

COPY SUPREME COURT COPY

In the Supreme Court of the State of California

**CALIFORNIA REDEVELOPMENT
ASSOCIATION, LEAGUE OF
CALIFORNIA CITIES, CITY OF UNION
CITY, CITY OF SAN JOSE, and JOHN F.
SHIREY,**

Petitioners,

v.

**ANA MATOSANTOS, in her official
capacity as Director of Finance, JOHN
CHIANG, in his official capacity as the
Controller of the State of California,
PATRICK O'CONNELL, in his official
capacity as the Auditor-Controller of the
County of Alameda and as a representative
of the class of county auditor-controllers,**

Respondents.

Case No. S194861

**SUPREME COURT
FILED**

SEP -9 2011

Frederick K. Ohnigh Clerk

Deputy

**REQUEST FOR JUDICIAL NOTICE AND MEMORANDUM OF
POINTS AND AUTHORITIES IN SUPPORT OF REQUEST**

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Pursuant to Evidence Code sections 459 and 452, respondent Ana Matosantos, Director of the California Department of Finance, respectfully requests that the Court take judicial notice of the documents attached hereto as Exhibits A through C. Exhibit A is a copy of a Policy Brief by the Legislative Analyst entitled *Should California End Redevelopment Agencies?*, issued February 9, 2011. Exhibit B is a copy of the Analysis of the 2011-12 Budget by the Legislative Analyst, *Governor's Redevelopment Proposal*, issued January 18, 2011. Exhibit C is a copy of an excerpt from the Preliminary Offering Statement dated September 6, 2011 for \$5,400,000,000 State of California 2011-12 Revenue Anticipation Notes, Series A-1 and Series A-2, Introduction, page A-15.

The relevance of the materials subject to this request is set forth in respondent's Return to Petition for Writ of Mandate. The reports attached as Exhibits A and B describe aspects of the redevelopment system in California prior to the legislation at issue in this case. The materials attached as Exhibit C provide the State of California's official estimate of the financial impact of ABX1 26 and ABX1 27, and was prepared and certified in connection with the offering of bonds to the financial markets.

This request is based on this motion and the following points and authorities in support of this request.

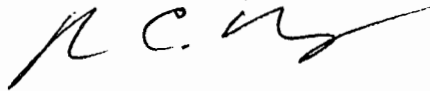
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Wherefore, respondent prays for an Order granting this request, and that the Court take judicial notice of the reports by the Legislative Analyst attached hereto as Exhibits A and B, and of the excerpt of the Preliminary Offering Statement attached as Exhibit C.

Dated: September 9, 2011

Respectfully submitted,

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POINTS AND AUTHORITIES IN SUPPORT OF REQUEST FOR JUDICIAL NOTICE

Under Evidence Code section 459, subdivision (a), “[t]he reviewing court may take judicial notice of any matter specified in Section 452.” And Evidence Code section 452, subdivision (c), provides for permissive judicial notice of “[o]fficial acts of the legislative, executive, and judicial departments of the United States and of any state of the United States.”

Reports prepared by the Legislative Analyst’s Office are the proper subject of judicial notice. (*CBS Broadcasting, Inc. v. Superior Court* (2001) 91 Cal.App.4th 892, 895, n 2.) Likewise, the Court “may take judicial notice of the report of a state executive officer as reflecting an ‘official act’” (*Aguilar v. Atlantic Richfield Co.* (2001) 25 Cal.4th 826, 855 n.3 (citations omitted).)

The reports by the Legislative Analyst attached as Exhibits A and B were prepared and distributed prior to the passage of ABX1 26 and ABX1 27 and provided important background to the legislators considering redevelopment reform. The Preliminary Offering Statement attached as Exhibit C provides the State’s official estimate of the fiscal impact of ABX1 26 and ABX1 27, and was prepared and certified for use by the financial markets. Thus, these materials are the proper subject of judicial notice, are relevant to the issues presented in this case, and are of substantial consequence to the determination of the action.

For the foregoing reasons, respondent's request for judicial notice is proper and should be granted.

Dated: September 9, 2011

Respectfully submitted,

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EXHIBIT A

The 2011-12 Budget: Should California End Redevelopment Agencies?

MAC TAYLOR • LEGISLATIVE ANALYST • FEBRUARY 9, 2011

INTRODUCTION

Californians pay over \$45 billion in property taxes annually. County auditors distribute these revenues to local agencies—schools, community colleges, the counties, cities, and special districts—pursuant to state law. Property tax revenues typically represent the largest source of local general purpose revenues for these local agencies.

More than 60 years ago, the Legislature established a process whereby a city or county can declare an area to be blighted and in need of redevelopment. After this declaration, most property tax revenue growth from the “project area” is distributed to the city or county’s redevelopment agency, instead of the other local agencies serving the project area.

During the early years of California’s redevelopment law, few communities established project areas and project areas typically were small—usually 10 to 100 acres. Over the last 35 years, however, most cities and many counties have created project areas and the size of project areas has grown—several cover more than 20,000 acres each. Partly as a result of this expansion in number and size of project areas, redevelopment’s share of total statewide property taxes has grown six fold (from 2 percent to 12 percent of total statewide

property taxes). In some counties, local agencies have created so many project areas that more than 25 percent of all property tax revenue collected in the county are allocated to a redevelopment agency, not the schools, community colleges, or other local governments.

California’s expansive use of redevelopment has engendered significant controversy. Advocates of the program contend that it is a much needed tool to promote local economic development in blighted urban areas. Program critics counter that redevelopment diverts property tax revenues from core government services and increases state education costs, and that the scale and location of many project areas bear little relationship to the program’s intended mission.

The Governor’s 2011-12 budget includes a plan for dissolving redevelopment agencies and distributing their funds (above the amounts necessary to pay outstanding debt) to other local agencies. To assist the Legislature in reviewing this proposal, this report explains how redevelopment redistributes and uses property tax revenues. The report then evaluates redevelopment, summarizes and assesses the Governor’s proposal, and offers suggestions for legislative consideration.

HOW REDEVELOPMENT REDISTRIBUTES AND USES PROPERTY TAXES

Property Tax Allocation in Areas Not Under Redevelopment

After property owners pay property taxes, county auditors distribute them to schools and other local agencies in the county. While the laws controlling allocation of the base 1 percent property tax rate are complex, they can be summarized in three steps.

