Additional Frequently Asked Questions 2-29-2012

Q. In the interim between January 1, 2012 and whenever a Recognized Obligation Payment Schedule (ROPS) is approved, can an Enforceable Obligation Payment Schedule (EOPS) be adopted or extended and obligations paid based on that?

A. ABx1 26 provide for an EOPS to be used to provide public review of obligations qualified to be paid before the ROPS could be established. Under the Supreme Court decision, the deadline for adopting a draft ROPS for the period from January 1, 2012 to June 30 2012 is extended to March 1, 2012 and payments of obligations on and after May 1, 2012 are to be made pursuant to the approved ROPS. We strongly encourage successor agencies and their oversight boards to develop the ROPS for this entire six-month period as soon as practicable and submit it to Department of Finance, the county auditor-controller, and the State Controller for review. Thus the ROPS will overlap any EOPS currently applicable but will cover the full period and clearly identify the funding source(s) for each obligation. We encourage successor agencies to share draft ROPSs with us so we can start our reviews of complex issues. Under the Supreme Court decision, ROPS must be submitted to reviewers by April 15, 2012.

The ROPS must cover this entire period even though it overlaps the EOPS because it will be used to determine the amount of funds that is due to be distributed to taxing agencies under Section 34183 from the first distribution of property taxes (tax increment) for the 2011-12 fiscal year. Successor agencies and oversight boards will also need to adopt administrative budgets for this period and designate the amount that needs to be funded from this distribution of property tax. This is limited to 5 percent of the property tax allocated to the successor agency for recognized obligations as defined in Section 34171 (b).

Q. For redevelopment agencies that received an allocation of tax increment from the fall 2011 property tax payments, how will the distribution of funds pursuant to Section 34183 be accomplished with respect to those funds? For such agencies, the distribution of property taxes included amounts for pass through payments.

A. The Supreme Court postponed the date for this distribution to May 16, 2012. We believe it did not intend that the distribution would be voided by its stay. Had it intended that result, we believe it would have been explicitly done so. As the Supreme Court stated the court action “ought not prevent the Legislature’s valid enactment from taking effect. Thus, the court reformed the dates not to eliminate the need for performance of any action but simply to delay that performance.

In order to accomplish the intent of the decision, we have consulted with county auditor-controllers and successor agencies to develop the following recommended procedures.

We assume redevelopment agencies have made the pass through payments associated with this revenue. If these payments have not yet been made, they are enforceable obligations of the successor agency.

We recommend that successor agencies report their Recognized Obligation Payment Schedule and the administrative cost allowance for the entire six month period from January 1, 2012 to June 30, 2012 as soon as practical to the review agencies and the county auditor-controller, and in no case later than April 15, 2012. For those agencies

that received the regular property tax allocation in December, those amounts determined to be due to taxing agencies for the January to June period should be deducted from the June 1 payments due to successor agencies for the July 1, 2012, through December 31, 2012 period. This will effectively recover the entire yearly amount of payments due to taxing agencies from the June 2012 property tax allocations. Successor agencies will retain the unspent balances of funds from the December or allocations. If there are insufficient funds available in the June allocations to pay the full amounts to taxing agencies, an enforceable obligation will exist for the successor agency to pay the difference to the county auditor-controller for subsequent distribution to the taxing agencies.

Q. If the Department of Finance does not approve one or more items on the Recognized Obligation Payment Schedule (ROPS) and the successor agency and its oversight board do not agree to remove the items from the ROPS, how can disputes be resolved without jeopardizing allocations of property tax on the statutorily required dates and without jeopardizing payments for obligations that are not in dispute?

A. Section 34179 (h) provides that the Department of Finance may review any oversight board action, including the adoption of an ROPS. Board actions are deemed approved if Department of Finance does not request more review time within three business days. If the Department desires to review any items in more detail, we must provide specific objections and return the action to the oversight board for reconsideration within 10 days. While we will endeavor to quickly review the ROPS and e-mail questions and requests for more information, we recognize that some items will be complex and require significant time to produce records, and for us to review and make determinations as to what constitute enforceable obligations in our view.

