

SPECIAL REORGANIZATION OF HOLLYWOOD
EXECUTIVE OFFICER'S REPORT

TO THE
LOCAL AGENCY FORMATION COMMISSION
FOR LOS ANGELES COUNTY

May 28, 2002

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INTRODUCTION

Purpose

Pursuant to the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (the “Hertzberg Act”)¹ the executive officer of a local agency formation commission is required to review each application for a change of organization or reorganization filed with the commission and prepare a report to the commission, including his recommendations on the application.² The objective of this Executive Officer’s Report is to provide the Local Agency Formation Commission for Los Angeles County (the “Commission”) with its Executive Officer’s recommendations regarding the application and proposal for special reorganization of the Hollywood area of the City of Los Angeles (“Hollywood Special Reorganization”).³

Context

The Executive Officer’s Report is based on studies conducted and proposals received in this process. This input includes, but is not limited to, the Comprehensive Fiscal Analysis (“CFA”) and supplemental report prepared by the Commission’s consultant, the State Controller’s review of the CFA, comments at public hearings, the written proposals of the City of Los Angeles and the Hollywood Special Reorganization applicant (the “Applicant”)⁴, and the recommendations of the Commission’s Subcommittee on Findings, Terms and Conditions (the “Subcommittee”), which held a hearing and adopted recommendations on findings, terms and conditions for consideration by the Commission. All of the above submissions, reports and proposals, and all other written submissions which have been provided by the parties and interested third parties, and all recordings, transcripts and minutes of all meetings and hearings are incorporated in this Report by reference for consideration by the Commission.

Caveats

This Report includes analysis and recommendations on fiscal findings and terms and conditions for the Commission to consider as it makes its determinations with respect to the Hollywood Special Reorganization. The decision whether or not to approve or disapprove the proposal, with or without amendment, wholly, partially or conditionally, rests entirely with the Commission. This Report is not a substitute for those discretionary decisions yet to be made by the Commission.

¹ California Government Code section 56000, *et seq.* The Cortese-Knox Local Government Reorganization Act of 1985 (the “Cortese-Knox Act”) was amended by the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (the “Hertzberg Act”), which became effective January 1, 2001. The Hollywood proposal is being processed under the Hertzberg Act because the Hollywood application was accepted for filing by the Executive Officer after January 1, 2001.

² Government Code section 56665.

³ Pursuant to Government Code section 56075.5, a “special reorganization” means a reorganization that includes the detachment of territory from a city or city and county and the incorporation of that entire detached territory as a city. The Hollywood Special Reorganization, therefore, consists of a detachment of the Hollywood territory from the City of Los Angeles and incorporation of that area as an independent city.

⁴ The proposed terms and conditions of the City of Los Angeles set forth in this Report were proposed for the Valley and Harbor Special Reorganizations, unless otherwise indicated, and are assumed to be equally applicable to the Hollywood Special Reorganization (City of Los Angeles, *Terms and Conditions for a LAFCO Resolution Making Determinations Proposed by the City of Los Angeles (First Set)*, December 21, 2001). The Applicant’s proposals are derived from the Applicant’s preliminary comprehensive fiscal analysis (Hollywood Vote, *Hollywood Proposal for Special Reorganization, Preliminary Comprehensive Fiscal Analysis*, October 1, 2001).

This Report and the recommendations herein are subject to revision and reconsideration as additional and updated data and information becomes available or as may otherwise be directed by the Commission during the course of its deliberations.

BACKGROUND

PROCEDURAL REQUIREMENTS

The special reorganization process for the proposed Hollywood Special Reorganization is set forth in the Hertzberg Act.⁵ While certain provisions of the Hertzberg Act are specific to special reorganization, most of the provisions that relate to incorporations are also applicable because a special reorganization includes an incorporation.⁶

Significant Voter Interest

In order to initiate proceedings for a special reorganization, an applicant is required to obtain the signatures of 25 percent of the registered voters in the territory seeking special reorganization.⁷ The Applicant filed its petitions in August 2000. In November 2000, the Executive Officer certified the petitions to be sufficient after the Los Angeles County Registrar/Recorder verified the requisite number of valid signatures of registered voters residing in Hollywood.⁸

Fiscal Viability

The Commission cannot approve a proposal for special reorganization unless it finds that the proposed city is financially viable, i.e. expected to receive revenues sufficient to provide public services and facilities and a reasonable reserve during the three fiscal years following incorporation.⁹ The Executive Officer is charged with causing the preparation of a comprehensive fiscal analysis, which reviews and documents each of the following:

- (a) The costs to the proposed city of providing public services and facilities during the three fiscal years following incorporation;
- (b) The revenues of the proposed city during the three fiscal years following incorporation;
- (c) The effects on the costs and revenues of any affected local agency during the three fiscal years of incorporation; and
- (d) Any other information and analysis needed to make the findings required by Section 56720.¹⁰

The Executive Officer submitted the Hollywood Comprehensive Fiscal Analysis (“CFA”) to the Commission on March 6, 2002.¹¹ The CFA concluded that the proposed city’s revenues would exceed its expenditures, and that the proposed city would have a modest reserve in its early years.¹² The City of Los Angeles requested that the State Controller review the CFA. The Controller’s report was released on May 9, 2002.¹²

⁵ Government Code section 56000, *et seq.*

⁶ Government Code section 56075.5.

⁷ Government Code sections 56764 and 56864.1.

⁸ Government Code section 56706.

⁹ Government Code section 56720.

¹⁰ Government Code section 56800.

¹¹ Public Financial Management, Inc., Hollywood Proposal for Special Reorganization Comprehensive Fiscal Analysis, March 6, 2002.

¹² See also Public Financial Management, Inc., *Fiscal Impact of Hollywood Boundary Alternatives*, May 27, 2002.

¹² California State Controller, California State Controller’s Review of the Proposed Hollywood Special Reorganization Comprehensive Fiscal Analysis, May 2002.

Mitigation of Negative Fiscal Effects (“Revenue Neutrality”)

Government Code section 56815 prohibits the Commission from approving a proposal that includes an incorporation unless it finds that the following are substantially equal:

- (a) revenues currently received by the agency transferring the affected territory which would accrue to the local agency receiving the affected territory; and
- (b) expenditures, including direct and indirect expenditures, currently made by the local agency transferring the affected territory for those services that will be assumed by the local agency receiving the affected territory.

If these amounts are not substantially equal, the Commission may only approve a proposal if it finds that: (1) the county and all other subject agencies agree, or (2) the negative fiscal effect of the special reorganization is adequately mitigated by tax sharing agreements, or other terms and conditions imposed by the Commission.¹³

The CFA contains an analysis of the “revenue neutrality” test set forth above, and concludes that the Hollywood Special Reorganization would not meet the revenue neutrality test because Hollywood currently generates more in revenue than the City of Los Angeles currently expends in providing the services that would transfer to the proposed Hollywood city. As such the Commission can only approve the proposed Hollywood Special Reorganization with the agreement of the County and the City of Los Angeles, or if it finds that the negative fiscal effect of the proposal has been adequately mitigated.

Mitigation of Negative Environmental Effects

The California Environmental Quality Act of 1970 (“CEQA”)¹⁴ requires that significant environmental impacts be taken into consideration by the Commission prior to the Commission’s discretionary approval of a proposal for a change in local government organization or reorganization. The Commission has retained a consultant to prepare an environmental impact report (“EIR”) for the proposed Hollywood Special Reorganization. The draft EIR has been released and distributed for review. The final EIR should be released at the end of May 2002, and must be taken into consideration by the Commission before making its determinations regarding the Hollywood Special Reorganization.

Terms and Conditions

The Commission must adopt a resolution making determinations—a document indicating whether or not the Commission approves or disapproves the proposal and listing any terms and conditions for approval.¹⁵

In making its decision, the Commission is charged with taking into consideration such factors as:

- the likelihood of significant growth in the area, and in adjacent incorporated and unincorporated areas, during the next 10 years,
- the present cost and adequacy of governmental services and controls in the area,
- the probable effect of the proposed incorporation ... and of alternative courses of action on the cost and adequacy of services and controls in the area and adjacent areas, and

¹³ Government Code section 56815.

¹⁴ California Public Resources Code section 22000, *et seq.*

¹⁵ Government Code section 56880.

- the effect of the proposed action and of alternative actions, on adjacent areas, on mutual social and economic interests, and on the local governmental structure of the county.
- the ability of the newly formed or receiving entity to provide the services to the area and the sufficiency of revenues for those services.¹⁶

The Legislature has given the Commission broad discretion regarding the terms and conditions that may be included in the resolution. The discretionary terms and conditions may include provisions regarding continuation of service delivery, the establishment of an effective date for the special reorganization, allocation of City assets and outstanding debts, and public employee rights and benefits, among other issues.

A resolution making determinations typically includes the following components:

- reasons for the reorganization,
- boundaries of the territory involved,
- a distinctive short-term designation to the affected territory and a description of the territory,
- property tax revenue to be exchanged by the affected local agencies,
- provisional appropriations limit of the proposed city, and
- directions for the conducting authority to initiate protest proceedings.

After the Commission adopts its resolution, there is a 30-day period during which parties may request reconsideration of the Commission's decision or propose amendments to the resolution.¹⁷ If any such requests are received, the Commission must consider the request and may choose to wholly, partially or conditionally approve or disapprove the request, which may require amendment of the resolution.

Conducting Authority Proceedings

Under the Cortese-Knox Act, the conducting authority designated by the Commission conducted protest proceedings, and if required, called for an election on the question of special reorganization. Under the Hertzberg Act, conducting authority proceedings are now conducted by the Commission. The Commission will hold a protest hearing at which time it will accept written protests against the proposed special reorganization. Special reorganization proceedings must be terminated if the Commission receives written protests from a majority of the registered voters residing in the area.¹⁸ In the absence of a majority protest, the Commission is required to call an election on the question of special reorganization.¹⁹ The Commission must adopt a resolution calling for the election by August 9, 2002 in order for the proposal to be considered in the November 2002 general election.²⁰

Voter Approval

The Commission is required to call the election for special reorganization in the territory ordered to be detached from the city and the entire territory of the city from which the detachment is ordered

¹⁶ Government Code section 56668.

¹⁷ Government Code section 56895.

¹⁸ Government Code sections 57077 and 57078.

¹⁹ Government Code section 57077.

²⁰ Government Code section 57132.5.

to occur.²¹ A majority of the votes cast in both the City of Los Angeles and the proposed Hollywood Special Reorganization area must approve the proposal for special reorganization.

In addition to voting on the question of special reorganization, voters residing in Hollywood will also be asked to select five city council members. The city council candidates will be selected at large within the proposed Hollywood Special Reorganization area.

The election is expected to take place on November 5, 2002.

SPECIAL REORGANIZATION HISTORY

Only two cities have been created from existing cities in California's history. In 1890, the City of Coronado was formed from a part of San Diego, and in 1920, the City of Montebello was created from a part of Monterey Park. Both cases predate the Legislature's establishment of local agency formation commissions, and the current legal requirements for special reorganization.

Coronado seceded from the City of San Diego a few years after the first beach resort was built on the peninsula, and after a battle over boundaries was waged in both the Legislature and the courts. The San Diego City Council opposed the detachment, but was compelled by the California Supreme Court to let the voters decide. A few months later, Coronado's detachment and incorporation were approved at a special election by a majority of the voters, both in Coronado and citywide.

The detachment of Montebello from Monterey Park was amicable. Monterey Park had incorporated only four years prior to the break-up "as a defensive measure to prevent neighboring Alhambra, Pasadena, and South Pasadena from converting the area into a sewer farm."²² Shortly after stopping the sewer farm project, the Monterey Park City Council approved a detachment proposal from residents of the territory that was to become Montebello.²³

From 1977 until 1997, a city council could require the termination of any proceeding involving the detachment of territory from its jurisdiction. Legislation adopted in 1997 (AB 62) exempted special reorganizations from this provision, and the Legislature instituted the requirement of voter approval in both the area of special reorganization and the city as a whole.²⁴ AB 62 also provided for the preservation of existing collective bargaining agreements, existing retiree benefits, and recognition of exclusive employee representatives.

Hollywood

The Hollywood area is generally located east of the City of West Hollywood and south of the San Fernando Valley. Hollywood incorporated as a city in 1903, but voted to consolidate with the City of Los Angeles in 1910 just as the City was building its aqueduct.

Several property owners and homeowners associations have requested that Commission exclude certain areas from the Hollywood Special Reorganization. These include the Farmer's Market, the Beverly Center mall, the Melrose Neighborhood Association, the Hancock Park Neighborhood Association, the Larchmont Village Homeowners Association, the Mid-Wilshire Neighborhood Council, the Wilshire Homeowners Alliance, the Beverly/Wilshire Homeowners Association, the

²¹ Government Code section 57119.

²² Leonard Pitt and Dale Pitt, *Los Angeles A to Z: An Encyclopedia of the City and County*, University of California Press, 1997.

²³ Commission on Local Governance for the 21st Century. *Financing The Fiscal Study For San Fernando Valley Secession*. Sacramento: Commission on Local Governance for the 21st Century, June 11, 1999.

²⁴ Government Code sections 57079 and 57103.1.

East Hollywood Community Association, Universal Studios, and Mount Sinai and Forest Lawn Memorial Parks.

On January 23, 2002, the Commission adopted a motion for staff to analyze two additional Hollywood boundary scenarios. The recommended scenario would exclude the area south of Melrose Avenue where the following are located: the Farmer’s Market, the Beverly Center mall, the southern half of the Melrose Neighborhood Association area, the Hancock Park Neighborhood Association area, the Larchmont Village Homeowners Association area, part of the Mid-Wilshire Neighborhood Council area and the Beverly/Wilshire Homeowners Association area. The “all exclusions” scenario would exclude all territory for which the Commission has received exclusion requests, which is generally south of Willoughby Avenue and east of Western Avenue.

Subsequent to that action, the Valley and Hollywood proponents have jointly proposed to divide the Cahuenga Pass neighborhood in the northwestern portion of the Hollywood territory. This area had also been included in the San Fernando Valley special reorganization proposal.

Removing the western Cahuenga Pass area from the proposed Hollywood Special Reorganization area had only a marginal effect on the fiscal mitigation payment estimate for Hollywood.