- **Step 1.** Every year, each local agency receives the same amount of property tax revenues that it received the year before.
- **Step 2.** Each local agency receives a share of any growth (or loss) in property tax revenues that occurred within its jurisdiction. (The share an agency receives is based on historical factors and is often referred to as its “AB 8 share” after the 1979 law that established the formula to create these shares.)
- **Step 3.** Each city and county receives additional revenues (shifted from the schools’ property tax revenues) to offset its losses from the state’s reduction of the local sales tax rate (the “triple flip”) and vehicle license

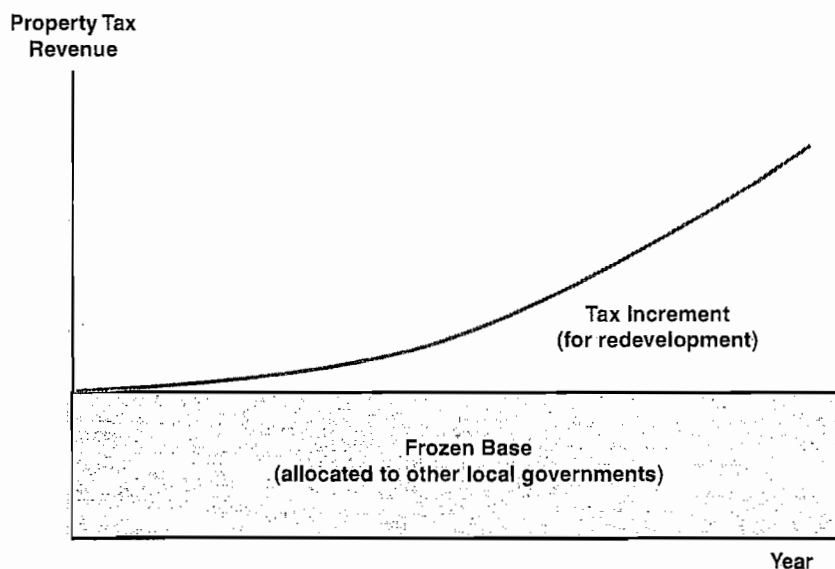
fee (the “VLF swap”). Each city and county receives funds equal to its current sales tax losses and its 2004 VLF losses, adjusted by the agency’s change in assessed valuation since 2004.

Property Tax Allocation in Areas Under Redevelopment

If a community establishes a redevelopment project area, the amount of property tax revenues flowing to local agencies serving the area is frozen. K-14 districts, the counties, cities, and special districts continue to receive all of the property tax revenues they had received up to that point. This amount is known as the frozen base.

As shown in Figure 1, all of the growth in property taxes in the project area—over the frozen

Figure 1
Allocation of Property Tax Revenues After Redevelopment Project Is Established



base—is allocated to the redevelopment agency as tax-increment revenue. In other words, local agencies receive the same amount of property tax revenues they received in the past, but none of the growth.

This redirection of property tax revenues lasts for the life of the redevelopment project—typically 50 years, although some older projects have longer lifetimes. (A nearby box provides some information about how this element of California’s redevelopment law compares with other states with similar programs.)

Viewed from the county auditor’s perspective, Steps 1 and 3 of the property tax allocation system (described previously) stay the same. Step 2, however, is revised so that the auditor distributes all revenue growth in the project area to the redevelopment agency—and not to other agencies.

How Redevelopment Uses Property Tax Revenues

State law allows redevelopment agencies to use property tax increment revenues to finance a broad array of projects. Redevelopment agencies typically use these revenues—often in conjunction with private developer funds or other governmental resources—to finance capital improvements, land and real estate acquisitions, affordable housing, and

planning and marketing programs.

As shown in Figure 2 (see next page), however, not all of the property tax increment revenue is available for broad redevelopment purposes. State law requires redevelopment agencies to spend 20 percent of tax-increment funds for low- and moderate-income housing. Additionally, in order to partially offset the loss of growth in property tax revenues for other local agencies, state law requires redevelopment agencies to “pass through” to other agencies a portion of their tax-increment revenues.

Statewide, redevelopment agencies pass through an average of about 22 percent of their property tax increment revenues. This pass-through percentage varies across project areas, based on the date the redevelopment project area was formed and other factors. (Redevelopment law was amended in 1993 to establish a statewide formula for sharing property tax increment revenue derived from *newly* created redevelopment project areas. This formula increases the pass-through share over time. In redevelopment areas established prior to 1993, redevelopment agencies and affected local agencies typically negotiated the amount of revenues contained in a pass-through agreement.)

COMPARISON WITH OTHER STATES

California’s redevelopment law provides for a 50-year diversion of all property tax revenue growth in redevelopment areas. This feature of California law is somewhat unusual in comparison with other states with redevelopment programs (often called “tax increment financing” elsewhere in the country). Many other states, for example, authorize some local agencies to “opt out” of the redevelopment program (that is, to *not* have their property tax revenue growth included in the diversion) or statutorily exclude school property taxes from the program. Still other states limit to shorter periods how long redevelopment agencies may redirect property taxes. California redevelopment law partially mitigates the fiscal effect of its program design by requiring redevelopment agencies to “pass through” a portion of the revenues diverted from other local agencies.

Figure 2
Use of Tax Increment Revenues
2008-09

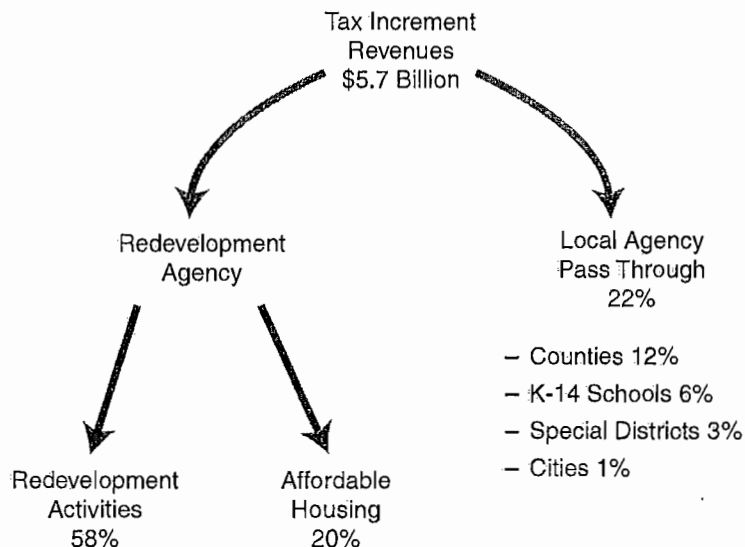
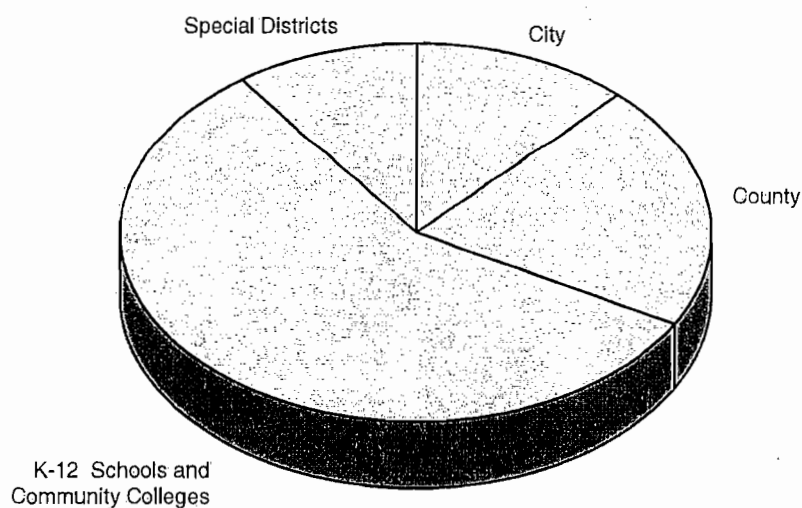


Figure 3
Estimated Statewide Allocation of Property Taxes
When Redevelopment Projects End



Property Taxes After Redevelopment Projects End

After a redevelopment project ends, the county auditor distributes all of the revenues that formerly were considered “tax increment revenues” to local agencies in the area. Each agency serving the area receives a portion of the revenues as determined by its AB 8 share. From a county auditor’s standpoint, these revenues do not trigger additional allocations pursuant to Step 3 (the triple flip and VLF swap adjustments) because the end of a redevelopment project does not affect a local agency’s sales tax revenue losses or calculation of the VLF swap amount. As shown in Figure 3, we estimate that schools and community colleges would receive over half of the revenues made available after a redevelopment project ends. While very few redevelopment projects have ever ended to date, a significant number are expected to end within next 15 years.

