

SOUTH PASADENA REDEVELOPMENT AGENCY

ASSET TRANSFER REVIEW

Review Report

January 1, 2011, through January 31, 2012



JOHN CHIANG
California State Controller

November 2014



JOHN CHIANG
California State Controller

November 17, 2014

Sergio Gonzalez, City Manager
South Pasadena Redevelopment/Successor Agency
1414 Mission Street
South Pasadena, CA 91030

Dear Mr. Gonzalez:

Pursuant to Health and Safety Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the South Pasadena Redevelopment Agency (RDA) to the City of South Pasadena (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 to the City or any other public agency have been reversed.

Our review found that the RDA transferred \$4,224,273 in assets after January 1, 2011, including an unallowable transfer to the City totaling \$253,250, or 6% of transferred assets. These assets must be turned over to the Successor Agency.

If you have any questions, please contact Elizabeth González, 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: David Batt, Finance Director
South Pasadena Redevelopment/Successor Agency
Gary E. Pia, Chair
Oversight Board
South Pasadena/Redevelopment Successor Agency
John Naimo, Auditor-Controller
County of Los Angeles
David Botelho, Program Budget Manager
California Department of Finance
Richard J. Chivaro, Chief Legal Counsel
State Controller's Office
Elizabeth González, Bureau Chief
Division of Audits, State Controller's Office
Betty Moya, Audit Manager
Division of Audits, State Controller's Office
Venus Sharifi, Auditor-in-Charge
Division of Audits, State Controller's Office
Gerry Kwan, Auditor
Division of Audits, State Controller's Office

Contents

Review Report

Summary	1
Background	1
Objective, Scope, and Methodology	2
Conclusion	2
Views of Responsible Officials	2
Restricted Use	2
Finding and Order of the Controller	3
Attachment—City’s Response to Draft Review Report	

Asset Transfer Review Report

Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the South Pasadena Redevelopment Agency (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 \$4,224,273 in assets after January 1, 2011, including an unallowable transfer to the City of South Pasadena totaling \$253,250, or 6% of transferred assets. These assets 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 and oversight boards 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 an asset transfer that occurred after January 1, 2011, between the RDA, the City and/or any other public agency. 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's operations and procedures.
- Reviewed meeting minutes, resolutions, and ordinances of the City, the RDA, the Successor Agency, and the Oversight Board.
- 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 South Pasadena Redevelopment Agency transferred \$4,224,273 in assets after January 1, 2011, including an unallowable transfer to the City of South Pasadena totaling \$253,250, or 6% of transferred assets. These assets must be turned over to the Successor Agency.

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

Views of Responsible Officials

We issued a draft report on August 14, 2014. Sergio Gonzalez, City Manager, responded by letter dated September 2, 2014, disagreeing with the review results. The City's response is included in this final review report as an attachment.

Restricted Use

This report is solely for the information and use of the City of South Pasadena, 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

November 17, 2014

Finding and Order of the Controller

**FINDING—
Unallowable asset
transfer to the City
of South Pasadena**

The South Pasadena Redevelopment Agency (RDA) made an unallowable asset transfer of \$253,250 to the City of South Pasadena (City). The transfer occurred after January 1, 2011, and the assets were not contractually committed to a third party prior to June 28, 2011.

On March 2, 2011, the RDA transferred \$253,250 in cash to the City's Water Fund for repayment of principal and interest under a loan agreement dated February 21, 1996, between the RDA and the City Water Fund.

Pursuant to Health and Safety (H&S) Code section 34167.5, the RDA may not transfer assets to a city, county, city and county, or any other public agency after January 1, 2011. The assets must be turned over to the Successor Agency for disposition in accordance with H&S Code section 34177(d).

Order of the Controller

Pursuant to H&S Code section 34167.5, the City of South Pasadena is ordered to reverse the transfer in the amount of \$253,250 and turn over the assets to the Successor Agency. The Successor Agency is directed to properly dispose of the assets in accordance with H&S Code section 34177(d).

City's Response

The City disagrees with the State Controller's Office's (SCO) finding that the final payment of \$253,250 owed to the City was "unallowable" because it was made in the spring of 2011. The City believes that the SCO failed to recognize that the loan made by the City to the former RDA for valid redevelopment purposes was an "enforceable obligation" under H&S Code section 34167(d) and not subject to "claw back" under H&S Code section 34167.5.

SCO's Comment

The asset transfer review performed by the SCO is a different and separate review from the Department of Finance's Due Diligence Reviews (DDR). As such, transfers not identified through the DDR process may be identified in the asset transfer review. The RDA transferred assets to the City after January 1, 2011; therefore, the transfers are unallowable under H&S Code section 34167.5.

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.

The Finding and Order of the Controller remain as stated.