Special Reorganization Areas, Population 2000	
Community	Population
Remaining City of Los Angeles	2,015,415
San Fernando Valley area	1,349,875
Hollywood Proposed	209,093
Hollywood Recommended	184,347
Harbor area	145,183

Source: County of Los Angeles, Urban Research Division

The Commission has also received a request from Universal Studios to exclude two parcels from the Hollywood Special Reorganization area and include those parcels in the Valley Special Reorganization area.²⁵ Universal Studios has requested this modest boundary change in order to have all of its non-county properties under the jurisdiction of one municipality. Universal Studios is currently within County unincorporated territory and City of Los Angeles territory. As the special reorganization boundaries were originally drawn, portions of Universal Studios were in both the Valley and Hollywood, as well as unincorporated County territory. The subject parcels are uninhabited. Modification of the boundary had a negligible effect on the fiscal mitigation payment estimate.

A request for exclusion has also been submitted by Mount Sinai and Forest Lawn Memorial Parks, the cemeteries located near the northern most boundary of the original special reorganization proposal. The City of Los Angeles has requested exclusion of all portions of Griffith Park from the proposed boundary of Hollywood.

The Executive Officer’s recommended boundaries exclude the western portion of the Cahuenga Pass area from the Hollywood territory, the two Universal Studios parcels, the two cemeteries, and the Fern Dell Drive portion of Griffith Park.

The Hollywood Special Reorganization area as originally proposed is relatively large, and would be the fourth largest city in Los Angeles County if special reorganization is approved by the voters. The originally proposed Hollywood Special Reorganization area constitutes 5.7 percent of the City of Los Angeles population. Under the boundaries recommended by the Executive Officer, the

²⁵ Latham & Watkins, Universal Studios, Inc.’s Request to Modify New City Boundary Lines, February 6, 2002.

Hollywood area constitutes 5 percent of the City of Los Angeles population. If the recommended Hollywood area is approved, Hollywood would be the fifth largest city in the county, ranking just after the City of Glendale.²⁶

The reasons cited for Hollywood special reorganization are unresponsiveness and inadequacy of current services provided by the City of Los Angeles. The Applicant believes that Hollywood Special Reorganization would provide:

- Greater local control over local neighborhoods and decisions affecting their quality of life,
- Improved basic services,
- Lower taxes and fees,
- Safe, clean and green neighborhoods and business districts,
- Short, medium, and long term planning based on the public's priorities,
- A business environment that encourages new businesses, seeks to retain existing businesses, and seeks to create new high-quality jobs,
- Equal opportunity and fair local representation for all residents,
- Equity in the distribution of services and representation, and,
- Government that is accessible, accountable, and responsive.²⁷

²⁶ Population based on County of Los Angeles, Urban Research Division estimates from 2000 Census data.

²⁷ Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

FISCAL FINDINGS

Pursuant to Government Code section 56720, the Commission cannot approve a proposal for special reorganization unless it finds that the proposed city is financially viable, i.e. expected to receive revenues sufficient to provide public services and facilities and a reasonable reserve during the three fiscal years following incorporation.

COMPREHENSIVE FISCAL ANALYSIS

The Commission's consultant Public Financial Management, Inc. has prepared a comprehensive fiscal analysis ("CFA") of the proposed reorganization.²⁸ The CFA must review and document each of the following:

- a) The costs to the proposed city of providing public services and facilities during the three fiscal years following incorporation.
- b) The revenues of the proposed city during the three fiscal years following incorporation.
- c) The effects on the costs and revenues of any affected local agency during the three fiscal years following incorporation.
- d) Any other information and analysis needed to make the findings required by Section 56720 (i.e., fiscal viability).²⁹

The CFA found that Hollywood's revenues would exceed its expenditures by \$11 million, but that the new city would need to reduce its annual service costs by \$10 million by the third year after incorporation to generate reasonable reserves.³⁰

The City of Los Angeles requested that the State Controller review the comprehensive fiscal analysis with a focus on the City's concerns. For the most part, the State Controller's review of the comprehensive fiscal analysis validated that the fiscal analysis was both reasonable and accurate.³¹ However, the Controller did raise concerns about the adequacy of the new city's reserves. The Controller's concerns regarding reserves and transition costs are addressed in the fiscal viability section of this Report.

EXECUTIVE OFFICER'S FISCAL RESULTS

This Report sets forth adjusted and updated fiscal calculations of current revenues and expenditures and fiscal projections for the new city's first three years of incorporation. The Executive Officer's fiscal estimates are detailed in the Appendix of this Report. These fiscal estimates differ from those presented in the CFA in the following ways:

²⁸ Public Financial Management, Inc., Hollywood Proposal for Special Reorganization Comprehensive Fiscal Analysis, March 6, 2002.

²⁹ Government Code section 56800.

³⁰ At the time the CFA was prepared, the Executive Officer recommended boundary scenario SC3, which excludes the area south of Melrose Avenue. The recommended boundaries have subsequently been revised (SC4) to exclude western Cahuenga Pass, two Universal Studios parcels, two memorial parks, and the "panhandle" area west of Fairfax and north of Melrose Avenue.

³¹ California State Controller, California State Controller's Review of the Proposed Hollywood Special Reorganization Comprehensive Fiscal Analysis, May 2002.

- 1) **Financial Basis:** The fiscal calculations are based upon the actual City of Los Angeles revenues and expenditures in the base year (fiscal year 2000-01) which were recently released in the Mayor's proposed fiscal year 2002-03 budget. Previously, the CFA had calculated the fiscal findings based upon the adopted budget for the base year rather than the actual figures, which were unavailable.
- 2) **Geography:** The Executive Officer's estimates are based on the geographic boundary scenario recommended in this report (SC4) which excludes the area south of Melrose Avenue, western Cahuenga Pass, two Universal Studios parcels, two memorial parks, and the "panhandle" area north of Melrose Avenue and west of Fairfax Boulevard. The recommended geography (SC4) removed areas that housed three percent of the population assessed by the CFA under the boundary scenario (SC3) recommended at the time the CFA was prepared.
- 3) **Terms and Conditions:** The Executive Officer's fiscal estimates reflect the terms and conditions included in the draft Resolution, including debt allocations based on revenue contribution, fund balance transfers to the new city, and allocation of a pro rata share of the County's Public Safety Augmentation Fund as well as the City's tobacco settlement revenues.
- 4) **Transition costs:** The Executive Officer's fiscal estimates reflect the most recent information on transition and contract administration costs supplied by the City of Los Angeles to the State Controller in its request for review of the Hollywood CFA.
- 5) **Data Updates:** The Executive Officer's fiscal estimates reflect data updates in the number of registered voters, and in allocation factors for property tax and documentary transfer tax.
- 6) **Special Purpose Funds:** Special purpose fund appropriations have been reassessed to ensure that revenues and appropriations in each fund are allocated in a consistent manner. These final calculations use the same allocation factors for revenue received in a particular special fund, as are used for the appropriations made from that fund.

REVENUE NEUTRALITY FINDING

The Executive Officer finds that the current revenues generated in Hollywood that would accrue to the new city are \$183 million based on actual base year revenues, and \$174 million based on budgeted base year revenues. For purposes of the revenue neutrality test, revenues reflect the documentary transfer tax that would accrue to the new city.

By comparison, the Executive Officer finds that the current expenditures for services that would be assumed by the new city are \$166 million based on actual base year expenditures, and \$161 million based on budgeted base year expenditures. For the purposes of the revenue neutrality test, the budget surplus has been allocated based on general fund proportionate share to the new city as an expenditure item.

The Executive Officer concludes that the proposed special reorganization is not revenue neutral, as current revenues exceed current expenditures by \$18 million based on actuals and by \$13 million based on budgeted fiscal information. By comparison, the CFA found that for purposes of the revenue neutrality test, revenues exceed expenditures by \$7 million.

FISCAL IMPACT ON THE CITY OF LOS ANGELES

In assessing the fiscal impact on the remaining City of Los Angeles, Government Code section 56815 requires the comparison of current revenues that would accrue to the new city and current expenditures for services that the new city would assume. The Executive Officer finds that current revenues that would accrue to the new city exceed current expenditures that would be assumed by the new city by approximately \$17.7 million. The Executive Officer has recommended that the fiscal mitigation payment include an additional \$3.6 million to compensate the City of Los Angeles for its loss of documentary transfer tax revenues generated in Hollywood.

The Code grants the Commission the discretion to determine the fiscal mitigation payment amount that would adequately mitigate the negative fiscal effect on the City of Los Angeles. Although the Commission has the discretion to determine a mitigation payment that adequately mitigates the negative fiscal impact on the City of Los Angeles, the Commission is neither required nor directed by the Government Code to include “stranded costs” in the mitigation payment.

The Government Code Section 56815(a) defines the expenditure component of the revenue neutrality calculation as “expenditures currently made by the local agency transferring the affected territory for those services which will be assumed by the local agency receiving the affected territory”. By comparison, the City of Los Angeles has argued that the expenditure component of the fiscal mitigation payment should be based on the savings that the City of Los Angeles would realize if a) Hollywood were no longer part of the City, and b) Hollywood was not relying on the City of Los Angeles for contract service.

CFA Approach

The Comprehensive Fiscal Analysis apportioned field staff like front-line fire fighters, street cleaners, refuse collectors, police patrol officers, and librarians to the respective area based on the geographic area served by that particular worker. The CFA consultant reviewed budget documents, organizational charts and other city records. In addition, the CFA consultant interviewed City department managers about workload indicators, service levels, and the impact of special reorganization on their operations. The City department managers had difficulty identifying cost savings if the special reorganizations were to occur. Despite repeated requests by the CFA consultant, City representatives did not provide workload indicators useful in determining its employees’ workload attributable to servicing Hollywood. The CFA proceeded by allocating administrative staff based on the proportion of field staff serving Hollywood.

For purposes of illustration, the CFA approach is demonstrated through its allocation of the Police Department. Based upon organizational charts of the Police Department, the CFA identified 396 staff assigned to Hollywood police stations of a total 7,486 citywide staff assigned to police stations.³² Thus, the CFA found that 5.3 percent of field staff was serving Hollywood. The CFA then allocated 5.3 percent of the Police Department’s personnel, emergency dispatch, specialized policing units, crime lab and other centralized personnel costs to Hollywood.

City of Los Angeles Approach

In the case of the San Fernando Valley, the City of Los Angeles argued that the CFA had overstated the cost savings that would be realized by the post-special reorganization City of Los Angeles by over \$200 million, or about one-fifth of the expenditures that would transfer to the new city. The

³² The CFA methodology allocated budgeted and authorized positions as reflected in City of Los Angeles organizational charts. Similarly, the City of Los Angeles consultant’s stranded cost report focused on budgeted positions.

City of Los Angeles has not provided comparable estimates for the impact of the Hollywood special reorganization.

The City views its centralized operations as requiring a minimum level of staffing with associated costs that could not be divided or reduced if the City were to be reduced to two-thirds of its current size.³³ In particular, the City views its accounting, payroll, human resources, purchasing, contracting, and computer system maintenance functions to be staffed at minimum levels and difficult to divide or reduce if the scope of the City's field operations were reduced by special reorganization. The City argues that the workloads for such functions do not disappear if the Valley and Hollywood depart because the workload is dependent "upon the performance of a specific function" rather than population, geography or the size of the City.³⁴ The City recommended that the best method of assessing the negative fiscal impact on the City is to look at current service levels. If the workload is not affected by the departure of the Valley and Hollywood, the City reasons that budget cuts in those areas would result in a decrease in service to the remaining City of Los Angeles.³⁵ The City concludes that "if service levels are decreased from their existing levels (and all other conditions are assumed to be fixed), then one can reasonably assume a negative fiscal impact from the departure of the Valley." (ibid. page 2, emphasis added.)

The logical thread of the City's argument assumes that:

- 1) The City's administrative units are currently staffed at minimum levels;
- 2) The workload of the City's administrative functions is unaffected by the size of the City, i.e. the number of criminals, fires, potholes, library card holders, garbage bins, taxpayers or City employees providing direct service to the public;
- 3) A special reorganization-related reduction in the City's budget for administrative functions would reduce service levels in the remaining City of Los Angeles; and
- 4) The post-special reorganization City of Los Angeles would be organizationally identical to the existing City of Los Angeles. In other words, the post-special reorganization City of Los Angeles would not reorganize its units, branches, bureaus and departments, would not streamline its job classifications, would not rewrite job descriptions, and would not rely more heavily on outside specialists.

The City's second assumption—that the workload of administrative functions is dependent on the performance of a specific function—is tautological. The notion that the City's administrative workload is unrelated to the size of the City is inconsistent with the budgets of other cities, which indicate that administrative costs tend to be proportional to city size. The City's fiscal consultant has acknowledged that if the City were 30 percent smaller, its leaders would allocate the same percent of resources to central senior management as is currently devoted to such overhead costs.³⁶ In other words, the City's fiscal consultant believes that such administrative costs would shrink in proportion to the reduction in the size of the City's budget.

The City's third assumption would require the City to draw a connection between the activities of centralized staff and service levels provided to the taxpayers. If the City were to draw a connection

³³ Fujioka, William T. *City Response to LAFCO Regarding Valley Secession Proposal and Initial Fiscal Analysis*. City of Los Angeles Office of Administrative and Research Services, June 13, 2001, page 4.

³⁴ Ibid. page 5

³⁵ Ibid. page 3

³⁶ Hamilton, Rabinovitz & Alschuler, Inc. *The Division of Service Cost Burdens Following Separation of the San Fernando Valley from the City of Los Angeles: An Independent Appraisal*. Los Angeles, May 13, 2002, page 15.