EVALUATING REDEVELOPMENT

The Governor's proposal to end redevelopment raises fundamental questions regarding the extent to which this program benefits the state. To help the Legislature evaluate redevelopment programs, we reviewed available academic studies on their effectiveness. In addition, because published academic articles on California redevelopment programs are rare, we reviewed studies on other states' tax-increment financing districts—the common term for redevelopment finance nationwide. Finally, we reviewed state agency and other reports on redevelopment performance producing affordable housing and compared the key elements of accountability for redevelopment and other programs. Figure 4 summarizes our findings, which we discuss in more detail below.

Figure 4
Redevelopment:
Findings From Research and Studies

Positive

Flexible tool that can improve targeted areas.
 Helps build affordable housing.

Negative

No evidence that redevelopment increases overall regional or statewide economic development.
 Diverts revenues from other local governments and increases state education costs.
 Has limited transparency and accountability.

Flexible Tool to Improve Targeted Areas

Under the powers granted to them in redevelopment law, cities can target areas within their jurisdiction for economic development. (Although counties also form redevelopment agencies, we focus on cities in this report because they account for more than 90 percent of active redevelopment areas.) While cities have other tools to encourage economic development, establishing a redevelopment area is one of the easiest ways to raise

significant sums. Most other local options for generating revenue for economic development—such as issuing general obligation bonds or establishing a business improvement district—require approval by voters and businesses and/or residents to pay increased sums. Redevelopment requires neither.

The use of redevelopment has improved many areas of the state through the revitalization of downtown and historic districts, improvements in public infrastructure, and increased commercial investment. Many of these investments have improved the quality of life for residents in specific areas. In terms of quantifiable measures, most of the academic literature indicates that property values within project areas increase more than comparable areas within a region. This is not surprising as we would expect areas receiving public subsidies to outperform those that do not.

Funds Affordable Housing

As mentioned above, state law requires redevelopment agencies to deposit 20 percent of their tax increment revenues into low- and moderate-income housing funds and spend these funds on affordable housing. Redevelopment agencies are authorized to spend housing funds to acquire property, rehabilitate or construct buildings, provide subsidies for low- and moderate-income households, or preserve public subsidized housing units at risk of conversion to market rates. While other federal, state, and local programs also provide funds for affordable housing efforts, redevelopment represents one of the largest funding sources.

In terms of housing production efficiency and effectiveness, we are not aware of any studies that compare redevelopment agencies' results in producing affordable housing with other financing approaches. We note, however, that state audits

and oversight reports frequently conclude that a significant number of redevelopment agencies take actions that have the effect of reducing their housing program productivity, including:

- Maintaining large balances of unspent housing funds. (The Department of Housing and Community Development's most recent report indicates that the agencies collectively had an unencumbered balance of more than \$2.5 billion.)
- Using most of their housing funds for planning and administrative costs.
- Spending housing funds to acquire land for housing, but not building the housing for a decade or longer.

No Reliable Evidence That Redevelopment Increases Regional or Statewide Economic Development

While redevelopment leads to economic development *within* project areas, there is no reliable evidence that it attracts businesses to the state or increases overall regional economic development. Instead, the limited academic literature on this topic finds that—viewed from the perspective of an entire city or region—the effect of this program on property values is minimal. That is, redevelopment may cause some geographic shifts in economic development, but does not increase the overall amount of economic activity in a region. Studies in Illinois and Texas, for example, found that their redevelopment programs did little more

CRA Report Inaccurately Calculates Employment Effects of Redevelopment

The California Redevelopment Association (CRA) recently circulated a document asserting that eliminating redevelopment agencies would result in the loss of 304,000 jobs in California. We find the methodology and conclusion of CRA's report to be seriously flawed. In our view, it vastly overstates the economic effects of eliminating redevelopment and ignores the positive economic effects of shifting property taxes to schools and other local agencies.

The CRA's job loss estimate is based on a consultant's report using data from 2006-07. To estimate the number of jobs resulting from redevelopment agencies, the report calculated the total expenditures on construction projects completed within a sample of redevelopment areas for 2006-07, as well as for any projects completed outside the area with agency participation. Based upon that sample, the report then estimated the total construction expenditures for redevelopment agencies statewide in 2006-07 and used a computer model to calculate through various multipliers the total effect of those expenditures on the state's economy and employment. The report concluded that redevelopment was responsible for the creation of about 304,000 full and part-time jobs in 2006-07. Therefore, the CRA asserts that the elimination of redevelopment would result in the loss of 304,000 jobs.

To our knowledge, the consultant's study has never been subjected to any independent or academic scrutiny. Our review indicates that the report has three significant flaws that cause it to vastly overstate the net economic and employment effects of redevelopment agencies.

Assumes Redevelopment Agencies Participate in All Project Area Construction. The study's calculation of construction expenditures includes *all* construction completed in a redevelopment project area in 2006-07, even if the redevelopment agency was not a participant. We find implausible

than displace commercial activity that would have occurred elsewhere in the region.

In addition to examining the effect of redevelopment on property values in a region, some research has focused on the effect of this program on jobs. The independent research we reviewed found little evidence that redevelopment increases jobs. That is—similar to the analyses of property values—the research typically finds that any employment gains in the project areas are offset by losses in other parts of the region. We note that one study, commissioned by the California Redevelopment Association, vastly overstates the employment effects of redevelopment areas (please see nearby box).

Diverts Revenues From Other Local Governments and State

Redevelopment agencies receive over \$5 billion of tax increment revenues annually. Lacking any reliable evidence that the agencies' activities increase statewide tax revenues, we assume that a substantial portion of these revenues would have been generated anyway elsewhere in the region or state. For example, a redevelopment agency might attract to a project area businesses that previously were located in other California cities, or that were planning to expand elsewhere in the region. In either of these cases, property taxes paid in the project area would increase, but there would be no change in statewide property tax revenues.

the report's implicit assumption that *no* construction with solely private financing would have occurred within a redevelopment area in the absence of the redevelopment agency. This is particularly true, given the large geographic scale of California redevelopment project areas. In our view, it is likely that much of the new business or residential construction (and the associated jobs) would have occurred independently of the redevelopment agency.

Assumes Private and Public Entities Participating in Redevelopment Agency Projects Would Not Invest in Other Projects. Most redevelopment agency projects include significant financing from private investors or other public agencies. By asserting that all of the jobs associated with redevelopment construction would be lost if redevelopment agencies were eliminated, the CRA implicitly assumes that these private and public partners would not invest in other economic activities in the state. The report provided no explanation for this assumption that the existing private capital and public agency grants would remain unused without redevelopment agency participation. In most cases, we would expect developers, investors, and public agencies to find alternative projects to pursue—either within the redevelopment area or elsewhere in the state.