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



CITY OF SOUTH PASADENA

OFFICE OF THE CITY MANAGER
1414 MISSION STREET, SOUTH PASADENA, CA 91030
TEL: 626.403.7210 ■ FAX: 626.403.7211
WWW.CI.SOUTH-PASADENA.CA.US

September 2, 2014

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

RE: South Pasadena Response to SCO Draft Asset Transfer Review

Dear Ms. Gonzalez:

The City of South Pasadena (the City) received the written Draft Asset Transfer Review on August 25, 2014 and makes this response.

The City objects to the State Controller's Office's (SCO) erroneous finding that the final payment of \$253,250 owed to the City was "unallowable," simply because it was made in the spring of 2011. The SCO misconstrues its authority and the law under Health & Safety Code Section 34167.5 by failing to recognize that the loan made by the City to the former South Pasadena Redevelopment Agency (RDA) for valid redevelopment purposes was an "enforceable obligation" under Health & Safety Code Section 34167(d) and not subject to "claw back" under Health & Safety Code Section 34167.5.

The loan in question was made in 1996 by the City to the RDA, in the amount of \$190,000. This loan was consolidated with outstanding loans in the amount of \$1,036,034, for a total loan of \$1,226,034, which accrued interest at a rate of 5%. As provided by the written loan agreement—a copy which was provided to SCO staff for its review—the loan was to be repaid as the RDA had sufficient funds to make such repayments, with the loan maturing upon the dissolution or termination of the Redevelopment Plan. The loan was expressly authorized under Health & Safety Code Section 33610, and this section has not been repealed by either AB 1X26 or AB 1484.

In 1998, the City and the RDA modified the loan to reduce to the interest rate to 0%. The RDA made payments to the City as it obtained sufficient funds, and by March 2011, only \$253,250 of the original principle amount remained owing. The RDA, having recently received its distribution of tax increment, had sufficient funds to fully retire the debt and did

so with a final payment on March 2, 2011. The history of these transactions shows that the City loaned these funds to the RDA to enable the RDA to operate pending its receipt of sufficient tax increment to carry out the purposes of the Redevelopment Plan. The City had every legitimate expectation of being reimbursed, and unlike other agencies, it even forgave all interest, seeking only the return of its principle to the Water Fund from which the money was advanced to the RDA. This loan agreement falls squarely within the definition of "enforceable obligation" under Health & Safety Code Section 34167(d) subsection (2) ("Loans of moneys borrowed by the redevelopment agency for a lawful purpose...to the extent they are legally required to be repaid pursuant to a required repayment schedule or other mandatory loan terms") and subsection (5) ("any legally binding and enforceable agreement or contract that is not otherwise void as violating the debt limit or public policy").

The intent of the legislature in drafting Health & Safety Code Section 34167.5 was not to disturb valid and long existing loan agreements between a redevelopment agency and its sponsoring entity, but rather, to reverse the wholesale transfer of assets with no existing redevelopment purpose or project encumbering them, which occurred between January 1, 2011 and June 28, 2011 among many redevelopment agencies and their sponsoring entities. Your attention is drawn to Health & Safety Code Section 34167(f) which states:

"(f) Nothing in this part shall be construed to interfere with a redevelopment agency's authority, pursuant to enforceable obligations as defined in this chapter, to (1) make payments due, (2) enforce existing covenants and obligations, or (3) perform its obligations."

This provision authorized the RDA to continue to make any payments of an enforceable obligation when due, prior to June 28, 2011. After that date, all payments of an enforceable obligation could only be made after being included on an enforceable obligation payment schedule. (Health & Safety Code Section 34167(h)).

Accordingly, the SCO has no authority under Health & Safety Code Section 34167.5 to "claw back" these lawful payments because such authority only exists "to the extent not prohibited by state and federal law." Since the very same law that SCO relies upon to order the return of assets also confirms the same loan payments as lawful and in accordance with state law, the SCO's findings in this draft report are in error.

During the SCO on-site audit, SCO staff was provided copies of all loan documentation proving that this loan and the payments made were legal enforceable obligations, but this evidence was either ignored or misunderstood. It is also important to note that the repayment of the final \$253,250 was included in the Successor Agency's Due Diligence Review (DDR) as a transfer made per an enforceable obligation and the Department of Finance did not object or consider this loan repayment an unallowable transfer. The SCO also received a copy of the DDR and did not object to this or any other transfer reflected on that document.

We respectfully request that the SCO reverse its erroneous findings on this matter and issue a "clean" asset transfer review letter. At no time did the former RDA, or the Successor Agency thereto, make any transfer of assets which were not authorized by Community Redevelopment Law, AB 1X 26 and AB 1484, and the SCO report may not lawfully reflect otherwise.

Sincerely,

A handwritten signature in blue ink, appearing to read "Sergio Gonzalez".

Sergio Gonzalez
City Manager

cc: Teresa L. Highsmith, City Attorney

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

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