

Alive Not Dead: The Revival of Redevelopment Post-*Matosantos*

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Introduction

In the 2011 case of *California Redevelopment Association v. Matosantos*, the California Supreme Court eliminated redevelopment agencies in the state.¹ Created after World War II, these redevelopment agencies' purpose was to eradicate and redevelop blighted communities, and has been part of the local government landscape for over six decades.² From 2009 to 2010, over eighty percent of California's 480 cities and thirty-one of the state's fifty-eight counties had a redevelopment agency, totaling about 425 redevelopment agencies throughout the state.³ Redevelopment agencies were credited for creating Hollywood, San Diego's Gaslamp Quarter, a large number of office towers highlighting city skylines, large industrial and commercial spaces, and affordable housing units.⁴ Not only do redevelopment agencies improve the city landscape, but they also generate economic activity. The Center for Economic Development ("CED") estimated that every dollar spent on

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1. Cal. Redev. Ass'n v. Matosantos, 53 Cal. 4th 231, 262 (2011).
2. *Id.* at 245–46.
3. Peter Detwiler, *Broken Promises: The End of California Redevelopment*, 64 PLAN. & ENVTL. L. No. 6, 2012, at 4.
4. *Id.*; Billy Hamilton, *The Fight for Hollywood's Soul: Redevelopment and Incentives*, 64 ST. TAX NOTES, Apr. 30, 2012, at 321.

redevelopment projects led to about fourteen dollars in in-state sales of goods and services.⁵

In 2011, the California state government faced a \$25 billion budget deficit.⁶ As a result, the California Legislature passed two bills, Assembly Bill 1X 26 (“AB 1X 26”) and Assembly Bill 1X 27 (“AB 1X 27”), hoping to divert funds from redevelopment agencies to school districts and special districts.⁷ The two bills were challenged in the California Supreme Court.⁸ In December 2011, the Court ruled that AB 1X 27 was unconstitutional, but held that AB 1X 26 was constitutional.⁹ Despite the California Supreme Court’s clear ruling on the constitutionality of AB 1X 26, lawsuits have since erupted challenging the constitutionality of AB 1X 26 on different grounds.¹⁰

The *Matosantos* decision led to dissension within California as city officials opposed the dissolution of redevelopment agencies, and blamed the dissolutions for their cities’ economic woes.¹¹ While redevelopment was problematic and controversial prior to *Matosantos*, city officials cited the elimination of redevelopment agencies as the cause for bankruptcies, fiscal emergencies, and uncompleted development projects.¹² For example, Culver City planned to declare a fiscal emergency and raised taxes because of the lost revenue caused by the dissolution of redevelopment agencies.¹³ Cities such as Stockton, Mammoth Lakes, and San Bernardino claimed that the “state raid on redevelopment funds helped push them over the brink” and into bankruptcy.¹⁴ These problems caused by the eradication of redevelopment agencies highlight these

5. Estimates based on data from the 2002-2003 fiscal year. Andrew Schouten, *Clear as Mud: Chapter 98 and California’s Community Redevelopment Law*, 38 MCGEORGE L. REV. 216, 216 (2007) (internal citation omitted).

6. Marc M. Schneier, *California Supreme Court Rules that Redevelopment Agencies Are Not Constitutionally Immune from Dissolution by the Legislature*, 33 No. 3 CONSTRUCTION LITIG. REP. 15 (2012).

7. *Id.*

8. See *Matosantos*, 53 Cal. 4th at 242.

9. *Id.*

10. See League of California Cities, *Statewide Summary of Redevelopment Litigation* (Feb. 2014), available at www.cacities.org/UploadedFiles/LeagueInternet/7d/7d11e9fe-c72e-47c8-81c3-ea5390299e4e.pdf (listing the lawsuits that have been filed concerning redevelopment).

11. See generally Billy Hamilton, *The Mermaid’s Tale: California’s Redevelopment Agency Fight*, 65 STATE TAX NOTES 743 (2012).

12. *Id.*

13. *Id.*

14. *Id.*

agencies' importance within California's economy and also explain why organizations and local governments are trying to revive redevelopment by filing lawsuits to challenge the constitutionality of AB 1X 26.

This Note examines the state of redevelopment after the California Supreme Court's decision in *Matosantos*. It also looks at the constitutionality of AB 1X 26 and its subsequent "clean up" bill, AB 1484. Part I provides a brief history of redevelopment in California and the financing scheme for redevelopment. Part II looks at the events giving rise to AB 1X 26 and AB 1X 27 and details the California Supreme Court's decision in *Matosantos*. Part III discusses the state of redevelopment post-*Matosantos* and describes the clean up bill, AB 1484. Part IV surveys the different redevelopment lawsuits currently pending in California courts and discusses the constitutional and legal issues at the center of these lawsuits. Finally, Part V analyzes the legal arguments regarding the constitutionality of AB 1X 26 and AB 1484, such as: (1) whether reduced bond ratings of municipal bonds constitute an impairment of contracts; (2) whether the failure to honor existing obligations is an impairment of contracts; (3) whether the penalties imposed by AB 1484 violated the California Constitution regarding sales, use, and property taxes; and (4) whether AB 1484 violated the non-delegation doctrine.

I. Redevelopment Agencies in California

In 1945, through the Community Redevelopment Act, the California Legislature created redevelopment agencies ("RDAs") to improve blighted communities in the interest of the "health, safety, and welfare" of the people in California.¹⁵ RDAs were administered through local sponsoring agencies, which were tasked with preparing and carrying out "plans for improvement, rehabilitation, and redevelopment of blighted areas."¹⁶ A local agency could acquire real property through the power of eminent domain, dispose of property by lease or sale without public bidding, clear land and construct infrastructure necessary for building on project sites, and undertake certain improvements to other facilities in the area.¹⁷

15. CAL. HEALTH & SAFETY CODE § 33037(a), (c) (2014). *See also id.* § 33000.

16. *Id.* § 33131(a).

17. Schneier, *supra* note 6. *See* CAL. HEALTH & SAFETY CODE §§ 33391(b), 33420, 33421, 33430, 33431, 33445 (2014).

Though redevelopment officially began in 1945, its implementation stalled until 1952 due to lack of funding.¹⁸ In 1952, California voters passed a bill to help finance redevelopment.¹⁹ As a result of that bill, Article XIII, section 19 was added to the California Constitution, which created a tax increment funding (“TIF”) scheme to help finance redevelopment.²⁰ Under the TIF scheme, RDAs would be funded through tax revenue generated by the increased value of redeveloped property.²¹

Through the TIF framework, public entities receiving property tax revenue for RDAs would be “allocated a portion [of the property tax revenue] based on the assessed value of the property prior to the effective date of the redevelopment plan.”²² The tax increments that RDAs received were based on the taxes collected on real property within the redevelopment area “that exceed[ed] the property taxes received in the tax year prior to the redevelopment plan’s adoption.”²³ Once the property taxes in the redevelopment area were collected, the revenue was split between the taxing agency and the RDA.²⁴ The taxing agency would receive the revenue it would have received under a value that was assessed at the time the city started the redevelopment project; the RDA would receive the tax revenue that was in excess of the assessed value distributed to the other taxing entities.²⁵ This was based on the belief that the increased value was the result of redevelopment.²⁶ Consequently, RDAs would receive an increasing proportion of tax revenue, whereas other agencies’ tax revenue would remain the same.²⁷ The increment the RDAs received would be “deposited into a special fund” that would be used to pay off debt the RDA incurred.²⁸

In a way, TIF was “self-financing” because the “incremental revenues that [were] generated [were] used to pay for the program

18. Detwiler, *supra* note 3, at 5.

19. *Id.*; Schouten, *supra* note 5, at 220.

20. CAL. CONST. art. XVI, § 16 (2014).

21. Daniel S. Maroon, *Redevelopment in the Golden State: A Study in Plenary Power Under the California Constitution*, 40 HASTINGS CONST. L.Q. 453, 455 (2013).

22. Cal. Redev. Ass’n v. Matosantos, 53 Cal. 4th 231, 246 (2011).

23. Schouten, *supra* note 5, at 220.

24. *Id.* at 220–21.

25. *Id.*

26. *Id.* at 221; Maroon, *supra* note 21, at 455.

27. *See id.*

28. Schouten, *supra* note 5, at 221.

that spurred the growth.”²⁹ To illustrate,³⁰ assuming the value of a property is \$100,000, this would generate \$1,000 in property taxes (based on property tax rate of one percent). After redevelopment, the property value increased to \$1,000,000 and would therefore generate \$10,000 in property taxes. The taxing agencies in the redevelopment area, such as the city, school district, or other would still receive \$1,000 of the property taxes divided amongst all the taxing agencies. The additional \$9,000 in property taxes would all go to the RDA. Funds generated through the TIF were to be spent on redevelopment “that largely benefit the project area,” such as creating sidewalks and other “improvements that a private developer would otherwise build.”³¹ Twenty percent of the TIF funds were to be used to construct low- and moderate-income housing.³²

II. *Matosantos* and Prior Events

A. Budget Crisis in California

Although the TIF funding scheme undoubtedly led to increased economic and redevelopment activity, it has also been criticized.³³ Because of the TIF scheme, RDAs received a disproportionate amount of real property taxes at the expense of school districts and special districts as money was essentially diverted from local governments to the RDAs.³⁴ This problem was exacerbated by the passage of Proposition 13 (codified as Article XIII A of the California Constitution) in 1978, which capped property tax rates at one percent.³⁵ As a result, funds from the property tax that were distributed to local governments declined by sixty percent.³⁶ More importantly, this meant that the California state government bore the burden of meeting the mandatory funding levels for public schools required by the California Constitution via Proposition 98.³⁷ This

29. Maroon, *supra* note 21, at 455.

30. The numbers in this hypothetical are based on the hypothetical found in Schouten, *supra* note 5, at 221.

31. *Id.*

32. *Id.*

33. Hamilton, *supra* note 11.

34. *Id.*

35. CAL. CONST. art. XIII A, §1(a) (2014). *See also* Schouten, *supra* note 5, at 220; Maroon, *supra* note 21, at 460.

36. Schouten, *supra* note 5, at 222.

37. *Id.*; Cal. Redev. Ass'n v. Matosantos, 53 Cal. 4th 231, 245 (2011). In 1988, Proposition 98 amended the California Constitution to add minimum funding levels for

posed a real problem for local governments, such as counties, cities, school districts, community college districts, and special districts that depended on the incremental tax revenue to provide vital public services.³⁸ Under the California Constitution, these forms of local governments could not receive any funds from the property tax increment until the RDA closed its project area.³⁹

While RDAs received about \$1.9 billion in property tax increment revenues from 1999-2000, that number grew to about \$5.4 billion in 2009-2010, with unmatured tax allocation bonds of \$19.1 billion.⁴⁰ The amount received by RDAs grew significantly while the numbers for other local governments remained the same.⁴¹ From 1982-1983, RDAs only received 3.6 percent of the total property tax revenues.⁴² By 2009-2010, RDAs were receiving twelve percent of total property tax revenue.⁴³

B. AB 1X 26 and AB 1X 27: Potential Solutions to Budgetary Problems

In response to the declared fiscal emergency in California, Governor Jerry Brown proposed to eliminate redevelopment in order to funnel some of the redevelopment monies to special districts.⁴⁴ As a result, the California Legislature passed both AB 1X 26 and AB 1X 27 to help balance the state budget by rediverting funds back to local governments—especially school districts.⁴⁵ There were two different components to AB 1X 26. The first component, called the “freeze,” prevented RDAs from incurring new or expanding existing monetary

education and required the state to “set aside a designated portion of the General Fund for public schools.” *Id.* In 1990, Proposition 111 amended the Constitution by increasing the minimum funding for public schools. *Id.* To meet the requirements of Proposition 98, the state Legislature created the county educational revenue augmentation funds (“ERAF”), which is an “accounting device” to “reallocate property taxes to school districts from other government entities.” *Id.* The amount of property tax given to other governmental entities was reduced and the difference was deposited into the ERAF. The money in the ERAF was classified as part of the General Fund, and then distributed to school districts. *Id.*

38. Detwiler, *supra* note 3, at 6.

39. *Id.*

40. *Id.* at 5.