Assumes Other Local Agencies' Use of Property Tax Revenues Would Not Yield Economic Benefits. Under the Governor's proposal, the property tax revenues that currently support redevelopment would flow over time to schools and other local agencies in the county. By asserting that all of the jobs associated with redevelopment construction would be lost if redevelopment agencies were eliminated, the CRA implicitly assumes that these other local agencies' use of property tax revenues would not result in any economic activity. The report provided no explanation for this assumption. In our view, spending by school districts, counties, and other local agencies also would yield significant economic and employment benefits.

To the extent that a redevelopment agency receives property tax revenues without generating an overall increase in taxes paid in the state, the agency reduces revenues that otherwise would be available for local agencies to spend on non-redevelopment programs, including law enforcement, fire protection, road maintenance, libraries, and parks.

The fiscal effect of redevelopment on K-12 schools and community colleges, in contrast, is somewhat different. This is because, under California school finance laws, the state is responsible for ensuring that each district receives sufficient total revenues (from state and local sources) to meet a statutorily defined funding level. Thus, property tax revenues redirected to redevelopment agencies usually are replaced by increased state aid. In this way, K-14 districts are largely unaffected by redevelopment, but state education costs increase.

Fiscal Effect on Local Agencies and the State.

Based on the available evidence, we estimate that the amount of property tax revenues diverted from non-school local agencies (principally, counties and special districts) is about \$1.5 billion annually net of pass-through payments. We further estimate that the increased cost to the state associated with the diversion of K-14 district property taxes is over \$2 billion annually net of pass-through payments.

GOVERNOR'S PROPOSAL

The administration proposes to dissolve the state's redevelopment agencies. Tax increment revenues that currently go to redevelopment agencies would be redirected to retire redevelopment debts and contractual obligations and to fund other local government services. In place of redevelopment, the administration indicates that it will propose a constitutional amendment to allow local voters to approve tax increases and general obligation bonds for economic development

In addition to these amounts, we note that some K-14 districts with unusually high property tax revenues per pupil ("basic aid" districts) also sustain property tax revenue losses associated with redevelopment, but we are not able to estimate the magnitude.

Limited Transparency and Accountability

Redevelopment agencies lack some of the key accountability and transparency elements common to other local agencies. Specifically, unlike other local agencies, redevelopment agencies can incur debt without voter approval. Redevelopment agencies can also redirect property tax revenues from schools and other local agencies without voter approval or the consent of the local agencies.

In addition, although redevelopment programs are authorized in state law and increase state costs, redevelopment programs lack the key accountability elements that are common to state-supported local assistance programs. Specifically, no state agency reviews redevelopment economic development activities or ensures that project areas focus on the program's mission. We also note that use of redevelopment is not limited to communities with low property wealth—some of California's most affluent cities have declared large sections of their jurisdictions "blighted."

purposes by a 55 percent majority. While many of the details of the Governor's proposal still are under development, we outline its key elements below.

Successor Agency Assumes Debt Obligations

Redevelopment agencies currently have the authority to issue debt, own and lease property, and enter into other long-term contractual obligations. While enactment of the Governor's proposal as

urgency legislation would prohibit redevelopment agencies from entering into additional obligations, existing debts would need to be paid. The Governor proposes to transfer the responsibility for managing these obligations to a local successor agency—most likely the city or county that authorized the redevelopment area, guided by an oversight board. The successor agency would receive the redevelopment agency’s existing balances and future shares of tax increment revenue to pay the agency’s debts. Any funds above the amounts needed to pay these debts would be used for other purposes as described below. The one exception is that the successor agencies would shift any unspent redevelopment housing funds to local housing authorities to use for low- and moderate-income housing.

Use of Redevelopment Funds in 2011-12

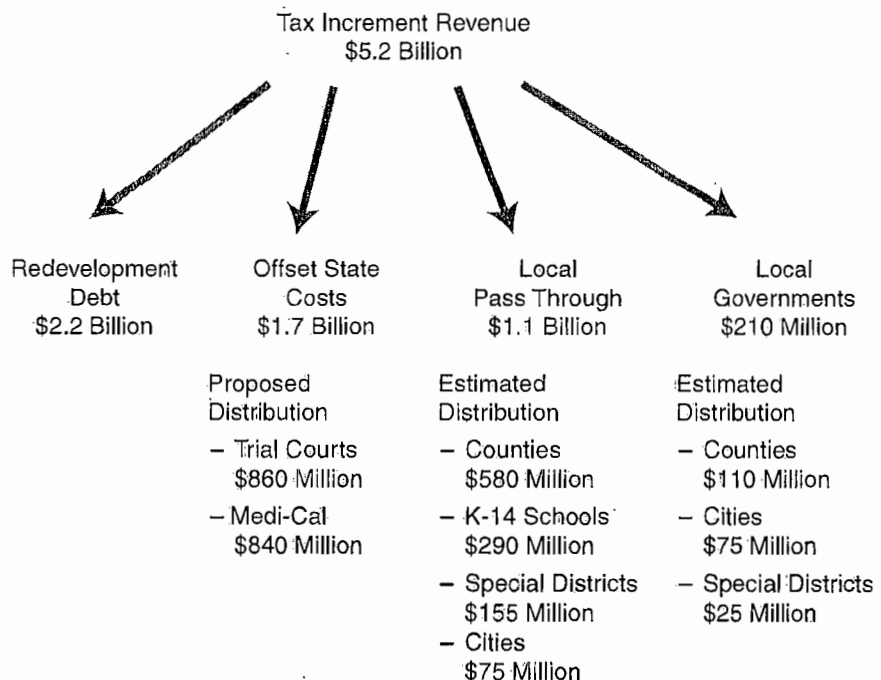
The Governor’s budget assumes that tax increment revenues from dissolved redevelopment areas would be approximately \$5.2 billion in 2011-12. (The most recent report from the State Controller’s Office identifies \$5.7 billion of redevelopment tax increment revenues in 2008-09. The Governor’s lower tax increment estimate reflects its assumptions regarding the decline of property values statewide.) Of this amount, an estimated \$2.2 billion would be used to pay redevelopment debts and obligations during the first year. As outlined in Figure 5,

the remainder of the tax increment revenues (\$3 billion) would provide funding to local governments and offset state General Fund costs. The Governor’s proposal would continue to provide redevelopment’s existing pass-through payments to local agencies. It would also offset \$1.7 billion in state Medi-Cal and trial court costs and distribute \$200 million to cities, counties, and special districts in proportion to these agencies’ AB 8 shares of the property tax.

