

EL CERRITO REDEVELOPMENT AGENCY

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 31, 2014

Scott Hanin, City Manager
City of El Cerrito/Successor Agency
10890 San Pablo Avenue
El Cerrito, CA 94530

Dear Mr. Hanin:

Pursuant to Health and Safety Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the El Cerrito Redevelopment Agency (RDA) to the City of El Cerrito (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 \$22,800,178 in assets after January 1, 2011, including unallowable transfers to the El Cerrito Municipal Services Corporation, totaling \$12,550,550, or 55.05% 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/mh

cc: Lori Trevino, Senior Financial Analyst
City of El Cerrito
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City of El Cerrito
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Asset Transfer Review Report

Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the El Cerrito 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 \$22,800,178 in assets after January 1, 2011, including unallowable transfers to the El Cerrito Municipal Services Corporation, totaling \$12,550,550, or 55.05% 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 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 El Cerrito Redevelopment Agency transferred \$22,800,178 in assets after January 1, 2011, including unallowable transfers to the El Cerrito Municipal Services Corporation, totaling \$12,550,550, or 55.05% of transferred assets. These assets must be turned over to the Successor Agency.

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

Views of Responsible Official

We issued a draft review report on May 27, 2014. Scott Hanin, City Manager, responded by letter dated June 9, 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, the RDA, the El Cerrito Municipal Services Corporation, 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 31, 2014

Finding and Order of the Controller

**FINDING—
Unallowable asset
transfers to the El
Cerrito Municipal
Services
Corporation**

The El Cerrito Redevelopment Agency (RDA) made unallowable asset transfers totaling \$12,550,550 to the El Cerrito Municipal Services Corporation (MSC). The asset transfers to the MSC occurred after January 1, 2011, and the assets were not contractually committed to a third party prior to June 28, 2011.

- On February 28, 2011, and various dates thereafter, the RDA transferred a total of \$2,382,231 in current assets to the MSC. These transfers were accomplished pursuant to an amended and restated cooperation agreement, and pursuant to Resolution 607.
- On March 22, 2011, the RDA transferred \$4,634,789 in land held for redevelopment and \$5,533,530 in capital assets to the MSC. These transfers were accomplished pursuant to an amended and restated cooperation agreement, and pursuant to Resolution 612.

Pursuant to provisions of 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 City contends that the MSC is a public nonprofit corporation created to provide charitable or other public purposes and that transfers from the RDA to the MSC are not prohibited under H&S Code section 34167.5.

However, H&S Code section 34167.10 states the following:

(a) Notwithstanding any other law, for purposes of this part and Part 1.85 (commencing with Section 34170), the definition of a city, county, or city and county includes, but is not limited to, the following entities:

- (1) Any reporting entity of the city, county, or city and county for purposes of its comprehensive annual financial report or similar report.
- (2) Any component unit of the city, county, or city and county.
- (3) Any entity which is controlled by the city, county, or city and county, or for which the city, county, or city and county is financially responsible or accountable.

(b) The following factors shall be considered in determining that an entity is controlled by the city, county, or city and county, and are therefore included in the definition of a city, county, or city and county for purposes of this part and Part 1.85 (commencing with Section 34170):

- (1) The city, county, or city and county exercises substantial municipal control over the entity's operations, revenues, or expenditures.
- (2) The city, county, or city and county has ownership or control over the entity's property or facilities.

(3) The city, county, or city and county and the entity share common or overlapping governing boards, or coterminous boundaries.

(4) The city, county, or city and county was involved in the creation or formation of the entity.

(5) The entity performs functions customarily or historically performed by municipalities and financed through levies of property taxes.

(6) The city, county, or city and county provide administrative and related business support for the entity, or assumes the expenses incurred in the normal daily operations of the entity.

(c) For purposes of this section, it shall not be relevant that the entity is formed as a separate legal entity, nonprofit corporation, or otherwise or is not subject to the constitution debt limitation otherwise applicable to a city, county, or city and county. The provisions in this section are declarative of existing law as the entities described herein are and were intended to be included within the requirements of this part and Part 1.85 (commencing with Section 34170) and any attempt to determine otherwise would thwart the intent of these two parts.

The current relationship between the City and the MSC is described below, with the applicable H&S Code sections identified:

- The MSC's financial statements are part of the City's Comprehensive Annual Financial Report (H&S Code Section 34167.10(a)(1)).
- The City has ownership or control over the MSC's property or facilities (H&S Code section 34167.10(b)(2))
- The controlling Board of Directors for the MSC was made up of City Council members, who previously acted as the governing board of the RDA, and the corporate officers are City/RDA employees (H&S Code sections 34167.10(b)(1) and 34167.10(b)(3)).
- The City was responsible for creating the MSC (H&S Code section 34167.10(b)(4)).
- The City provides administrative and related business support for the MSC (H&S Code section 34167.10(b)(6)).

Therefore, the MSC is considered part of the City for purposes of H&S Code section 34167.5.

