SENATE COMMITTEE ON APPROPRIATIONS
Senator Anthony Portantino, Chair
2021 - 2022 Regular Session

SB 438 (Laird) - Redevelopment: enforceable obligations: City of Atascadero

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Policy Vote: GOV. & F. 5 - 0
Mandate: No
Consultant: Mark McKenzie

Bill Summary: SB 438 would deem specified loan agreements between a redevelopment agency (RDA) and the City of Atascadero to be enforceable obligations that can be repaid from property tax increment revenues, as specified.

Fiscal Impact: Estimated increased General Fund expenditures of up to $1.3 million over a period of years, as a result of the designation of $2.3 million in outstanding loan balances between the City of Atascadero and the former RDA as enforceable obligations.

Staff notes that approximately 57% to 59% of residual property tax increment revenues in the City of Atascadero RDA project area are allocated to K-14 school entities. Repayment of loans to the City of Atascadero would encumber property tax increment that would otherwise be redistributed to taxing entities, including schools. The General Fund must generally backfill any amounts that would otherwise go to schools under Proposition 98's minimum funding guarantees, if Test 2 or 3 are operative. If Test 1 is operative, as is the case currently, reductions in property tax allocations to local taxing entities would not be backfilled by the General Fund. (see staff comments below)

Background: Historically, the Community Redevelopment Law has allowed a local government to establish redevelopment agencies (RDAs) and capture all of the increase in property taxes that is generated within the project area beyond the base year value (referred to as "tax increment") over a period of decades. Prior to their dissolution pursuant to ABx1 26 (Blumenfield) Chap 5/2011, RDAs used tax increment financing, oftentimes issuing long-term debt in the form of tax allocation bonds, to address issues of blight, construct affordable housing, rehabilitate existing buildings, and finance development and infrastructure projects.

Existing law establishes procedures for winding down RDA activity, including a requirement that successor agencies dispose of former RDAs' assets under direction of an oversight board. Successor agencies are required to make any payments related to enforceable obligations from former RDA property tax revenues that are deposited into a Redevelopment Property Tax Trust Fund (RPTTF), as specified in an adopted biannual recognized obligation payment schedule (ROPS). Enforceable obligations include RDA bonds, bond-related payments, certain loans (including loan agreements between and RDA and the city or county that created it within two years of the creation of the RDA), payments required by the federal government, obligations to the state or imposed by state law, payments to RDA employees, judgements or settlements, and other legally binding and enforceable agreements or contracts. Unencumbered balances of RDA funds are remitted to the county auditor-controller for distribution to local taxing entities in the county, including schools. Successor agencies cannot enter into new enforceable obligations.

The Department of Finance (DOF) reviews each ROPS to determine if the listed payments meet the statutory criteria for repayment, and has the authority to disallow any payments that do not meet those criteria. Existing law, AB 1484 (Budget Committee), Chap 26/2012, requires DOF to provide a successor agency with a "finding of completion" after the agency remits specified RDA property tax allocations and unencumbered cash assets to the county auditor-controller through a due diligence process. Once the successor agency receives a finding of completion, the agency is authorized to:

- Transfer former RDA properties to the city or county, or otherwise dispose of the property in accordance with a DOF-approved long-range property management plan (LRPMP), as specified.
- Repay loans made by the city or county to the RDA, if the loan is deemed to have been made for legitimate redevelopment purposes, and it meets other specified requirements. For loans between a former RDA and the city or county that established it, the loan agreement must include a requirement that the RDA was obligated to repay the loan pursuant to a required repayment schedule. Twenty percent of repayment proceeds must be transferred to the Low and Moderate Income Housing Asset Fund, as specified.
- Expend bond proceeds in excess of the amounts needed to satisfy approved enforceable obligations in a manner consistent with the original bond covenants.

