

MERCED REDEVELOPMENT AGENCY

ASSET TRANSFER REVIEW

Review Report

January 1, 2011, through January 31, 2012



BETTY T. YEE
California State Controller

July 2015



BETTY T. YEE
California State Controller

July 30, 2015

Christopher Jicha, Senior Consultant
Kosmont Companies
865 S. Figueroa Street, Suite 3500
Los Angeles, CA 90017

Dear Mr. Jicha:

Pursuant to Health and Safety Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the Merced Redevelopment Agency (RDA) to the City of Merced (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 \$42,065,255 in assets after January 1, 2011, including unallowable transfers totaling \$42,065,255, or 100% of transferred assets, to the Public Financing and Economic Development Authority (PFEDA) of the City of Merced. These assets must be turned over to the Successor Agency.

However, after February 1, 2012, the PFEDA turned over \$7,050,342 in assets to the Entity Assuming the Housing Functions. Therefore, the remaining \$35,014,913 in unallowable transfers 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,

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/ljs

cc: Lisa Cardella-Presto, Auditor-Controller
Merced County
Jim Sanders, Oversight Board Chair
Merced Redevelopment/Successor Agency
John M. Bramble, City Manager
City of Merced
Bradley R. Grant, Finance Director
City of Merced
Teri Albrecht, Deputy Finance Director
City of Merced
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
Scott Freesmeier, Audit Manager
Division of Audits, State Controller's Office
Cecilia Michaels, 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 Merced 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 \$42,065,255 in assets after January 1, 2011, including unallowable transfers totaling \$42,065,255, or 100% of transferred assets, to the Public Financing and Economic Development Authority (PFEDA) of the City of Merced. These assets must be turned over to the Successor Agency.

However, after February 1, 2012, the PFEDA turned over \$7,050,342 in assets to the Entity Assuming the Housing Functions. Therefore, the remaining \$35,014,913 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 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 asset transfers 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 Merced Redevelopment Agency transferred \$42,065,255 in assets after January 1, 2011, including unallowable transfers totaling \$42,065,255, or 100% of transferred assets, to the Public Financing and Economic Development Authority (PFEDA) of the City of Merced. These assets must be turned over to the Successor Agency.

However, after February 1, 2012, the PFEDA turned over \$7,050,342 in assets to the Entity Assuming the Housing Functions. Therefore, the remaining \$35,014,913 in unallowable transfers 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 review report on August 13, 2014. John M. Bramble, City Manager/Executive Director, responded by letter dated August 28, 2014. 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 Merced, 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.

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

July 30, 2015

Finding and Order of the Controller

FINDING— Unallowable asset transfers to the City of Merced

The Merced Redevelopment Agency (RDA) made unallowable asset transfers of \$42,065,255 to the Public Financing and Economic Development Authority of the City of Merced (PFEDA). The transfers occurred after January 1, 2011, and the assets were not contractually committed to a third party prior to June 28, 2011.

On January 31, 2011, the RDA transferred \$42,065,255 in cash and other assets to the PFEDA (see Schedule).

Due to the fact that the City of Merced (City) declined to serve as the Successor Agency for the former RDA, Governor Brown appointed a three-member governing board to serve as the Designated Local Authority (DLA)/Successor Agency for the former Merced Redevelopment Agency, in accordance with Health and Safety (H&S) Code section 34173(d)(3)(A), which states:

If no local agency elects to serve as a successor agency for a dissolved redevelopment agency, a public body, referred to herein as a “designated local authority” shall be immediately formed, pursuant to this part, in the county and shall be vested with all the powers and duties of a successor agency as described in the part. The Governor shall appoint three residents of the county to serve as the governing board of the authority. The designated local authority shall serve as successor agency until a local agency elects to become the successor agency in accordance with this section.

Pursuant to 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) and (e). Some of those assets also may be subject to the provisions of H&S Code section 34181(a). H&S Code section 34181(a) states, “The oversight board shall direct the successor agency to do all of the following:

- (a) Dispose of all assets and properties of the former redevelopment agency that were funded by tax increment revenues of the dissolved redevelopment agency; provided however, that the oversight board may instead direct the successor agency to transfer ownership of those assets that were constructed and used for a government purpose, such as roads, school buildings, parks, police and fire stations, libraries, and local agency administrative buildings, to the appropriate public jurisdiction pursuant to any existing agreements relating to the construction or use of such as asset....”

Order of the Controller

Pursuant to H&S Code section 34167.5, the City is ordered to turn over the assets in the amount of \$42,065,255 to the Designated Local Authority (DLA)/Successor Agency.

However, after February 1, 2012, the PFEDA turned over \$7,050,342 in assets to the Entity Assuming the Housing Functions. Therefore, the remaining \$35,014,913 in unallowable transfers must be turned over to the Successor Agency.

