

ARCADIA REDEVELOPMENT AGENCY

ASSET TRANSFER REVIEW

Review Report

January 1, 2011, through January 31, 2012



JOHN CHIANG
California State Controller

November 2013



JOHN CHIANG
California State Controller

November 22, 2013

Dominic Lazzaretto, City Manager
City of Arcadia
240 West Huntington Drive
Arcadia, CA 91066

Dear Mr. Lazzaretto:

Pursuant to Health and Safety (H&S) Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the Arcadia Redevelopment Agency to the City of Arcadia 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 it 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 of Arcadia or any other public agencies have been reversed.

Our review found that the Arcadia Redevelopment Agency transferred \$30,312,663 in assets after January 1, 2011. This amount included an unallowable transfer to the City of Arcadia totaling \$7,712,333, or 25.44% of the transferred assets. However, on May 31, 2012, the City of Arcadia reversed the transfer of \$4,049,000 and returned the funds to the Successor Agency. The remaining amount of \$3,663,333 is subject to H&S Code section 34167.5, and must be turned over to the Successor Agency.

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

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/kw

Attachment

cc: Jason Kruckeberg, Assistant City Manager/
Development Services Director/Oversight Board Chair
City of Arcadia
Jerry Schwartz, Economic Development Manager
City of Arcadia
Shannon Huang, Financial Services Manager
City of Arcadia
Wendy L. Watanabe, Auditor-Controller
Los Angeles County
David Botelho, Program Budget Manager
California Department of Finance
Richard J. Chivaro, Chief Legal Counsel
State Controller's Office
Elizabeth Gonzalez, Bureau Chief
Division of Audits, State Controller's Office
Scott Freesmeier, Audit Manager
Division of Audits, State Controller's Office
Trisha L. Quiambao, Auditor-in-Charge
Division of Audits, State Controller's Office

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Asset Transfer Review Report

Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the Arcadia Redevelopment Agency 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 Arcadia Redevelopment Agency transferred \$30,312,663 in assets after January 1, 2011. This amount included an unallowable transfer to the City of Arcadia (City) totaling \$7,712,333, or 25.44% of the transferred assets. However, on May 31, 2012, the City reversed the transfer of \$4,049,000 and turned the funds over to the Successor Agency. The remaining amount of \$3,663,333 is subject to Health & Safety (H&S) Code section 34167.5 and 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 H&S Code beginning with section 34161.

In accordance with the requirements of H&S Code section 34167.5, the State Controller is required to review the activities of RDAs, "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," and the date on which the RDA ceases to operate, or January 31, 2012, whichever is earlier.

The SCO has identified transfers of assets that occurred after January 1, 2011, between the Arcadia Redevelopment Agency, the City of Arcadia, 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 order 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 RDA, the City of Arcadia, 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 Arcadia Redevelopment Agency transferred \$30,312,663 in assets after January 1, 2011. This amount included an unallowable transfer to the City of Arcadia totaling \$7,712,333, or 25.44% of the transferred assets. However, on May 31, 2012, the City reversed the transfer of \$4,049,000 and returned the asset to the Successor Agency. The remaining amount of \$3,663,333 is subject to Health & Safety (H&S) Code section 34167.5 and must be turned over to the Successor Agency.

Details of our finding are in the Finding and Order of the Controller section of this report. We also have included a detailed schedule of assets to be turned over to, or transferred to, the Successor Agency.

Views of Responsible Officials

We issued a draft review report on September 24, 2013. Jason Kruckeberg, Assistant City Manager/Development Services Director responded by letter dated October 3, 2013, 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 Successor Agency, the Oversight Board, the City of Arcadia, 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 22, 2013

Finding and Order of the Controller

FINDING— Unallowable asset transfers to the City of Arcadia

The Arcadia Redevelopment Agency (RDA) made unallowable asset transfers to the City of Arcadia (City) after January 1, 2011, totaling \$7,712,333.

The unallowable asset transfers consisted of the following:

- On April 30, 2011, the RDA transferred \$4,049,000 in cash to the City for various public improvement projects per a Cooperative Agreement, which was approved by City Resolution Nos. 6761 and 6762, and RDA Resolution Nos. 242 and 243, signed on April 5, 2011. However, this transfer was reversed on May 31, 2012, and the funds were turned over to the Successor Agency. No further action is necessary.
- After January 1, 2011, the RDA transferred a total of \$3,663,333 in cash to the City for a loan that was entered into on July 1, 2010. This amount included a total of \$163,333 in interest. Payments were made from January 2011 through June 2011, including a \$3,500,000 principal payment, which was paid on August 19, 2011. (See Schedule 1).

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

Order of the Controller

Based on H&S Code section 34167.5, the City would have been ordered to reverse the transfer of \$7,712,333 in assets. However, because the City previously turned over \$4,049,000 to the Successor Agency, the remaining amount of \$3,663,333 must be turned over to the Successor Agency.

The Successor Agency is directed to properly dispose of the remaining assets in accordance with H&S Code section 34177(d) and (e).

City Response to Draft Report

The Successor Agency to the Arcadia Redevelopment Agency (“SA”) has reviewed the Draft Asset Transfer Review Report prepared by the State Controller’s Office (“SCO”) pursuant to Health and Safety Code section 34167.5. The SA disagrees with the Finding and Order of the Controller. Specifically, the SCO has determined that the transfer of \$3,663,333 from the Redevelopment Agency to the City between January 1, 2011 and August 19, 2011 was invalid and those funds must be returned to the SA. The loan in question, between the City and the Redevelopment Agency was approved as part of the 2010-2011 Arcadia City budget, and was completely legal at that time. The payment of interest and principal during FY 2010-2011 was also legal when performed. It is in hindsight that the SCO has declared the actions to be invalid...