Department of Finance recognizes that a primarily goal of ABx1 26 is to ensure that contractual obligations are performed and payments made in a timely manner. Another primary objective is to allow funds not needed to satisfy enforceable obligations to flow promptly to taxing agencies and successor agencies on statutorily specified dates. In order for funds to flow promptly and be available to successors to pay obligations (especially undisputed ones), a ROPS must be available to the county auditor in sufficient time to determine the amount of property tax to distribute to Recognized Obligation Trust Funds and to taxing agencies.

While we hope that most issues can be resolved before the time that the auditor must make the property tax distribution, we recognize that some may require extensive review and some will simply be matters to be disputed. The most expeditious way for a ROPS to be adopted timely is for a successor agency with a disputed item or items to agree to remove the disputed items from the ROPS, while retaining the right to continue the discussion or resolution of the dispute. If items can be satisfied from retained funds rather than current period property tax revenues, then Finance may agree to the establishment of reserves for such items to be included in the ROPS, with the expressed understanding that no expenditures may be made from those reserves without a subsequent amendment of the ROPS, also subject to Finance review. If a dispute is resolved, the item may be amended into the ROPS and property tax can be allocated for it on a future distribution date, if that is the appropriate funding source.

Based on our discussion with county auditors, we believe it is essential that they receive an approved ROPS no later than five business days before the date property tax must

be distributed to successor agencies and taxing agencies. Department of Finance will deem whatever items that are not disputed at that time to be the valid ROPS for that time period and will transmit that information to the county auditor.

Any taxing agency, Department of Finance, and the State Controller may litigate to enforce any provision under the dissolution provisions of ABx1 26. While we prefer not to take this course, this may be one way of resolving disputes. Successor agencies or other parties may also initiate litigation. Again we do not see this as the best way to resolve most disputes and it will often not be very timely, thus we will endeavor to resolve as many disputes as we can outside of the litigation process.

Q. Should pass through payments made under Section 34183 (a) be limited to the amount of property tax share of net of amounts of redevelopment property tax after payment of obligations and administration as indicated by Section 34188 (a) (2)?

A. Department of Finance believes that the intent of ABx1 26 was to preserve existing property tax allocations for current revenues, including pass through payments. Section 34183 controls those allocations. Finance believes the intent of that paragraph in Sec 34188 is to apply a limitation only to payments of other moneys than those that are distributed through the Redevelopment Property Tax Trust Fund. For the distribution of other money, such as proceeds from asset sales, an agency with a pass through agreement can receive additional money to the extent the amount of funds exceeds its share of the property tax after debt service, administration, and the amount of pass through payments it has already received under Sec. 34183 for that six month fiscal period.

Q. How can successor agencies and oversight boards ensure that variations in obligations payment requirements between the six month periods ABx1 26 sets up can be accommodated and bills paid in a timely fashion?

A. The architecture of AB 26x1 is that current payments due should typically be funded with current revenues or the funds that were previously raised for those purposes. ABx1 26 provides for a priority to use existing balances and dedicated funds before using current tax allocations. We recognize that some future payments may be much higher than typical payments, e.g. bullet payments for bonds, and payments on large construction projects. To the extent bond funds or grant funds are available for such construction payments; they must be used until exhausted. If it is necessary to create reserves to ensure large bond payments can be made, such reserves should be created. However, we recommend that they not be funded all at once or from current balances unless a level contribution approach cannot be made to work. This will preserve current and future stability of revenues to taxing agencies.

Finance suggests that successor agencies develop a long term budget that incorporates estimates of periodic payments and revenues, such as staff compensation, debt service on bonds and payments on projects and a long term asset and liability disposition plan discussed below. This should be revised as assets and liability values are determined and payment dates are firmed up. Such a long term plan will help avoid surprises that could result in payments to taxing agencies being significantly reduced or reserves redirected to purposes other than what they were created for because payments were not anticipated.

