party contracts. The Legislature's overreaching into the City's municipal affairs is all the more egregious, considering the constitutional violations discussed, above.

In closing, our office sends this letter to clearly delineate the Successor Agency's position with respect to certain provisions of AB 1484. The issues raised in this letter are not intended to be exhaustive of the legal grounds for payment under protest. The Successor Agency made the Residual Payment to mitigate damages to the City, and did not intend to waive any constitutional, statutory, legal, or equitable rights by making the payment. It expressly reserved and continues to reserve any and all rights, privileges, and defenses available whether existing under law or equity.

Very truly yours,


MARSHA JONES MOUTRIE
City Attorney

MJM/bcm

cc: Ms. Kristina Burns, Program Specialist III, Los Angeles County
Rod Gould, City Manager, City of Santa Monica
Joseph Lawrence, Assistant City Attorney
Andy Agle, Director of Housing and Economic Development, City of Santa Monica
Gigi Decavalles, Finance Director, City of Santa Monica
Alan Seltzer, Chief Deputy City Attorney, City of Santa Monica
Susan Y. Cola, Deputy City Attorney, City of Santa Monica
Murray O. Kane, Special Counsel, Kane Ballmer & Berkman