

**City of Watsonville**  
***Redevelopment and Housing Department***

**M E M O R A N D U M**

APPROVED  
By Carlos J. Palacios at 6:35 pm, Aug 21, 2012



**DATE:** August 14, 2012

**TO:** Carlos J. Palacios, City Manager

**FROM:** Jan Davison, Redevelopment and Housing Director  
Ezequiel Vega, Administrative Services Director

**SUBJECT:** Resolutions Authorizing two City/Successor Agency Loans in the Aggregate Amount of \$1,149,288 for Successor Agency Enforceable Obligations, Administrative Expenses and newly required Due Diligence Audit

APPROVED  
By Jan Davison at 5:15 pm, Aug 16, 2012

**AGENDA ITEM:** August 28, 2012 City Council/Successor Agency

**RECOMMENDATION:** It is recommended that the City Council and the Successor Agency to the Redevelopment Agency of the City of Watsonville:

1. Adopt resolution authorizing the City Manager, on the behalf of the City and on behalf of the Successor Agency to the Redevelopment Agency of the City of Watsonville, to Execute a Loan Agreement for Successor Agency Enforceable Obligations, Administrative Costs and Project Related Expenses for the Period of July 1 through December 31, 2012 in the amount of \$1,129,888, and
2. Adopt resolution authorizing the City Manager, on the behalf of the City and on behalf of the Successor Agency to the Redevelopment Agency of the City of Watsonville, to execute a Loan Agreement for the newly required Due Diligence Review Audit for the Period of July through December 31, 2012, in the amount of \$20,000.

**DISCUSSION:** ABX1-26, which was enacted by the State legislature on June 27, 2011 and the subsequent decision rendered by the California Supreme Court in the Matosantos case, called for the dissolution of all redevelopment agencies in California as of February 1, 2012. As a result, the Watsonville Redevelopment Agency ceased to exist and the City elected to serve as the Successor Agency to its dissolved redevelopment agency (“Successor Agency”). This has created some unique financial challenges in that the City and its former redevelopment agency had operated under a long standing loan agreement wherein the City would advance funds to the redevelopment agency to allow it to meet its obligations. The City would then be reimbursed out of future installments of tax increment. Tax increment was transmitted from the County of Santa Cruz to the redevelopment agency twice each fiscal year. This agreement recognized:

1. In order for redevelopment agencies to receive tax increment, there had to be outstanding redevelopment debt, and
2. Cash flow challenges caused when obligations are incurred on a fiscal year basis and revenue is received in two installments.

The former redevelopment agency received its last installment of tax increment in December 2011, prior to the dissolution of redevelopment agencies and prior to the Matosantos case decision. Immediately prior to this receipt of tax increment, the redevelopment agency had a negative cash balance in its non-housing funds. However, upon the enactment of ABX1-26, these types of City-Agency loans were not considered enforceable obligations and the State Department of Finance's (DOF) interpretation and implementation of ABX1-26 demanded that the last installment of tax increment received by redevelopment agencies could only be used prospectively to fund expenses during the January through June 2012 time period. The legislation ignored the possibility that there may have been legal prior commitments on any of this money. This interpretation was not clearly transmitted to former redevelopment agencies until late May 2012.

In late May 2012, at the direction of DOF, our County Auditor-Controller performed a "true-ups" or reconciliation of the prospective expenditures identified on our January through June 2012 Recognized Obligation Payment Schedule (ROPS) against the amount of tax increment received in December 2011. As you may recall, successor agencies are now required to prepare ROPS on a prospective six-month basis wherein all anticipated expenditures and the associated funding sources during that six-month time period are identified. Once approved by the Oversight Board, ROPS are then forwarded to DOF for its approval. The ROPS then becomes the budget document for the Successor Agency.

As a result of this "true-up" the Auditor-Controller reduced the June 1<sup>st</sup> distribution from what is now the Redevelopment Property Tax Trust Fund (previously tax increment) to the Successor Agency by \$1,129,888. This reduction represents the amount that the tax increment received in December 2011 exceeded Oversight Board and DOF approved expenses in the January through June 2012 ROPS and ignoring the fact that there was a negative cash balance when this money was received. This same amount, or \$1,129,888, was then subsequently distributed by the Auditor-Controller to affected taxing entities such as schools, special districts, and cities and counties. The City received \$233,122 from this distribution as property tax. However, the Successor Agency then had insufficient funds to meet its obligations in the July through December 2012 time period.

As such, in adopting the FY 2012-13 budget, the City Council authorized additional funds to meet this shortfall, with the bulk of the money (\$700,907) to be paid from the City's own Affordable Housing Fund towards an enforceable obligation for the Sunny Meadows Affordable Housing Project. The remaining balance was to be funded from the additional unexpected general fund revenue realized from the distribution and the balance through the absorption of Successor Agency administrative expenses.

Since then, AB 1484 was enacted on June 27, 2012, that allows for new City-Successor Agency loans with the approval of Oversight Boards. This item was taken to the Oversight Board on August 15, 2012 and was approved, subject to the approval of both the City and the Successor Agency. Accordingly, staff recommends that the City loan the Successor Agency \$1,129,888 so

that the Successor Agency can fully meet its enforceable obligations and administrative expenditures during the DOF approved July-December 2012 ROPS period. This loan would accrue interest at the Local Agency Investment Fund rate and would be repaid in two installments, with the first due on January 31, 2013 with the balance due on July 31, 2013.

AB 1484 also mandated that successor agencies also undergo an additional due diligence audit with the purpose of determining the unencumbered fund balances of redevelopment agencies' housing and non-housing funds as of the date of their dissolution. This audit is to be performed by a licensed accountant. The selected accountant has to be approved by the county auditor-controller. The Santa Cruz County Auditor-Controller has approved the City's auditor, Moss, Levy and Hartzheim, to do the required work. The estimated cost of this audit is in the range of \$20,000. As such, staff is also recommending that the City and Successor Agency authorize a second loan agreement in the amount of \$20,000 to fund the cost of the due diligence audit, which also must be completed within the July-December 2012 time period. This loan would be repaid in full on January 31, 2013.

Both loans are included on the Oversight Board approved January through June 2013 ROPS which is now undergoing DOF review. Under AB 1484, DOF has the unilateral ability to eliminate or modify any enforceable obligation included on a ROPS.

**FINANCIAL IMPACT:** Approving the two new City/Successor Agency Loans totaling in the aggregate \$1,149,888 provides the City with the ability to recover local funds committed in the 2013-14 budget process that are necessary to fully fund the Successor's Agency's obligations during the July – December 2012 time period. The ability to recover these funds only became a possibility with the enactment of AB 1484 on June 27, 2012. These loans will be funded as follows:

- \$700,907 from the City's Affordable Housing Fund
- \$233,122 from the unanticipated additional General Fund property tax realized from the Auditor-Controller's distribution of residual tax increment funds and
- \$215,859 from the Sewer Fund

**ALTERNATIVES:** The City Council and the Successor Agency could elect not to approve one or both of these loans, but doing so leaves the City with no opportunity to recover these funds.

**ATTACHMENTS:** None

cc: City Attorney/Successor Agency Counsel