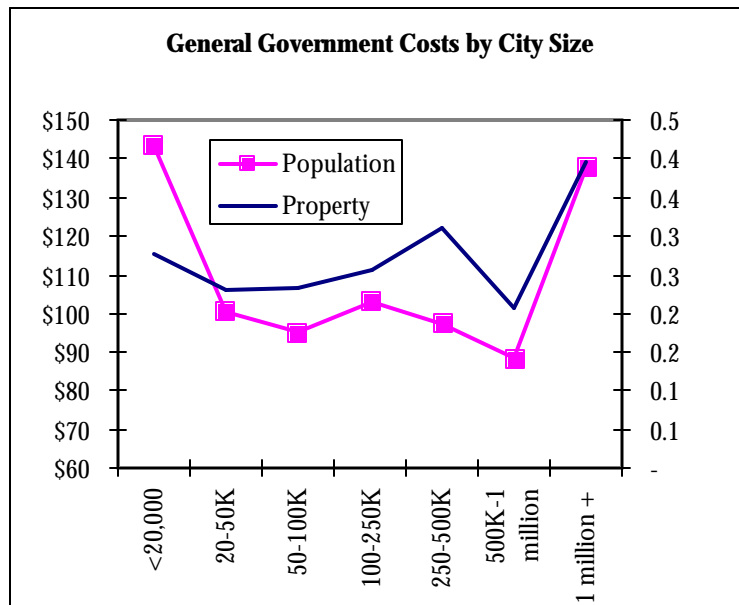
between the activities of administrative staff and service levels, the City would then invalidate the second assumption. If payroll clerks are busy cutting paychecks for refuse collectors, if human resources specialists are busy recruiting to fill vacant police officer positions, if purchasing clerks are busy buying park sprinklers or if computer maintenance staff are busy keeping the local library computers running, then these administrative staff are providing municipal services to the public. If administrative workers are providing directly or indirectly services to the public, then their workload is clearly driven by the volume of the public's needs, which is in turn driven by the size of the city.

The fourth assumption is not credible. Even the City's fiscal consultant envisions the post-special reorganization City of Los Angeles undergoing a reorganization involving unprecedented employee turnover, re-training of employees and managers as well as changes in employee and managerial assignments.³⁷ The elected officials of the City of Los Angeles would undoubtedly reorganize the various units, branches, departments and worker assignments to achieve service cost efficiencies. For example, a post-special reorganization City of Los Angeles could economize on service costs by deploying specialists to assist the various small departments, rather than constraining specialists to serve a narrow function within a small department or unit. Another example is that the City could economize on supervisory costs by consolidating compatible units or departments.

The CFA authors rejected the City of Los Angeles allegations because the City failed to produce empirical evidence on the workloads and the factors driving the workloads of City staff. The State Controller found the City of Los Angeles argument about cost savings irrelevant because Government Code Section 56815 "validates the CFA's methodology to base mitigation payments solely on the difference between current revenue and current expenditures."³⁸

Empirical Evidence

The Executive Officer has conducted additional research into expenditures at other cities to determine whether there is evidence of fixed costs. If costs per capita are lower among larger cities than among smaller cities, that would lend support to the City's argument that it would be limited in its ability to reduce costs if the City were to become smaller.



Using a Government Finance Officers Association database of municipal expenditures of approximately 1,500 cities in the United States, the Executive Officer has found that general government costs are higher at larger cities than at smaller cities. In order to test whether this relationship relates to the cost of living in larger cities rather than size, we plotted the general government costs as a percent of property values and found again that the costs were higher at the

³⁷ Hamilton, Rabinovitz & Alschuler, Inc. The Division of Service Cost Burdens Following Separation of the San Fernando Valley from the City of Los Angeles: An Independent Appraisal. Los Angeles, May 13, 2002, page 7.

³⁸ California State Controller, California State Controller's Review of the Proposed Hollywood Special Reorganization Comprehensive Fiscal Analysis, May 2002, page 21.

larger cities. In other words, among American cities general government costs tend to be higher at larger cities than at smaller cities.

By comparing the City of Los Angeles budget for central services to San Diego and San Jose, the Executive Officer finds no evidence for stranded costs in the City Attorney and City Clerk departments. Other large California cities manage to keep their expenditures on these central services roughly in proportion to their city size. San Diego's population is approximately one-third of the Los Angeles population, and San Diego's City Attorney and City Clerk budgets are one-third the size of their counterparts at the City of Los Angeles. Similarly, San Jose's population is about one-fifth of the Los Angeles population, and San Jose manages to keep its City Attorney and City Clerk expenses roughly proportional.

The Executive Officer investigated the relationship between city size and government costs for public safety and public works as well. Public safety costs are the lowest for cities with 20-50,000 residents, and tend to increase with city size. Thus, larger cities tend to have higher costs than smaller cities even after controlling for city size and cost of living. Street maintenance costs tend to be comparable at larger cities, and perhaps slightly less expensive than at smaller cities.

The Executive Officer concludes that American cities tend to have overhead costs that are proportional to the size of the city, and that larger cities tend to spend proportionately more on general government and public safety than smaller cities. The Executive Officer rejected the City's "stranded cost" argument after finding that other cities manage to keep their expenditures in line with the size of the population being served.³⁹

Revised City Approach

In response, the City of Los Angeles retained a consulting firm to conduct an "independent" estimate of the "stranded costs." In a one-month period, the City provided its consultant with interview access to representatives of each individual unit of the largest City departments and with "objective" workload data documenting the need for a particular level of staffing, and the consultant produced a fiscal analysis report. Generally, the consultant found that the post-special reorganization City of Los Angeles could reduce its field staff engaged in direct service provision, but could make only limited, 10-15 percent reductions in administrative and centralized support staff without affecting service levels. The City's consultant concluded that the fiscal mitigation payment should be at least \$98 million higher than the CFA estimate in the case of the San Fernando Valley.

The City of Los Angeles consultant's report provided tables indicating which City employees would be needed to sustain current service levels in a post-special reorganization City of Los Angeles, and a brief summary of the general methodology used to derive the estimates.⁴⁰ The consultant's report does not share any of the particulars relating to the interviews of City staff, does not share any of the objective workload data documenting the need for post-special reorganization staffing levels, and does not provide a rationale for its City staff allocations. The consultant's report lacks documentation on the derivation of the post-special reorganization cost estimates.

The City's consultant has separately analyzed each unit in the major City departments, an approach that restricts the flexibility of reorganizing or "rightsizing" city government. Where there were fewer than three employees in a particular job title, the consultant has typically assumed that all of those staff are critical to maintaining City service levels. Thus, most of the centralized supervisory positions were assumed to be critical to maintaining City service levels. Where there are a significant

³⁹ Calemine, Larry J. Special Reorganization of the San Fernando Valley: Executive Officer's Report, April 24, 2002.

⁴⁰ Hamilton, 2002.

number of staff with the same job title in a particular unit, the City’s consultant has defined a greater than proportionate share as necessary to maintain City service levels.

The accompanying table demonstrates the difference between the CFA allocation and the City consultant’s allocation of staff to the remaining City of Los Angeles in the case of the crime lab. While the CFA provides a rationale for apportioning staff costs based on the proportion of patrol officers stationed in the San Fernando Valley, the City’s consultant does not explain why a post-special reorganization City of Los Angeles would need more photographers, typists or chemists to maintain service levels.

In the General Services department, the CFA allocated 24 percent of costs to the San Fernando Valley using explicit allocation factors. For example, the CFA allocated building maintenance costs based on the percent of City buildings located in the San Fernando Valley. By comparison, the City’s consultant indicated that the City could eliminate only 17 percent of its positions in this department, but provides no details or explanation as to why additional positions were deemed necessary after special reorganization.

	CFA	City Consultant
Total	182	219
Captain	1	1
Secretary	1	1
Forensic print specialists	56	66
Criminalists	45	50
Photographers	28	33
Typists	15	18
Police officers	13	18
Surveillance specialists	6	7
Chemists	2	3
Polygraph examiner	3	4
Management analysts	3	4
Document examiner	3	4
Lab technicians	3	4
Drafting technician	1	1
Composite artist	1	1
Storekeeper	1	1
Student workers	2	3

Conclusion

The City’s latest report does not provide evidence or adequate analysis substantiating the City’s claim of stranded costs. The Executive Officer concludes that the recent report reflects the opinions of the City’s consultant without the benefit of concrete evidence of stranded costs. Furthermore, the Executive Officer notes that if indeed there are high fixed costs that the City would face if the Valley and Hollywood were to incorporate, then the Valley and Hollywood would have strong financial incentives to contract with the City of Los Angeles for centralized services. In absence of compelling evidence, the Executive Officer recommends that the City’s stranded cost estimates be disregarded in the fixing of the fiscal mitigation payment and that the Commission determine that the \$21.3 million mitigation payment adequately mitigates the negative fiscal effect of the proposed special reorganization on the City of Los Angeles.

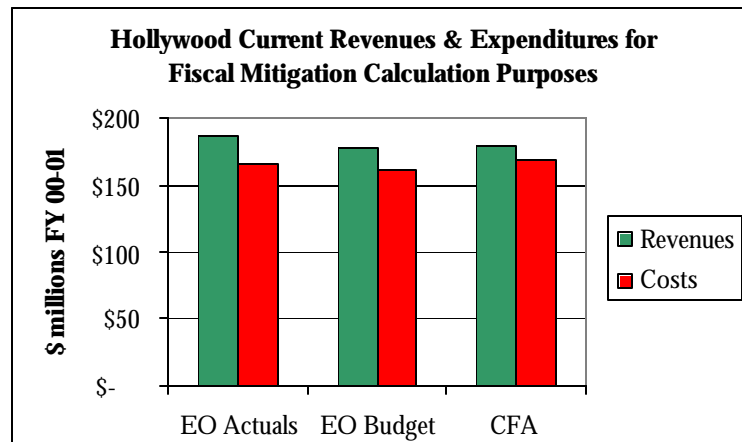
FISCAL MITIGATION PAYMENT AMOUNT

For purposes of calculating the fiscal mitigation payment, the Executive Officer recommends inclusion of the documentary transfer tax so that the negative fiscal impact on the City of Los Angeles reflects the effect of this reduced revenue stream. This approach diverges from the recommendations of the State Controller, who found that the negative fiscal impact on the City of

Los Angeles should be calculated based on the revenue neutrality test and should not include lost documentary transfer taxes.

In calculating the fiscal mitigation payment, the Executive Officer has followed Government Code section 56815, which focuses on the current expenditures for services that will be assumed by the transferring territory rather than the budget cutbacks that the City of Los Angeles anticipates making after special reorganization. On this issue, the Executive Officer concurs with the State Controller, who found that the City of Los Angeles' "stranded costs" are not relevant to the calculation of the fiscal mitigation payment. This issue is discussed in greater length in the previous section of this Report.

Based on the above, the Executive Officer finds that the negative fiscal impact on the City of Los Angeles had special reorganization occurred in the base year would have been \$21.3 million. This represents an increase of \$10 million over the CFA estimate of the fiscal mitigation payment based on budgeted revenues and expenditures. The difference is primarily due to the fact that the Executive Officer allocated a share of the Public Safety Augmentation Fund and reserve fund transfers, whereas the CFA did not allocate these revenues to the new city.



Conclusion

Based on the above, the Executive Officer recommends that the Commission find that the Hollywood Special Reorganization would have an annual negative fiscal effect on the City of Los Angeles of \$21.3 million that should be mitigated.⁴¹

⁴¹ Pursuant to Government Code section 56815(d), if current revenues and current expenditures are not substantially equal, the Commission may only approve a proposal if it finds that: (1) the county and all other subject agencies agree, or (2) the negative fiscal effect of the incorporation is adequately mitigated by tax sharing agreements, a lump sum payment over a fixed period of time or other terms and conditions imposed by the Commission.

FISCAL VIABILITY FINDING

The Executive Officer has recalculated the fiscal estimates based on actual City revenues and expenditures in the base year for purposes of evaluating the fiscal viability finding. Further, the Executive Officer has updated other fiscal estimates that affect the fiscal viability finding as detailed below.

State Subventions

The State allocates vehicle license fees and gas tax to local government on the basis of population and, in the case of new cities, on the basis of triple the number of registered voters. The Urban Research Division has estimated that there were 77,723 registered voters in the special reorganization area in March 2001. Based on this figure, the population estimate used for purposes of allocating state subventions would be 26 percent higher than the estimated population based on 2000 Census data. Because the current revenues generated in Hollywood are based on population, the actual distribution of state subventions to the new city would be more favorable.

The Executive Officer estimates that the new city would receive \$12.5 million in vehicle license fees based on fiscal year 2000-01 actual revenues, of which \$2.5 million reflects new revenues for Hollywood. Similarly, the new city would receive \$7.4 million in gas taxes based on fiscal year 2000-01 actual revenues, of which \$1.2 million reflects new revenues.

Documentary Transfer Tax

As reported previously in the CFA, Hollywood would not be authorized to levy a documentary transfer tax at the City of Los Angeles current rate of \$2.25 per \$500 in property sales, and instead would have only half of the County's tax rate of \$.55 per \$500 in property sales. The new city's revenues would be \$3.6 million lower than current revenues generated in the territory due to this reduction in the documentary transfer tax rate.

Transition Costs

For purposes of fiscal viability computations, the Executive Officer has used the most recently provided transition costs. The City informed the State Controller in its request for review of the Hollywood CFA that it estimated that one-time transition costs associated with redistricting were \$500,000, with bond validation were \$20,000, and with revenue collection were \$95,000, during the transition year. The Executive Officer has used the City of Los Angeles CAO \$1.4 million estimate of annual contract administration costs for providing services to Hollywood.⁴²

The City estimated that its incremental election costs associated with holding two elections after redistricting the city council boundaries would be approximately \$274,000; however, the Executive Officer recommends that this cost be borne by the City of Los Angeles. In addition, the City estimated that its on-time contract administration costs would include a \$16 million Information Technology Agency contract negotiation expense. However, this cost estimate was deemed unreasonable by the State Controller, and the Executive Officer has not included that cost estimate in the fiscal viability calculations.

⁴² City of Los Angeles City Administrative Officer, Estimated Costs for the City of Los Angeles to Administer a Contract for Municipal Services With the Proposed New Hollywood City as Proposed by LAFCO, April 23, 2002. The table provided by the City includes both the City departments' and the CAO's estimates. The State Controller found that annual contract administration costs would be \$2.2 million (the City departments' estimate) in an apparent oversight.

The Executive Officer estimates that the new city would pay approximately \$250,000 annually to reimburse the costs of the third party fiscal agent. This expense of the new city has been included in the fiscal viability calculations.