41. *See id.* at 6.

42. *Id.*

43. *Id.*

44. *Id.* at 7; Cal. Redev. Ass’n v. Matosantos, 53 Cal. 4th 231, 241 (2011).

45. *Id.* at 250.

or legal obligations.⁴⁶ This restricted the powers of RDAs, and prohibited RDAs from issuing and selling bonds, incurring debt, accepting loans, giving refunds, restructuring or refinancing indebtedness or obligations, and creating new redevelopment agencies.⁴⁷ The freeze component however, did not eliminate any previous enforceable obligations.⁴⁸ In fact, AB 1X 26 required all successor agencies to continue making all “scheduled payments for enforceable obligations.”⁴⁹ The purpose of the Act’s freeze provision was to “preserve, to the maximum extent possible, the revenues and assets of redevelopment agencies so that those assets and revenues that [were] not needed to pay for enforceable obligations [could] be used by local governments to fund core governmental services” such as schools.⁵⁰ The second component, known as the “dissolution” component, eliminates RDAs within the state.⁵¹ Control of the assets would transfer to successor agencies, such as the cities or counties that created the RDAs.⁵² The successor agencies would then be tasked with making payments and meeting existing obligations under previous RDA agreements.⁵³

On the other hand, AB 1X 27 was an escape hatch that allowed RDAs to continue to exist as long as they were able to meet certain requirements.⁵⁴ Specifically, RDAs would not dissolve as long as the city or county with an RDA agreed to make payments that would go to both the “county ERAF and a new county special district augmentation fund on behalf of the redevelopment agencies.”⁵⁵ This would then benefit the state’s schools and special districts.⁵⁶ If the city or county elected to make the payments, it had to adopt a resolution

46. *Id.*

47. CAL. HEALTH & SAFETY CODE §§ 34162(a), 34166 (2011).

48. *Id.* § 34169.

49. *Id.* § 34169(a).

50. *Id.* § 34167(a).

51. *Id.* § 34172.

52. Cal. Redev. Ass’n v. Matosantos, 53 Cal. 4th 231, 251 (2011).

53. *Id.*

54. See Paul Esformes & Zane Gresham, *Redevelopment Agencies: Dead, But Not Buried*, MORRISON FOERSTER CLIENT ALERT, Jan. 4, 2012, at 1, available at <http://www.mofo.com/files/Uploads/Images/120104-Redevelopment-Agencies.pdf> (classifying AB 1X 27 as the “alternative survival scheme” to AB 1X 26).

55. *Matosantos*, 53 Cal. 4th at 251; see also *supra* note 37.

56. *Matosantos*, 53 Cal. 4th at 241.

of intent.⁵⁷ The RDA would not dissolve as long as it made timely remittances.⁵⁸

C. The California Supreme Court's Decision

The possible dissolution of RDAs was especially troublesome for cities because “redevelopment had become so deeply embedded in the structure of every municipality in the state” and served as the only way for cities to “capture a greater portion of property tax revenue.”⁵⁹ As a result, in *California Redevelopment Association v. Matosantos*, the California Redevelopment Association and the League of California Cities sued California’s Director of Finance, Ana Matosantos.⁶⁰ The suit challenged the constitutionality of both AB 1X 26 and AB 1X 27, specifically alleging that that the legislation was invalid because it violated Proposition 22 (codified under Article XIII, section 25.5(a)(7) of the California Constitution), which limited the state’s ability to collect payments from RDAs.⁶¹ The California Supreme Court held AB 1X 27 was unconstitutional because it violated Proposition 22.⁶² It violated Proposition 22 because AB 1X 27 required cities to make payments that would benefit the state and because it would replace funding that the state otherwise would have to provide under Proposition 98.⁶³ Thus, the Legislature’s only alternative to dissolution was eliminated.

AB 1X 26, however, was held constitutional, effectively allowing the end of RDAs in California.⁶⁴ The basis for the court’s decision was the notion that “[w]hat the Legislature has enacted, it may repeal.”⁶⁵ Therefore, it was well within the Legislature’s ability to eliminate RDAs. The “freeze” component of AB 1X 26 was also

57. CAL. HEALTH & SAFETY CODE § 34193(b) (2011), *invalidated by Matosantos*, 53 Cal. 4th 231 (2011).

58. CAL. HEALTH & SAFETY CODE § 34193(a) (2011), *invalidated by Matosantos*, 53 Cal. 4th 231 (2011).

59. Josh Stephens & William Fulton, *A Quickie Divorce: Local Government and Redevelopment Agencies in California*, 64 PLAN. & ENVTL. L. No. 6, 2012, at 9.

60. *Matosantos*, 53 Cal. 4th at 242 (citing CAL. HEALTH & SAFETY CODE § 25.5(a)(7) (prohibiting the Legislature from enacting a statute that would require an RDA “to pay, remit, loan, or otherwise transfer, directly or indirectly, taxes on ad valorem real property and tangible personal property pursuant to Section 16 of Article XVI to or for the benefit of the state, any agency of the state, or any jurisdiction”)).

61. *Id.*

62. *Id.* at 264.

63. *Id.*

64. *Id.* at 265.

65. *Id.* at 255.

held constitutional.⁶⁶ Since the Legislature has the power to terminate RDAs, it follows that the Legislature would have the “ability to decide when redevelopment agencies could cease to exist . . . or at what point, as part of winding up and dissolving, they would be relieved of the ability to make new binding commitments and engage in new business.”⁶⁷ It would not be reasonable to expect an existing entity to “dissolve instantaneously.”⁶⁸ Therefore, the California Supreme Court upheld the constitutionality of AB 1X 26, resulting in the dissolution of RDAs effective February 1, 2012.⁶⁹

III. Redevelopment Agencies Post-*Matosantos*

While the California Supreme Court’s decision in *Matosantos* was a death sentence to redevelopment in California, the decision did not end the story for redevelopment. In fact, it marked the beginning of a fight by cities to restore some remnants of redevelopment. The state could not have anticipated the problems that would erupt as a result of upholding AB 1X 26 and striking down AB 1X 27. In addition, AB 1484, the cleanup bill enacted to further enforce AB 1X 26, has been met with opposition and litigation.⁷⁰

A. Enforcing AB 1X 26: Winding Down Redevelopment and Managing Existing Obligations

One of AB 1X 26’s main goals was to wind down redevelopment—mainly by paying off existing obligations.⁷¹ After the court’s holding in *Matosantos*, however, AB 1X 26 created more questions than answers. Most notably, what would happen to the RDAs’ existing obligations and assets? Which “enforceable obligations” would be recognized as part of the winding down process?⁷² Moreover, no information was given as to how assets should be disposed of,⁷³ and AB 1X 26 did not address how to handle

66. *Id.* at 264.

67. *Id.* at 263.

68. *Id.*

69. *Id.* at 265.

70. *League of California Cities Reacts to AB 1484, the Redevelopment Budget Trailer Bill*, LEAGUE OF CALIFORNIA CITIES, June 27, 2012, available at <https://www.cacities.org/Top/News/News-Articles/2012/June/League-of-California-Cities-React-to-AB-1484,-the>.

71. CAL. HEALTH & SAFETY CODE § 34175(a) (2014).

72. See Esformes & Gresham, *supra* note 54, at 2.

73. Ursula Hyman et al., *California Supreme Court Eliminates Redevelopment Agencies*, MONDAQ (Jan. 27, 2012), <http://www.mondaq.com/unitedstates/x/162514/Environmental+Law/California+Supreme+Court+Eliminates+Redevelopment+Agencies>.

contracts that are in the midst of performance.⁷⁴ Because a number of redevelopment projects were in the middle of performance, the end of RDAs would mean that many projects would terminate mid-performance, thus impairing contractual obligations.⁷⁵ Moreover, although some of the projects were contracted prior to the RDAs' dissolution, the actual performance in certain cases does not take place until after the dissolution.⁷⁶ How should these obligations be treated? Contracts with bondholders were also under the threat of impairment.⁷⁷ In all, the dissolution of RDAs did not “produce a clean break,” but rather “creat[ed] problems about as fast as it created cash for the state.”⁷⁸

Once RDAs were dissolved under AB 1X 26, successor agencies, such as the city or county that created the RDA, were tasked with honoring obligations incurred by the existing RDAs.⁷⁹ These successor agencies—vested with all the authority, rights, powers, and duties once belonging to former RDAs—were under the authority of a seven-member oversight board that would “approve and direct certain actions of the successor agency.”⁸⁰ Assets of the former RDAs were transferred to the new successor agencies.⁸¹ The former TIF funds were characterized as property tax revenues, and deposited into a Redevelopment Property Tax Trust Fund (“RPTTF”), which was administered by each of the counties' Auditor-Controllers.⁸² The funds in the RPTTF are administered for the “benefit of the holders of former redevelopment agency enforceable obligations and the taxing entities that receive pass-through payments and distributions of property taxes.”⁸³

One of the first responsibilities of the successor agencies was to continue making payments that were due under the RDAs' “enforceable obligations.”⁸⁴ Under AB 1X 26, enforceable

74. See Stephens & Fulton, *supra* note 59, at 9.

75. Hyman et al., *supra* note 73.

76. *Id.*

77. See Stephens & Fulton, *supra* note 59, at 9 (discussing the issue of whether prior development activities would continue post *Matosantos*).

78. Hamilton, *supra* note 11.

79. CAL. HEALTH & SAFETY CODE §§ 34169, 34177 (2014).

80. Hyman et al., *supra* note 73.

81. CAL. HEALTH & SAFETY CODE § 34175(b) (2014).

82. *Id.* § 34182(c)(2).

83. *Id.*

84. *Id.* § 34177(a).

obligations generally included bonds, loans of money borrowed by an RDA, payments and preexisting obligations required by federal government or state law, judgments or settlements entered against a former RDA, any legally binding and enforceable agreement or contract not otherwise void, contracts or agreements necessary for the administration or operation of a successor agency, and amounts borrowed from or payments owed to an RDA's Low and Moderate Income Housing fund.⁸⁵ Despite this statutory prescription, confusion still exists as to whether certain existing projects and obligations started by the former RDAs qualify as "enforceable obligations" under AB 1X 26.⁸⁶ Specifically, the successor agencies and the Department of Finance were at odds as to what obligations should be honored: Successor agencies wanted to honor all existing contracts so that all existing or pending projects could be completed, whereas the Department of Finance wanted to "accelerat[e] dissolution to free up tax increment funds for other purposes."⁸⁷

The California Department of Finance tried to further clarify this requirement by stating that "[p]lans, statements of intent, statements of intent to award, designations of project areas, descriptions or lists of projects, or commitments by the agency without any counter party . . . will not be considered enforceable obligations."⁸⁸ Additionally, contracts that are vague, intended to develop future proposals or contracts, or "a contract to design something" are not contracts.⁸⁹ Conversely, enforceable obligations include "written contracts for specific performance with parties that are not the sponsoring agency."⁹⁰

To fulfill its responsibilities of honoring existing obligations, successor agencies were required to prepare a Recognized Obligation Payment Schedule ("ROPS"), which listed all of the enforceable obligations owed by the RDA and the sources for paying the

85. *Id.* § 34171(d)(1)(A)-(G).

86. *See* Hyman et al., *supra* note 73.

87. Seth Merewitz & Ethan J. Walsh, *Redevelopment After RDAs: The demise of California's redevelopment agencies obliges local governments and developers to explore new financing methods*, 35 L.A. LAWYER No. 11, Feb. 2013, at 24, 28.

88. CALIFORNIA DEPARTMENT OF FINANCE, REDEVELOPMENT AGENCY DISSOLUTION UNDER ABX1 26: FREQUENTLY ASKED QUESTIONS, *available at* http://www.dof.ca.gov/assembly_bills_26-27/documents/RDA%20Web%20Page_%20Non%20Bond%20FAQs_Exhibit4.pdf.

