

REDEVELOPMENT AGENCY OF THE CITY OF SANTA CRUZ

ASSET TRANSFER REVIEW

Review Report

January 1, 2011, through January 31, 2012



JOHN CHIANG
California State Controller

July 2014



JOHN CHIANG
California State Controller

July 7, 2014

Martin Bernal, City Manager
Redevelopment/Successor Agency of the City of Santa Cruz
809 Center Street, Room 10
Santa Cruz, CA 95060

Dear Mr. Bernal:

Pursuant to Health and Safety Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the Redevelopment Agency of the City of Santa Cruz (RDA) to the City of Santa Cruz (City) or any other public agency after January 1, 2011. This statutory provision states, "The Legislature hereby finds that a transfer of assets by a redevelopment agency during the period covered in this section is deemed not to be in furtherance of the Community Redevelopment Law and is thereby unauthorized." Therefore, our review included an assessment of whether each asset transfer was allowable and whether the asset should be turned over to the Successor Agency.

Our review applied to all assets including, but not limited to, real and personal property, cash funds, accounts receivable, deeds of trust and mortgages, contract rights, and rights to payment of any kind. We also reviewed and determined whether any unallowable transfers of assets to the City or any other public agencies have been reversed.

Our review found that the Santa Cruz Redevelopment Agency (RDA) transferred \$81,894,784 in assets after January 1, 2011, including unallowable transfers to the City of Santa Cruz totaling \$7,733,444 or 9.44% of transfers.

However, on March 31, 2011, the City turned over \$6,714,642 in cash to the RDA. Therefore, the remaining \$1,018,802 in unallowable transfers must be turned over to the Successor Agency.

If you have any questions, please contact Elizabeth González, Bureau Chief, Local Government Compliance Bureau, by telephone at (916) 324-0622.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/kw

cc: Bonnie Lipscomb, Executive Director
City of Santa Cruz
Kim Wigley, Senior Accountant
City of Santa Cruz
Mary Jo Walker, CPA, Auditor-Controller
County of Santa Cruz
Cynthia Mathews, Oversight Board Chairperson
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Asset Transfer Review Report

Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the Redevelopment Agency of the City of Santa Cruz (RDA) after January 1, 2011. Our review included, but was not limited to, real and personal property, cash funds, accounts receivable, deeds of trust and mortgages, contract rights, and rights to payments of any kind from any source.

Our review found that the RDA transferred \$81,894,784 in assets after January 1, 2011, including unallowable transfers to the City of Santa Cruz totaling \$7,733,444 or 9.44% of transfers.

However, on March 31, 2011, the City turned over \$6,714,642 in cash to the RDA. Therefore, the remaining \$1,018,802 in unallowable transfers must be turned over to the Successor Agency.

Background

In January of 2011, the Governor of the State of California proposed statewide elimination of redevelopment agencies (RDAs) beginning with the fiscal year (FY) 2011-12 State budget. The Governor's proposal was incorporated into Assembly Bill 26 (ABX1 26, Chapter 5, Statutes of 2011, First Extraordinary Session), which was passed by the Legislature, and signed into law by the Governor on June 28, 2011.

ABX1 26 prohibited RDAs from engaging in new business, established mechanisms and timelines for dissolution of the RDAs, and created RDA Successor Agencies to oversee dissolution of the RDAs and redistribution of RDA assets.

A California Supreme Court decision on December 28, 2011 (*California Redevelopment Association et al. v. Matosantos*), upheld ABX1 26 and the Legislature's constitutional authority to dissolve the RDAs.

ABX1 26 was codified in the Health and Safety (H&S) Code beginning with section 34161.

H&S Code section 34167.5 states in part, ". . . the Controller shall review the activities of redevelopment agencies in the state to determine whether an asset transfer has occurred after January 1, 2011, between the city or county, or city and county that created a redevelopment agency or any other public agency, and the redevelopment agency."

The SCO identified asset transfers that occurred after January 1, 2011, between the RDA, the City, and/or other public agencies. By law, the SCO is required to order that such assets, except those that already had been committed to a third party prior to June 28, 2011, the effective date of ABX1 26, be turned over to the Successor Agency. In addition, the SCO may file a legal action to ensure compliance with this order.