City's Response

In its response, the City lists three subsequent events that it believes should have been included in the draft review report, specifically:

- “On or about July 15, 2012, a total of \$5,634,827 in former Merced Redevelopment Agency cash assets was turned over the Auditor of the County of Merced for the benefit of the Designated Local Authority.”
- “Although the City elected *not* to become the successor agency for non-housing functions of the Merced Redevelopment Agency..., the City became the housing successor....”
- “The City, PFEDA and the Parking Authority dispute the legality of the proposed SCO's order that the former Merced Redevelopment Agency assets be turned over to Designated Local Authority....”

SCO's Comment

H&S Code section 34167.5 states in part, “the RDA may not transfer assets to a city, county, city and county, or any other public agency after January 1, 2011.”

The City remitted \$5,634,827 to the Merced County Auditor-Controller on or about July 15, 2012. We verified the transfers and determined that the payment made in July 2011 was for a current tax increment payment and not part of the RDA cash that was transferred in January 2011. The July payment would be in addition to funds being clawed back. Therefore, no adjustment will be made to the Order of the Controller for these funds.

Pursuant to H&S Code section 34167.5, the transfer of assets, housing and non-housing, to the PFEDA in 2011, was an unallowable transfer. Per the City, \$16,895,308 in housing assets were transferred to the Entity Assuming the Housing Functions from the PFEDA after the City was designated as the Entity Assuming the Housing Functions. The City provided a schedule documenting the book value of housing assets as of January 31, 2012, in the amount of \$10,992,600, of which \$3,942,258 was identified as unencumbered cash; the remaining \$7,050,342 were non-cash assets. Therefore \$7,050,342 will be reduced from the amount of clawback, and the remaining \$3,942,258 in unencumbered cash should be turned over the county auditor-controller for distribution to the taxing entities.

The Order of the Controller has been modified accordingly.

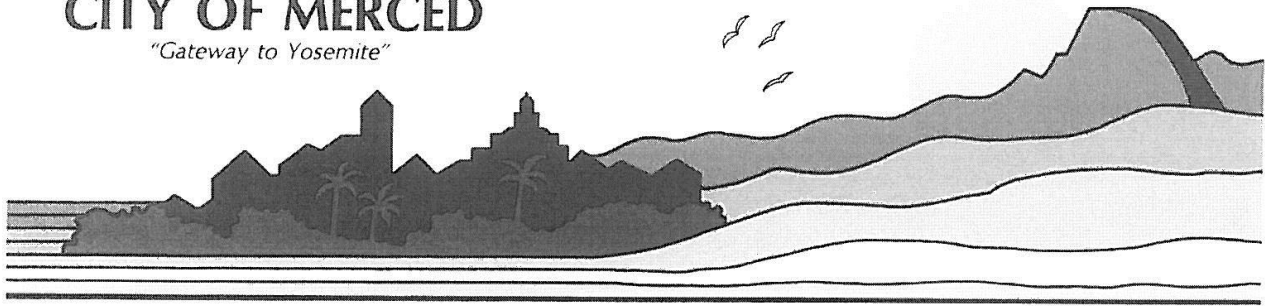
Schedule—
Unallowable Asset Transfers to the City of Merced
January 1, 2011, through January 31, 2012

Current assets (January 31, 2011):	
Cash and investments	\$ 11,177,516
Accounts receivable	3,410
Interest receivables – loans and notes	106,842
Notes receivable	6,130,711
Due from other governments	702,225
Advances on the Merced Theater	2,357,500
Fixed assets held for resale	3,936,205
Non-depreciable capital assets:	
Land and improvements	1,093,282
Construction in progress	4,617,052
Depreciable capital assets less accumulated depreciation:	
Buildings and structures	11,216,099
Machinery and equipment	2,694
Other	630,030
Accumulated depreciation	<u>91,689</u>
Total assets transferred to the PFEDA	\$ 42,065,255
After February 1, 2012 the city turned over non-cash assets to the Entity Assuming the Housing Functions	<u>(7,050,342)</u>
Total assets subject to H&S Code section 34167.5	<u><u>\$35,014,913</u></u>

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

CITY OF MERCED

"Gateway to Yosemite"



OFFICE OF THE CITY MANAGER
(209) 385-6834 • (209) 723-1780 FAX

August 28, 2014

BY EMAIL AND FIRST CLASS MAIL
egonzalez@sco.ca.gov

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

Re: Draft Asset Transfer Review Report and Letter of
August 13, 2014

Dear Ms. Gonzalez:

This letter is written in response to the draft Merced Redevelopment Agency Asset Transfer Report (the "Draft Report") from the State Controller's Office (SCO) dated August 2014 and the cover letter dated August 13, 2014 from Jeffrey V. Brownfied, Chief, Division of Audits. In the Draft Report, the SCO has indicated that the former Merced Redevelopment Agency:

"made unallowable transfers totaling \$42,065,255,
or 100% of transferred assets, to the Public
Financing and Economic Development Authority of

678 West 18th Street • Merced, California 95340

X:\Special Projects\Redevelopment Agency Unwinding & Successor Agency\State Controller Issues\Ltr to Gonzalez,
Elizabeth Re Draft Asset Transfer Review Report 8.27.14.docx

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the City of Merced. These assets must be turned over to the Successor Agency.”