89. *Id.*

90. *Id.*

enforceable obligations.⁹¹ Only those enforceable obligations listed and approved on the ROPS may be paid by funds from the RPTTF.⁹² After the ROPS are prepared by the successor agencies, they are submitted to the oversight board for approval.⁹³ After the oversight board reviews the ROPS, it sends the ROPS to the Department of Finance for approval.⁹⁴ If the Department of Finance chooses to review the ROPS, it has forty-five days to review and make a final determination on the ROPS.⁹⁵ Thus, even though the successor agencies have the power to list projects that would require payment on the ROPS, the ROPS is still subject to the approval of the oversight board, the Department of Finance, and the County Auditor-Controller.⁹⁶ Any of these administrative bodies can object to items they deem an unenforceable obligation and remove those items from the ROPS.⁹⁷ If the successor agency disputes the Department of Finance's determination, the parties can convene a "meet and confer," which includes an informal meeting between the successor agency and the Department of Finance, and culminates in a final determination by the Department of Finance.⁹⁸

Once the Department of Finance approves the ROPS and any disputes are resolved, the County Auditor-Controller allocates and remits monies from the RPTTF to the successor agencies every six months.⁹⁹ The money that the successor agency receives should be used for payments listed on the ROPS, in the following order of priority:

1. Debt service payments scheduled to be made for tax allocation bonds.
2. Payments scheduled to be made on revenue bonds, but only to the extent the revenues pledged for them are insufficient to make the payments and

91. CAL. HEALTH & SAFETY CODE § 34177(a)(1) (2014).

92. *Id.* § 34177(a)(3).

93. *Id.* §§ 34177(1)(2)(B), 34180(g).

94. *Id.* § 34179(h).

95. *Id.* § 34177(m).

96. *Id.* §§ 34177(m), 34179(h), 34182.5.

97. *Id.* §§ 34177(m), 34179(h), 34182.5.

98. *Id.* § 34177(m).

99. *Id.* § 34183(a).

only if the agency's tax increment revenues were also pledged for the repayment of the bonds.

3. Payments scheduled for other debts and obligations listed in the [ROPS] that are required to be paid from former tax increment revenue.¹⁰⁰

After the county auditor-controller has made the appropriate allocations to the successor agencies to pay their enforceable obligations, pass-through payments, and other administrative costs, the remaining funds in the RPTTF go to the taxing entities.¹⁰¹

B. Enacting AB 1484: The True-Up Payment Scheme and Due Diligence Review

On June 27, 2012, the California Legislature passed AB 1484 as a budget trailer bill¹⁰² to assist with the enforcement of AB 1X 26. When the *Matosantos* case was pending before the California Supreme Court, the Court stayed the implementation of AB 1X 26 for four months.¹⁰³ Because of the stay, the state was concerned that the taxing agencies did not receive the full funds they were entitled to from the RPTTF during the 2011-2012 fiscal year.¹⁰⁴ The “true-up” provision in AB 1484 was enacted to ensure that property tax revenues were properly distributed to the taxing agencies for the 2011-2012 fiscal year by recapturing payments that should have been

100. *Id.* § 34183(a)(2). In addition to funds remitted to pay enforceable obligations listed on the ROPS, the auditor-controller also remits funds to local agencies and school entities based on pass-through payment obligations, and administrative costs set forth in the administrative budget. Any remaining monies would go to local agencies and school entities pursuant to California Health and Safety Code § 34188. CAL. HEALTH & SAFETY CODE §§ 34183(a)(1), (3), (4) (2012).

101. *Id.* § 34183(a)(4).

102. Budget trailer bills are budget implementation bills passed alongside the Budget Bill to facilitate the changes that may take place in light of the newly passed Budget Bill. These budget trailer bills are heard and passed concurrently with the Budget Bill. *California's Budget Process*, CALIFORNIA DEPARTMENT OF FINANCE (Sept. 2012), available at <http://www.dof.ca.gov/fisa/bag/process.htm>. As a budget trailer bill, AB 1484 took effect immediately when it was signed. It did not attain the two-thirds vote in each chamber of the Legislature. William Dottinga, *Cities Fight California's Giant Money Grab*, COURTHOUSE NEWS SERVICE (Oct. 12, 2012, 10:05 AM), <http://www.courthousenews.com/2012/10/12/51224.htm>.

103. Cal. Redev. Ass'n v. *Matosantos*, 53 Cal. 4th 231, 274 (2011).

104. See CAL. HEALTH & SAFETY CODE § 34183.5 (2012) (acknowledging that the delayed implementation of AB 1X 26 due to *Matosantos* decision may have caused “disruption” to distribution of payments to taxing entities).

made to taxing entities during the 2011-2012 fiscal year but for the court staying AB 1X 26's implementation.¹⁰⁵ AB 1484 outlined new procedures governing the transfer of properties to successor agencies by introducing the true-up payment scheme and the submission of Due Diligence Reports ("DDR").¹⁰⁶

1. *True-Up Payments*

Under the true-up provision of AB 1484, the County Auditor-Controller determined whether the successor agency owed any true-up payments to the taxing agencies according to what was listed on the ROPS.¹⁰⁷ A successor agency owed payment under AB 1484 if the taxing agency did not receive the full funds during the 2011-2012 fiscal year.¹⁰⁸ If the successor agency owed a payment, the County Auditor-Controller sent a demand for payment to the successor agency requesting payment no later than July 12, 2012.¹⁰⁹ Then, the County Auditor-Controller made the required payments to the appropriate taxing entities no later than July 16, 2012.¹¹⁰ Any successor agency that failed to remit payment by the deadline would be subject to the following penalties:

1. The successor agency cannot pay any other obligations other than bond debt until payment is remitted to the county auditor-controller;¹¹¹
2. The city or county that created the RDA would not receive the "distribution of sales and use tax" or any payment "up to the amount owed to taxing entities, until the payment" is made;¹¹²
3. The successor agency and the city or county that created the RDA would be subject to a civil penalty in the amount equal to ten percent of amount owed to taxing entities plus an additional

105. *See id.* § 34183.5(b).

106. *Id.* §§ 34183.5(b), 34179.5, 34179.6.

107. *Id.* § 34183.5.

108. *Id.* § 34183.5(a).

109. *Id.* § 34183.5(b)(2).

110. *Id.*

111. *Id.* § 34183.5(b)(2)(C).

112. *Id.*

1.5 percent per month for each month the payment is late;¹¹³ and

4. The county auditor-controllers would deduct from future distributions of property taxes from the RPTTF the amount by which the successor agency owes. These funds from the RPTTF would otherwise be used to pay enforceable obligations.¹¹⁴

2. *Due Diligence Review*

AB 1484 also imposed on successor agencies the responsibility of conducting a Due Diligence Review (“DDR”)—a more rigorous approach than the ROPS—meant “to determine the unobligated balances available for transfer to taxing entities.”¹¹⁵ Essentially, the DDR requirement exists to determine the amount of cash assets a former RDA possesses (that are not tied to enforceable obligations) so that these funds can be distributed to the taxing entities.¹¹⁶ AB 1484 required a “licensed accountant, approved by the county auditor-controller . . . with experience and expertise in local government account” to perform the reviews.¹¹⁷ The first DDR was made for the Low and Moderate Income Housing fund due October 15, 2012, and the second was for all other funds due January 15, 2013.¹¹⁸ Once the amount of cash (and cash equivalent) available to the taxing entities is determined, the reports are then submitted to the oversight board, the county auditor-controller, the state controller, and the Department of Finance for review.¹¹⁹ The administrative bodies can make any adjustments to the amounts based on their own findings.¹²⁰ While the Department of Finance must meet and confer with the successor agency regarding any disputes to the adjustments made, ultimately, the Department of Finance makes the final

113. *Id.*

114. *Id.* § 34183.5(b)(3).

115. *Id.* § 34179.5.

116. *Aftermath of the Dissolution of Redevelopment Agencies in California—What Happens Next?* (85th Annual Meeting), STATE BAR OF CALIF. (Oct. 13, 2012), available at <http://html.documentation.com/cds/SBC2012/Support/PDFs/088.pdf>; CAL. HEALTH & SAFETY CODE § 34179.5 (2012).

117. CAL. HEALTH & SAFETY CODE § 34179.5(a) (2012).

118. *Id.* § 34179.5(c)(5).

119. *Id.* § 34179.6.

120. *Id.* § 34179.6(d).

determination as to the amounts of funds owed.¹²¹ After the Department of Finance determines how much money the successor agency is to remit to the county auditor-controller for distribution to other taxing entities, the successor agency receives notice of the amount owed and must make payment by the statutorily imposed deadlines.¹²² Once the payment is made, the Department of Finance awards the successor agency a “Finding of Completion.”¹²³ If the successor agency fails to make a payment, it is subject to a set of penalties, including:

1. The Department of Finance may order an offset to the distribution of sales and use tax revenue equal to the amount that is owed;¹²⁴
2. The county auditor-controller may reduce the property tax allocations to the city or county;¹²⁵ and
3. The Department of Finance can “direct the county auditor-controller to deduct the unpaid amount from future allocations of property tax to the successor agency” until the payment is made.¹²⁶

Thus, changes to the redevelopment dissolution process would introduce new requirements with potentially dangerous penalties to both the cities and counties should the *successor agency* fail to comply with the new provisions.

IV. Recent Legal Disputes¹²⁷

Despite the California Supreme Court’s determination that AB 1X 26 is constitutional, lawsuits have erupted in recent years challenging the constitutionality of AB 1X 26, as well as AB 1484. In

121. *Id.* § 34179.6(e).

122. *Id.* § 34179.6(d)-(f).

123. *Id.* § 34179.7

124. *Id.* § 34179.6(h)(1)(C).

125. *Id.*

126. *Id.* § 34179.6(h)(2).

127. Given that 150 lawsuits have been filed on numerous grounds, this Note addresses only the main constitutional arguments. The list of constitutional arguments and legal disputes in this section is not meant to be exhaustive. A list of all redevelopment-related lawsuits is available at <http://www.cacities.org/UploadedFiles/LeagueInternet/7d/7d11e9fe-c72e-47c8-81c3-ea5390299e4e.pdf>.

fact, over 150 lawsuits (and counting) have been brought by cities, successor agencies, and special districts against the State of California, California's Department of Finance and public officials associated with finance and redevelopment, such as Governor Jerry Brown, Department of Finance Director Ana J. Matosantos (now Michael Cohen), Controller John Chiang, and various county auditor-controllers.¹²⁸ Each lawsuit is at different stages of litigation.¹²⁹ A majority of the lawsuits allege infringements of both the state and federal constitutions.¹³⁰

The constitutional claims regarding redevelopment allege that the application of AB 1X 26 and AB 1484 violate either the state or federal constitution.¹³¹ A selection of the main constitutional arguments is examined below.

A. AB 1X 26: Impairment of Contracts for Reduced Bond Rating Violating Article XVI of the California Constitution

AB 1X 26's passage resulted in a decrease in bond value of the loans used to fund the many redevelopment projects.¹³² At least two lawsuits have been filed on the grounds that this lowering of the bond value is an impairment of the Contracts Clause in the U.S. Constitution.¹³³ The plaintiffs in *City of Cerritos v. State* were the first to raise an impairment of contracts argument.¹³⁴ The plaintiffs argued that AB 1X 26 "unconstitutionally impairs, negates, diminishes, denigrates, and abrogates numerous agreements, covenants, and legally enforceable commitments between and among redevelopment agencies, cities, counties, and private third parties, including bondholders and private corporations"¹³⁵ In *Syncora Guarantee Inc. v. State*, bond insurer Syncora brought suit against the State of

128. Jim Miller, *Redevelopment—One year after dissolution, litigation and dissension*, THE PRESS ENTERPRISE (Feb. 11, 2013, 7:47 A.M.), <http://www.pe.com/local-news/politics/jim-miller-headlines/20130211-redevelopment-one-year-after-dissolution-litigation-and-dissension.ece>. See also League of California Cities Summary, *supra* note 10.

129. See League of California Cities Summary, *supra* note 10.

130. See *id.*

131. See *id.*

132. Michael J. Kiely & Phillip M. Tate, *Redevelopment: Rising From The Ashes Or Final Death Rattle?*, MARTINDALE.COM (Oct. 4, 2012), http://www.martindale.com/government-law/article_Sheppard-Mullin-Richter-Hampton-LLP_1598768.htm.

133. See *id.*

134. See Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandate at 3, *City of Cerritos v. State*, No. 34–2011–80000952 (Cal. Super. Sept. 26, 2011).