Use of Redevelopment Funds In Subsequent Years

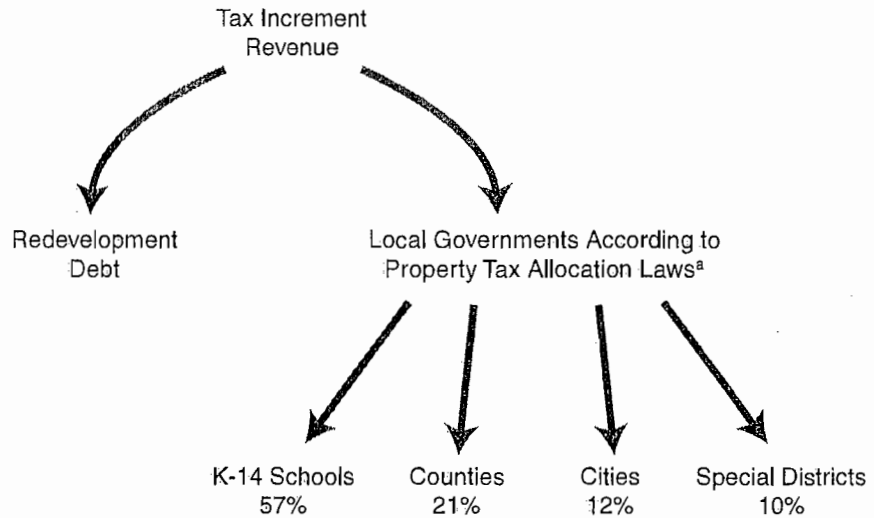
Beginning in 2012-13, any property tax revenues remaining after the successor agencies pay redevelopment debt would be distributed to other local governments in the county. Instead of offsetting state costs or continuing pass-through payments as in 2011-12, distributions of

**Figure 5
Governor’s Proposal for Use of Redevelopment Revenue in 2011-12**



these revenues to local governments generally would follow provisions in existing law. One exception is that property taxes that otherwise would be distributed to enterprise special districts (primarily fee-financed water and waste disposal districts) would be allocated instead to counties. As shown in Figure 6, we estimate more than half of the remaining revenue would be distributed to schools. (The exact allocation of property tax revenues, however, varies significantly across the state.) As redevelopment debts are repaid over time, the amount of revenue available to local governments would steadily increase.

Figure 6
Governor’s Proposal for Use of Redevelopment Revenue in Future Years



^aEstimated statewide percentages. Counties would also receive a small portion of funds allocated to special districts. Specifically, property tax revenues that would currently be allocated to enterprise special districts would instead go to counties.

Economic Development Could Continue at Local Level

While the Governor’s plan would phase out the existing redevelopment system, it also proposes a constitutional amendment to allow local voters to approve tax increases and general obligation bonds

for economic development purposes by a 55 percent majority. At this time, details on this portion of the proposal are not available. As we understand it, cities and counties would retain the powers granted to them under redevelopment law except for the use of property tax increment revenue. In the place of tax increment revenue, the proposal would lower the voter threshold for other financing mechanisms that local governments could use to pursue economic development activities that are currently carried out by redevelopment agencies.

LAO ASSESSMENT

In our view, the Governor’s proposal merits consideration. The proposal places the responsibility to pay for local economic development activities with the level of government benefiting from these policies. The proposal also heightens local accountability for its economic development policies and provides local governments increased

general purpose revenues. Finally, the proposal would make a significant contribution towards helping the state address its serious fiscal difficulties in 2011-12. We discuss these advantages, as well as some additional considerations related to the proposal, below.

Links Program Control, Benefit, and Costs

Redevelopment agencies determine the types of projects they undertake. Decisions regarding spending tax increment revenues—to remedy local infrastructure problems, provide amenities for an auto mall, or subsidize business relocation—are made at the local level. In addition, the research on tax increment financing indicates that it provides localized economic benefits, but does not necessarily increase statewide economic development.

Given these factors—local control over the use of tax increment funds and local benefits—we see little reason for the state to continue its financial support for this program. The Governor’s proposal adheres to a key policy principle that, whenever possible, beneficiaries should pay for services that do not have larger societal benefits.

Improves Government Accountability And Transparency

Local residents and elected officials can best assess the advantages and disadvantages of raising new funds for economic development activities versus shifting funds from other government programs. Under the current system, however, local residents and most elected local officials do not have a role in making these decisions. This is because a redevelopment agency’s decision to form a project area can divert property tax revenues from other agencies without their consent or voter approval. The agency forming a project area also does not have to confront the tradeoffs associated with diverting property tax revenues from its local schools because the state backfills virtually all of these property tax losses. Ending state-assisted redevelopment would require individual communities to confront the full policy implications of funding economic development within their borders, thereby improving transparency and accountability.

Redirects Funds to Local Governments

Under the Governor’s proposal, schools, counties, special districts, and cities would receive increased property tax revenues. While existing property tax increment revenues are restricted to redevelopment purposes, local governments would have the flexibility to direct these new revenues to their highest priority programs, including public safety, education, health, or social services. Local governments also could elect to use these increased funds for economic development activities.

Provides a One Year State Fiscal Benefit

The proposal would help address the state’s 2011-12 budget problem by offsetting state General Fund costs for Medi-Cal and trial courts by \$1.7 billion. While there is little policy rationale for using property taxes permanently for these purposes, we think this one-time use is reasonable in recognition of the magnitude of the state’s prior-year subsidies for redevelopment.

Additional Factors and Considerations

At the time this brief was prepared, the administration was still developing the statutory provisions to implement its proposal. While we cannot provide the Legislature with a detailed assessment of the proposed plan, we highlight below three issues that merit the Legislature’s consideration.

Early Plan Complicated School Funding and Property Tax Allocation Systems. Early versions of the Governor’s plan provided a special allocation system for the additional property tax revenues to schools. Instead of being allocated as property taxes to K-14 districts where the revenues were generated, the administration’s plan allocated these revenues to K-14 districts *countywide* as a *supplement* to their existing funds. In our view, this approach does not make sense and would further complicate the already complicated K-14 district finance and

property tax allocation systems. This approach also would increase state costs over the long term (relative to current law) because the state would not receive the financial relief associated with the expected expiration of redevelopment projects. The state also would forgo considerable ongoing state savings because the increased K-14 property taxes would not offset the state's spending for schools. In our view, any property tax revenue from the former redevelopment areas—above the amounts needed to pay existing debt—should be allocated as property taxes pursuant to existing laws. Should the Legislature wish to provide increased support for K-14 districts or to modify the AB-8 property tax allocation system, it could do so separately.

Few Other Options for Ongoing Redevelopment Relief. In some ways, the Governor's proposal is similar to many previous actions of the Legislature. Specifically, ten times over the last two decades the Legislature has required redevelopment agencies to shift funds to schools, thereby partly mitigating the state's increased education costs associated with redevelopment. In 2009-10, for example, the Legislature required redevelopment agencies to shift \$2 billion of redevelopment funds to schools over two years. The voter's recent approval of Proposition 22, however, prohibits the Legislature from enacting these types of revenue shifts in the future. Thus, the Legislature has few options for mitigating

the major ongoing costs of redevelopment other than dissolving the program. In the future, the Legislature could consider creating an alternative, more targeted, economic development program.

Dissolving Redevelopment Will Be Complicated and Disruptive. Program changes of this magnitude inevitably pose administrative, policy, and legal difficulties. Ending redevelopment, a program that California local governments have used for decades, will not be an exception. Many communities have significant numbers of people and projects currently funded through redevelopment revenues, as well as plans for additional redevelopment expenditures over the coming months. In addition, a significant portion of redevelopment agency funds are committed to the payment of bonded indebtedness, and three voter approved measures—Proposition 18 (1952), Proposition 1A (2004), and Proposition 22 (2010)—contain provisions limiting the state's authority to shift property taxes and/or redirect tax increment revenues. Drafting a plan for local governments to carefully unwind their redevelopment programs and successfully navigate the many legal, administrative, and financial factors will be complex. The Legislature will need to weigh the costs and benefits of dissolving redevelopment agencies versus the costs and benefits of other major budget alternatives.

CONCLUSION

Given the significant policy shortcomings of California's redevelopment program, we agree with the Governor's proposal to end it and to offer local governments alternative tools to finance economic development. Under this approach, cities and counties would have incentives to consider the full range of costs and benefits of economic development proposals.