See Attachment 1 for the City’s complete response.

SCO Comment

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.

Upon receiving a Department of Finance Finding of Completion, the Successor Agency may place loan agreements between the RDA and the City on the Recognized Obligation Payment Schedule, as an enforceable obligation, provided that the Oversight Board finds that the loan was for legitimate redevelopment purposes.

The Finding and Order of the Controller remains as stated.

**Schedule 1—
Unallowable RDA Asset Transfers to
the City of Arcadia
January 1, 2011, through January 31, 2012**

Unallowable asset transfers to the City of Arcadia:		
Per Cooperative Agreement signed on April 5, 2011		\$ 4,049,000
Per Loan Agreement signed on July 1, 2010		
Interest payment (various dates)	\$ 163,333	
Principal payment (August 19, 2011)	<u>3,500,000</u>	<u>3,663,333</u>
Total unallowable asset transfers		7,712,333
Less assets returned to Successor Agency on May 31, 2012		<u>(4,049,000)</u>
Total unallowable assets transferred subject to H&S Code section 34167.5		<u>\$ 3,663,333</u> ¹

¹ See the Finding and Order of the Controller section.

**Attachment—
City of Arcadia’s Response to
Draft Review Report**



City of Arcadia

Development Services Department

Jason Kruckeberg
*Assistant City Manager/
Development Services
Director*

October 3, 2013

Mr. Steven Mar, Chief
Local Government Audits Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94259-5874

SUBJECT: City of Arcadia Comments on Draft Report on Asset Transfers

Dear Mr. Mar:

The Successor Agency to the Arcadia Redevelopment Agency ("SA") has reviewed the Draft Asset Transfer Review Report prepared by the State Controller's Office ("SCO") pursuant to Health and Safety Code section 34167.5. The SA disagrees with the Finding and Order of the Controller. Specifically, the SCO has determined that the transfer of \$3,663,333 from the Redevelopment Agency to the City between January 1, 2011 and August 19, 2011 was invalid and those funds must be returned to the SA. The loan in question, between the City and the Redevelopment Agency, was approved as part of the 2010-2011 Arcadia City budget, and was completely legal at that time. The payment of interest and principal during FY 2010-2011 was also legal when performed. It is in hindsight that the SCO has declared the actions to be invalid.

The SCO originally took the position that the transfer was invalid pursuant to Health and Safety Code Section 34171(d)(2). The preliminary finding by the SCO indicated that because the loan was not entered into within the first two years following the formation of the Agency the loan can only be repaid through the ROPS process. However, HS 34171(d)(2) also includes an exception for written agreements between the City and the RDA that are entered into at the time of issuance, but no later than December 31, 2010, of indebtedness obligation and solely for the purpose of securing/repaying the indebtedness. Indebtedness is defined, in Section 34171(e), to mean bonds, notes, certificates of participation, or other evidence of indebtedness, issued or delivered by the RDA to a third party investor or bondholder to finance the redevelopment projects undertaken. In this case, although the loan from the City to the Redevelopment Agency wasn't directly tied to certificates of participation or another bond document, the funds were loaned for the specific purpose of acquiring land and completing public improvements. The money was used for land acquisition at 101-159 North Santa Anita Avenue. Those parcels are now due to be sold pursuant to the Successor Agency's Long Range Property Management Plan with an escrow closing date of November 18, 2013. Arcadia's Long Range Property Management Plan was approved by the

Mr. Steven Mar, Chief
State Controller's Office
City of Arcadia Comments on Draft Report on Asset Transfers
October 3, 2013
Page Two

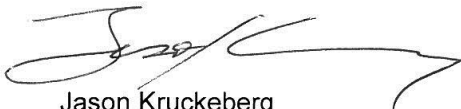
Department of Finance (DOF) on April 4, 2013. It was the first Long Range Plan in the State approved by the DOF. A key tenant of the Long Range Plan is the sale of those properties, purchased with funds loaned by the City to the Agency, and the distribution of the proceeds to the taxing entities.

To require repayment by the City of the \$3.6m to the Successor Agency and then require that the proceeds from the sale of the property acquired with the loan proceeds also remain with the SA and be distributed to the affected taxing entities ("ATE") will unjustly enrich the taxing entities. The ATEs will receive both the cash and the value of the property. We believe the equitable resolution is for the proceeds from the sale of the property to be distributed to the ATEs and the loan repayment remain with the City. The loan agreement in question was entered into for the sole purpose of acquiring the properties identified above.

After SCO staff met with SA staff and SA staff had the opportunity to explain the issues surrounding the payment of this loan, SCO has now issued a draft Asset Transfer Review with an entirely different theory as to why the funds must be returned to the SA. The SCO has now simply stated that because the transfer occurred during the designated time period the funds must be returned to the SA pursuant to Health and Safety Code Section 34167.5.

The SCO's new position disregards the facts previously provided to SCO staff that by returning the \$3.6m in funds back to the SA for distribution to the affected taxing entities the SA will have paid the ATE's twice for the same transaction: once through the distribution of the \$3.6m in cash and again through the distribution from the proceeds of the sale of the land acquired with the funds from the loan. The SCO should order that the \$3.6m in cash does not need to be returned to the SA as the SA will be making the ATEs substantially whole with the distribution of the proceeds from the sale of the land.

Sincerely,



Jason Kruckeberg
Assistant City Manager/Development Services Director

Cc: Dominic Lazzaretto, City Manager
Jerry Schwartz, Economic Development Manager
Shannon Huang, Financial Services Manager
Steve Deitsch, Esq., Best Best & Kreiger
Elizabeth Hull, Esq., Best Best & Krieger
Scott Freesmeier, Audit Manager, State Controller's Office
Trisha L. Quiambao, Auditor-in-Charge, State Controller's Office

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