135. *Id.* at 7.

California challenging the constitutionality of AB 1X 26 based on violations of both the federal and California constitutions.¹³⁶ Specifically, Syncora argued that AB 1X 26 is unconstitutional because RDAs' dissolution would impair existing contracts, thereby violating the Contracts Clause.¹³⁷ On May 29, 2013, the *Syncora* action was dismissed on the grounds that the claims were premature because there was no evidence that any of the insured bonds were in default or that defaults would "inevitably . . . occur."¹³⁸

Historically, RDAs raised funds for redevelopment projects by issuing bonds, which were constitutionally secured and backed by tax increment financing.¹³⁹ Section 16 of Article XVI of the California Constitution provides that the:

[P]ortion of the levied taxes each year in excess of that amount shall be allocated to and when collected shall be paid into a special fund of the redevelopment agency to pay the principal of and interest on loans, moneys advanced to, or indebtedness . . . incurred by the redevelopment agency to finance or refinance, in whole or in part, the redevelopment project.¹⁴⁰

Furthermore, the California Constitution provides that tax incremental financing "may be irrevocably pledged for the payment of the principal and interest on such loans, advances, or indebtedness."¹⁴¹ A pledged collateral by an RDA to "secure . . . the payment of the principal or redemption price of, or interest on, any bonds, or any reimbursement agreement with any provider of credit to bonds . . . issued by or entered into by an agency shall be valid and binding in accordance with the terms of the pledge document . . ."¹⁴²

The pledge constitutes a lien and security interest, which would be "enforceable against the pledgor, its successors, purchasers of

136. See Complaint and Petition for Writ of Mandate at 1–3, *Syncora Guarantee Inc. v. State*, No. 34–2012–80001215 (Cal. Super. Aug. 1, 2012), 2012 WL 3317082.

137. *Id.* at 3.

138. Ruling on Submitted Matter: Petition for Writ of Mandate and Complaint for Declaratory and Injunctive Relief at 8, *Syncora Guarantee Inc. v. State*, No. 34–2012–80001215 (Cal. Super. May 29, 2013), 2012 WL 3317082.

139. CAL. HEALTH & SAFETY CODE §§ 33640, 33641.5 (2014).

140. *Id.* § 33670(b). Section 33670 "fulfills the intent of Section 16 of Article XVI of the [California] Constitution." *Id.* § 33670.5.

141. *Id.* § 33671.

142. *Id.* § 33641.5(b).

collateral, creditors, and all others”¹⁴³ By pledging that tax increment funding would be used for redevelopment projects, it “increase[ed] the likely availability of increasing property tax increment streams to pay such bonds.”¹⁴⁴ People bought the bonds materially relying on this constitutional protection that the bonds would be secured by tax incremental financing.¹⁴⁵ Thus, to raise funds for redevelopment projects, the RDA would enter into contracts with bondholders and bond insurers where tax increment revenue was pledged to secure the bonds.¹⁴⁶ For example, the bond insurer Syncora would enter into a contract with Hesperia RDA, stating that the bonds would be secured by a “pledge of and lien on all of the Tax Revenues.”¹⁴⁷

AB 1X 26 eliminated this security provision of these contracts by transforming all of the tax increment revenue into general property tax revenue.¹⁴⁸ Funds from the general property tax revenue would be distributed amongst other taxing entities and, therefore, lack the secure and consistent funding stream that the tax increment provided.¹⁴⁹ Moreover, all remaining debt from the former RDA was transferred to the successor agencies even though the former RDAs were listed as the principal on each of the bond contracts.¹⁵⁰ Because of these new changes and the uncertainty with the new funding stream, plaintiffs alleged that AB1X26 violated the contracts clause of the Constitution because an important security provision within the contracts—tax increment revenues—was eliminated.¹⁵¹ Since the payment for the bonds was changed from a secured payment source to an unsecured payment source, the value of the bond decreased, as evaluated by Moody Investor Services.¹⁵² California tax allocation bonds that were rated Baa3 or higher were downgraded to a rating of

143. *Id.*

144. Kiely & Tate, *supra* note 132; CAL. HEALTH & SAFETY CODE § 33671.5 (providing that irrevocable pledge “shall have priority over any other claim”).

145. Memorandum of Points and Authorities in Support of Plaintiffs’/Petitioners’ Complaint and Writ of Mandate at 5, *Syncora Guarantee Inc. v. State*, No. 34–2012–80001215 (Cal. Super. Mar. 19, 2013), 2012 WL 3317082.

146. *Id.*

147. *Id.* at 6.

148. Kiely & Tate, *supra* note 132.

149. *Id.*

150. Memorandum of Points and Authorities in Support of Plaintiffs’/Petitioners’ Complaint and Writ of Mandate, *supra* note 145, at 1–2.

151. Kiely & Tate, *supra* note 132.

152. *Id.*

Ba1: junk bond status.¹⁵³ Central to Moody's determination in reducing the status of the bonds was the "increased uncertainty over timely debt repayments" because of the dissolution of RDAs.¹⁵⁴ The reduction of the bond status is especially problematic because California is the "country's biggest issuer of municipal debt."¹⁵⁵ Thus, AB 1X 26 changed the repayment source for the bonds by making it more susceptible to shortfall, which impaired the bondholders' contractual rights.¹⁵⁶

B. AB 1X 26: Failing to Recognize Enforceable Obligations as an Impairment of Contracts

Despite AB 1X 26's flaws, cities have tried to comply with its requirements. Under AB 1X 26, the county auditor-controller will only allocate funds for those items listed on the approved ROPS, subject to the authority of the county auditor-general, the oversight board, and the Department of Finance.¹⁵⁷ While section 34171(1)(a) of the California Health and Safety Code lists the different types of enforceable obligations, there has not been any agreement as to which projects would qualify as an enforceable obligations.¹⁵⁸ As of May 2012, the Department of Finance questioned whether \$350 million worth in projects were in fact enforceable obligations.¹⁵⁹ Many projects deemed by the city as an enforceable obligation were struck down by the Department of Finance—meaning that cities would be forced to "abandon projects that have been promised to citizens and bondholders and that are key to revitalizing recession-battered neighborhoods."¹⁶⁰ Most importantly, the cities would inevitably be breaking a contract with the private party if they cannot secure funds to pay the private parties to complete the project. Additionally, the

153. Hamilton, *supra* note 11. Baa3 is a bond credit rating classifying bonds that are subject to moderate credit risk. Bonds with a Ba1 rating are subject to substantial credit risk. *Financial Glossary*, NASDAQ (2011), <http://www.nasdaq.com/investing/glossary/b/baa3>, <http://www.nasdaq.com/investing/glossary/b/ba1>.

154. Kiely & Tate, *supra* note 132.

155. Hamilton, *supra* note 11.

156. Geoffrey K. Willis, *Redevelopment Law Unconstitutional Because of Impairment of Contract?*, MARTINDALE.COM (Mar. 14, 2012), http://www.martindale.com/litigation-law/article_Sheppard-Mullin-Richter-Hampton-LLP_1472714.htm.

157. CAL. HEALTH & SAFETY CODE § 34171(d)(1) (2012).

158. See Hyman et al., *supra* note 73.

159. Jessica Garrison, *Cities to Battle California in Court for Redevelopment Money*, L.A. TIMES (May 30, 2012), <http://articles.latimes.com/2012/may/30/local/la-me-redevelopment-fight-20120530>.

160. *Id.*

Department of Finance's actions have caused a rift between cities and the state, and angered many city officials who characterize the rejection by the Department of Finance as "unjust."¹⁶¹ Many city officials question the state's decision to reject some of the projects, claiming that the state only wants to "shut these projects down so they can take the money."¹⁶²

Successor agencies' only recourse if they wish to appeal the Department of Finance's decision to reject certain enforceable obligations is a "meet-and-confer" with the Department.¹⁶³ However, the meet-and-confers have not been fruitful, and as a result, many successor agencies, as well as private third parties, have filed lawsuits against the state challenging the state's rejection of redevelopment projects that should be included as enforceable obligations.¹⁶⁴ For example, the City of Irvine filed suit against the Department of Finance because the Department denied payment for the construction of a park on the former site of the El Toro Marine Corps Air Station.¹⁶⁵ The city entered into an agreement with a private third-party entity to construct the park in 2010.¹⁶⁶ The project was to be funded through tax increment, and not through the city's general fund.¹⁶⁷ It was approved by the oversight board, but rejected by the Department of Finance.¹⁶⁸ Thus, Irvine sued the Department of Finance in order to receive funds to pay for the project.¹⁶⁹ Without the funds, Irvine was unable to pay for the project.¹⁷⁰ In another suit, the City of Bakersfield alleged that the Department of Finance erroneously ruled that \$4.2 million in outstanding obligations for two senior housing projects were not enforceable, despite their approval in September 2010.¹⁷¹ These examples are only a small sample of the

161. Miller, *supra* note 128.

162. Garrison, *supra* note 159 (internal quotation marks omitted).

163. CAL. HEALTH & SAFETY CODE § 34177(m) (2014).

164. Miller, *supra* note 128.

165. Petition for Writ of Mandates and Complaint for Declaratory and Injunctive Relief at 1, *City of Irvine v. Matosantos*, Case No. 34–2012–80001161 (Cal. Super. May 25, 2012).

166. *Id.* at 9.

167. *Id.*

168. *Id.* at 13.

169. *Id.* at 16.

170. *Id.*

171. Verified Petition for Writ of Mandate and Complaint for Declaratory and Injunctive Relief at 26, *City of Bakersfield v. Matosantos*, Case No. 34–2013–80001400 (Cal. Super. Feb. 13, 2013).

wide variety of different projects that are now being contested by cities all over California.¹⁷² The cities that initiated lawsuits regarding enforceable obligations argue that the State's failure to provide funds for these projects would violate the California and federal Constitution by failing to honor existing contracts and obligations.¹⁷³

C. AB 1484: Unconstitutionality of the True-Up Payment Plan and Due Diligence Review Penalty Provisions¹⁷⁴

AB 1484's enactment has been just as controversial as the passage of AB 1X 26. Particularly problematic are the penalties that AB 1484 imposes on cities and counties. A central claim of lawsuits challenging AB 1484 is that the authority granted to the "Department of Finance to take tax revenues as penalties . . . goes too far."¹⁷⁵ Although AB 1484 was enacted to create more funds for the state budget, practically speaking, AB 1484 also puts "property and sales tax revenues of cities at risk at a time of great fiscal uncertainty" because these threatened funds may otherwise be used to provide "vital public safety and other city services" to city residents.¹⁷⁶ To overturn certain aspects of AB 1484, plaintiffs such as cities and successor agencies have disputed the constitutionality of the act based on the infringement of certain provisions of the California Constitution, specifically sections 24(b) and 25.5 of Article XIII of the California Constitution, which were added as a result of the passage of Proposition 1A and Proposition 22.¹⁷⁷

172. Other examples include loans that needed to be repaid, payments for affordable housing units, costs for bridge projects, etc. See, e.g., *Update on Recent Decisions Relating to the Dissolution of Redevelopment Agencies in California (April 2014)*, GIBSON DUNN, (Apr. 16, 2014), available at <http://www.gibsondunn.com/publications/Documents/Update-on-Recent-Court-Decisions-Relating-to-Dissolution-of-Redevelopment-Agencies-in-California-April2014.pdf> (summary of recently decided lawsuits concerning redevelopment).

173. See, e.g., Verified Petition for Writ of Mandate and Complaint, *supra* note 171, at 32.

174. Lawsuits challenging the constitutionality of the AB 1484 True-Up Payment Plan have also challenged the method of calculation for the true-up payments. See *Aftermath of the Dissolution of Redevelopment Agencies in California*, *supra* note 116. This will not be addressed in this Note.

175. Loretta Kalb, *CA Cities Fight Transfer of Assets*, SACRAMENTO BEE (Nov. 1, 2012), reprinted in MUNICIPAL INSIDER, available at <http://www.municipalinsider.com/ca-cities-fight-transfer-of-assets>.

176. Press Release, League of California Cities, League of California Cities Challenges Constitutionality of Portions of AB 1484, the Redevelopment Budget Trailer Law (Sept. 24, 2012), available at <http://www.cacities.org/UploadedFiles/LeagueInternet/a8/a86d3532-fb2d-4789-aded-97e00d1c332f.pdf>.