Objective, Scope, and Methodology

Our review objective was to determine whether asset transfers that occurred after January 1, 2011, and the date upon which the RDA ceased to operate, or January 31, 2012, whichever was earlier, between the city or county, or city and county that created an RDA, or any other public agency, and the RDA, were appropriate.

We performed the following procedures:

- Interviewed Successor Agency personnel to gain an understanding of the Successor Agency operations and procedures.
- Reviewed meeting minutes, resolutions, and ordinances of the City, the Successor Agency, the Oversight Board, and the RDA.
- Reviewed accounting records relating to the recording of assets.
- Verified the accuracy of the Asset Transfer Assessment Form. This form was sent to all former RDAs to provide a list of all assets transferred between January 1, 2011, and January 31, 2012.
- Reviewed applicable financial reports to verify assets (capital, cash, property, etc.).

Conclusion

Our review found that the Redevelopment Agency of the City of Santa Cruz transferred \$81,894,784 in assets after January 1, 2011, including unallowable transfers to the City of Santa Cruz totaling \$7,733,444 or 9.44% of transfers.

However, on March 31, 2011, the City turned over \$6,714,642 in cash to the RDA. Therefore, the remaining \$1,018,802 in unallowable transfers must be turned over to the Successor Agency.

Details of our findings are described in the Finding and Order of the Controller section of this report.

Views of Responsible Officials

We issued a draft review report on March 10, 2014. Martin Bernal, City Manager, responded by letter dated March 21, 2014, disagreeing with the review results. The City's response is included in this final review as an attachment.

Restricted Use

This report is solely for the information and use of the City, the Successor Agency, the Oversight Board, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record when issued final.

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

July 7, 2014

Finding and Order of the Controller

FINDING— Unallowable asset transfers to the City of Santa Cruz

The Redevelopment Agency of the City of Santa Cruz (RDA) made unallowable asset transfers of \$7,733,444, described in Schedule 1, to the City of Santa Cruz (City). The asset transfers occurred after January 1, 2011, and were not contractually committed to a third party prior to June 28, 2011.

Unallowable asset transfers consisted of the following:

- On February 28, 2011, the RDA transferred cash, totaling \$860,802, to the City as a final repayment of an advance from the City to the RDA for the Mission Street Utility Undergrounding Project. Of this total, \$832,899.42 was principal and \$27,902.13 was loan interest.
- On March 9, 2011, the RDA conveyed two properties (APNs 009-363-42 and 005-144-14), valued at \$158,000, to the City.
- On March 9, 2011, the RDA transferred cash to the City totaling \$6,714,642. The individual transfers are as follows:
 - \$291,892 for the Pacific-Beach Streetscape project
 - \$2,850,000 for the Riverside Avenue improvements
 - \$3,572,750 for a prepayment of a cooperative agreement between the City and the RDA

However, on March 31, 2011, the City reversed \$6,714,642 in unallowable transfers. Therefore no further action is necessary.

Pursuant to Health and Safety (H&S) Code section 34167.5, the RDA may not transfer assets to a city, county, or city and county after January 1, 2011, unless the assets are contractually committed to a third party prior to June 28, 2011.

Order of the Controller

Pursuant to H&S Code section 34167.5, the City is ordered to reverse the assets transferred totaling \$7,733,444. However, the City reversed transfers in the amount of \$6,714,642. Therefore, only assets in the amount of \$1,018,802 are to be reversed and turned over to the Successor Agency. The Successor Agency is directed to properly dispose of the assets in accordance with H&S Code sections 34177 (d) and (e) and 34181(a).

City's Response to Draft Report

(Attachment 1 contains a copy of the City's response).

The City disagreed with SCO's draft finding, stating that the transfer of \$860,802 under question by the SCO relates to an enforceable obligation and was legally permissible at the time of the transfer. However, the City stated that the Successor Agency has received a Finding of Completion,

dated November 20, 2013. If necessary, the Successor Agency will place the enforceable obligation before the Oversight Board for approval.

The City also stated in its response that the SCO's draft finding and order to reverse the tax increment received by the former RDA violates Proposition 22 in various respects.

In addition, the City believes that as the SCO's draft findings are the subject of several pending lawsuits, the City should retain the disputed funds until the issues are resolved by the courts.

SCO Comment

The SCO agrees that the former RDA paid off an outstanding loan obligation to the City of Santa Cruz for the Mission Street Undergrounding project.