Order of the Controller

Pursuant to H&S Code sections 34167.5 and 34167.10, the MSC is ordered to turn over the above assets, described in Schedule 1, to the Successor Agency in the amount of \$12,550,550.

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

City's Response

The City disagreed with the finding. The City stated in its response that the SCO's report misapplies the law and does not take into consideration the facts surrounding the transaction at issue. The City further described the El Cerrito Municipal Services Corporation as a nonprofit public benefit corporation pursuant to its Articles of Incorporation executed December 20, 1982.

The City further states that the Corporation's Board of Directors consists of five members from the City Council and City, but that the Corporation is controlled by the Board, not the City Council or City. Furthermore, the City believes that the Corporation is separate and distinct from the City, and that the transactions occurred at time when California law was well settled concerning the definition of a separate legal entity.

Lastly, the City believes that there is no indication that H&S Code section 34167.10 was intended to be applied retroactively and cites another court case in support of this view.

Based on the above reasons, the City believes the SCO's report should be revised and that the transactions in question were valid and cannot be subject to clawback.

See attachment for the City's full response.

SCO's Comment

SCO disagrees with the City's assertion that the El Cerrito Municipal Services Corporation is a separate legal entity and not subject to H&S Code section 34167.10. As described in the Finding section of the report, the City has achieved control of the Corporation by items (1), (2) (3) (4) and (6) of Section 34167.10. Furthermore, it is the position of the SCO that Section 34167.10 is correctly applied when assessing the transfers to the Corporation.

The Finding and Order of the Controller remain as stated.

**Schedule 1—
Unallowable Asset Transfers to
the El Cerrito Municipal Services Corporation
January 1, 2011, through January 31, 2012**

Unallowable Transfers to the El Cerrito Municipal Services Corporation

	<u>Transfer Date</u>	<u>Amount</u>
Cash transfer to MSC per Cooperative Agreement	1/31/2012	\$ 139,920
Cash transfer to MSC per Cooperative Agreement	1/6/2012	491,420
Cash transfer to MSC per Cooperative Agreement	1/31/2012	400,000
Cash transfer to MSC per Cooperative Agreement	2/28/2011	950,649
2004 Uncommitted tax-exempt bond proceeds transfer to the MSC	2/28/2011	<u>400,242</u>
Subtotal		2,382,231
Land Held for Redevelopment	3/22/2011	4,634,789
Capital Assets	3/22/2011	<u>5,533,530</u>
Total asset transfers subject to Health and Safety Code section 34167.5		<u>\$ 12,550,550</u>

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



June 9, 2014

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

Re: Draft El Cerrito Redevelopment Agency Asset Transfer Review Report, May 2014

Dear Ms. González:

The City of El Cerrito ("City") and El Cerrito Redevelopment Agency Successor Agency ("Successor Agency") appreciate and welcome the opportunity to comment on and provide corrections to the Draft El Cerrito Redevelopment Agency Asset Transfer Review Report (January 1, 2011 through January 31, 2012), dated May 2014. These comments are respectfully submitted to ensure that a proper review and report is prepared that complies with AB x1 26, AB 1484 and other applicable law.

This response does not waive the right of the Successor Agency or the City to later provide additional information or statements as part of the review process. The Successor Agency and the City retain the right to raise new materials or positions as required.

GENERAL RESPONSE

1. The City's and the Successor Agency's review of the State Controller preliminary findings is ongoing. These responses and objections are made without prejudice to, and are not a waiver of, the City's and the Successor Agency's right to rely on other facts, documents, responses, or information in the State Controller review process or at a later proceeding.
2. By making the accompanying responses and objections, the City and the Successor Agency do not waive, and hereby expressly reserve, their right to assert any and all objections as to the State Controller findings and statements in this review, or in any other proceedings, on any and all grounds including, but not limited to, jurisdiction, scope, competency, relevancy, and materiality. Further, the City and the Successor Agency make the responses herein without in any way implying that they consider all of the State Controller findings and statements, to be legally valid or within the scope of AB x1 26 and AB 1484 relevant or material to the subject matter of this action.
3. The City and the Successor Agency reserve the right to supplement, clarify, revise, or correct any or all of the responses and statements herein, and to assert additional information, in one or more subsequent supplemental response(s).

SPECIFIC RESPONSE

Finding – Unallowable asset transfers to the El Cerrito Municipal Services Corporation

The Report states that the El Cerrito Redevelopment Agency ("RDA") made unallowable asset transfers totaling \$12,550,550 to the El Cerrito Municipal Services Corporation, including \$2,382,231 in current assets, \$4,634,789 in land held for redevelopment and \$5,533,530 in capital assets. The Report orders the return of these assets on the ground that, pursuant to Health and Safety Code Section 34167.10, the El Cerrito Municipal Services Corporation is treated as the City and that Health and Safety Code Section 34167.5 requires the return of all assets transferred by the RDA to the City after January 1, 2011 that are not contractually committed to third parties.