177. See, e.g., Petitioner's Memorandum of Points and Authorities in Support of Petition for Writ of Mandate and Complaint for Injunctive and Declaratory Relief, at 7,

Plaintiffs' main argument on the unconstitutionality of AB 1484 concerns the penalties imposed by the True-Up Payment Plan and DDR provisions.¹⁷⁸ AB 1484 requires the county auditors to determine whether or not the successor agencies owe any true-up payments or DDR payments. If the successor agencies fail to make the payments within the required timeframe, they are then subject to penalties, which include the withholding of sales and use tax until payment is made, and the deduction of property taxes from the RPTTF.¹⁷⁹

Plaintiffs allege that withholding sales and use tax from cities violates section 24 of Article XIII of the California Constitution, which provides that the "Legislature may not reallocate, transfer, borrow, appropriate, restrict the use of, or otherwise use the proceeds of any tax imposed or levied by a local government solely for the local government's purposes."¹⁸⁰ In addition, the state is not allowed to change the method of distributing revenues under the Bradley-Burns Uniform Sales and Use Law.¹⁸¹ By withholding sales and use taxes, AB 1484 essentially violates the aforementioned constitutional provisions by reallocating, using, and changing the "method of distributing local sales tax revenue."¹⁸²

Generally, the state Board of Equalization collects the local sales and use tax and remits the payment to each city or county under the Bradley-Burns Uniform Sales and Use Tax Law ("Bradley-Burns") (codified under sections 7200–7226 of the California Revenue & Tax Code).¹⁸³ The city or county can then use the sales and use tax revenue for their own intended purpose.¹⁸⁴ By withholding general sales and use tax from cities and counties, penalties under both the True-Up Payment Plan and the DDR strip funds from cities' and

League of California Cities v. Matosantos, No. 34-80001275 (Cal. Super. Feb. 1, 2013); Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandate, City of Bellflower v. Matosantos, No. 34-2012-80001269 (Cal. Super. Nov. 19, 2012), 2012 WL 4903340.

178. *See id.* at 8–12.

179. *Id.* §§ 34183.5(b)(2)(C), 34183.5(b)(3) ("any city, county or city and county that created the redevelopment agency that fails to make the required payment . . . shall not receive the distribution of sales and use tax").

180. CAL. CONST. art. XIII, § 24(b) (2010).

181. *Id.* § 25.5(a)(2)(A).

182. *See id.*

183. CAL. REV. & TAX. CODE § 7202 (2012).

184. *Id.*

counties' general purpose funds.¹⁸⁵ This contravenes the intended purpose of Proposition 22—namely, to allow city councils to determine how sales and use taxes should be used and to “conclusively and completely prohibit state politicians in Sacramento from seizing, diverting, shifting, borrowing, transferring, suspending, or otherwise taking or interfering with revenues that are dedicated to funding services provided by local government.”¹⁸⁶ AB 1484 punishes cities and counties by taking away their sales and use tax revenue to pay taxing entities, thereby stripping them of their power to determine how to use their sales and use taxes.¹⁸⁷

Plaintiffs further allege that the penalties deducting property tax revenues violate sections 25.5(a)(1)(A) and 25.5(a)(3) of Article XIII of the California Constitution by reallocating and changing the method of distributing property taxes.¹⁸⁸ Section 25.5(a)(1)(A) prohibits the legislature from altering the method in which “ad valorem property tax revenues are allotted . . . so as to reduce for any fiscal year the percentage of the total amount of ad valorem property tax revenues in a county that is allocated among all of the local agencies . . . for the same fiscal year.”¹⁸⁹ Section 25.5(a)(3) prohibits the legislature from reallocating property taxes between cities, counties, and special districts without a two-thirds vote by the state legislature.¹⁹⁰ Given these provisions, plaintiffs allege that the penalties related to property tax are an offset or reduction of property tax that would reduce the city's pro rata share of property taxes, as well as reallocate property taxes between cities, counties, and special districts without a two-thirds vote by the legislature.¹⁹¹ By reducing the distribution of property taxes given to the cities and transferring it to the taxing entities in order to pay debts owed by the successor agency, it would effectively reduce the “pro rata share of property taxes allocated to the city.”¹⁹² This, plaintiffs contend, is a direct violation of the California Constitution.¹⁹³

185. See CAL. HEALTH & SAFETY CODE §§ 34183.5(b)(2)(C), 34179(h)(1)(C) (2012).

186. CAL. CONST. art. XIII, § 24 Statement of Purpose.

187. Petitioner's Memorandum, *supra* note 177, at 9–10.

188. *Id.* at 8.

189. CAL. CONST. art. XIII, § 25.5(a)(1)(A) (2010).

190. *Id.* § 25.5(a)(3).

191. Petitioner's Memorandum, *supra* note 177, at 11.

192. *Id.* at 12.

193. *Id.* at 10.

D. AB 1484: The California Department of Finance’s Violation of the California’s Constitution’s Legislative Non-Delegation Clause

In the same suits challenging the constitutionality of the True-Up Payment Plan and the DDR requirement, another challenge raised against AB 1484 is that the provisions promulgated by AB 1484 impermissibly delegate legislative power to an executive agency, namely the Department of Finance.¹⁹⁴ This is because several provisions of AB 1484 grant the Department of Finance authority to make substantial policy decisions within the Department’s “unfettered discretion.”¹⁹⁵ Specifically, AB 1484 allows the Department of Finance to withhold sales and property tax from cities and successor agencies and also to decide which obligations are “enforceable obligations.”¹⁹⁶

Plaintiffs alleged that AB 1484 is arbitrary because it does not include any “standards to govern application of many of its most significant provisions,” which have resulted in many different interpretations.¹⁹⁷ The main complaints regarding the delegation of power to the Department of Finance include:

1. AB 1484 allows the Department of Finance to “review all oversight board actions and reject or accept the actions” without any clear standards or criteria governing such determinations;¹⁹⁸
2. AB 1484 does not impose any standards or criteria for the Department of Finance in determining which item on the ROPS should be rejected or modified;¹⁹⁹
3. AB 1484 allows the Department of Finance to adjust the balance owed by the successor agencies through the due diligence review process. There

194. Verified Petition for Writ of Mandate and Complaint for Injunctive and Declaratory Relief at 33, *League of California Cities v. Matosantos*, No. 34-2012-80001275 (Cal. Super. Sept. 24, 2012).

195. *Id.* at 32–34.

196. *Id.* at 33.

197. *Id.* at 32.

198. *Id.* at 33. *See also* CAL. HEALTH & SAFETY CODE § 34179(h) (2012).

199. Verified Petition for Writ of Mandate, *supra* note 194, at 33.

are no standards governing whether or not an adjustment should be made;²⁰⁰

4. AB 1484 does not set out any standards governing how the Department of Finance can determine whether the amount owed by the successor agency is feasible;²⁰¹ and
5. AB 1484 does not provide any procedure or administrative process where cities and successor agencies could appeal the Department of Finance's decision regarding true-up payments, or any other payments or penalties.²⁰²

Plaintiffs alleged that it is unconstitutional for the Legislature to fail to provide “adequate direction for implementation of policies adopted by the Legislature” and to give “absolute legislative discretion” to an administrative body.²⁰³ Here, many of AB 1484's provisions lack the standards necessary to guide the successor agencies, oversight boards, and the Department of Finance in making important decisions.²⁰⁴ As a result, the Department of Finance arguably has complete discretion in making such decisions affecting successor agencies and cities.²⁰⁵

V. The Constitutional Problems Analyzed

A. Impairment of the United States Constitution's Contracts Clause

The U.S. Constitution's Contracts Clause provides that “[n]o state shall . . . pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts.”²⁰⁶ In its seminal case, *U.S. Trust Co. v. New Jersey (U.S. Trust)*, the United States Supreme Court found that for a law to be unconstitutional under the Contracts

200. *Id.* at 33–34. *See also* CAL. HEALTH & SAFETY CODE § 34179.5.

201. Verified Petition for Writ of Mandate, *supra* note 194, at 34. *See also* CAL. HEALTH & SAFETY CODE § 34179.6(h)(3) (2012).

202. Verified Petition for Writ of Mandate, *supra* note 194, at 34–35. *See also* CAL. HEALTH & SAFETY CODE § 34183.5(b) (2014).

203. Petitioner's Memorandum, *supra* note 177, at 13.

204. *Id.* at 14.

205. *Id.*

206. U.S. CONST. art. I, § 10, cl. 1 (2014).

Clause, it must impair a contract in a manner that is constitutionally impermissible.²⁰⁷ The purpose of the Contracts Clause was to limit the “power of the states to modify their own contracts as well as to regulate those between private parties.”²⁰⁸ The Contracts Clause helps to “encourage trade and credit by promoting confidence in the stability of contractual obligations.”²⁰⁹ Specifically, *U.S. Trust* held that a contractual impairment is unconstitutional when: (1) there is a contractual obligation, (2) the legislation in question imposes an impairment, and (3) the legislation does not reasonably and necessarily serve an important public purpose.²¹⁰

B. AB 1X 26: Contractual Impairment of Bondholders

Even if courts find the matter of reduced rating of RDA bonds’ reduced rating ripe for adjudication, the plaintiffs likelihood of prevailing remains unclear. Analyzed under the factors articulated in *U.S. Trust*, it remains unclear whether the reduced bond rating could constitute a contractual impairment.²¹¹

1. Is There a Contractual Obligation?

The “obligation of a contract is ‘the law that binds the parties to perform their agreement.’”²¹² In cases contesting that a decrease in bond value is an impairment of contract, the parties do not seem to dispute that a contract was formed between the city, bondholders, and the bond insurers. Here, in exchange for bonds from different private parties, the RDAs have agreed to secure the bonds with tax increment financing, thereby creating a contractual obligation.

2. Is There a Substantial Impairment?

A contract is impaired when a law “renders them invalid, or releases or extinguishes them and impairment . . . has been predicated of laws which without destroying contracts derogate from substantial contractual rights.”²¹³ The impairment cannot be minimal.²¹⁴ On the other hand, a total destruction of a contractual obligation is not

207. *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 20 (1977).

208. *Id.* at 17 (internal citation omitted).

209. *Id.* at 15 (citing *Home Bldg. & Loan Ass’n v. Blaisdell*, 290 U.S. 398, 427–28 (1934)).

210. *Id.* at 22–27.

211. See Kiely & Tate, *supra* note 132.

212. *Blaisdell*, 290 U.S. at 429.

213. *Id.* at 431.

214. *Bd. of Admin. v. Wilson*, 52 Cal. App. 4th 1109, 1153 (1997).

required for a substantial impairment of a contract.²¹⁵ The U.S. Supreme Court reasoned that an elimination of an important security provision could constitute an impairment of contract.²¹⁶ *U.S. Trust* is instructive here. The situation at hand regarding redevelopment is similar to *U.S. Trust* in that both cases revolve around municipal bonds where one of the parties is a public entity.²¹⁷

At issue in *U.S. Trust* was whether the State of New Jersey's repeal of a 1962 covenant impaired the contractual obligations between it and the bondholder.²¹⁸ In *U.S. Trust*, New York and New Jersey entered into a covenant to allow the Port Authority to "acquire, construct, and operate the Hudson & Manhattan Railroad and the World Trade Center."²¹⁹ The funds for the project came from the sale of bonds to private investors.²²⁰ The two states and the bondholders agreed that neither the states nor the Port Authority would use revenues or reserves pledged as security for the bonds except in certain limited circumstances.²²¹ The covenant was repealed in 1973 because the states intended to limit the number of private automobiles on the streets; the states felt that this interest was a sufficient public purpose to justify repeal.²²²

Here, as in *U.S. Trust*, an important provision has been eliminated, which impairs a contract. AB 1X 26 eliminated the tax increment funds that were used to secure the bonds, which ultimately altered the repayment obligation.²²³ The State has argued that AB 1X 26 does not impair existing contracts at all—let alone impair them substantially.²²⁴ The basis for this argument is that AB 1X 26 honors these existing obligations and protects both bondholders and

215. *Energy Reserves Grp., Inc. v. Kan. Power & Light Co.*, 459 U.S. 400, 411 (1983) (citing *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 26–27 (1977)).