Debt Payments

The fiscal viability calculations include debt payments by the new city to the City of Los Angeles for debt issued as of the election date. The resolution requires the new city to pay a proportionate share of lease obligation debt, Convention Center lease obligation debt, judgment obligation bonds, sanitation equipment revenue debt, parking revenue bonds, tort liability and workers' compensation claims.⁴³ Further, property owners in Hollywood would continue to bear liability for general obligation bonds, Proposition K debt, and special assessment debt that is included in the property tax bill. These debt payments made by Hollywood property owners would be remitted directly to the City of Los Angeles for use in defeasing the debt.

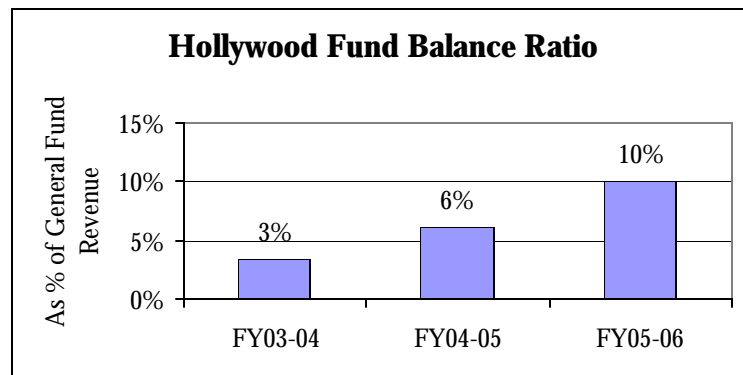
Reserve Fund and Fund Balances

The Executive Officer's fiscal viability estimates include a transfer of a general fund proportionate share of the City of Los Angeles' emergency reserve fund. Although the resolution provides for a portion of the special purpose fund balances to be allocated to the new city, the fiscal viability computations assume that no such fund balances would transfer and do not reflect additional funding available to the new city through the transfer of such balances.

New City's Reserves

The Executive Officer estimates that the expected cash balance of the new city would be 10 percent of general fund revenues by the end of new city's third year.

In order to approve a special reorganization, the Commission must find that the proposed city would generate "reasonable reserves" during its first three years. The Government Finance Officers Association recommends a minimum unreserved fund balance of "no less than 5 to 15 percent of regular general fund operating revenues, or of no less than one to two months of regular general fund operating expenditures."⁴⁴



In its request for the Controller's review, the City expressed concerns about the adequacy of the proposed city's reserves in its first year. Further, the City questioned the CFA estimate of an

⁴³ In the fiscal viability appendix table, the sanitation equipment revenue debt payment is included in the cost of purchased services. The resolution requires the new city to make payments on this debt regardless of whether the new city relies on the City of Los Angeles for refuse collection service.

⁴⁴ Government Finance Officers Association. "Governmental Accounting Focus: New Recommendations from GFOA", *GAAFR Review*, Vol. 19, No. 2, February 2002.

eventual 3 percent reserve: “the CFA has assumed a level of fiscal stability in the proposed new city greater than that of comparably sized cities without a basis for doing so.”⁴⁵

The Controller concluded that “there is no authoritative basis for determining a ‘sound financial management’ level of reserves.”⁴⁶ However, the Controller asserted that the CFA estimates of the new city’s projected reserves are considerably lower than the 14.3 percent average for 38 California cities with population comparable to the proposed Hollywood city. Further, the Controller indicated that undesignated reserves tend to fluctuate significantly from year to year, and that projections of reserve levels are unreliable.

Indeed, the City of Los Angeles general fund reserves have fluctuated significantly over the last several years. The City entered fiscal year 1997-98 without any undesignated reserves; in fact, the City’s financial statements reported slightly negative reserves as of June 1997.⁴⁷ By the end of fiscal year 2000-01, which is the base year for purposes of the CFA, the City’s reserves were \$159 million or 5.4 percent of annual general fund revenues.⁴⁸ However, the City has apparently depleted a good portion of that reserve in the current fiscal year due to unanticipated revenue shortfalls, and is currently attempting to maintain a \$60 million emergency reserve.⁴⁹ This represents 1.9 percent of general fund revenues. If the City uses all or part of the \$60 million reserve fund to balance its budget this year, the reserves available in fiscal year 2002-03 may be lower than 2 percent.

The Controller took issue with the CFA methodology for determining the proposed city’s reserve ratio. In her review of the Hollywood CFA, the Controller took issue with construing the proposed city’s cash balance to be the proposed city’s reserves. Specifically, the Controller argued that the reserves should be defined as the cash balance before factoring in any loans or budget cutbacks that the proposed city might undertake. In essence, the Controller is defining reserves under a strict accounting approach in which the fund balance is the difference between the assets and liabilities of the proposed city.

The Controller’s accounting approach to the definition of reserves is impractical for evaluation of the proposed cities for three reasons. First, the CFA was conducted on the basis of the City of Los Angeles budget, due to the greater programmatic detail provided in the budget as opposed to the City’s financial statements. Second, the Controller’s approach to defining reserves would require financial statements on the new cities, which are not expected to be available until after the City of Los Angeles has produced financial statements for activity ending on the special reorganization effective date. Third, the Controller’s approach would require a valuation of assets transferred to the proposed city which is not available.

The year-end cash balance reflected in the Executive Officer’s fiscal viability calculations reflects the overall budget surplus of the proposed city. As such, it includes both general and special purpose funds. For the most part, the Executive Officer’s fiscal estimates have assumed that appropriations from special purpose funds are allocated to the proposed city in proportion to the special purpose

⁴⁵ Letter from City of Los Angeles Mayor James K. Hahn to LAFCO Executive Officer Larry Calemine. “Request by the City of Los Angeles for the State Controller’s Review of the Comprehensive Fiscal Analysis for the Proposed Special Reorganization for Hollywood”, April 5, 2002.

⁴⁶ California State Controller, California State Controller’s Review of the Proposed Hollywood Special Reorganization Comprehensive Fiscal Analysis, May 2002.

⁴⁷ City of Los Angeles, Office of the Controller, Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 1997, December 22, 1997.

⁴⁸ City of Los Angeles, Office of the Controller, Comprehensive Annual Financial Report for the Fiscal Year Ended June 30, 2001, January 18, 2002.

⁴⁹ City of Los Angeles, Office of the Controller, *Estimate of Revenue for Fiscal Year 2002-03*, March 1, 2002.

revenues allocated to the new city. Thus, the year-end balance primarily reflects a general fund balance. Given that future debt payments have been budgeted in the fiscal viability calculations, the year-end balance approximates the undesignated, unreserved general fund balance that is reflected in the “reasonable” reserve ratios discussed above.

Conclusion

The Executive Officer concludes that the proposed city’s cash balance would meet the Government Finance Officers Association standard for reasonable reserves. The Executive Officer finds that the proposed city is expected to generate reasonable reserves during the first three fiscal years following incorporation, and that the proposed city will be financially viable.

TRANSITION PERIOD

The Hertzberg Act provides for a period of time, typically called the “transition period,” when a county is required to continue to provide services to a newly incorporated city formed from unincorporated territory.⁵⁰ The purpose of the transition period is to provide continuity of services to the new territory while the new city is establishing itself. In this case, the transition period is the period of time when the new city would rely on the City of Los Angeles for services under terms specified by the Commission in its resolution making determinations.

The Hertzberg Act provides for a transition period extending from the effective date to the end of the fiscal year in which incorporation occurs, or longer by agreement of the parties.⁵¹ Elsewhere the Act extends flexibility to the Commission in setting terms and conditions providing for the continuation of services and payment for those services for a longer period of time, so long as the Commission’s decision to do so is supported by substantial evidence in the record.⁵²

EFFECTIVE DATE

The Commission must establish an effective date for the proposed city. The effective date must occur within nine months of the election approving the special reorganization.⁵³

Effective dates established for other California incorporations are listed in the accompanying table. Past practice indicates that effective dates for incorporations approved in November elections are typically set for the following January 1 or February 1, but have been set as early as December 1 and as late as July 1.⁵⁴

California Incorporation Effective Dates		
City	Election	Effective Date
Goleta	Nov. 6, 2001	Feb. 1, 2002
Aliso Viejo	Mar. 6, 2001	Jul. 1, 2001
Elk Grove	Mar. 7, 2000	Jul. 1, 2000
Rancho Santa Margarita	Nov. 2, 1999	Jan. 1, 2000
Laguna Woods	Mar. 2, 1999	Mar. 24, 1999
Citrus Heights	Nov. 5, 1996	Jan. 1, 1997
Truckee	Mar. 2, 1993	Mar. 23, 1993
Windsor	Nov. 5, 1991	Jul. 1, 1992
Buellton	Nov. 5, 1991	Feb. 1, 1992
Chino Hills	Nov. 5, 1991	Dec. 1, 1991
Murrieta	Nov. 6, 1990	Jul. 1, 1991

Commission Alternatives

Although there are a number of alternatives that the Commission may consider, the parties have proposed and discussed three alternatives:

- 1) The later of the date of certification of the election results or 15 days after the election (“November 2002 effective date”): the effective date proposed by the Applicant,

⁵⁰ Government Code section 57384.

⁵¹ Government Code section 57384.

⁵² Government Code section 56886.

⁵³ Government Code section 57202.

⁵⁴ Incorporation precedents include all incorporations since 1990 with both an election date and effective date listed in the LAFCO resolution.

- 2) January 1, 2003: the effective date recommended by the Subcommittee;⁵⁵ and
- 3) July 1, 2003: the effective date proposed by the City of Los Angeles and recommended by the Executive Officer.⁵⁶

There are three major considerations in the establishment of the effective date: revenue and cash flow issues, accounting costs, and transition period length.

The Applicant specifically proposed a November 2002 effective date to ensure that the new city meets state deadlines for sales tax, property tax and subventions that will initiate these revenue flows to the new city. The Applicant seeks to minimize the time period between the new city's approval and its official start, and possibly avoid a time period where the City of Los Angeles has authority to make policy decisions affecting Hollywood before the new Hollywood city council takes office. The City of Los Angeles has expressed indifference between an earlier effective date and a July 1, 2003 effective date. The City would benefit from an earlier effective date if it reduces the length of the transition period. The City has also indicated, however, that a July 1 effective date is appealing from an accounting and cash flow standpoint, and would provide a longer time period for negotiation of service contracts.

The Subcommittee recommended a January 1, 2003 effective date in order to avoid the accounting complexities of a mid-month effective date. Although staff originally recommended a July 1, 2003 effective date, the Subcommittee preferred the January 1 effective date, in consideration of the Applicant's desire to get the new city started as soon after the election as possible.

Although earlier the City of Los Angeles had not expressed a strong preference for a particular effective date, it is now proposing a July 1, 2003 effective date. The City indicated that a January 1, 2003 effective date would present substantial difficulties for the City because it anticipates that its cash flow position at that time of year would be negative. The City uses its \$60 million reserve fund and \$200-250 million in short-term debt in the form of tax and revenue anticipation notes, to alleviate cash flow deficits early in the fiscal year. The City is concerned that the special reorganization will impact its ability to issue and reimburse short-term debt during a mid-fiscal year cash flow deficit. The City has also indicated that a July 1 effective date is appealing from its standpoint because it would reduce the length of the transition period service obligation.

Pros:

- 1) There will be an additional six months of time for the new city to recruit a city manager and department heads, to conduct strategic planning and budgeting, and to prepare the ordinances of the new city.
- 2) The City of Los Angeles will be obligated to provide transition period services without service contracts for a twelve-month period rather than an eighteen-month period, reducing the City's exposure to a service obligation that is not defined by contract.
- 3) The City of Los Angeles will be able to redistrict and conduct city council elections between the special reorganization election and the effective date. .
- 4) The July 1 effective date will better accommodate the allocation of a share of the City's reserve funds to the new city. The City of Los Angeles predicts that it will not have reserves

⁵⁵ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

⁵⁶ City of Los Angeles, *Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions*, April 2, 2002.

available for allocation to the proposed city on January 1, as the City is likely to be in a negative cash-flow position at that time of year.⁵⁷

- 5) The City of Los Angeles will be unencumbered by special reorganization when it issues and reimburses its fiscal year 2002-03 tax and revenue anticipation notes. The City of Los Angeles and the new city may separately issue and reimburse short-term debt in fiscal year 2003-04 and thereafter.
- 6) The July 1 effective date simplifies special reorganization from an accounting standpoint. There will be no need for the City to close its books in the middle of the fiscal year. The July 1 effective date eliminates the need for a property tax transfer from the City of Los Angeles to the new city, and eliminates the need for a business tax revenue offset to be computed and applied to the transition period service payment.

Cons:

- 1) A July 1 effective date gives the City of Los Angeles an eight-month window during which it may make policy decisions affecting Hollywood without accountability, whereas a January effective date limits that window to two months.
- 2) The new city would not exist as a legal entity, and would be unable to defend itself against a legal challenge by the City of Los Angeles between the election and the effective date.
- 3) The new city would not exist as a legal entity, which would limit its ability to conduct negotiations with the City of Los Angeles between the election and the effective date.

Executive Officer's Recommendation

The Executive Officer has evaluated the Applicant's concerns regarding a July 1 effective date, and continues to recommend a July 1 effective date. A January 1 effective date would have a negative fiscal impact on the proposed city by creating additional accounting transition costs, require the apportionment and crediting of revenue sources that would continue to flow to the City of Los Angeles, and create cash flow issues that are avoided by a July 1 effective date. The draft resolution has been structured to avoid long-term impacts of City of Los Angeles decisions, such as the issuance of debt, after the election date. Potential legal challenges prior to the effective date would likely be directed to the Commission's decision and defended by Legal Counsel.

TRANSITION PERIOD LENGTH

Although the Government Code provides that the transition period end at the end of the fiscal year during which incorporation takes place, the Commission has discretion over the length of the transition period. The Applicant proposes a transition period of up to three years to provide for the gradual and orderly transfer of municipal services and personnel. The City of Los Angeles proposed that the transition period be limited to no more than one year to reduce the length of what the City predicts will be a contentious period. The City is concerned about potential conflict arising from a service obligation which is not defined by contract. The draft resolution establishes a twelve-month transition period, from July 1 to June 30 of the following year.

⁵⁷ City of Los Angeles. Attachment: Fiscal Comments and Questions on the Valley Secession Draft Resolution of Determination and the LAFCO Executive Director's [sic] Report on Valley Secession Dated April 19, 2002, May 15, 2002.