The City of Atascadero, a city of over 30,000 people in San Luis Obispo County, created its RDA in 1986. The RDA did not start receiving property tax increment until 2011 to revitalize its downtown. The City made three loans to its RDA between 1998 and 2002, totaling $1.375 million, to (1) start-up the RDA, (2) provide a revolving loan fund, and (3) purchase the building of an adult store and the adjacent abandoned gas station. These loans did not include a payment schedule for the RDA to repay the City. While the RDA intended to repay the loans from the City over the next few years, the 2003 San Simeon earthquake concentrated the focus of the RDA on repairing the heavily damaged downtown city hall and other disaster relief, and the Great Recession further delayed plans to repay these loans. The RDA did not repay these loans before RDAs dissolved in 2011, but did make consistent interest payments on loans 1 and 3, and principal and interest payments on loan 2. In 2013, the City was able to reoccupy City Hall and received a finding of completion from DOF for its RDA. Since these loans were not initiated in the first two years following the creation of the RDA, and the loan agreements did not have repayment terms, state law prevented them from becoming enforceable obligations repayable with RPTTF revenue.

Despite these statutory constraints, the City of Atascadero's oversight board adopted a resolution on July 30, 2018 approving an agreement to reinstate these three loans from the City to the RDA. The DOF objected to the oversight board action and disapproved the reinstatement of the loans in September of 2018. Regardless, the successor agency included proposed payments of $180,000 to the City from RPTTF revenues in its 2019-20 ROPS for the three City loans that had a projected outstanding balance of $2.26 million, including accrued interest. Following a meet and confer process, DOF disallowed these payments because the loan agreements do not include specific terms of repayment to illustrate the former RDA was obligated to repay the loans, pursuant to the dissolution statutes.

Proposed Law: SB 438 would deem loan agreements between an RDA and the City of Atascadero between January 1, 1999 and January 1, 2003 to be enforceable obligations, notwithstanding specified requirements in existing law.

Staff Comments: Proposition 98, a constitutional amendment approved by the voters in 1988 and modified in 1990, establishes a minimum funding requirement for K-12 schools and community colleges, referred to as the minimum funding guarantee. The state meets the minimum guarantee through a combination of General Fund and local property tax revenues, as specified in the three main tests for calculating the guarantee. Each test takes into account certain inputs, including General Fund revenue, per capita personal income, and student attendance. In Test 1 years, where schools receive a set percentage of State General Revenue, local reductions of property tax revenues decreased property tax revenues *are not backfilled* by the State General Fund. If either Test 2 or Test 3 are operative, in which case the funding guarantee is based on prior year funding levels (including local property tax revenue) and other economic factors, the State General Fund *must backfill* any decreased property tax revenues for nonbasic aid districts, as specified. The Legislative Analyst's Office (LAO) most recent forecasts predict that Test 1 will be operative through 2023-24, with increased uncertainty in the latter part of the forecast period. These uncertainties are exacerbated by questions surrounding the COVID-19 pandemic and its impacts on projected economic recovery.

This bill would result in increased payments of RPTTF funds to the City of Atascadero at the expense of other local taxing entities, including schools, over an unknown period of years beginning in 2022-23. The amount allocated each year for loan repayments, and the impacts to local taxing entities, depends upon a number of factors that determine the availability of RPTTF revenues after paying down other obligations of the former RDA. For illustrative purposes, the successor agency proposed to pay the City $180,000 for the outstanding balance of $2.26 million on the three loans in its proposed 2019-20 ROPS. Assuming a similar amount of payments each year, the repayment period would be approximately 12 years, and would result in approximately $100,000 in reduced payments to schools each year over the repayment period. As noted above, the state General Fund impact of this bill would depend upon which Proposition 98 test is operative. The LAO estimates that Test 1 will be operative through 2023-24, while noting some uncertainty, in which case the bill would result in reduced revenues available to local schools and other taxing entities, but would not impact the state General Fund in the short term. To the extent economic factors change in the next several years and Test 2 or 3 become operative, the state General Fund will backfill any losses to local school entities that occur as a result of the bill.

Staff notes that numerous cities made loans to their RDAs for many reasons over the years. The dissolution statutes were structured to allow repayment of loans made in the first two years of an RDA's existence, recognizing the need for startup funds for redevelopment activity before tax increment was generated. In addition, the dissolution statutes allow for repayment of loan agreements between a city and its RDA after DOF issued a finding of completion, as long as the loan agreements included a definitive obligation for repayment of the loan, as evidenced by a defined repayment period. This bill would allow for repayment of loans that the City of Atascadero made to its RDA, despite those limitations specified in the dissolution statutes. The Committee may wish to consider whether the justification for providing this special benefit to the City of Atascadero is warranted, considering other cities may have made similar loan agreements with their RDAs prior to dissolution that have never been repaid.

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