216. *U.S. Trust Co.*, 431 U.S. at 19.

217. *Id.* at 27.

218. *Id.* at 17.

219. *Id.* at 9.

220. *Id.*

221. *Id.*

222. *Id.* at 29.

223. See CAL. HEALTH & SAFETY CODE § 34182(c)(1) (2012) (amount of property taxes that "would have been allocated to each redevelopment agency . . . are deemed property tax revenues").

224. Memorandum of Points and Authorities in Opposition to Motion for Preliminary Injunction and/or Stay at 17, *City of Cerritos v. State*, No. 34-2011-80000952 (Cal. Super. Jan. 17, 2012).

creditors.²²⁵ For instance, AB 1X 26 requires that successor agencies honor the enforceable obligations of the former RDAs, which include, but are not limited to, paying off the RDAs' debts, disposing of RDA assets "in a manner aimed at maximizing value," collecting monies owed to the RDAs, and "oversee[ing] development of properties until the contracted work has been completed or the contractual obligations of the former redevelopment agency can be transferred to other parties."²²⁶ These enforceable obligations include "bonds . . . required debt service, reserve set-asides, and any other payments required under the indenture or similar documents."²²⁷ The successor agencies are still required to honor the bonds as an enforceable obligation, which leaves the repayment guarantees intact.²²⁸ Even though the tax increment funding was eliminated, the bonds are still secured.

Although AB 1X 26 requires successor agencies to repay bondholders, the contract is arguably still impaired. In *U.S. Trust*, for example, the Supreme Court considered whether the covenant was "modified or replaced by an arguably comparable security provision."²²⁹ The Court concluded that the state did not provide any comparable security provision, so the repeal of the covenant was an outright impairment of the obligation in the contract.²³⁰ In this case, although the state argues that AB 1X 26 sufficiently secures the bonds by requiring successor agencies to honor the previous obligations, plaintiffs could reasonably argue that a bare repayment obligation, absent a source of funding, is not a comparable security provision. Under the tax increment financing scheme, bondholders and bond insurers had greater assurance that the bond obligation would be repaid because there was a reliable funding stream to finance obligations incurred by the RDA.²³¹ By eliminating this reliable funding stream and failing to procure an alternative funding source to secure the bonds, AB 1X 26 has reduced the degree to which the state has secured its debt instruments.²³²

225. *Id.* at 17.

226. *Id.* at 17–18. *See also* CAL. HEALTH & SAFETY CODE §§ 34177(a), (e), (f), (i) (2012).

227. Memorandum of Points and Authorities in Opposition, *supra* note 224, at 20.

228. CAL. HEALTH & SAFETY CODE §§ 34175(a), 34177(a).

229. *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 19 (1977).

230. *Id.*

231. *Marek v. Napa Cmty. Redev. Agency*, 46 Cal. 3d 1070, 1083 (1988).

232. Memorandum of Points and Authorities in Support, *supra* note 145, at 15.

The present obligations are now less secure for several reasons. First, the obligations must now be paid from general property tax revenues, which are disbursed among various taxing agencies.²³³ Repaying bond obligations from general property tax revenues, rather than from a designated funding source, makes repayment contingent upon funding that may be constrained by allocation to other agencies as well as other funding priorities. The bondholders are put in the position of having to compete with other creditors. The bondholders and bond insurers went from having the “senior-most priority pledge of particular tax revenues[—]the tax increment[—to] a claim for payment out of property taxes generally, with the same priority as all other claimants against such property taxes.”²³⁴ Essentially, the bondholders and bond insurers went from having the most protection under the contract to a security provision with less protection. The downgrade of the former RDA bonds is a good indication that the new security provisions provided by AB 1X 26 were not comparable to the former security guarantee of tax increment financing.

Additionally, plaintiffs could argue that the impairment was even more substantial than the impairment at issue in *U.S. Trust*.²³⁵ In that case, plaintiffs argued that the valuation of the Port Authority bonds downgraded, but overall, the bonds still retained an “A” rating.²³⁶ While the Court in *U.S. Trust* never held the valuation as determinative in the analysis, plaintiffs here could argue that the impairment was more substantial than in *U.S. Trust* because here the bonds were downgraded to “junk” status. Thus, the elimination of the security provision, as in *U.S. Trust*, may be sufficient to qualify the impairment as “substantial.”

3. *Reasonable and Necessary for Public Purpose?*

Finding that the contract was substantially impaired is only the beginning of the inquiry. Even if the contract is substantially impaired, the state acts unconstitutionally only if the impairment not

233. Kiely & Tate, *supra* note 132.

234. *Id.*

235. Memorandum of Points and Authorities in Support, *supra* note 145, at 15–16 (“[AB 1X 26] works a greater impairment of contract than in *U.S. Trust*, for it *eliminates* all future security on the bonded indebtedness and further requires that security *already accrued* in RDA reserves be redistributed to local agencies . . . whereas in *U.S. Trust*, the States’ repeal of the covenant merely threatened future depletion of bondholder security by uneconomical investment.”).

236. *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 19 (1977).

“reasonable and necessary” to serve an important public purpose.²³⁷ Arguably, AB 1X 26 is constitutional because the legislation was reasonable and necessary to serve the public purpose of funding important taxing entities during a fiscal emergency. When evaluating whether the impairment is reasonable and necessary, the Supreme Court does not completely defer to legislative intent because it recognizes that the state itself has an interest in the legislation as a commercial actor.²³⁸ Complete deference to the legislature would render the Contracts Clause meaningless because a governmental entity “can always find a use for extra money” to justify an impairment based on a need to provide for a public purpose.²³⁹ In *U.S. Trust*, the Supreme Court recognized public transportation, energy conservation, and environmental protection as legitimate public purposes; nevertheless, the Supreme Court found it inappropriate for the Legislature to ignore the “private welfare of its creditors.”²⁴⁰

As stated above, AB 1X 26 was passed in response to California’s 2011 fiscal crisis. Important taxing entities, including school districts and other public services, were not receiving enough funds to provide for important social services because of the tax incremental financing.²⁴¹ The Supreme Court has recognized, however, that an economic emergency may be sufficient to justify impairing a contract.²⁴²

In *Home Building & Loan Association v. Blaisdell*, the Supreme Court upheld a Minnesota statute that postponed execution sales and extended the time to redeem mortgages from foreclosures.²⁴³ The statute was enacted during the Great Depression when there were an increasing number of home foreclosures.²⁴⁴ The statute was upheld based on four different factors considered by the Supreme Court: (1) Minnesota was undergoing an economic emergency (the Great Depression), which is a “potent cause” that justified the use of state power to provide for the community interests; (2) the legislation was used for a legitimate end and not for the advantage of particular

237. *Id.* at 22.

238. *Id.* at 25–26.

239. *Id.* at 26.

240. *Id.* at 29.

241. Detwiler, *supra* note 3, at 6.

242. See *Home Bldg. & Loan Ass’n v. Blaisdell*, 290 U.S. 398, 415 (1934).

243. *Id.*

244. *Id.* at 419.

individuals; (3) the relief sought was appropriate to that emergency and were reasonable; and (4) the legislation was temporary and limited to the exigent circumstances.²⁴⁵ These factors have been recognized and used by both the California Supreme Court and the U.S. Supreme Court.²⁴⁶ However, since *Blaisdell*, the Court has held that these factors may be considered, but are not dispositive.²⁴⁷

Several California court cases have found a fiscal emergency insufficient to justify an impairment of contract. In *Valdes v. Cory*, the California Supreme Court held that a statute that suspended funding for public employees' retirement plans constituted an impairment of contract because, despite a fiscal emergency, alternative means were not considered, and there was no indication that the emergency was only temporary.²⁴⁸ Additionally, in *Board of Administration v. Wilson*, budget cuts in health, education and welfare programs, as well as hiring freezes, were held to be insufficient justifications to support an impairment of contracts claim.²⁴⁹ Lastly, in *Sonoma County Organization of Public Employees v. County of Sonoma*, the California Supreme Court held that a law eliminating wage increases to local government employees per a contract agreement was an unconstitutional impairment of contract, even though the law was enacted because of a fiscal emergency.²⁵⁰

At the time that AB 1X 26 was enacted, California was arguably undergoing a fiscal crisis. However, it is unclear whether a court would hold that the fiscal emergency qualifies as a public purpose sufficient to justify contractual impairment. Unlike in *Blaisdell*, where the impairment was only temporary and "limited to the exigency that provoked the legislative response," the dissolution of RDAs and the elimination of the security provisions are permanent.²⁵¹ Moreover, a fiscal emergency does not automatically allow the Legislature to impair existing contractual obligations, as evidenced by California courts' rejections of the State's defense in *Valdes*, *Wilson*, and *Sonoma County Organization*. Also, the fiscal crisis does not appear to be so severe that the state would be forced to shut down if

245. *Id.* at 444–47.

246. *Valdes v. Cory*, 139 Cal. App. 3d 773, 790–91 (1983).

247. *See Veix v. Sixth Ward Bldg. & Loan Ass'n of Newark*, 310 U.S. 32, 39 (1940) (upholding state statute even though it was not drafted at time of economic emergency).

248. *Valdes*, 139 Cal. App. 3d at 791.

249. *Bd. of Admin. v. Wilson*, 52 Cal. App. 4th 1109, 1160–61 (1997).

250. *Sonoma Cty. Org. of Pub. Emp. v. County of Sonoma*, 23 Cal. 3d 296, 310 (1979).

251. *Id.* at 306.

the legislation did not pass.²⁵² Here, the state has acknowledged that the fiscal condition of California is recovering, albeit slowly, which would weaken any argument that AB 1X 26 is for a public purpose.²⁵³ Therefore, it is unlikely that a fiscal crisis can serve as a basis for constitutionally impairing a contract.

The impairment of contracts here could also be unconstitutional because it is neither reasonable nor necessary for the public purpose. The Court in *U.S. Trust* stated that necessity can be construed in two ways: first, whether or not there is a “less drastic modification,” and second, whether or not the state could have “adopted alternative means of achieving their . . . goals.”²⁵⁴ Here, even if the fiscal crisis resulted in fund shortages for schools and other important services, the dissolution of RDAs and the elimination of tax increment funding to fulfill contractual obligations were perhaps not the best solutions to fix the problem. While AB 1X 26 certainly acts to channel funds to important social services that lack funds, the Supreme Court will have to consider whether alternative, less drastic means were considered to raise funds for these important services, such as raising taxes or eliminating costs in other areas. However, those alternatives would likely be challenged given the unpopularity of taxes and eliminating other services. One way out could be for the State to argue that it did consider alternatives, such as passing AB 1X 27, but that was struck down by the courts. Therefore, there were no other alternatives other than eliminating the RDAs.

C. AB 1X 26: Enforceable Obligations

1. *Timing Issues*

Perhaps the most litigated issue concerning redevelopment revolves around disagreements between the Department of Finance and the successor agencies as to what constitutes an enforceable obligation.²⁵⁵ Though the same analysis would be used to determine whether the state has impaired contracts the former RDAs held with private third parties, the main dispute here seems to be a factual determination of whether the contracts fall under the statutory

252. See *Subway-Surface Supervisors Ass’n v. N.Y.C. Transit Auth.*, 44 N.Y.2d 101 111–13 (1978) (holding that a statute deferring a wage increase in a collective bargaining agreement did not violate the Contracts Clause because the fiscal emergency was so severe that the city would cease to operate).

253. A.B. 1X 26, 2011-2012 Leg., Reg. Sess. (Cal. 2011).

254. *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 29–30 (1977).

255. Miller, *supra* note 128.

definition of “enforceable obligations.” Whether an obligation is an “enforceable obligation” under AB 1X 26 would likely involve an in-depth analysis of the actual contract, including the terms, the type of contract, and the pledges that were made. Therefore, the result for each independent lawsuit may differ depending on the type of obligation that was impaired.