The Controller's Report misapplies the law and fails to take into consideration the fact surrounding the transactions at issue. The El Cerrito Municipal Services Corporation ("Corporation") was formed as a California nonprofit public benefit corporation pursuant to Articles of Incorporation (the "Articles") executed on December 20, 1982, and filed with the California Secretary of State on January 4, 1983.

The purposes for which the Corporation was formed were "(a) to establish and maintain an adequate line of communication between the City of El Cerrito and its resident citizens to the end that the residents will be aware of the general conditions, including the problems, of the City and of general matters of continuing interest to residents of the City of El Cerrito; and (b) any other purpose beneficial to the public." The Corporation's activities were primarily facilitating communications with City residents through the production and mailing of publications through the mail at nonprofit bulk mail rates. The Corporation has also facilitated financing arrangements for the City, including participating in the sale-leaseback financing of a fire station. The Corporation was in fact formed to perform functions that the City itself was not legally allowed to perform.

The bylaws of the Corporation were adopted on December 20, 1982; amended on January 17, 1989; and then amended again on May 3, 2011 and on March 3, 2013 (the "Bylaws"). According to the Bylaws, there are seven (7) members of the board of directors of the Corporation. The board of directors consists of the five members of the City Council of the City, as well as the City Manager and the Assistant City Manager. Throughout its existence, the Corporation has been operated and controlled by its Board of Directors, not the City Council of the City.

At all times since the Corporation was created:

- The Corporation has maintained separate financial records from the City;
- Since February, 2012, the Corporation has maintained a checking account separate from the City;
- The Corporation has held regularly scheduled board meetings;
- The Corporation elects its own officers, including its Chairperson, Vice Chairperson, Executive Director, Secretary, and Chief Financial Officer; and,
- The Corporation conducts business separate and apart from the City.

As the above facts demonstrate, the Corporation is a separate and distinct corporation from the City of El Cerrito and was so at the time that the transactions occurred. At the time the transactions at issue occurred, the law was well settled in California – cities or counties are in general separate entities from entities created by the city or county, including redevelopment agencies, water districts, and nonprofit

corporations. Under the case law authorities, the two entities were held to be separate and distinct legal entities, even where there was some overlap in the governing body of the entities or their physical boundaries, and where the city/county had significant involvement in the creation of the separate entity. (See *Rider v. County of San Diego* (1991) 18 Cal.4th 1035, 1041-1044 [joint powers agency is separate entity from county]; *County of Solano v. Vallejo Redevelopment Agency* (1999) 75 Cal.App.4th 1262, 1267 [redevelopment agency is separate entity from city]; *Pacific States Enterprises, Inc. v. City of Coachella* (1993) 13 Cal.App.4th 1414, 1422-1425 [same]; *Vanoni v. County of Sonoma* (1974) 40 Cal.App.3d 743, 748-751 [water district is separate entity from county].) As the court held in *Cerritos*, “[w]e are not at liberty to ignore the corporation’s status; it has a “genuine separate existence” from the City and Agency, so ‘it does not matter whether the City ‘essentially controls’ [the nonprofit corporation] Cuesta Villas.” (*City of Cerritos vs. Cerritos Taxpayers Assn.*, (2010) 183 Cal.App.4th 1417, 1442, quoting *Rider*, 18 Cal.4th at 1044.) The Controller’s Order relies upon Section 34167.10 as the basis for the order to return assets, but at the time the transfers occurred Section 34167.10 did not exist and the law in effect at that time directly contradicts the provisions of Section 34167.10.

For the Controller’s Order to be valid, Section 34176.10 would not only have to truly be declarative of existing law, which it is not, but would also have to be applied retroactively. There is no indication in Section 34167.10 of legislative intent to make the section retroactive. Generally, statutes operate prospectively only, and there is a strong presumption against retroactivity. (*McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 475-476.) The presumption against retroactivity is “deeply rooted in our jurisprudence, and embodies a legal doctrine centuries older than our Republic.” (*Id.* at 475.) It has “long been established that a statute that interferes with antecedent rights will not operate retroactively unless such retroactivity be the unequivocal and inflexible import of the terms, and the manifest intention of the legislature.” (*Id.*) Most significantly, *McClung* concludes that a legislative statement that the amendment was “declarative of existing law” is insufficient to overcome the strong presumption against retroactivity, especially where, as here, the legislature’s statement is demonstrably erroneous. (*Id.* at 476.) The legislature’s erroneous statement in subdivision (c) to the effect that the provisions of Section 34167.10 are “declarative of existing law” is therefore insufficient to overcome the strong presumption against retroactivity.

For the above reasons, the Controller’s Report must be revised to find that the transactions between the El Cerrito Redevelopment Agency and the El Cerrito Municipal Services Corporation were valid payments and conveyances to a separate corporation that cannot be clawed back.

Sincerely,



Scott Hanin
City Manager

cc: Sky Woodruff, Meyers Nave
Deborah Fox, Meyers Nave
Karen Tiedemann, Goldfarb & Lipman
James T. Diamond, Goldfarb & Lipman
Lisa Malek-Zadeh, Finance Director
Lori Treviño, Senior Financial Analyst

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