The Subcommittee recommended a transition period end-date of June 30, 2004. With the recommended effective date of January 1, 2003, the transition period would be 18 months. The recommendation of the Subcommittee reflects an attempt to accommodate the competing interests of both parties.⁵⁸

The Executive Officer recommends that the transition period end date coincide with the end of the fiscal year. Further, the Executive Officer concurs with the City of Los Angeles that the transition period will be a time of uncertainty and potential conflict over service scope and payment, and thus seeks to limit that period of time. However, the Executive Officer considers the nineteen-month period between the election and the end of the transition period to be adequate time to accommodate negotiation of service contracts and the establishment of the new city.

The Executive Officer continues to recommend a twelve-month transition period that commences on the July 1 after the election and ends on the following June 30.

TRANSITION PERIOD SERVICE DISCONTINUATION NOTICE

The purpose of the transition period is to ensure that public services are delivered while the new city is establishing itself. Although Government Code section 57384 provides that the new city council may request the discontinuance of transition period service at its sole option at any time during the transition period, the Commission may impose terms and conditions modifying that provision, such as requiring a reasonable notification period to protect the City of Los Angeles from fiscal harm.⁵⁹

The Subcommittee recommended a six-month notification requirement. During the notification period, the new city would be required to continue to pay for transition period service; however, the transition period for a particular service would automatically be terminated on the effective date of a service contract between the parties.⁶⁰ The City of Los Angeles has proposed that it be entitled to reduce or terminate service in its discretion, if the new city does not timely reimburse the City for transition period service and that the County be required to provide service if the City cannot or does not provide transition service.⁶¹ The City of Los Angeles has not offered to provide advanced notice of its actions in a set time frame. The Applicant has proposed that the new city council be entitled to implement its “reorganization plan” at any time during the transition period.

Executive Officer’s Recommendation

Consistent with the Subcommittee’s recommendation, the Commission should impose a six-month notification requirement upon the new city for cancellation of transition period service. During the notification period, the new city should be required to continue to pay for transition period services. It is recommended, however, that the transition period for a particular service automatically be terminated on the effective date of a service contract between the parties. This term will avoid the possibility of any conflict between application of the terms and conditions for the transition period and the obligations of the parties pursuant to contract, and will encourage the parties to enter into more permanent contractual relationships as soon as possible.

⁵⁸ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

⁵⁹ County of Los Angeles, Office of the County Counsel, *The Transition Period*, November 21, 2001; see also Government Code section 56886.

⁶⁰ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

⁶¹ City of Los Angeles, *Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions*, April 2, 2002.

The Executive Officer does not recommend imposing a term and condition requiring the County of Los Angeles to assume the transition period service obligations of the City of Los Angeles as proposed by the City of Los Angeles. To do so would only serve as a disincentive to the parties to resolve service-related issues between themselves, and places an unreasonable burden upon the County, given the relatively short time period involved and the financial and physical impracticality of requiring the County to provide municipal services on a large scale without the necessary infrastructure and personnel resources available to it.

SERVICE LEVELS

Government Code section 57384 also provides that during the typical transition period, “all services furnished to the area prior to incorporation” continue to be furnished. In five of the last seven California incorporations, the LAFCO resolution has required that the county maintain pre-incorporation service levels during the transition period.

The Applicant has proposed that the City of Los Angeles “provide the new Hollywood City with at least the same level of service the Hollywood region is currently receiving.” The City of Los Angeles has proposed that it retain the right to adjust service levels in the event of emergency, natural disaster or changed economic conditions.⁶²

The Subcommittee recommended that the Commission incorporate both proposals in the terms and conditions.⁶³

Executive Officer’s Recommendation

Consistent with the Subcommittee’s recommendation, the Commission should require the City of Los Angeles to maintain current service levels in the new city except as may be required for management of emergencies or revenue shortfalls. The provision should also authorize the City of Los Angeles to reduce service levels in a proportional manner in the event that Hollywood’s actual transition period service payments fall short of baseline costs.

TRANSITION SERVICE SCOPE

The transition service scope is a definition of the types of services that the new city anticipates needing during the transition period. The Applicant’s preliminary comprehensive fiscal analysis is not entirely clear on the question of transition service scope. On the one hand, the Applicant has proposed that the City of Los Angeles “provide the new Hollywood City with at least the same level of service the Hollywood region is currently receiving,” and on the other hand its budget only provides for contract services for the following City of Los Angeles departments: police, fire, animal services and recreation and parks. The City of Los Angeles has proposed that it control the scope of services provided to the new city during the transition period, except as otherwise mutually agreed to by the parties through service contracts.⁶⁴

Government Code section 57384(a) acknowledges that the city council of a newly incorporated city may want to discontinue transition period services prior to the end of the transition period, presumably when the new city is capable of providing those services or determines that particular

⁶² City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

⁶³ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

⁶⁴ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

services are no longer needed. Generally speaking, service scope determinations should be left to the new city council. If prior recommendations are followed, the new city council could discontinue services provided by the City of Los Angeles after providing six months' notice. With this safeguard, it is less likely that service interruptions will arise, and the new city will still be afforded some flexibility in managing its service delivery and service costs.

Executive Officer's Recommendation

The Executive Officer recommends that the transition period service scope include all services currently provided to the Hollywood special reorganization area, and that the discontinuance of particular services should be left to the discretion of the new city council.

PAYMENT CALCULATION

The Subcommittee, based upon staff recommendation, had recommended that the Commission incorporate meaningful components of the Gonzalves rule⁶⁵ in its resolution, particularly with respect to the mayor and city council.⁶⁶ Specifically, this would mean that the new city would not be required to pay for the costs associated with City of Los Angeles elected officials and department heads, along with their chiefs of staff and executive secretaries. Legal Counsel has since advised that pursuant to Government Code section 57384, the transition period service provider is typically reimbursed for the "total direct and indirect expenses ... of providing services."

The new city is required to reimburse the old jurisdiction for the cost of transition period services at "net cost." The statute directs the Commission to compute the net cost, which must include direct and indirect costs that were funded by general revenues of the old jurisdiction during the prior fiscal year. Any revenues generated in the territory during the transition period that are retained by the old jurisdiction must be deducted from the net cost.

The net cost approach as defined in Government Code section 57384(b) does not include service costs and overhead that the City of Los Angeles finances from federal grants, user fees and special purpose funds. As discussed earlier, Government Code section 57302 authorizes the Commission to develop alternative conditions that deviate from general statutory requirements such as this net cost provision.

Transition period service costs are also offset by any revenues generated in the new city during the transition period that are retained by the City of Los Angeles, including first quarter sales tax. The City of Los Angeles has asked for clarification of the sales tax revenue offset for the first quarter of the transition period. The Board of Equalization has informed the Executive Officer that it will be unable to process the new city's application in a one-day period, and that the new city's sales tax allocation in the first quarter of the transition period will be remitted to the City of Los Angeles.

⁶⁵ Government Code section 51350. This statute prohibits counties from billing contract cities for countywide services and for general county overhead costs that the county would incur regardless of whether it provides contract service to cities. These excluded costs relate to the functions of the Board of Supervisors and the department executives.

The preceding requirement, also known as the Gonsalves rule, does not apply to cities providing contract service and is not directly applicable to this special reorganization.

⁶⁶ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

Thus, the City of Los Angeles will be directly receiving the new city's sales tax payment in the first quarter of the transition period. The sales tax offset is designed to ensure that sales tax revenues generated in Hollywood after the effective date are credited toward transition period service costs.

Precedent

In most cases, the LAFCO requires the new city to reimburse the old jurisdiction for the net cost of providing transition services. In the case of Goleta and Rancho Santa Margarita, the respective counties waived all or some of the cost of transition services.

Proposals

The City of Los Angeles has proposed that the new city reimburse all costs of continued service, including, without limitation, direct costs (e.g. labor costs), overhead, capital costs, related liability claims, administration costs, and costs not fully reimbursed through fees and charges.⁶⁷

Analysis

The statutory approach to defining net cost does not require the new city to reimburse any costs that the old jurisdiction formerly financed through special purpose funds and dedicated grants. To the extent that the old jurisdiction continues to receive these funding sources after a reorganization, the statutory approach is sensible. However, to the extent that special purpose funds (e.g., gas tax) are directed to the new city, this approach would require the old jurisdiction to subsidize some of the transition costs.

Executive Officer's Recommendations

The Commission should require the new city to reimburse the City of Los Angeles for all direct and indirect expense of providing services in accordance with Government Code section 56384(b), except that the definition of "net costs" should not exclude costs to be paid from special funds that have been transferred to the new city. Transition period service costs should be limited to those direct and indirect costs generated on or after the date of incorporation; the City of Los Angeles should not charge the new city for operating costs incurred prior to the effective date, regardless of when actual invoicing or payment occurs.

TRANSITION SERVICE REIMBURSEMENT

The City of Los Angeles and the Applicant appear agreeable to a timely reimbursement schedule on a monthly basis for transition period services. Further, both parties have agreed in principle to the reimbursement mechanism occurring in the form of a share of revenues guaranteed to the City of Los Angeles.

Cash Flow Considerations

While the parties agree in principle, there remain differences of opinion regarding certain cash flow elements of the reimbursement schedule and a third party fiscal agent. The Applicant has proposed

⁶⁷ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

that regular payments be made in the form of a fixed amount, not-to-exceed a fixed percentage of total revenues accruing to the new city, approximating projected service costs, with a reconciliation of cost and revenue balances at the end of the transition period or periodically during the transition period. The City has proposed that the new city pay invoiced estimates of the City's anticipated costs for a particular month by the tenth of the month or, in other words, prior to the costs being incurred by the City. Furthermore, the City has indicated disagreement with the Subcommittee's decision to credit the new city with one-half of the fiscal year 2002-03 property taxes, despite the fact that these revenues would clearly finance Hollywood services if special reorganization were not to occur.⁶⁸

A consideration in structuring the transition period reimbursement relates to revenues from Hollywood residents and businesses that would be received and could be retained by the City of Los Angeles after Hollywood incorporation. For the most, however, these cash flow issues would be avoided through the imposition of a July 1 effective date. The following concerns arise with an effective date other than July 1.

The most significant cash flow issues relate to appropriate crediting of fiscal year 2002-03 property tax and business tax revenues. The property tax revenues will flow to the City of Los Angeles in December 2002 and April 2003. If the proposed special reorganization did not occur, the City would likely use these funds to finance Hollywood services. While the Auditor/Controller will remit these funds to the City of Los Angeles, it would be appropriate for the Commission to require that the City of Los Angeles credit, consistent with Government Code section 57384, one-half of the fiscal year 2002-03 property tax receipts generated in Hollywood toward the new city's transition period service costs in the event the Commission adopts a January 1, 2003 effective date.

Similarly, the business license tax presents a potential cash flow problem. Most Hollywood business license taxes will be paid in March 2003 for the privilege of doing business in Hollywood during the 2003 calendar year.⁶⁹ As with the property taxes, the Commission should require that the City of Los Angeles credit one-half of the fiscal year 2002-03 business license tax receipts generated in Hollywood toward the new city's transition period service costs in the event the Commission adopts a January 1, 2003 effective date.

The sales tax presents yet a third cash flow problem. The State Board of Equalization is not expected to remit sales tax payments for taxable activity that occurs in Hollywood during the first quarter following the effective date to the new city. The Hollywood portion of the sales tax payment for taxable activity that occurs after the effective date will most likely be remitted to the City of Los Angeles. The Commission should require that the City of Los Angeles credit 6.3 percent (the estimated share of City sales taxes generated in Hollywood) of sales tax receipts for the first quarter following the effective date toward the city's transition period service costs in the event the Board of Equalization includes the Hollywood portion in its payment to the City of Los Angeles.

Precedent

The Hertzberg Act provides for a reimbursement period of up to five years for transition period costs. With the county's consent, the reimbursement period may be extended.⁷⁰ In the case of Citrus

⁶⁸ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

⁶⁹ Annual business license fees compose the vast majority of revenues, and are received in February and March of the calendar year.

⁷⁰ Government Code section 57384(b).

Heights, the new city council defaulted on transition service reimbursement, the county sued and the parties eventually settled for a lesser amount. In subsequent incorporations, the parties have been cautious about securing both the transition service payment and the mitigation payment on revenue streams that would otherwise flow to the new city. In recent incorporations, LAFCOs have required that a portion of the new city's property tax and/or sales tax revenue streams be dedicated to repayment of transition costs.

Government Code section 57384 requires that the county credit to the payment of transition costs any revenues that it retains that were generated in the incorporated territory during the transition period. This typically only extends to the end of the fiscal year, wherein because of the Board of Equalization filing requirements, the new city cannot collect its portion of the property tax. For the subsequent fiscal year, it is relatively simple to use the property tax as a payment guarantee with relevant terms in the LAFCO resolution and a written agreement between the parties to transfer the taxes. The county's Auditor-Controller would administer the property tax revenue diversion.

The sales tax revenue for the first quarter after incorporation will flow to the old jurisdiction if the effective date is on or after the first day of the calendar quarter. In the case of Elk Grove and Citrus Heights, the county credited this revenue toward transition period service. In the case of Aliso Viejo, the sales tax increment⁷¹ was dedicated to repayment of transition period service costs.

There exists a barrier in securing sales tax revenue streams after the first quarter. Although Fresno and Alameda counties do have sales tax sharing agreements in place that divert a portion of their cities' share of sales tax to the counties, these agreements were approved by the respective legislative bodies with a two-thirds vote, as required by the State Constitution.⁷²

Fiscal Agent

The Commission faces challenges in guaranteeing revenues to the City of Los Angeles for purposes of covering transition costs. The resolution making determinations can, and typically does, require that the new city adopt any revenue neutrality or tax-sharing agreements agreed to by the applicant and the transferring agency. At this point, however, it appears that the City of Los Angeles and the Applicant will not complete the negotiation of a revenue neutrality or tax sharing agreement in time for inclusion in the resolution.