In contrast with the administration's proposal, however, we think revenues freed up from the dissolution of redevelopment should be treated as what they are: property taxes. Doing so avoids further complicating the state's K-14 financing system or providing disproportionate benefits to K-14 districts in those counties where redevelopment was used extensively. Treating the revenues

2011-12 BUDGET

as property taxes also phases out the state's ongoing costs for this program and provides an ongoing budget solution for the state.

Ordinarily, we would recommend that the state phase out this program over several years or longer to minimize the disruption an abrupt ending likely

would engender. Given the state's extraordinary fiscal difficulties, however, the Legislature will need to weigh the effect of this disruption in comparison with other major and urgent changes that the state would need to make if this budget solution were not adopted.

2011-12 BUDGET

AN LAO REPORT

LAO Publications

This report was prepared by Mark Whitaker and reviewed by Marianne O'Malley. The Legislative Analyst's Office (LAO) is a nonpartisan office which provides fiscal and policy information and advice to the Legislature.

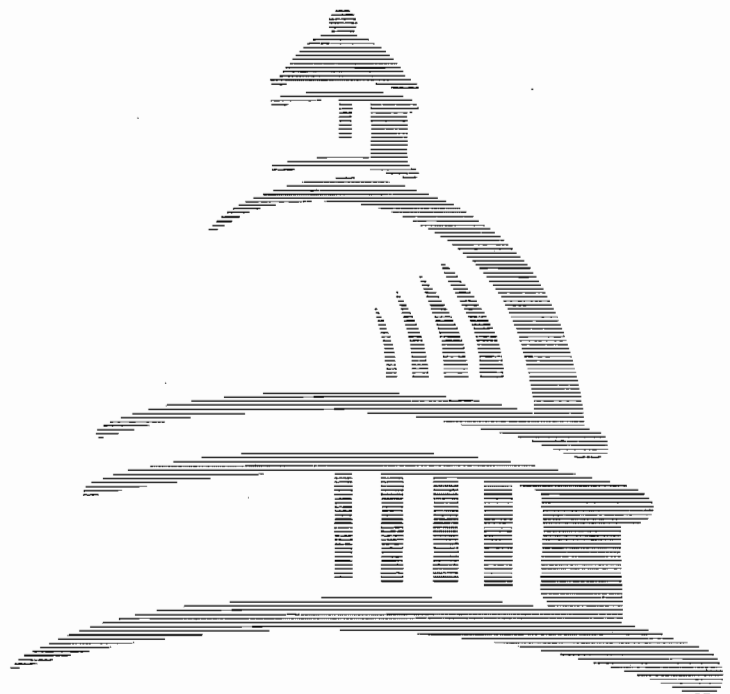
To request publications call (916) 445-4656. This report and others, as well as an email subscription service, are available on the LAO's website at www.lao.ca.gov. The LAO is located at 925 L Street, Suite 1000, Sacramento, CA 95814.

EXHIBIT B

January 18, 2011

Governor's Redevelopment Proposal

LEGISLATIVE ANALYST'S OFFICE





Redevelopment Background

	Property Taxes to Redevelopment
Selected Counties	
San Bernardino	31%
Riverside	26
Butte	20
Solano	20
Selected Other Counties	
Los Angeles	12
Sacramento	5
San Francisco	7
Statewide Totals	12%



Enacted by Statute, Modified by Constitutional Amendment.

The California Community Redevelopment Law, which was first enacted in 1945 and substantially expanded in 1951, allows cities and counties to establish redevelopment agencies. In 1952, voters approved a constitutional amendment to allow redevelopment agencies to use the property tax as a funding source.



Property Tax Increment Is Main Revenue Source. If a city or county creates a redevelopment project area to address urban blight, its redevelopment agency receives the future growth in property taxes from the area, known as the property tax increment. (Absent redevelopment, schools and other local agencies receive these tax revenues.)



Redevelopment Receives Increased Share of Statewide Property Tax Revenues. The expansion of redevelopment agencies has gradually shifted property tax revenues away from schools and other local agencies. Redevelopment currently receives about 12 percent of statewide property tax revenues compared to 4 percent in 1983-84.



Redevelopment Background

(Continued)



Use of Redevelopment Varies Across State. The percentage of property tax revenues allocated to redevelopment varies significantly at the local level. Some agencies have placed so much property under redevelopment that as much as one-fifth of their countywide assessed property values is under redevelopment. The City of Fontana's redevelopment agency receives more than two-thirds of property taxes paid in the city.



LAO Assessment of Current Redevelopment Program

- No Reliable Evidence That Redevelopment Agencies Improve Overall Economic Development in California.*** There is no reliable evidence that redevelopment projects attract businesses to the state or increase overall economic development in California. The presence of a redevelopment area might shift development from one location to another, but does not significantly increase economic activity statewide.

- Redevelopment Diverts Property Taxes From K-14 Education and Other Local Programs.*** Redevelopment agencies receive approximately \$5 billion of property tax revenue that would otherwise fund school districts, cities, counties, and special districts. The redevelopment agencies “pass through” about \$1.1 billion to local agencies based upon negotiated agreements and state statute. Of this amount, approximately \$300 million is passed through to schools with only \$40 million offsetting state education costs. The state General Fund must backfill the remaining property tax revenues diverted from K-14 schools, at a cost of over \$2 billion annually.

- Proposition 22 Greatly Constrains the State’s Authority to Redirect Redevelopment Property Tax Revenues.*** The state has periodically enacted laws requiring redevelopment agencies to give shares of the property tax increment to school districts. For example, the state required redevelopment agencies to shift \$2 billion to school districts over the last two fiscal years. Voter approval of Proposition 22 in 2010 greatly constrains the Legislature’s authority to enact future revenue shifts.



Governor's Proposal

- End Redevelopment Agencies.** The Governor's proposal would dissolve existing redevelopment agencies by July 1. Local successor agencies would receive the property tax increment that currently goes to redevelopment agencies.

- Create Alternative Mechanism for Local Governments to Raise Revenue for Economic Development.** To give communities greater capacity to promote economic development in the absence of redevelopment agencies, the Governor proposes a constitutional amendment to allow local voters to approve tax increases and general obligation bonds for these purposes by a 55 percent majority.

- Use Property Tax Increment to Offset General Fund Costs for One Year.** In 2011-12, the successor agencies would use the redevelopment revenues to:
 - Pay redevelopment debts and obligations, estimated by the administration to cost \$2.2 billion.
 - Offset \$1.7 billion of state Medi-Cal (\$840 million) and trial court (\$860 million) costs.
 - Allocate \$1.1 billion to schools and other local agencies pursuant to existing pass through agreements.
 - Distribute \$210 million to cities, counties, and special districts in proportion to these agencies current shares of the property tax.



Shift Property Tax Increment to Local Agencies After 2011-12.

Beginning in 2012-13, any property tax revenues remaining after the successor agencies pay redevelopment debt would be distributed to other local governments in the county following provisions in existing law, except that:

- The additional K-14 property taxes would augment their existing state funding (not offset state education spending under Proposition 98) and would be distributed to districts throughout the county based on enrollment.
- The property taxes that otherwise would be distributed to enterprise special districts would be allocated instead to counties. (These districts primarily are fee-financed water and waste disposal districts.)



Shift Existing Housing Balances to Local Housing

Authorities. Many redevelopment agencies maintain large housing fund balances meant to support low- and moderate-income housing. The Governor proposes to shift the existing balances to local housing authorities.