However, the SCO's authority under H&S Code section 34167.5 extends to all assets transferred after January 1, 2011, by the RDA to the city or county, or city and county that created the RDA, or any other public agency. This responsibility is not limited by the other provisions of the RDA dissolution legislation.

Pending litigation does not preclude the City from turning over unallowable asset transfers to the Successor Agency pursuant to H&S Code section 34167.5.

The finding and Order of the Controller remains as stated.

**Schedule 1—
Summary of Asset Transfers to the
City of Santa Cruz after January 1, 2011**

Transfer Date	Description	Total	Allowable	Unallowable	Adjustments	Clawback
February 28, 2011	Transfer of cash to City (Advance Pay-off)	\$ 860,801	\$ —	\$ 860,802	\$ —	\$ 860,802
March 9, 2011	Transfer of properties to the City	158,000	—	158,000	—	158,000
March 9, 2011	Transfer of cash to City (City-Agency Cooperative Agreements)	6,714,642	—	6,714,642	6,714,642	—
February 1, 2012	Current Assets transferred to Successor Agency	60,855,944	60,855,944	—	—	—
February 1, 2012	Properties transferred to Successor Agency	13,305,397	13,305,397	—	—	—
		<u>\$ 81,894,784</u>	<u>\$ 74,161,341</u>	<u>\$ 7,733,444</u>	<u>\$ 6,714,642</u>	<u>\$ 1,018,802</u> ¹
			90.56%	9.44%		

¹ See the Finding and Order of the Controller section.

**Attachment—
City's Response to
Draft Review Report**



OFFICE OF THE CITY MANAGER

809 Center Street, Room 10, Santa Cruz, CA 95060 • (831) 420-5010 • Fax: (831) 420-5011 • www.cityofsantacruz.com

March 21, 2014

Ms. Elizabeth Gonzalez, Chief
Local Government Compliance Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

RE: State Controller's Office Review of Asset Transfers by the Redevelopment Agency of the City of Santa Cruz

Dear Ms. Gonzalez:

I am in receipt of your letter dated March 10, 2014 regarding the State Controller's Office (SCO) review of asset transfers by the Redevelopment Agency of the City of Santa Cruz (Agency). Pursuant to your request, please find below comments related to the draft report by the SCO to be considered prior to and incorporated into the final report.

The transfer of \$860,802 under question by the SCO relates to an enforceable obligation that is not disputed by the Department of Finance. As was legally permissible at the time of transfer, the former Agency paid off an outstanding loan obligation to the City of Santa Cruz for the Mission Street Undergrounding Project. Additionally, as is allowable under AB 1484, a former Agency upon receiving a Finding of Completion may place any enforceable obligation between the Agency and the City before the Oversight Board for approval. The Successor Agency received a Finding of Completion from the Department of Finance on November 20, 2013. Should the process be necessary, the Successor Agency will place the enforceable obligation before the Oversight Board for approval at the next regularly scheduled meeting of the Oversight Board.

Ms. Elizabeth Gonzalez
March 21, 2014
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To the extent your order requires the transfer of tax increment received by the former Agency prior to its dissolution, we believe the order violates Proposition 22, which provides, in part: “[T]he Legislature shall not . . . [r]equire a community redevelopment agency . . . to pay, remit, loan, or otherwise transfer, directly or indirectly, taxes on ad valorem real property and tangible personal property allocated to the agency pursuant to Section 16 of Article XVI to or for the benefit of the State, any agency of the State, or any jurisdiction.” (Cal. Const., Art. XIII, Sec. 25.5(a)(7).) Interpreting this language, the California Supreme Court in *California Redevelopment Association v. Matosantos* (2011) 53 Cal. 4th at p. 261-262 held: “[I]f the Legislature exercises its constitutional power to authorize allocation of property taxes to redevelopment agencies, and if a redevelopment plan so provides, then those taxes so allocated to an operating redevelopment agency may not be restricted to benefit the state by any further legislative action.”

This issue is currently the subject of several pending lawsuits. (See, e.g., *City of Brentwood v. California Department of Finance*, Sacramento Superior Court No. 34-2013-80001568.) Until this issue is finally resolved by the Courts, we believe that the City should retain the disputed funds.

Sincerely,



Martin Bernal
City Manager

cc: Bonnie Lipscomb, Successor Agency Director

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874**

<http://www.sco.ca.gov>