The City of Los Angeles has proposed that the new city's property tax, business tax and utility users taxes be remitted to and retained by the County Auditor-Controller as the third-party fiscal agent. The City of Los Angeles proposes that, during the transition period, its claims for payment from these revenues be given first priority, and that after the transition period, it continue to have first priority over the new city's property taxes to secure payment of the new city's portion of the outstanding debt, workers' compensation and contingent liabilities. The City has also requested that the Commission require the new city to pay by the tenth of each month for the estimated cost of services anticipated for the month.⁷³

The fiscal agent's work volume is expected to be substantial during the transition period; the work is expected to keep at least one seasoned accountant occupied full-time, related costs have been estimated at a minimum of \$250,000 annually. The new city would have to approve a contract with, and compensate, the fiscal agent. Although both parties prefer that the Auditor-Controller serve as

⁷¹ The post-incorporation growth in revenues.

⁷² Cal. Const., Art. XIII, § 29.

⁷³ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

fiscal agent, a private sector bank could serve in this capacity as well. If the Auditor-Controller does not serve as fiscal agent, the Commission should require that Hollywood retain a fiscal agent that is acceptable to the City of Los Angeles.

The Subcommittee recommended that the Commission require both the new city and the City of Los Angeles remit all revenues collected by or on behalf of the new city to a third party fiscal agent throughout the transition period, and that all property tax revenues collected on behalf of the new city should be remitted to a third party fiscal agent until all debt liability existing as of the effective date is retired or the parties agree otherwise. It also recommended that the new city should reimburse the third party fiscal agent for the costs of collecting and remitting tax revenues, and that the third party fiscal agent should be acceptable to both the new city and the City of Los Angeles. Finally, the Subcommittee recommended that the third party fiscal agent make payments to the City of Los Angeles on a monthly basis for transition period service costs and liabilities, fiscal mitigation, and outstanding debt.⁷⁴

Regarding instructions for the priority of payments, the Executive Officer recommends that the treatment of expenditures be compatible with the treatment of revenues. Given that revenues generated in Hollywood prior to incorporation are not being distributed to the new city, neither should expenditures incurred prior to incorporation be allocated to the new city. The City's proposal that Hollywood essentially advance transition period service costs before such costs have been incurred would impose cash flow asymmetries on the new city, essentially requiring payment prior to revenue receipt. The City's transition period service reimbursement proposal is impractical.

Further, the City has proposed that the new city's obligations to the City of Los Angeles—debt payments, fiscal mitigation and transition period service costs—be prioritized above any expenditures for Hollywood personnel or facilities.

Given the statutory imperative that bondholders not be harmed by special reorganization conditions, the new city's debt payments to the City of Los Angeles should be granted first order of payment priority. Although debt payments should be granted first order of priority, the new city should not be required to make such debt payments to the City until shortly before the City must make the relevant debt service payment. The new city should not be required to make payments for City of Los Angeles costs before they have materialized, in which case the City would be collecting interest revenue otherwise due to the new city.

The second order of priority for the fiscal agent's payment should be reimbursement of debt incurred by the new city for the payment of transition period service costs. The new city may borrow funds during the transition period either from a bank or through tax and revenue anticipation notes to finance transition period service costs. With prudent financial management, the new city would likely structure debt repayment terms to spread these costs out over a lengthy time period so that the new city can keep up with its transition period service payments and fiscal mitigation payments. However, the new city would have difficulty acquiring such a loan if its repayment were not prioritized in the accounts payable scheme.

So long as the parties do not negotiate a tax-sharing agreement to accommodate the fiscal mitigation payment, the third order of priority for the fiscal agent's payment should be the fiscal mitigation payment. Without a tax-sharing agreement, the fiscal mitigation payment obligation is a fixed dollar

⁷⁴ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

amount and must be budgeted with a higher priority level than the more flexible payments for transition period service costs and the new city's operating costs.

The fourth priority for payment shall be the transition costs owed by the new city to the City of Los Angeles for bond validation, revenue collection, redistricting and other services provided by the City. The City of Los Angeles has requested that transition costs be ranked higher than transition service reimbursement.⁷⁵

The fifth priority for payment should be the transition period service reimbursement to the City of Los Angeles. Although the statute permits the Commission to treat payment of transition period service costs as a loan to be repaid over a five-year period,⁷⁶ the City of Los Angeles has indicated that the volume of transition period service costs would make such a loan impractical. Elsewhere, it is recommended that the City of Los Angeles not be required to extend a loan to the new city for transition period service reimbursement. Furthermore, it is recommended that the City of Los Angeles be authorized to reduce transition period services in the event of revenue shortfalls in order to accord both parties budgeting flexibility.

The final priority for payment should be the new city's operating costs. The CFA has estimated that the new city would require about \$1.3 million to staff its basic functions in the first partial fiscal year.⁷⁷ By according a lower priority to the new city's operating costs, it is anticipated that the new city will engage in cautious and prudent budgeting of its direct operating costs.

Finally, it is recommended that the Commission accord the parties flexibility to make future agreements regarding payment priorities during the transition period.

Executive Officer's Recommendations

Consistent with the Subcommittee's recommendations, the Commission should require that all tax revenues generated in Hollywood during the transition period be remitted to the third party fiscal agent, and that the third party fiscal agent be responsible for allocating the revenues appropriately to the City of Los Angeles and the new city. The Commission should require that the third party fiscal agent be compensated by the new city for the costs of collecting and remitting revenues, and that the agent be acceptable to both parties.⁷⁸

The Executive Officer recommends, however, that "revenues" be defined to exclude direct charges and fees for services, including Department of Water and Power ("DWP") charges for water and electricity (which are retained by the DWP for the provision of those utility services), Public Works, Bureau of Sanitation charges for sanitation equipment, wastewater charges, fees related to the issuance of permits and licenses, other similar administrative fees and charges, and fines. To the extent generated in Hollywood through the provision of transition period services, those amounts should be directly credited by the City of Los Angeles to the transition period service payment or the new city's portion of debt repayment, as appropriate, and not remitted to the fiscal agent.

⁷⁵ Fujioka, William T. Draft Resolution of Determination and LAFCO Executive Officer Report regarding the Valley Special Reorganization dated April 19, 2002, Attachment: Fiscal Comments and Questions on the Valley Secession Resolution of Determination and the LAFCO Executive Director's [sic] Report on Valley Secession Dated 4/19/02, May 14, 2002.

⁷⁶ Government Code section 57384.

⁷⁷ Public Financial Management, Inc., Hollywood Proposal for Special Reorganization Comprehensive Fiscal Analysis, March 6, 2002.

⁷⁸ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

The Executive Officer also recommends that the fiscal agent determine, on an annual basis, the amount of property tax revenue that must be remitted to pay Hollywood's share of the City's outstanding debt payments for that year, and that the remainder of the property tax revenue be retained by the new city.

The Executive Officer further recommends that the Commission only require the new city to advance funds to the City of Los Angeles for purposes of debt payments, and that the new city be authorized to deduct appropriate interest expense from any advanced funds. For any late payment made by the new city, the fiscal agent should add interest at a rate equal to the City's general pool investment yield to the disbursement made to the City.

Regarding the priority of payments to be made by the new city and its fiscal agent, the priority ranking should be debt payments to the City of Los Angeles, debt payments to the new city's creditors, fiscal mitigation payment, transition costs, transition period service reimbursement, and lastly the new city's direct operating costs.

BUDGETED GRANT FUNDS

The issue of the disposition of grant funding during the transition period was not analyzed for or addressed by the Subcommittee. Both the Applicant and the City of Los Angeles, however, have proposed terms and conditions on this issue.

The City of Los Angeles received approximately \$441 million in federal and state grant funds in fiscal year 2001-02 for job training, nutrition, poverty, anti-crime and other social programs.⁷⁹ In incomplete documentation of these grant funds, the City indicated that at least 69 percent of the funds were entitlement grants that the City receives on the basis of a funding formula. The remaining grants are competitive grants, for which the City has applied and competed with other municipalities.

Most of the grant funds are essentially pass-through funds which the City distributes to non-profit service organizations, some of which are located in Hollywood. With the exception of administrative fees and certain police services included in certain grant funds, most of the grant funds are not included in the City's budget and have not been allocated in the Comprehensive Fiscal Analysis. The CFA did allocate the \$1 million in budgeted grant funds to the proposed Hollywood city.⁸⁰ Given that these budgeted grant funds are related to entitlement grants, it is sensible to allocate the funds to the new city because the new city will eventually receive the funds directly from the granting agency.

In many cases, the new city will not directly receive grant funds until late in the transition period. The formula-driven grants rely on statistical data, and allocations are determined on an annual funding cycle. In the case of the U.S. Housing and Urban Development ("HUD") entitlement grants, the federal agency must compile data on Hollywood population, poverty and housing conditions in the fall of 2003 for entitlement grants funds that are distributed in April 2004. U.S. Department of Justice would require three past years of Hollywood crime statistics before allocating law enforcement related grants directly to Hollywood. The U.S. Department of Labor would require Hollywood data on mass layoffs, unemployment, and dislocated workers for purposes of allocating Workforce Investment Act funds to the new city. The California Department on Aging would require an updated agreement between the City and the County on the portion of the

⁷⁹ City of Los Angeles. Budget, Fiscal Year 2001-02, Modified and Adopted by the Council on June 6, 2001.

⁸⁰ Public Financial Management, Inc., Hollywood Proposal for Special Reorganization Comprehensive Fiscal Analysis, March 6, 2002.

population aged 60 and over in each area, before allocating the Hollywood share of funds to the County Area Agency on Aging.

For most of the transition period, the City of Los Angeles will continue to receive grant funds based on its size prior to special reorganization. Thus, the resolution making determinations should address the disposition of grant funds during the transition period.

The City of Los Angeles has proposed the following term relating to grants:

If the City has been awarded state, county or federal grant funds prior to the effective date of incorporation that must be used in the detached territory, the City will facilitate an amendment to its grant agreement with the granting agency, so that the moneys can be deleted from the City's grant agreement and the new city may enter into a direct grant agreement with the granting agency for use of those funds. The new city shall not be entitled to any other division or allocation of grant funds, and shall not be included within future City applications for, or allocation of, grant funds. Notwithstanding the above, any grant funds that may legally be expended within the boundaries of the City not including the territory encompassed in the new city, may, at the option of the City be used by the City within its boundaries, or the City may seek to amend its grant agreement to delete those funds as described earlier in this paragraph.⁸¹

The Applicant has proposed the following terms relating to grants:

The City of Los Angeles will provide a proportional and equitable share of existing and pending grant funding to the new Hollywood city. Grant funds received by the City of Los Angeles pursuant to applications that pre-date the effective date of the new Hollywood city will be allocated on a pro rata proportional and equitable basis to the new Hollywood city appropriately construed under the terms of the grant.⁸²

The draft resolution requires the City of Los Angeles to allocate budgeted grant funds to the new city during the transition period. The Executive Officer has reviewed the budgeted entitlement grants, and determined that the granting agencies are not likely to allocate funds directly to the new city during the transition period. Thus, the Executive Officer has recommended that in lieu of a direct allocation by the granting agencies or any other legal prohibitions or requirements, these grant funds be allocated to the new city during this interim period.

The City of Los Angeles has asked for clarification of the provision allowing the City to transfer funds directly to the fiscal agent or to credit the grant funds toward the transition period service cost. The provision requires the City of Los Angeles to transfer the appropriate share of budgeted grant funds directly to the third party fiscal agent, or to deduct the appropriate share of budgeted grant funds from the transition service cost invoice. This provision would allow the City to deduct the HUD grant administration allocation from the Community Development Department's cost of administering grants in Hollywood during the transition period.

⁸¹ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

⁸² Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

The City argued that HUD grant apportionments be determined by HUD formula rather than the proportion of low- and moderate-income households in Hollywood. The Executive Officer notes that at least 70 percent of HUD grant funds are required to benefit the low and moderate income population, and that any HUD directives on transition period grant allocations would, by the terms of the draft resolution, supercede the resolution.

The Executive Officer has assessed the likely timing of future grant receipts, and determined that the grant-related terms need only cover the transition period. The Executive Officer notes that the new city could receive HUD grants directly as early as April 2004, if it were to begin applying for grant funds soon after the effective date. Further, the resolution does not prevent the new city from contracting with the City of Los Angeles for grant administration services after the transition period.

The Applicant's proposal on grant allocations relates to competitive grants as well as entitlement grants, whereas the recommended provision in the resolution relates only to entitlement grants. The Executive Officer notes that the new city may appeal directly to granting agencies as to the appropriateness of a requirement that competitive grant funds be expended in Hollywood during the transition period.

The Executive Officer continues to recommend that the City of Los Angeles be required to allocate directly or through a credit towards the transition period service payment a proportionate share of budgeted entitlement grant funds unless and until the granting agencies direct otherwise.

OFF-BUDGET GRANT FUNDS

Most entitlement grant funds received by the City are excluded from the City's budget, because they are essentially pass-through funds allocated to non-profit social service providers. The draft resolution does not require the City of Los Angeles to transfer off-budget grant funds to the new city, but does require that the City of Los Angeles continue to provide social services through grant funds in the new city unless instructed otherwise by the granting agency.

The City of Los Angeles did not express opposition to this provision.

The Applicant's proposal that grant funds be shared relates to both competitive and entitlement grants. The off-budget grant provision in the draft resolution is not limited to entitlement grants, and requires the City of Los Angeles to continue to provide grant funding to social service providers in Hollywood throughout the transition period.

The resolution provision refers to grant funding during the transition period. The Executive Officer notes that the new city could apply for HUD entitlement grants for receipt in April 2004. The resolution does not prevent the new city from requesting grant allocation extensions from the granting agency directly, in the event that the granting agency is unable to allocate funds to the new city by the end of the transition period.

The Executive Officer recommends that the City of Los Angeles be required to maintain off-budget grant funding for social service providers located in Hollywood throughout the transition period. Any transition period grant allocation instructions by the granting agency would, by the terms of the draft resolution, supercede the resolution.

Executive Officer's Recommendation

The Commission should require the City of Los Angeles to either distribute Hollywood's share of budgeted grant funds to Hollywood or to extend a revenue credit to Hollywood for its share of grant funds that the City retains, unless and until the funds are distributed directly to the new city or

to the new agency distributing Hollywood grant funds. In lieu of a specific re-allocation of grant funding by the granting agency or other legal requirements, the Commission should require that grant funds be distributed in the manner set forth below.

For purposes of the HUD grants—Community Development Block Grant, HOME Investment Partnership Act, and Emergency Shelter Grant—the allocation for Hollywood should be based on the percent of the City low and moderate income households that reside in Hollywood. The reason for this simplification is that 70 percent of the HUD funds are required to be used for the benefit of the low- and moderate-income households.