Here, the lawsuits stem from the state’s rejection of certain “enforceable obligations” that were listed on the ROPS by the successor agencies.²⁵⁶ One of the state’s main contentions with this issue is that the disputed enforceable obligations were unlawfully made, even at their inception.²⁵⁷ AB 1X 26 prohibits the successor agencies to incur “new or expand existing monetary or legal obligations” after the effective date of the act, which was June 28, 2011.²⁵⁸ Those contracts that existed after June 28, 2011, are considered “void from the outset and shall have no force or effect.”²⁵⁹ Therefore, the main inquiry under this argument would be when the enforceable obligations were created and what was the pledged funding source in the contracts. If these contracts were created after June 28, 2011, these “contracts” are not enforceable obligations under AB 1X 26 and would not be entitled to funds from the RPTTF. If, however, the contracts were entered into prior to June 28, 2011, the state would enforce those obligations and use the funds from the RPTTF to pay for such projects. Therefore, the dispute surrounding these contractual obligations hinges on very particular details, such as when the obligation was established, the type of enforceable obligation that was created, the types of funds that were pledged (such as general property taxes or tax increment), and the terms and duration of the obligation and the pledge.

Lawsuits concerning enforceable obligations occupy most of the redevelopment docket.²⁶⁰ Currently, it appears that there is neither a clear definition nor consistent interpretation of what is considered an “enforceable obligation” with respect to the timing of the obligation. A current lawsuit exemplifies the confusion and inconsistent results

256. See League of California Cities Summary, *supra* note 10.

257. Memorandum of Points and Authorities in Support of Defendant Director of Finance Ana J. Matosantos’ Demurrer to Complaint for Declaratory Relief and Petition for Writ of Mandate at 5–6, *County of Orange v. Matosantos*, No. 34–2012–80001224 (Cal. Super. Sept. 5, 2012).

258. CAL. HEALTH & SAFETY CODE § 34161 (2012).

259. *Id.* § 34162(b) (2011).

260. See League of California Cities Summary, *supra* note 10 (detailing all the lawsuits regarding redevelopment).

caused by the lack of a proper definition. In a lawsuit against the Department of Finance, Ana J. Matosantos, and the Orange County Auditor-Controller, the plaintiff alleged the Department of Finance found a settlement negotiation from 1984 to be an unenforceable obligation.²⁶¹ The settlement negotiation promised that “20% of the ‘tax increments or tax increments generated or related revenues, or moneys repayable from tax increments’ from the project area would be ‘set aside.’”²⁶² The pledge of tax increment to pay indebtedness would be in effect until July 6, 2035.²⁶³ The settlement agreement at issue appears, on its face, to be an enforceable obligation, as defined by AB 1X 26 because it is a “legally binding and enforceable agreement or contract that is not otherwise void as violating the debt limit or public policy.”²⁶⁴ Despite the fact that the settlement agreement was created before the dissolution date, the trial court ruled that the settlement agreement was not an enforceable obligation.²⁶⁵ The trial court reasoned that finding the settlement agreement to be an enforceable obligation would mean that the settlement agreement “safeguards a continuing stream of funding for additional redevelopment projects for the next twenty years, despite the dissolution of the redevelopment agency,” which could not have been the intention of the Legislature.²⁶⁶ The trial court further stated that even if those were enforceable obligations, it could not allocate future tax increment revenues.²⁶⁷ The court’s interpretation appears to go far beyond the enforceable obligations of AB 1X 26.

2. *Creating New Obligations or Amending an Obligation*

Another area of dispute surrounding the enforceability of an obligation is whether the successor agency has created a new obligation, or merely amended an existing obligation. In *CRFL Family Apartments, L.P. v. Matosantos*, the issue was whether an

261. See generally Petition for Writ of Mandate and Verified Complaint for Declaratory and Injunctive Relief, *Peebler v. Cal. Dep’t of Fin.*, No. 34–2012–80001172 (Cal. Super. June 7, 2012).

262. Tentative Ruling: Final Judgment Denying Petition for Writ of Mandate at 4, *Peebler v. Cal. Dep’t of Fin.*, No. 34–2012–80001172 (Cal. Super. Mar. 18, 2013).

263. *Id.*

264. Memorandum of Points and Authorities in Support of Petition for Writ of Mandate at 14, *Peebler v. Cal. Dep’t of Fin.*, No. 34–2012–80001172 (Cal. Super. Dec. 18, 2012). See also CAL. HEALTH & SAFETY CODE § 34171(d)(1) (2014).

265. Tentative Ruling, *supra* note 262, at 8.

266. *Id.* at 7.

267. *Id.* at 8.

agreement made before the enforcement date of AB 1X 26, but then later assigned to another organization after the enforcement date, created a new obligation or amended an existing obligation.²⁶⁸ The trial court ruled that it was not a new obligation, but rather a permissible transfer, and therefore an enforceable obligation.²⁶⁹ Again, AB 1X 26 did not explicitly state that re-assigning former obligations to a new agency would remain an enforceable obligation. Thus, to reduce the number of lawsuits regarding enforceable obligations, it would be necessary to further define and clarify what an enforceable obligation is.

D. AB 1484: Diverting Sales and Use and Property Taxes

Currently, there is a split even within the state trial court as to whether AB 1484 is unconstitutional. A plain reading of the penalties provisions under AB 1484 would suggest a violation of the California Constitution concerning sales and use tax revenue, and at least one California trial court, in *League of California Cities, et. al. v. Matosantos*, has reached that conclusion.²⁷⁰ However, trial courts have also ruled otherwise by concluding that the penalties provision of AB 1484, is not unconstitutional.²⁷¹ In *League of California Cities*, the trial court ruled that the sales and use penalties provision of AB 1484 violated the California Constitution because it changed the method of distributing sales and use tax revenue.²⁷² Under section 24(b) of Article XIII of the California Constitution, it is impermissible for the Legislature to “reallocate, transfer, borrow, appropriate, restrict the use of, or otherwise use the proceeds of any tax imposed . . . solely for the local government’s purpose.”²⁷³ The *League of California Cities* court suggested that this section of the California Constitution indicates a “total prohibition on the taking of local tax revenues for

268. Final Ruling at 3–4, CFRL Family Apartments, L.P., v. Matosantos, No. 34-2012-80001354, (Jan. 17, 2013).

269. *Id.* at 5.

270. Ruling on Submitted Matter: Complaint for Declaratory and Injunctive Relief and Petition for Writ of Mandate, at 7–8, *League of California Cities v. Matosantos*, No. 34-2012-80001275-CU-WM-GDS, (Dec. 9, 2013) (ruling that AB 1484 provisions on sales and use tax is unconstitutional but denying relief as to the property tax reduction provision).

271. Ruling on Submitted Matter, at 12, *City of Bellflower v. Matosantos*, No. 34-2012-80001269, (Nov. 7, 2013).

272. Ruling on Submitted Matter, *supra* note 270, at 7, 9.

273. CAL. CONST. Art XIII, § 24(b) (2010).

any reason,” even for “remedial or penalty purposes.”²⁷⁴ Here, penalizing cities and counties by withholding, deducting and offsetting a city’s sales and use tax until the amount is paid is unconstitutional under section 24(b) because it changes and restricts the allocation of the sales and use tax revenue.²⁷⁵

While the trial court in *League of California Cities* ruled otherwise, the property tax reallocation penalties also appear to directly conflict with the California Constitution. Specifically, section 25.5 of Article XIII of the California Constitution prohibits the Legislature from altering the “manner in which ad valorem property tax revenues are allocated . . . so as to reduce . . . the percentage of the total amount of those revenues that would be allocated.”²⁷⁶ Section 25.5 also prohibits the Legislature from changing the “pro rata shares in which ad valorem property tax revenues are allocated among local agencies” without a two-thirds vote.²⁷⁷ Offsetting or deducting the city’s property taxes when a successor agency fails to pay the amount owed under AB 1484 would essentially reduce the city’s pro rata share or property taxes and impermissibly reallocate the property taxes. Thus, there appears to be a clear conflict between the penalty provisions of AB 1484 and the California Constitution.

However, a finding that the penalties from the True-Up Payment Plan and the DDR payments directly conflict with sections 24(b) and 25.5 does not end the analysis because the Legislature has the broad authority to impose civil penalties.²⁷⁸ Certainly, the Legislature has the authority to impose civil penalties if the penalties are fair and reasonably related to a proper legislative goal.²⁷⁹ Civil penalties have been a commonly used tool in order to implement a statutory policy.²⁸⁰ Here, the State argues that because it has the authority to demand payments from the successor agencies, it also has the

274. Ruling on Submitted Matter, *supra* note 270, at 9. See also *Update on Recent Decisions Relating to the Dissolution of Redevelopment Agencies in California (April 2014)*, *supra* note 172, at 1.

275. See Ruling on Submitted Matter, *supra* note 270, at 7, 9 (purpose of Art. XIII, § 24(b) is to “conclusively and completely prohibit state politicians . . . from seizing, diverting, shifting, borrowing, transferring, suspending, or otherwise taking or interfering with revenues that are dedicated to funding services provided by local government” and AB 1484 frustrates that purpose).

276. CAL. CONST § 25.5(a)(1)(A).

277. *Id.* § 25.5(a)(3).

278. *Home Depot U.S.A., Inc. v. Superior Court*, 191 Cal. App. 4th 210, 225 (2010).

279. *Id.*

280. *Hale v. Morgan*, 22 Cal. 3d 388, 398 (1978).

authority to impose penalties to ensure compliance.²⁸¹ Moreover, since no penalties have been imposed thus far, plaintiffs carry a higher burden when bringing a facial challenge.²⁸² Plaintiffs need to show either that the statute poses a total and fatal conflict with applicable constitutional prohibitions, or that the statute conflicts with constitutional principles in general or in a great majority of cases.²⁸³ Here, it is unlikely that plaintiffs could meet the facial challenge because the provision is not unconstitutional in all or in a majority of circumstances. As long as the successor agencies comply with the statutory provisions, then the “unconstitutional” penalties would not be imposed.

Additionally, central to the court’s holding *City of Bellflower* was the fact that the penalties provision does not upset the purpose of Propositions 22 and 1A.²⁸⁴ The intent of Proposition 1A is to ensure that tax dollars are available for local purposes by disallowing the state from “(1) shifting local tax revenues to schools or other state-funded agencies, and (2) placing strict limits on the State’s ability to alter the allocation of tax revenues among local governments.”²⁸⁵ Similarly, the purpose of Proposition 22 is to “restrict the State’s ability to temporarily borrow or redirect tax revenues dedicated for transportation and local government services.”²⁸⁶ Because the purpose of these two propositions is to reduce the state’s ability to limit local tax revenues, it does not directly contravene AB 1484.²⁸⁷ This is due to the fact that the penalties provisions in AB 1484 are intended to restore “wrongfully-obtained funds,” and not to limit existing local funds.²⁸⁸

As to the property tax reallocations, the court noted that Proposition 22 does not protect tax allocations to successor agencies because Proposition 22 only applies to redevelopment agencies, which have been dissolved.²⁸⁹ Thus, Proposition 22 has no sway in this argument. However, given the increasing number of lawsuits

281. Ruling on Submitted Matter, *supra* note 271, at 11.

282. *City of Los Angeles v. Superior Court*, 29 Cal. 4th 1, 10–11 (2002).

283. *See In re Guardianship of Ann S.*, 45 Cal. 4th 1110, 1126 (2009).

284. Ruling on Submitted Matter, *supra* note 271, at 13.

285. *Id.*

286. *Id.*

287. *Id.*

288. *Id.*

289. *Id.* at 12.

regarding this issue and the possibility for appeal, it is likely that this issue will still be relevant to the redevelopment debate.

E. AB 1484: Violation of the Non-Delegation Doctrine

Lastly, another main area of contention is whether AB 1484 violates the non-delegation doctrine of the California Constitution. Article III, section 3 of the California Constitution provides that the “[p]ersons charged with the exercise of one power [(legislative, executive, or judicial)], may not exercise either of the others except as permitted by the Constitution.”²⁹⁰ This non-delegation clause is premised on the idea that the Legislature must “resolve the truly fundamental issues.”²⁹¹ Plaintiffs challenging AB 1484 argue that it is unconstitutional because it confers on an administrative agency unrestricted authority to make or implement fundamental policy decisions.²⁹² An unconstitutional delegation of authority occurs when the legislative body “(1) leaves the resolution of fundamental policy issues to others or (2) fails to provide adequate direction for the implementation of that policy.”²⁹³ There need not be express standards and “case law makes clear that the requisite standards . . . are [often] implied by the statutory purpose.”²⁹⁴ Moreover, the real concern behind the non-delegation doctrine is focused not on the need for clear standards, “but for safeguards” against arbitrariness.²⁹⁵ At least one court, the trial court in *League of California Cities*, have decided that AB 1484 does not violate the non-delegation doctrine.²⁹⁶ This decision makes sense given the arguments posed by the two sides.