The City of Merced (“City”), City of Merced Public Financing and Economic Development Authority (“PFEDA”) and the Parking Authority of the City of Merced (“Parking Authority”) dispute the findings of the Draft Report based upon the following:

1. On or about July 15, 2012, a total of \$5,634,827 in former Merced Redevelopment Agency cash assets was turned over the Auditor of the County of Merced for the benefit of the Designated Local Authority.¹ Because these former Merced Redevelopment Agency funds have already been turned over to the fiscal agent for the Designated Local Authority, this should be reflected in the Draft Report as a *reduction* in the amount of assets that the SCO has characterized as “unallowable transfers”.

2. Although the City of Merced elected *not* to become the successor agency for non-housing functions of the Merced Redevelopment Agency (those functions have been assumed by the Designated Local Authority), the City became the housing successor agency of the Merced Redevelopment Agency. Once the City elected to become the housing successor agency, PFEDA transferred former Merced Redevelopment Agency housing assets to the City that had a book value of \$16,895,308. Accordingly, the amount of “unallowable transfers” should be reduced by the additional amount of \$16,895,308.

3. The City, PFEDA and the Parking Authority dispute the legality of the proposed SCO’s order that the former Merced Redevelopment Agency assets be turned over to Designated Local Authority (as successor agency) based upon the legal authorities and arguments raised in the litigation filed by League of California, City of Vallejo (successor agency for the former Vallejo Redevelopment) and Christopher K. McKenzie filed against Ana J. Matosantos in her

¹ The Designated Local Authority is the successor agency to the Merced Redevelopment Agency for non-housing purposes.

official capacity and other related parties, real parties in interest and interveners (Sacramento County Superior Court Case No. 34-2012-80001275-CU-WM-GDS)(hereafter "Vallejo Litigation").

Despite the positions outlined above, the City, PFEDA and the Parking Authority have a strong working relationship with the Designated Local Authority, the Oversight Board and their respective staff and legal counsel and have greatly appreciated their assistance with the winding down process for the former Merced Redevelopment Agency – especially given the very challenging and inconsistent processes outlined in AB1x 26 and AB 1484.

Once the SCO's "clawback" order is final, the City, PFEDA and Parking Authority are committed to working with the Designated Local Authority and Oversight Board to do the following:²

1. Take the necessary steps (if any) to obtain any necessary approvals for PFEDA's transfer of the former Merced Redevelopment Agency's housing assets to the City. (The Department of Finance has already approved the transfer.)

2. If not already acknowledged by the SCO, obtain recognition for the \$5,634,827 in former Merced Redevelopment Agency cash assets already transferred to the Designated Local Authority's fiscal agent (the Merced County Auditor).

3. Transfer specific non-housing former Merced Redevelopment Agency real property to the Designated Local Authority³ including, but not limited to:

- A. Merced Center Parcade at the corner of 18th and "M" Streets.

² Any transfers made by the City, PFEDA and/or Parking Authority to the Designated Local Authority after the date of this letter shall be deemed made under protest, incorporating by reference all the legal arguments against the validity of AB 1484 and any so-called "clawback" orders by State Controller's Office that were made in the Vallejo Litigation.

³ Some of the properties transferred to PFEDA as of January 31, 2011 were for existing projects already in progress, such as the very low income affordable housing project on Highway 59.

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- B. Vacant land at the corner of 19th and "N" Streets.
- C. Parking lot sites at 333 and 335 W. 16th Streets.

These three properties alone had a combined book value of \$13,786,615 as of February 1, 2011.⁴

4. Transfer non-housing accounts receivable and notes receivable from the former Merced Redevelopment Agency to the Designated Local Authority.

5. Address construction in progress items pursuant to enforceable obligations of the former Merced Redevelopment Agency.

In closing, the City, PFEDA and the Parking Authority and their respective governing bodies and staff look forward to the timely resolution of these matters so that we can focus on addressing the other important and challenging issues facing the Central Valley and the City of Merced in particular.

If you have any questions, please contact me. If you have any legal questions, please contact Kenneth Rozell, Senior Deputy City Attorney at (209) 385-6868.

Sincerely,



JOHN M. BRAMBLE
City Manager/Executive Director

⁴ As of February 1, 2011, the book value for the Merced Center Parcade was \$12,818,270, the book value for property at 19th and "N" Streets (606 W.19th Street) was \$688,286, and the book value for 333 and 335 W. 16th Street was \$280,059.

Ms. Elizabeth Gonzalez
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cc: Honorable Mayor and Members of the City Council, City of
Merced
Honorable Chairman and Members of the City of Merced Public
Financing and Economic Development Authority
Honorable Chairman and Members of the Parking Authority of
the City of Merced
Gregory G. Diaz, City Attorney, City of Merced
Bradley R. Grant, Finance Director, City of Merced
Frank Quintero, Economic Development Director, City of
Merced
Teri Albrecht, Deputy Finance Director
Kenneth D. Rozell, Senior Deputy City Attorney, City of Merced
Christopher Jicha, Senior Consultant, Kosmont Companies
Joy Heuser Otsuki, Esq.

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

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