In the case of the police-related grants—Local Law Enforcement Block Grant and Juvenile Accountability Incentive Block Grant, the City should be required to allocate a portion of grant funds to Hollywood based on population, or on the percent of city-wide Part I crimes that are committed in Hollywood. The City of Los Angeles should be required to share its crime data with Hollywood, and Hollywood should bear the cost of producing any data, such as Hollywood-specific crime data, needed to allocate the grant funds.

In the case of the Supplemental Law Enforcement Services Fund, Government Code section 30061-5 explicitly addresses how the funds should be distributed when a new city incorporates. In the case of the Older Americans Act grants like the Senior Citizen Nutrition Program, the City should be required to allocate a portion of the grant funds to Hollywood based on population aged 60 or more.

TRANSITION COSTS

COST OF ELECTIONS AND REDISTRICTING

Pursuant to Government Code section 57150(e), the City of Los Angeles and Hollywood are obligated to share the costs of the election on the question of special reorganization and selection of Hollywood city council members in proportion to the assessed value in those respective territories, if the Hollywood Special Reorganization is approved. If the voters reject special reorganization, the County of Los Angeles is obligated to bear these costs.

The Commission should also require that the City of Los Angeles, Hollywood and any other cities formed pursuant to these special reorganization proceedings be obligated to pay in proportionate shares based on assessed value the costs of redistricting the City of Los Angeles.

ACCOUNTING COSTS

The State Controller's Office found that the City's proposal to conduct revenue collection and separation and validation action for bond issuance on special taxes was reasonable, and that reasonable expenses for these transition costs along with redistricting related costs would be \$615,000.

The Commission should require that the Hollywood city and any other cities formed pursuant to these special reorganization proceedings pay in proportionate (assessed property value) shares the costs of producing City of Los Angeles financial statements effective December 31, 2002 (if the effective date is not July 1), establishing revenue collection procedures, analysis and separation of funds and outstanding debt and liabilities, preparation of a debt service schedule, and validation of pre-existing bonds.

OTHER TRANSITION COSTS

The City has also requested that Hollywood reimburse the City for a number of additional transition costs including the update of City maps, preparation of a transition plan, and processing quitclaims on easements for streets.

The City of Los Angeles Information Technology department has estimated that it needs to conduct a \$16 million assessment of the information systems. The manager of this department proposes that in order to administer a contract with a new city, the department would have to conduct a comprehensive assessment involving 147 person-years in total. The basis for this proposed transition cost is that it cost the City \$109 million to conduct its assessment of the City's information technology environment in preparation for January 1, 2000 (Y2K). The City proposes to negotiate a separate contract with the new city for each of 147 systems. These "critical" systems include the scheduling system in the mayor's office, a system for printing mailing labels, and a system for tracking property assessments in a Harbor area cemetery.⁸³

In its review of the CFA, the State Controller's Office dismissed the City's proposed one-time contract administration costs as unreasonable. "The City provided no justification to support which each critical system would require a separate contract or explain why each contract would require a person-year to negotiate, except to state that it was based upon past experience."⁸⁴

⁸³ California State Controller, California State Controller's Review of the Proposed Hollywood Special Reorganization Comprehensive Fiscal Analysis, May 2002.

⁸⁴ Id.

This issue raises concerns about the City of Los Angeles ability and incentives to contain transition costs to reasonable and necessary transition expenses.

The draft resolution includes a provision that imposes transition cost controls on the City of Los Angeles. The provision provides that the City of Los Angeles shall not be entitled to reimbursement for transition costs in excess of \$100,000 without the prior consent of the new cities.

The City of Los Angeles has argued that such consultation infringes upon the home rule authority of the City and will create unnecessary disputes. Further, “the City of Los Angeles has been forthright in identifying known transition costs at this time.”⁸⁵ While the City has identified categories of transition costs, the City has not identified all costs and certain estimates have been questioned.

The Executive Officer has defined the scope of reimbursable transition costs to include copying records and data, costs related to employee transfers, recording deeds for property transfers, street easement quitclaim processing, accounting costs, information technology and computer reprogramming, and other similar one-time costs related to the special reorganization. However, given that there may be unknown costs involved and given the fact that the new cities will have to bear the burden of these costs, it is reasonable to require the City of Los Angeles to inform and obtain the concurrence of the new cities with respect to these costs.

Executive Officer’s Recommendation

The Commission should require parties to pay for the costs of elections, redistricting the City of Los Angeles, the enumerated accounting costs, and other transition costs as set forth above. Further, the Executive Officer recommends that the City of Los Angeles to consult with the new city prior to incurring any of these enumerated transition costs in excess of \$100,000.

⁸⁵ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

FISCAL MITIGATION

BACKGROUND

Government Code section 56815 prohibits the Commission from approving a proposal that includes an incorporation unless it finds that the following are substantially equal:

- (c) revenues currently received by the agency transferring the affected territory which would accrue to the local agency receiving the affected territory; and
- (d) expenditures, including direct and indirect expenditures currently made by the local agency transferring the affected territory for those services that will be assumed by the local agency receiving the affected territory.

If these amounts are not substantially equal, the Commission may only approve a proposal if it finds that: (1) the county and all other subject agencies agree, or (2) the negative fiscal effect of the incorporation is adequately mitigated by tax sharing agreements, lump sum payments, payments over a fixed period of time, or other terms and conditions imposed by the Commission.⁸⁶

The CFA contains an analysis of the “revenue neutrality” test set forth above, and concludes that the Hollywood Special Reorganization would not meet the revenue neutrality test because Hollywood currently generates more in revenue than the City of Los Angeles currently expends in providing the services that would transfer to the proposed Hollywood city. As such the Commission can only approve the proposed Hollywood Special Reorganization with the agreement of the County and the City of Los Angeles, or if it finds that the negative fiscal effect of the proposal has been adequately mitigated.

Seven California incorporations have occurred since this “revenue neutrality” test was added by the Legislature in 1992. In the first two cases of Truckee and Citrus Heights, the relevant LAFCO placed related mitigation measures in the terms and conditions, but in neither case were the mitigation measures followed after incorporation. Subsequently, it has become standard practice for the parties to negotiate mitigation terms and for these mutually agreeable terms to be attached to the resolution making determinations, and imposed as a term and condition of the incorporation.

Since the parties have not negotiated such an agreement, the Commission must develop terms that adequately mitigate the negative fiscal effect before it can approve the special reorganization.

MITIGATION PAYMENT

The Executive Officer recommends that the mitigation payment should be \$21.3 million. For further discussion of the establishment of the fiscal mitigation payment, see the Fiscal Findings section of this Report and the Appendix tables with the Executive Officer’s Fiscal Allocations.

MITIGATION TERM

Government Code section 56815(c)(2) provides that mitigation may take the form of tax sharing agreements, lump sum payments, payments over a fixed period of time or any other terms and conditions imposed pursuant to Government Code section 56886. The Applicant has proposed a mitigation payment made over a term no longer than 10 years.⁸⁷ The City of Los Angeles has

⁸⁶ Government Code section 56815(c).

⁸⁷ Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

proposed a mitigation payment made on a monthly basis over a period of 25 years.⁸⁸ In past California incorporations, the mitigation payment term has been set at a 10 to 25-year length through negotiations between the respective county and cityhood proponents.

For Goleta, Santa Barbara County established two tax-sharing agreements--one for a ten-year mitigation term and another in perpetuity. Orange County has previously calculated the mitigation liability initially based on a 14-year term, and then compressed the actual payments into the first seven years following incorporation. Sacramento County has required a relatively long mitigation term of 25 years, with rapid phase-out of the payment during the final five years of the term.

California Incorporation Mitigation Term	
City	Years
Goleta	10 years/Perpetuity
Aliso Viejo	14 years
Elk Grove	25 years
Rancho Santa Margarita	14 years
Laguna Woods	14 years
Citrus Heights	25 years

With mitigation payments owed over a multi-year period, the issues of inflation and present value must be addressed. In the case of Goleta, Elk Grove and Citrus Heights, the mitigation obligation was calculated as a share of the new city’s revenues. The revenue-sharing approach addresses the problem of inflation eroding the value of the mitigation payment over time. In the case of the Orange County cities, the mitigation obligation was calculated as an annual dollar amount that increases with expected inflation as well as an additional factor representing expected borrowing costs. The Orange County cities were not expected to make a mitigation payment in the initial transition year.

Three approaches are presented in this Report for calculating the mitigation payment. In all three cases, the mitigation liability for each year has been adjusted for expected inflation of 2.5 percent, including expected inflation occurring between the CFA base year and the effective date.⁸⁹ In all three cases, the calculations assume that Hollywood would make a pro-rated mitigation payment during the first partial fiscal year, and that mitigation payments would be due to the City of Los Angeles by the last day of the respective fiscal year.

The recommended alternative structures the mitigation payment as a twenty-year payment with a gradual phase-out. This approach is based in part on the Elk Grove mitigation payment that was structured to gradually reduce the County’s reliance on the mitigation payment.⁹⁰ Under the recommended approach, the mitigation payment would be discounted by five percent annually beginning in the first full fiscal year following incorporation. This five percent phase-out rate is less than the City of Los Angeles’ staff attrition rate (7 percent), implying that the City of Los Angeles could adjust to the financial effect of Hollywood’s departure without laying off City workers. By the year 2022, Hollywood would make its final payment, which would be only 5 percent of the inflation-

⁸⁸ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

⁸⁹ U.S. Congressional Budget Office, *The Budget and Economic Outlook, Fiscal Years 2003-2012*, January 31, 2002.

⁹⁰ Elk Grove initially paid Sacramento County 90 percent of its property tax revenues, with the share declining by 5 percent every five years, and in the 19th year being phased out at a rate of 10 percent annually.

adjusted estimate in the CFA. The present value of the payment stream that would be made under this approach is \$191 million.⁹¹ The Subcommittee recommended this approach.⁹²

An alternate approach structures the mitigation payment over a ten year term. Under this approach, Hollywood would pay annually an amount equivalent to the CFA estimate with adjustments made for expected inflation. Hollywood would make a pro-rated half-year payment in its eleventh year. The present value of the payment stream under this approach is \$190 million.

Another alternative follows the City's proposal for a 25-year term to the mitigation payment with inflation adjustments and without any phase-out.⁹³ The present value of the 25 years of payments would be \$395 million.

Present Value of Mitigation Payment Streams Under Three Alternative Scenarios			
Term	20-year Phase-Out	10-year term	25-Year Term
20-Year	\$ 190,812,086	\$ 189,803,791	\$ 335,457,816
25-Year	\$ 190,812,086	\$ 189,803,791	\$ 395,038,444

Notes:
 (1) Inflation (2.5%) adjustment based on U.S. Congressional Budget Office forecast
 (2) Present value calculation based on ten-year Treasury security (constant maturity) yield rate of 5.25% on April 8, 2002.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation (with elaboration regarding inflation), the Commission should establish a mitigation payment amount and term in the following fashion:

- 1) the mitigation payment should be based on the staff-adjusted CFA estimate, adjusted over the term on an annual basis for actual inflation, as measured by the Consumer Price Index (CPI-U) for the Los Angeles metropolitan area, that occurred between January 2001 and January of that particular fiscal year; and
- 2) the mitigation payment should be discounted by a factor of five percent annually in a cumulative fashion, so as to completely phase out the mitigation payment after June 30, 2022.

For purposes of making provisional monthly fiscal mitigation payments, the new city should use the California Department of Finance forecasts of the Consumer Price Index for the Los Angeles area. Once the actual inflation data are available, the new city should adjust its next payment for any overpayment or underpayment made due to differences between the forecast and the actual inflation.

⁹¹ Present value calculations provide a method of comparing the value of a future stream of payments in today's dollars. Present value is calculated based on the yield rate for ten-year Treasury notes at constant maturity, as valued on April 8, 2002.

⁹² *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

⁹³ City of Los Angeles, *Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions*, April 2, 2002.

EMPLOYEES

Government Code section 56888 requires that collective bargaining agreements continue to be honored by the City of Los Angeles and a new city for the balance of the term, and that existing retirement benefits be maintained. Consistent with these restrictions, the Commission may impose conditions involving the employment, transfer, or discharge of employees, civil service rights, seniority rights, retirement rights, and other employee benefits and rights.⁹⁴

The resolution includes two provisions relating to employees. With respect to employee transfers, both the City of Los Angeles and the new city are required to comply with the provisions of Government Code section 56888. This requires the parties to honor collective bargaining agreements, and existing retirement benefits, and to meet and confer with the unions representing any transferred employees. More specifically the statute requires the following:

- a. All public employees to which Chapter 10 (commencing with Section 3500) of Division 4 of Title 1 applies shall continue to be deemed public employees of the original local agency or of the newly incorporated local agency for all the purposes of that chapter, including, but not limited to, the continuation and application of any collective bargaining agreement that applies to these employees, and all representational and collective bargaining rights under that chapter.
- b. Any existing collective bargaining agreement shall remain in effect and be fully binding on the original local agency or on the newly incorporated local agency, and on the employee organizations that are parties to the agreement for the balance of the term of the agreement, and until a subsequent agreement has been established.
- c. Any existing retiree benefits, including, but not limited to, health, dental, and vision care benefits, shall not be diminished.
- d. Notwithstanding any other provision of law, an employee organization that has been recognized as the exclusive representative of local agency public employees affected by a special reorganization shall retain exclusive representation of the unit employees of the original local agency, or of the newly incorporated local agency.

The City of Los Angeles has proposed that the new city pay for accrued vacation and sick leave of transferred employees. The Executive Officer notes that it is unnecessary to “cash out” the compensated time off of transferred employees. In order to accommodate this need, the new city shall accept responsibility and liability for accrued vacation, sick leave and other compensated time-off for City of Los Angeles employees who transfer to the new city as part of a transfer in service responsibility from the City of Los Angeles to the new city.

The City of Los Angeles has noted that the resolution does not provide a solution to mitigate fiscal harm to sworn Police and Fire employees who are not vested in the pension system. The Executive Officer notes that the City of Los Angeles has the power to prevent fiscal harm to unvested police officers and firefighters by amending its charter to allow the new city to participate in the City of Los Angeles Fire & Police Pension Fund.