In its reviews of oversight board actions, Finance will be endeavoring to both ensure maximum stable revenues to taxing agencies and prudent fiscal management to provide for payment of obligations, both present and future. To assist us in this we would appreciate receiving any long term budgets and asset and liability disposition plans. Deposits to reserves for extraordinary future obligations may be included in an ROPS. Finance is prepared to accept these if there is a demonstration of the need for them such as would be apparent from the long term budget.

Q. Is it permissible to carry or create reserves for contingencies such as potential liability due to current or expected litigation, claims related to construction contracts, unfunded liabilities for employees or other future period obligations?

A. ABx1 26 explicitly recognizes that there will be a need to create reserves for some bond payments. It generally recognizes that the successor and oversight boards have fiduciary duties to obligation holders and should take whatever actions are prudent to ensure payments. The statute does not currently recognize contingent or unknown obligations, thus creation of reserves for such things through a Recognized Obligation Payment Schedule is not permitted. It is expected that bond proceeds will be retained in reserves for future payments including close-out claims.

Q. How should successor agencies deal with the disposition of the many assets and longer term liabilities they have received from the former redevelopment agency and how should those be managed?

A. While ABx1 26 does not specify a time when such work should be done, it does direct that successor agencies conduct this work timely and with the intent to maximize value. Finance recommends that the oversight board direct staff to develop an overall asset and liability disposition plan. Each asset and liability should be cataloged, determinations made as to when payments may be due or received, and a value estimated. Agencies should be able to use the audits required under existing law and ABx1 26 to help in this work. To the extent that outside expertise is needed for valuations, this should be acquired at the direction of the oversight board. It is the intent of the bill that funds and asset values may be retained to the extent they are necessary or are already pledged to retire future liabilities (see Sec. 34177 (c) (e)).

Once a complete catalog of assets and liabilities values exist, the successor agency should develop a plan for retirement of debt that first uses dedicated funds, and secondly spreads the fiscal burden of payments over the remaining years of the liability so that proceeds to taxing agencies do not vary more than necessary. Alternately the oversight board may direct that existing balances or funds to be received from assets be paid or reserved for liabilities, to reduce overall costs. While it is our expectation that some large unencumbered balances may be available for distribution to taxing agencies soon, the oversight board should assure itself that it has a workable plan to retire all known or foreseeable debts before large disbursements are made.

Q. How should unfunded liabilities of pension systems contracted with the Public Employees Retirement System be handled? How should other public employee benefit liabilities, such as retiree health care, be handled?

A. These are liabilities transferred to the successor agency and constitute enforceable obligations when payments will become due. In the next few years, it is Finance's

expectation that the employees of successor agencies that are retaining employees covered by a PERS contract will continue to be active members and the successor agency will continue to pay regular rates. Once the successor agency reaches a stage where there are few employees left or a plan exists to reach that state, PERS will be able to reevaluate the actuarial liability. At that point, since tax proceeds can continue to pay liabilities until the agency would have ceased existence under prior law, there are options for how to deal with remaining employees and liabilities. The transfer of employees to the successor agency does not trigger an automatic termination of the PERS plan. No successor agency should terminate its retirement plan with PERS without consulting with them about the options. It will likely be more financially favorable to continue as an active system, an inactive system, or shift to sunset status for some period of time. Successor agencies should also estimate the value of other employee benefit obligations as part of their overall long-term asset and liability plan and establish a reserving plan to fund them.

Successor agencies whose employees are members of non-PERS plans should consult with the administrator of the plan regarding liabilities and payment options. To the extent that city, county, or JPA employees were doing work on contract with the redevelopment agency, and continue to so function, Finance believes no unfunded liability obligation exists to the city, county or JPA retirement system unless it was explicitly set forth and monetized in the contract.