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BAY AREA REAL ESTATE JOURNAL

SEPTEMBER 2011

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Crumbling Edifice

California redevelopment agencies face an uncertain future.

By **JoAnne Dunec** and **Bill Shiber**

Due to new legislation enacted in conjunction with California's 2010-2011 budget, the state's 400 redevelopment agencies are faced with a difficult choice: either operating by agreeing to make substantial annual financial contributions to local school and special districts, or going out of business before the end of the year. The legislation affects both existing and future real estate transactions involving redevelopment agencies.

As of June 29, the continuing activities of all California RDAs were severely restricted. Agencies cannot issue new bonds, incur new debt, enter into new agreements, amend existing agreements, adopt or amend redevelopment plans, acquire or convey property or commence eminent-domain proceedings.

The laws, ABX1 26 and ABX1 27, are *trailer bills* passed by the California Senate and Assembly and intended to help implement the state budget bill by reallocating tax revenue that would otherwise go to redevelopment. The legislature estimates that redevelopment agencies will divert about \$5 billion in property tax revenue from other taxing entities in the 2011-2012 fiscal year and wants to retain some of that revenue to fund education and other local government.

In short, ABX1 26 dissolves current redevelopment agencies as of Oct. 1, but ABX1 27 provides a mechanism for them to reinstate operations if the local jurisdiction adopts an ordinance requiring the jurisdiction to make specified payments for education and other local government. Redevelopment agencies view the required payments as a strong-arm attempt to contribute redevelopment revenue to fund other government agencies.

Unless and until a local jurisdiction adopts an ordinance pursuant to ABX1 27, referred to as a "continuation ordinance," there is a great deal of doubt as to the legality and enforceability of real estate transactions involving redevelopment agencies. While ABX1 26 permits RDAs to make payments due, enforce existing covenants and obligations, and otherwise perform "enforceable obligations" existing before June 29, it is far from



clear what this means for real estate transactions, especially those involving ongoing or phased-development activities.

Importantly from a real estate perspective "enforceable obligations" include typical redevelopment agreements, such as exclusive negotiation agreements, owner participation agreements and disposition and development agreements. Redevelopment agencies have 60 days from June 29 to prepare a list of enforceable obligations. But the determination of what that constitutes may not be easy. If, for example, the sole purpose of an existing ENA is to negotiate in good faith to achieve a mutually satisfactory DDA, the redevelopment agency has no authority to execute the DDA because it would be a new agreement. Thus, while the ENA is an "enforceable obligation" its reason for being—that is, negotiation and execution of a future DDA—is not achievable.

Other difficulties will likely arise. OPAs and DDAs that were executed years ago and intended to implement long-term phased development can no longer be amended to address changing market conditions or subsequent phases of development. Arguably, absent a need for modification, existing DDAs that contractually obligate a redevelopment agency to convey land to a private developer, for example, would be enforceable.

Other development obstacles may occur. For example, a redevelopment agency may have entered into a design contract with an architectural firm with the intention that the next step would be to enter into a construction contract with a general contractor to build the project. Absent any existing agreement that obligates the agency to enter into the construction contract, the new legislation prohibits the agency from entering into the agreement because it would be new.

Similarly, redevelopment agencies have the power of eminent domain to eliminate blight and accomplish redevelopment. The recent legislation withdraws all such powers unless the continuation ordinance is adopted. If a redevelopment agency is involved in a project in which eminent domain were contemplated, that tool is now taken away, potentially jeopardizing the project.

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ardizing the ability to proceed with the redevelopment or complete it in a coherent manner.

If a redevelopment agency does not elect to opt in by adopting a continuation ordinance and making the requisite payments, it will be eliminated as of Oct.1 and a successor agency will take over and wind down the agency's affairs. Presumably, such successor agencies would have the requisite power and authority to implement existing "enforceable obligations," such as DDAs and OPAs. But the legislation is unclear.

Even if a local jurisdiction adopts a continuation ordinance, the future remains tenuous. Should a jurisdiction fail to make a required annual payment, for instance, the redevelopment agency would presumably again be subject to ABX1 26 and eliminated. The payments are substantial and local jurisdictions are evaluating their financial capacity as part of their determination whether to opt in by adopting a continuation ordinance.

The California Redevelopment Association, the California League of Cities and the cities of San Jose and Union City have filed a lawsuit in the state's Supreme Court seeking to overturn the legislation. They allege that it improperly diverts funds from redevelopment agencies to other government entities and functions. Redevelopment agencies with ongoing capital improvement projects or that are in the midst of negotiating new agreements or modifications to existing agreements with private developers may not be able to delay their decision to opt in.

This fiscal year, RDAs are expected to pay \$1.7 billion; \$400 million would be due annually thereafter, according to the lawsuit. San Jose's RDA, already under extreme financial duress, estimates it will have to pay as much as \$53 million in the first fiscal year and up to \$13 million a year thereafter. "Dissolving RDAs unilaterally and suddenly will stop many important, half completed redevelopment projects dead in their tracks and expose cities and counties to legal liability for the obligations of their now dissolved RDAs," the petition says.

The best option may be to adopt the continuation ordinance for now, until there is greater clarity as to the ultimate status of this legislation. Presumably, the ordinance could be rescinded, and the position taken that activities undertaken in the interim were valid because the ordinance was in effect at that time.

These complex and ambiguous bills significantly affect past, present and future real estate transactions with redevelopment agencies. It is critical that anyone who is dealing with an agency understand and prepare for the impact while we all wait to see what the court decides. ■

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