Opponents of AB 1484 argue that the law violates the non-delegation doctrine in several ways, such as violating the doctrine’s second prong by failing to provide adequate direction for implementing the policy.²⁹⁷ First, AB 1484 provides that the Department of Finance can unilaterally decide if it is feasible for the successor agency to make DDR payments but does not provide any standards as to how the Department of Finance should make its

290. CAL. CONST. art. III, § 3 (2010).

291. *People ex rel. Lockyer v. Sun Pac. Farming Co.*, 77 Cal. App. 4th 619, 632–33 (2000).

292. *See Samples v. Brown*, 146 Cal. App. 4th 787, 804 (2007).

293. *Id.* (citation omitted).

294. *See id.* at 805–06 (citation omitted).

295. *Id.* at 805 (citation omitted).

296. Ruling on Submitted Matter, *supra* note 270, at 12–14.

297. Petitioner’s Memorandum of Points and Authorities in Support, *supra* note 177, at 13.

determination.²⁹⁸ The Department of Finance also has the authority to decide the amount of DDR funds the successor agency has available to divert to taxing entities.²⁹⁹ There are no enumerated standards to guide the department in determining the proper amount, other than the fact that it should consider any findings or opinions of the county auditor-controller.³⁰⁰ Additionally, the Department of Finance has the unfettered discretion to reject certain enforceable obligations from the ROPS with no explicit standard or guidance.³⁰¹ Without enumerated guidelines, different individuals within the Department of Finance can apply their own interpretations, thereby leading to a wide disparity in results—and this is precisely what has resulted.³⁰² The fact that there are so many lawsuits concerning the definition of an enforcement obligation reinforces the notion that both AB 1X 26 and AB 1484 lack standards to guide the Department of Finance in implementing its provisions.

In *Samples v. Brown*, the California Court of Appeal for the First District considered what guidelines would be sufficient to meet the second prong of the non-delegation doctrine.³⁰³ The issue in *Samples* was whether a vehicle code provision violated the non-delegation clause because there was no mechanism in place for an impounding agency to follow in determining what constitutes a mitigating circumstance under California Vehicle Code section 14602.6.³⁰⁴ Overturning the trial court, the court of appeal held that this provision does, in fact, provide some guidance and it provided examples as to what constitutes a mitigating circumstance, such as the owner's "lack of actual knowledge regarding the unlicensed status of the driver."³⁰⁵ Furthermore, the court found reasonable safeguards in

298. CAL. HEALTH & SAFETY CODE § 34179.6 (h)(3) (2012).

299. *Id.* § 34179.6(d).

300. *Id.*

301. *Id.* §§ 34177(m), 34179(h), 34182.5.

302. Petitioner's Memorandum of Points and Authorities in Support, *supra* note 177, at 14.

303. *Samples v. Brown*, 146 Cal. App. 4th 787, 810 (2007).

304. *Id.* at 805. The California Vehicle Code provisions were aimed at impounding vehicles driven by persons without valid licenses. *Id.* at 796. The provision challenged under the non-delegation doctrine, section 14602.6(b), provided that "[t]he registered and legal owner of a vehicle that is removed and seized under subdivision (a) or their agents shall be provided the opportunity for a storage hearing to determine the validity of, or consider any mitigating circumstances attendant to, the storage . . ." *Id.* The trial court ruled that section 14602.6(b) violated the non-delegation doctrine because there is no guidance for determining what a mitigating circumstance is, and would lead to varied and inconsistent interpretations by law enforcement agencies. *Id.* at 798.

305. *Id.* at 805.

place for how the administrative agency is to determine what qualifies as a mitigating circumstance.³⁰⁶ For example, the requirement that the vehicle be “stored for 30 days absent a showing of mitigating circumstances” is an important safeguard because it limits the “authority of the enforcement agency” and puts the public on notice.³⁰⁷ In addition, the purpose of the statute may provide insight as to what standards should be used.³⁰⁸ In *Samples*, the court held that the legislative purpose to punish and deter unlicensed driving is an important standard and safeguard for administrative agencies to consider when determining what constitutes a mitigating circumstance under the statute.³⁰⁹

Taking into consideration the court’s analysis in *Samples*, it is questionable whether the statutory provisions at issue in AB 1484 would be deemed unconstitutional for violating the non-delegation doctrine. Certainly, the Legislature is able to task other branches of government to carry out its “legislative will.”³¹⁰ Moreover, while plaintiffs in these cases claim that the Legislature granted the Department of Finance, an administrative agency, with unfettered discretion and control to decide important statutory provisions, it may be the case that there is still adequate guidance to help implement the policy. Moreover, it is also questionable whether the authority rises to the level of a fundamental policy decision. Similar to *Samples*, AB 1484’s provisions, in and of themselves, do not constitute a fundamental policy decision, but only serve as a mechanism to carry out its legislative purpose—namely, to ensure that the appropriate funds are properly returned to the taxing agencies that are in dire need of funds.³¹¹ The provisions at issue within AB 1484 are not entirely without standards. Rather, the amount of guidance that these provisions provide is similar to the minimal direction provided in the vehicle code provisions in *Samples*. For instance, the provision requiring the Department of Finance to determine the amount of unobligated balances owed by the taxing agencies is first determined by a licensed accountant employed by the successor agency.³¹² AB 1484 also sets out requirements that are to be included in the DDR,

306. *Id.* at 801–02.

307. *Id.* at 806.

308. *See id.* at 805–06.

309. *Id.*

310. *Mistretta v. United States*, 488 U.S. 361, 372 (1989).

311. A.B. 1484, 2011-2012 Leg., Reg. Sess. (Cal. 2012).

312. CAL. HEALTH & SAFETY CODE § 34179.5 (2012).

such as the “dollar value of assets transferred from the former redevelopment agency to the successor agency,” “expenditure and revenue accounting information,” “the dollar value of any cash or cash equivalents,” and “documentation of any enforceable obligations.”³¹³ The Department of Finance could consider all of these factors in addition to considering “any findings or opinions of the county auditor-controllers and the Controller.”³¹⁴

There are also reasonable safeguards in place throughout AB 1484 to keep the power of the Department of Finance in check. As provided in *Samples*, a reasonable safeguard could be as little as a thirty-day requirement to store an impounded automobile.³¹⁵ Here, AB 1484 allows the parties to dispute the determinations made by the Department of Finance and it requires the Department to explain the basis for its decisions.³¹⁶ Thus, there are protections to prevent the department from wielding complete authority.

Furthermore, the standards in place can be implied from the statutory purpose and do not need to be explicitly stated.³¹⁷ Here, the purpose behind AB 1484 is to return funds that were preemptively made to the successor agencies from the taxing agency, and this purpose serves as a form of guidance for the Department of Finance.³¹⁸ Because there is sufficient guidance as to what standards the Department of Finance should follow under AB 1484, the plaintiffs may have a difficult time arguing that AB 1484 is unconstitutionally violative of the non-delegation doctrine. The provisions of AB 1484 indicate that the decisions imparted on the administrative agency are not a fundamental policy concern. Also, a look into the legislative history of AB 1484 shows that there are standards and safeguards in place. Thus, it is unlikely that plaintiffs could prevail on a theory of a non-delegation doctrine violation. California trial courts have reached the same conclusion.³¹⁹

313. *Id.*

314. *Id.* § 34179.6.

315. *Samples v. Brown*, 146 Cal. App. 4th 787, 806 (2007).

316. CAL. HEALTH & SAFETY CODE § 34179.6(d)-(e) (2012).

317. *Samples*, 146 Cal. App. 4th at 805–06.

318. A.B. 1484, 2011-2012 Leg., Reg. Sess. (Cal. 2012).

319. See Ruling on Submitted Matter, *supra* note 270; Ruling on Submitted Matter, *supra* note 271.

Conclusion

While trial courts are starting to rule on redevelopment lawsuits, the debate over redevelopment will only continue as a number of redevelopment cases are currently pending before California appellate courts.³²⁰ As these cases progress, one can expect more decisions that will further shape California's redevelopment landscape.

If the courts again rule against redevelopment, it may be necessary to consider alternatives that would satisfy cities, counties, and the state. While it is important to ensure that school districts and other taxing agencies are properly funded, RDAs have been a vital part of the California economic landscape. RDAs have also been successful in generating property tax revenue for cash-strapped and developing cities. Thus, it is imperative that some form of redevelopment be restored. When developing a solution, however, legislators should also be mindful of the impact it would have on funding for other taxing entities. The challenge here would be to rework it in a way that would satisfy cities as well as the state. In response to the public outcry against the dissolution of redevelopment agencies and the host of problems that have resulted since then, several California legislators have proposed legislation to further address the problems caused by AB 1X 26 and AB 1484.³²¹ For example, AB 229, introduced in February 2013, would utilize infrastructure financing districts, which would then allow "cities and counties to issue bonds to fund public works projects" and would finance projects in RDA project areas for up to forty years.³²² This would be subject to a two-thirds voter approval.³²³ Another Assembly

320. See League of California Cities Summary, *supra* note 10 (referencing cases that are currently pending before the Third District Court of Appeal in California, including but not limited to *City of Cerritos v. California*, No. C070484; *City of Emeryville v. Matosantos*, No. C074186; *Peebler v. Department of Finance*, No. C073698); Martha Bridegam, *Brentwood files appeal on ruling that upheld post-redevelopment clawback*, CALIFORNIA PLANNING & DEVELOPMENT REPORT (Apr. 28, 2014), <http://www.cp-dr.com/node/3478>.

321. Stuart Waldman, *VICA: California Needs Alternatives to Dissolved Redevelopment Agencies*, SAN CLARITA VALLEY SIGNAL (July 23, 2013), <http://www.signalscv.com/archives/101404/>; Martha Bridegam, *Post-Redevelopment Legislation Seeks Direction*, CALIFORNIA PLANNING & DEVELOPMENT REPORT (Apr. 29, 2014), <http://www.cp-dr.com/node/3480> (for discussion on alternatives to redevelopment).

322. *Id.* See also A.B. 229, 2013-2014 Leg., Reg. Sess. (Cal. 2013).

323. A.B. 229, 2013-2014 Leg., Reg. Sess. (Cal. 2013). This bill was ordered to the "Inactive" file at the request of Assemblymember Toni Atkins on September 11, 2013.

Bill, AB 243, is virtually identical to AB 229, but requires fifty-five percent voter approval.³²⁴

It is difficult to think of a constitutional solution that would allow redevelopment projects to survive without contravening important constitutional provisions. AB 1X 27 would have been a compromise because it allowed those cities interested in redevelopment agencies to keep them, while infusing money into the state government.³²⁵ Perhaps the best solution, however, would be to allow some form of reformed redevelopment so that RDAs could not get a monopoly on property taxes. Redevelopment should be further reformed to avoid a repeat of previous abuses of redevelopment power.³²⁶ Due to the growing number of redevelopment lawsuits on the court's docket, there is no better time than now for the state to consider alternatives to redevelopment or to further clarify or modify AB 1X 26 or AB 1484.

324. A.B. 243, 2013-2014 Leg., Reg. Sess. (Cal. 2013). This bill was ordered to the "Inactive" file at the request of Assemblymember Toni Atkins on September 11, 2013. *See also* Waldman, *supra* note 321.

325. *See* Cal. Redev. Ass'n v. Matosantos, 53 Cal. 4th 231, 251 (2011).

326. William Fulton, *Getting real about redevelopment in California*, L.A. TIMES (Jan. 12, 2012), <http://articles.latimes.com/2012/jan/12/opinion/la-oe-fulton-redevelopment-2012-01-12> (stating that redevelopment has been used "to do anything and everything because the law has allowed them to").