Assessment of Governor's Proposal



Strengths

- ***Shifts Responsibility for Local Economic Development to Local Governments.*** Shifting responsibility for local economic development to local governments makes sense. Local communities are in the best position to determine the types of programs and assistance needed to promote development in their communities. Ending state-assisted redevelopment also makes sense as the benefits of the program accrue primarily to local governments.
- ***Provides One-Time General Fund Relief.*** The proposal would offset \$1.7 billion of state General Fund costs in 2011-12.
- ***Shifts Property Tax Revenue to Core Government Responsibilities.*** Given the size of the state's budget problem, it is necessary to reconsider the size and scope of state services. By ending state-supported redevelopment, the Governor's proposal reprioritizes state spending.
- ***Promotes Transparency in Future Local Redevelopment Activities.*** Redevelopment agencies have limited accountability compared to other local government agencies. Unlike most other local government entities, redevelopment agencies can incur debt without voter approval. Redevelopment agencies can also redirect property tax revenues from schools and other uses without voter approval or the consent of affected public agencies. The Governor's proposal to shift the responsibility for redevelopment to locals and require voter approval for economic development funding would improve transparency and accountability to the public.



Assessment of Governor's Proposal

(Continued)



Limitations

- **Many Details Need to Be Resolved.** The Governor's proposal raises several legal, financial, and policy issues. Some of the major issues include:
 - Does the state have the authority to dissolve all redevelopment agencies immediately?
 - What entities will serve as the successor agencies? Will they have the capacity and proper fiscal incentive for managing redevelopment's remaining obligations?
 - What happens to redevelopment agencies' physical assets?
- **Redevelopment Debt Costs Unclear.** The Governor's proposal assumes redevelopment's obligations will be limited to \$2.2 billion in 2011-12. Although the administration's approach for estimating redevelopment debt is reasonable, the actual level of ongoing redevelopment obligations is difficult to ascertain. If the amount is higher than the administration's estimate, then there would not be sufficient revenue to fully fund the remainder of the Governor's spending plan (offsets to state spending or the pass through to locals).
- **Rationale for Increased School Funding Not Clear.** The rationale for providing school districts with property tax revenues *in addition* to their existing property taxes is not clear. Such supplemental funding would create distributional issues among school districts in the state, further complicate an already complicated school finance system, and eliminate an opportunity to achieve ongoing General Fund savings.



Assessment of Governor's Proposal

(Continued)

-
- ***Disproportionate Impact on Some Local Agencies.*** Redistributing redevelopment's share of the property tax according to existing law would provide shares to local agencies based largely on the proportion of property taxes they received in the mid-1970s. Such a system does not allocate revenue in a way that reflects modern needs and preferences of local communities.

 - ***Future Responsibility for Low- and Moderate-Income Housing Not Defined.*** Redevelopment is required to set aside 20 percent of its property tax revenue for low- and moderate-income housing. Although there are questions about the effectiveness of redevelopment agencies in providing housing, the Governor's proposal does not provide an ongoing funding source.



Next Steps

- Pause New Redevelopment Activities.** New financial obligations could constrain the state's ability to redirect redevelopment revenues and to realize the state savings and local benefits anticipated in the administration's proposal. Accordingly, we recommend that the Legislature pass urgency legislation as soon as possible prohibiting redevelopment agencies—during this period of legislative review—from taking actions that increase their debt.
- Resolve Key Legal Questions.** The Legislature needs to answer key questions regarding its authority to end redevelopment agencies and the ownership of redevelopment assets.
- Gain Better Understanding of Redevelopment Finances and Ongoing Obligations.** In order to have a more accurate estimate of the revenue that would be available after paying redevelopment debts and obligations, the Legislature and administration will need more information regarding the existing assets and ongoing obligations of redevelopment agencies. In addition to bond debt, the agencies may have short-term obligations, pending transactions and projects, or cash reserves.
- Consider Key Policy Questions.** The Governor's proposal raises significant policy questions that the Legislature should address. The most notable policy decisions pertain to the ongoing use of property tax revenues:

 - Should additional property tax revenue to schools offset the state's Proposition 98 costs?
 - Should additional property tax revenue be distributed based upon local agencies' existing shares of base property tax?

EXHIBIT C

NEW ISSUE-BOOK-ENTRY ONLY

Moody's: MIG 1
 S&P: SP-1+
 Fitch: FI
 (See "RATINGS" herein.)

In the opinion of Note Counsel to the State, interest on the Series A Notes will be excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes. See "TAX MATTERS."

\$5,400,000,000*
 STATE OF CALIFORNIA
 2011-12 REVENUE ANTICIPATION NOTES
 SERIES A-1 AND SERIES A-2

SERIES	PRINCIPAL AMOUNT	INTEREST RATE	YIELD	CUSIP**
A-1	\$	%	%	
A-2				

Dated: Date of Delivery

Due: Series A-1 _____, 2012

Series A-2 _____, 2012

The Series A-1 Notes and the Series A-2 Notes (collectively referred to as "Series A Notes") are being issued to assist in cash flow management for the State's 2011-12 fiscal year. See "CASH MANAGEMENT."

The Series A Notes may be purchased in book-entry form only in denominations of \$5,000 or any integral multiple thereof. See "APPENDIX B — DTC AND THE BOOK-ENTRY SYSTEM."

Principal of and interest on all Series A Notes will be paid at maturity. The Series A Notes are not subject to redemption prior to maturity. See "THE SERIES A NOTES — Terms" and "—Redemption."

The Series A Notes are unsecured obligations payable from the General Fund during the fiscal year. Payment of the Series A Notes is subject to the prior use of moneys in the General Fund to make Priority Payments (as defined herein) when due as further described herein. See "SOURCE AND PRIORITY OF PAYMENT" and "CASH MANAGEMENT." The State's cash flow projections indicate that there will be sufficient revenues and internal borrowable resources available to pay the Series A Notes at maturity. See "GENERAL FUND CASH FLOW AND INTERNAL BORROWABLE RESOURCES FOR THE 2010-11 AND 2011-12 FISCAL YEARS" and "APPENDIX A — THE STATE OF CALIFORNIA — STATE FINANCES — The General Fund."

This cover page contains certain information for general reference only. It is not intended to be a summary of the security or terms of this issue. Investors are advised to read the entire Official Statement to obtain information essential to making an informed investment decision.

The Series A Notes are offered when, as and if issued and received by the Underwriters, subject to the approval of validity by the Honorable Kamala D. Harris, Attorney General of the State of California, and by Orrick, Herrington & Sutcliffe LLP, Note Counsel and Disclosure Counsel to the State. Orrick, Herrington & Sutcliffe LLP and Stradling Yocca Carlson & Rauth, a Professional Corporation, are serving as Co-Disclosure Counsel to the State regarding Appendix A. Certain legal matters will be passed upon for the Underwriters by their counsel, Squire, Sanders & Dempsey (US) LLP. Montague DeRose and Associates, LLC is serving as the Financial Advisor to the State in connection with the Series A Notes. The Series A Notes are expected to be available for delivery through the facilities of DTC on or about September 22, 2011.

HONORABLE BILL LOCKYER
Treasurer of The State of California

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Dated: September __, 2011

* Preliminary, subject to change.

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INTRODUCTION TO THE STATE OF CALIFORNIA AND APPENDIX A

APPENDIX A is the part of the Official Statement that provides investors with information concerning the State of California. This Introduction is intended to give readers a very brief overview of the main topics covered in APPENDIX A. Investors are advised to read the entire Official Statement, including APPENDIX A, to obtain information essential to making an informed investment decision. See "Certain Defined Terms" at the end of this section for certain defined terms used in this APPENDIX A.

Financial Stress

During the recent recession, which officially ended in 2009, the state experienced the most significant economic downturn since the Great Depression of the 1930s. As a result of continuing weakness in the state economy, state tax revenues declined precipitously, resulting in large budget gaps and occasional cash shortfalls. Most recently, the state's economy has grown slowly, and the 2011 Budget Act projects continuing growth in the state's major revenue sources from the recession's low point. Further information is set forth under "STATE FINANCIAL PRESSURE" and "CURRENT STATE BUDGET." See also EXHIBIT 2 for the most recent State Controller's Unaudited Statement of General Fund Cash Receipts and Disbursements.

There can be no assurances that the state will not continue to face fiscal stress and cash pressures and that such circumstances will not become more difficult, or that other impacts of the current economic situation will not further materially adversely affect the financial condition of the state.

State Revenues, Expenditures and Cash Management

The state receives revenues from taxes, fees and other sources, the most significant of which are the personal income tax, sales and use tax and corporation tax (which collectively constitute nearly 90 percent of total General Fund revenues and transfers). The state expends money on a variety of programs and services. Significant elements of state expenditures include education (both kindergarten through twelfth grade ("K-12") and higher education), health and human services, and correctional programs. For a discussion of the sources and uses of state funds, see "STATE FINANCES."

The 2011 Budget Act (for fiscal year 2011-12), which was signed by the Governor on June 30, 2011, closes a \$26.6 billion projected budget gap and makes substantial progress in addressing the state's long term structural budget deficit. It also shifts certain program responsibilities to local government (and provides certain funding for such program responsibilities to local governments).

The 2011 Budget Act makes substantial cuts to state programs in order to bring expenditures more in line with available resources, including slightly over \$15 billion in expenditure reductions over a two-year period. Expenditure reductions include significant cuts to Medi-Cal, Mental Health Services, and CalWORKs, among others in the Health and Human Services area, and reductions in K-12 education spending and support for the University of California and California State University systems. The 2011 Budget Act also provides for additional expenditure reductions without further action of the Legislature (called "trigger cuts") in the event that the revenue projections in the 2011 Budget Act are not realized. See "CURRENT STATE BUDGET."

The state manages its cash flow requirements during the fiscal year primarily with a combination of external borrowing and internal borrowing by the General Fund from over 700 special funds. The General Fund has typically ended each fiscal year with a net borrowing from these special funds. As of

In addition to the major solutions described above, the 2011 Budget Act contains the following major General Fund components:

- Proposition 98 – The Proposition 98 Guarantee for fiscal year 2011-12 is \$48.7 billion, of which \$32.9 billion is funded from General Fund. The Proposition 98 Guarantee was not suspended for fiscal year 2011-12. Transferring 1.0625 percent of the state sales tax to local governments as part of the realignment legislation described below reduced the Proposition 98 Guarantee by \$2.1 billion in fiscal year 2011-12. Other budget legislation would protect K-14 schools from this reduction by seeking a future ballot measure to provide additional funding. See “STATE FINANCES – Proposition 98 and K-14 Funding” below.
- K-12 Education – A total of \$35.8 billion for K-12 education programs for fiscal year 2011-12, of which \$34.3 billion is funded from the General Fund. The remaining funds include special and bond funds.
- Higher Education – Total funding of \$11.1 billion, including \$10.2 billion from the General Fund and Proposition 98 sources, for all major segments of Higher Education. The remaining funds include special and bond funds.
- Health and Human Services – Total funding of \$37.1 billion, including \$23 billion from the General Fund, for Health and Human Services programs. The remaining funds include special and bond funds.
- Prison Funding – Total funding of \$9.8 billion from the General Fund for the California Department of Corrections and Rehabilitation.
- Redevelopment Agencies – Legislation enacted as part of the 2011 Budget Act eliminates redevelopment agencies but optionally allows them to continue in existence if their sponsoring entity pays a fee to local schools and certain special districts. For those redevelopment agencies that are dissolved, the statute directs the property tax increment they would have received, after payment of redevelopment debt obligations, to be paid to local agencies and school districts according to their base property tax allocations. The 2011 Budget Act reflects an allocation of \$1.7 billion of these funds to offset K-14 Proposition 98 General Fund expenditures in fiscal year 2011-12. It is uncertain at this time which local agencies will choose to participate in the alternative redevelopment program under ABX1 27 and which redevelopment agencies will dissolve under the provisions of ABX1 26. It is also uncertain what actions the Supreme Court will take with respect to those two statutes in the pending case *CRA v Matosantos*. (See “LITIGATION.”) If most agencies dissolve under ABX1 26, the maximum amount of property tax that would flow to schools and offset General Fund costs in fiscal year 2011-12 would be approximately \$1.1 billion, but this funding level would continue and eventually grow in future years and continue to offset state General Fund Proposition 98 costs. If most agencies participate in the ABX1 27 program, the one-time offset of state General Fund costs is estimated to be \$1.7 billion in fiscal year 2011-12. Schools would benefit by about \$340 million in following years and this funding could potentially grow. If both statutes are upheld by the court, some mixture of these fiscal effects is likely but this will not be known until after the court decision and initial payments are received in January 2012 or whatever later date the court may provide.

DECLARATION OF SERVICE BY U.S. MAIL

Case Name: **California Redevelopment Association, et al. v. Matosantos, et al.**

No.: **S194861**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter. I am familiar with the business practice at the Office of the Attorney General for collection and processing of correspondence for mailing with the United States Postal Service. In accordance with that practice, correspondence placed in the internal mail collection system at the Office of the Attorney General is deposited with the United States Postal Service that same day in the ordinary course of business.

On September 9, 2011, I served the attached **REQUEST FOR JUDICIAL NOTICE AND MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF REQUEST** by placing a true copy thereof enclosed in a sealed envelope with postage thereon fully prepaid, in the internal mail collection system at the Office of the Attorney General at 455 Golden Gate Avenue, Suite 11000, San Francisco, CA 94102-7004, addressed as follows:

Steven L. Mayer Howard, Rice, Nemerovski, Canady, Falk & Rabkin Three Embarcadero Center, 7th Floor San Francisco, CA 94111-4024 (Attorneys for Petitioners)	Jennifer Rockwell Chief Counsel Department of Finance 915 "L" Street Sacramento, CA 95814
Claude Kolm Deputy County Counsel Alameda County Counsel's Office 1221 Oak Street, Room 450 Oakland, CA 94612-4296	Brian E. Washington Alameda County Counsel's Office 1221 Oak Street, Room 450 Oakland, CA 94612-4296
Richard J. Chivaro Chief Counsel State Controller's Office P.O. Box 942850 Sacramento, CA 94250	Lizanne Reynolds Deputy County Counsel Santa Clara County Counsel's Office 70 West Hedding Street, 9th Floor East Wing San Jose, CA 95125

I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on September 9, 2011, at San Francisco, California.

Janet Wong

Declarant

J Wong

Signature

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