⁹⁴ Government Code section 56886(l)

The Executive Officer recommends that the City of Los Angeles be allowed to resolve the pension portability problem for police officers and fire fighters, and recommends against the Commission imposing a term and condition on this matter.

The Applicant proposed that the Commission require the new city to honor the bumping rights, job certification list standing, and transfer rights of any employees who transfer from the City of Los Angeles to the new city. The Executive Officer considers this policy decision to be an appropriate decision of the elected officials of the new city.

ASSETS

With regard to assets of the City of Los Angeles, the Applicant has consistently asserted its position that the people of the City of Los Angeles are "shareholders" in all of the City's assets, and entitled to an equitable interest in all of the City's assets, facilities, etc. Generally speaking, the Applicant seeks a transfer of all assets located within the Hollywood Special Reorganization area, as well as a proportional interest or joint ownership of centralized assets.⁹⁵

The City of Los Angeles contends that there are constitutional constraints to the transfer of property held by a municipal corporation in its proprietary capacity. The City has asserted that municipal corporations hold property in their proprietary capacity in the same manner and with the same rights as private persons holding property, and based thereon, the California Constitution prohibits the State from taking such property without just compensation or the consent of the City. The City further asserts that the constitutional protections afforded the City's property is strengthened by the City's status as a charter city.⁹⁶

With respect to assets, the Commission has received differing legal opinions regarding the Commission's authority to transfer assets. The legal opinion of the County of Los Angeles Office of the County Counsel ("County Counsel"), the Commission's legal advisor, concluded that the Commission could only transfer proprietary assets of the City of Los Angeles subject to the payment of compensation or consent of the City, but could transfer assets held subject to a public trust without compensation.⁹⁷ The legal opinion of the California Legislative Counsel ("Legislative Counsel") concluded that the Commission has the discretion to allocate assets either with or without compensation.⁹⁸

To the extent that these opinions conflict with respect to the manner in which the Commission may handle the transfer of assets, staff provided dual recommendations for the Subcommittee's consideration. Where there was no conflict in the legal opinions or where, because of other considerations, staff recommended a particular course of action, only one recommendation was provided to the Subcommittee.

LEGAL OPINIONS

The County Counsel's legal opinion concluded that the Commission was not authorized to transfer proprietary property of the City of Los Angeles to a Hollywood city without compensation or the consent of the existing city. The County Counsel concluded, however, that assets held pursuant to a public trust, such as pueblo lands, roads, highways, donated parks and donated libraries, may be transferred without compensation.

The Legislative Counsel's legal opinion concluded that the Commission has the discretion to order a transfer of assets from the City of Los Angeles to a proposed new city as a condition of approving a special reorganization, with or without compensation. The Legislative Counsel believes that it was the intent of the Legislature to leave the decision as to whether or not to require compensation to

⁹⁵ Hollywood Vote, Inc. Hollywood City—List of Assets. Correspondence from Hollywood Vote Chairman Gene La Pietra to LAFCO Executive Officer Larry J. Calemine, May 1, 2002. Hollywood Vote, Inc. *Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis*, October 1, 2001.

⁹⁶ City of Los Angeles, Office of City Attorney, Opinion letter, dated November 13, 2001.

⁹⁷ County of Los Angeles, Office of the County Counsel, Authority to Require the Transfer of Assets as Terms and Conditions of the Proposed Special Reorganizations, November 21, 2001.

⁹⁸ California Legislative Counsel Opinion No. 128, *Special Reorganizations: Division of Assets*, January 8, 2002.

the Commission, and did not identify any constitutional restrictions on the Commission's authority to transfer assets without compensation.

PRECEDENTS

California LAFCOs have approached the transfer of assets in various ways. In looking at precedent cases, it is important to be mindful of whether or not there were any county-owned assets for providing purely local municipal services located in the incorporating areas, as well as the likelihood that the new jurisdiction would be directly providing those services for which those county-owned assets had been used.

In all cases of which we are aware, local streets and highways have transferred from the county to the newly incorporated city on the effective date pursuant to the Streets & Highways Code section 989, and Government Code section 57385. Although the streets automatically transfer, the Code does not explicitly state whether streetlights, traffic signals and the storm water and wastewater infrastructure beneath the streets should be transferred. In recent incorporations, Orange County has explicitly added that streetlights, local storm drain facilities and related easements transfer to the new city.

This Commission did not transfer any county assets or liabilities to Calabasas, Malibu or Santa Clarita when these cities incorporated. In the case of Malibu, the incorporation proponents requested transfer of the County's civic center building in Malibu; however, the Commission did not transfer this building. The City of Malibu has acquired use of portions of the building through a lease arrangement with the County.

The practices in other counties have varied. Sacramento LAFCO has not included any asset transfers (with or without compensation) in the resolutions for Citrus Heights or Elk Grove. In these areas, the county assets in the territories prior to incorporation primarily involved sheriff and fire stations. The new cities have continued to rely on the county for contract sheriff and fire services. San Bernardino LAFCO has transferred only the assets of dissolved county service areas to new cities.

Riverside County LAFCO placed all public facilities, land and fees into a trust fund, with the proviso that the parties negotiate a settlement of the assets following incorporation.

Parks and local storm water drainage facilities have been transferred from the county to the new cities in several incorporations. Sonoma, Santa Barbara and Orange County LAFCOs have transferred local parks and local storm water drainage facilities from the county to the new cities. In the case of Goleta, the asset transfer included in a written agreement between the county and the proponents, usually the transfer of such assets has been included only in the LAFCO resolution.

We are not aware of any incorporation where a transfer of county-owned assets was imposed by a LAFCO, and the county objected to the transfer.

TRUST ACCOUNT FUNDS & LIQUID ASSETS

Trust account funds, which are funds held by the City of Los Angeles in trust for location-specific uses, include development impact fees, development agreement funds, project-appropriated Capital Improvement Expenditure Program ("CIEP") funds⁹⁹, and Quimby fees (parkland dedication in lieu

⁹⁹ CIEP funds are for street maintenance, street lighting, wastewater, storm water and transportation projects; these funds are generated by gas tax, wastewater fees, Proposition C funds and transfers from the City's general fund.

fees). Liquid assets include fund balances in the City's general fund and 50-plus special purpose funds.

In terms of precedent, the Santa Barbara and Sacramento County LAFCOs have also transferred impact fees to new cities.

The Applicant has generally proposed that all cash assets be proportionally and equitably transferred. The Applicant has proposed the following term and condition:

Cash assets and receivables associated with allocated services will be allocated proportionally and equitably to those transferred services. Other cash assets and receivables will be allocated proportionally and equitably to population. Impact fee and other trust accounts dedicated to Hollywood purposes will be proportionally and equitably transferred. In any case, the new Hollywood City shall be entitled to a proportional and equitable share of all financial accounts, investments, reserves and cash assets.

The City of Los Angeles has proposed the following term and condition:

The City shall transfer to the new city impact fees and other special fees collected prior to the incorporation that are obligated to be used solely in the territory of the new city for construction of specific facilities or improvements, or the delivery of specific services, not yet constructed or delivered. The new city shall be required to expend those moneys for the original purposes for which the fees were collected, and shall be bound by all legal obligations with respect to use of the money that would otherwise bind the City, including but not limited to, time limits, if any, in which to expend the money, or obligations to refund unexpended fees. The transfer of fees shall not toll any time limits in which to expend the moneys. The new city shall indemnify and hold harmless the City from any actions alleging improper use of these moneys.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the transfer of trust account fund balances for projects specific to the Hollywood Special Reorganization area, and any unexpended general fund balances (including reserves) and special fund balances, except as set forth below.¹⁰⁰

Any general fund balances should transfer on the effective date to the third party fiscal agent in proportion to Hollywood's past general fund contributions (4.90 percent), as estimated by the Commission. Any special fund balances should transfer on the effective date to the third party fiscal agent in proportion to Hollywood's past revenue contributions to that fund, as estimated by the CFA. It is not recommended that the following special fund balances transfer, unless there is an agreement of the parties to transfer, because it is anticipated that the City of Los Angeles will retain control of the facilities that these funds support:

- Water Revenue Fund
- Power Revenue Fund

¹⁰⁰ Minutes of the Meeting of the Local Agency Formation Commission of the County of Los Angeles Findings, Terms & Conditions Subcommittee, February 25, 2002.

- Sewer Construction & Maintenance Fund
- Convention Center Revenue Fund
- Zoo Enterprise Trust Fund
- Special Police Communications/911 System Tax Fund
- City Employees Retirement Fund
- Fire and Police Pension Fund
- El Pueblo de Los Angeles Historical Monument Revenue Fund
- Staples Arena Special Fund
- Airport Revenue Fund
- Harbor Revenue Fund
- Tax and Revenue Anticipation Note Proceeds and Debt Service Funds, and
- Bond Redemption & Interest Funds.

The City of Los Angeles requested that fund balances available for transfer be defined as the fund balance net of reversions, required re-appropriations, outstanding loans and encumbrances. The draft resolution allocates fund balances net of outstanding loans, encumbrances and re-appropriations required for capital improvements.

The Executive Officer further recommends that the Commission require the new city to expend those impact fees and other special fees transferred for the original purposes for which the fees were collected, and be bound by all legal obligations with respect to use of those monies that would otherwise bind the City of Los Angeles, including but not limited to, time limits, if any, in which to expend the money, or obligations to refund unexpended fees. The new city should be required to indemnify and hold harmless the City from any actions alleging improper use of these moneys.

LOCAL SERVICE-RELATED ASSETS

Both the City of Los Angeles and the Applicant have agreed in principal that local assets related to municipal service provision that are located in Hollywood could transfer to the new city as an overall resolution of special reorganization issues, including transition period service costs, and debts and liabilities. The Applicant has proposed that a specific list of Hollywood facilities would transfer (see Appendix for facilities listing).¹⁰¹ The parties do not agree about the timing of the asset transfer. The City of Los Angeles has proposed that the assets transfer only after the transition period and after Hollywood has met several conditions, whereas the Applicant proposes that the property transfer to Hollywood on the effective date. The Applicant has explicitly proposed that such assets include buildings, infrastructure, furniture, equipment, vehicles and other assets “which substantially support the provision of municipal service to the new city”.¹⁰²

The City of Los Angeles has proposed the following term and condition:

Those local assets (e.g., parks, libraries) owned by the City located in the new city and as listed in appendix B shall be transferred to the new city without compensation when all of the following have occurred: (a) the transition period has ended, (b) the new city is not in default on any of its obligations under this resolution, and (c) the City and the new city have entered into an agreement which satisfies the City that

¹⁰¹ Hollywood Vote, Inc. City-Owned Properties in the City of Hollywood Proposed Boundaries, May 1, 2002.

¹⁰² Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

mechanisms are in place to guaranty [sic] that the new city will be able to meet all of its obligations to the City, including but not limited to, the mitigation payment, debt service and liability payments, service costs, and transition costs. No assets, property, rights of way, easements or other property interests related to operation of the water system, power system, wastewater system, and communications or other centralized systems will be transferred.¹⁰³

The Applicant has itemized the properties and buildings that it proposes would transfer to Hollywood, and has proposed the following terms and conditions:

All local physical assets as defined herein, including but not limited to distributed infrastructure such as streets, sidewalks, signage, localized structures, buildings, land, libraries, parks, police, fire and other facilities, infrastructure improvements, furniture, equipment, and vehicles and fungible assets, owned by the city of Los Angeles will be transferred to the new Hollywood City without adjustment as of the Effective Date. Local Hollywood physical assets will be those assets that are located within the new Hollywood City boundaries and which substantially support the provision of municipal services to the new Hollywood City. Fungible assets including furniture, equipment and vehicles, etc., will be distributed based on location where such items are utilized or deployed when necessary equitably and fairly by[sic] classed by age and condition of such items.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the transfer of title to all service-related local assets (itemized in Appendix Exhibit B) on the effective date without compensation. During the transition period, the City of Los Angeles should be entitled to use service-related assets, at no cost, for the provision of services to Hollywood.¹⁰⁴

LEASES

Certain facilities used by the City of Los Angeles are leased from another owner. The City leases temporary office space and certain other facilities. For example, most of the council members' district offices are leased from private parties. Some facilities are leased from the City's enterprise departments, the state of California, and other public sector agencies.

The City of Los Angeles has proposed the following term and condition:

Subject to the consent of the lessor or terms of the lease, the City, at its option, may terminate any existing leases that the City no longer needs for the provision of services in the area detached from the City, or assign the lease to the new city, which shall accept the lease. Should the new city not accept the lease, any costs incurred by

¹⁰³City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁰⁴ Minutes of the Meeting of the Local Agency Formation Commission of the County of Los Angeles Findings, Terms & Conditions Subcommittee, March 25, 2002.

the City as a result thereof shall be treated as transition costs and reimbursed in accordance with paragraph 2.¹⁰⁵

The Applicant has proposed:

All leasehold interests of property, facilities, equipment, etc., that are located within the new Hollywood City boundaries and meet the definition set forth for local physical assets will be transferred to the new Hollywood City as of the Effective Date.

Executive Officer's Recommendation

The new city should be entitled to assume existing leases of the City of Los Angeles within the special reorganization area, at the option of the new city and with the consent of the lessor, if any consent is required, without the payment of compensation to the City of Los Angeles.

STREETS AND HIGHWAYS

In annexations and incorporations of previously unincorporated territory, the streets and highways transfer to the new jurisdiction.¹⁰⁶ Cities hold street and highway rights of way dedicated for public use as a public trust. As a public trust, these rights of way are typically transferred to whatever local entity has jurisdiction over the territory in which they are located. LAFCOs typically transfer the streets and highways without defining which street-related assets would transfer. In the Rancho Santa Margarita incorporation, the Orange County LAFCO transferred public roads, bridges, adjacent slopes, streetlights, traffic signals and any appurtenant slopes, sidewalks, trails, landscaped areas, medians and other adjacent property.

In addition to the street infrastructure, the rights of way contain wastewater, water, power and communications pipes, cables, and lines. The new city will have the power to confer utility franchises for utility improvements within the rights of way. Local government agencies typically negotiate franchise agreements with utility providers that allow a utility company to use the rights of way in exchange for franchise fees.

Beneath the streets lie both local sewer pipes and the major sewer pipes conveying sewage to treatment plants. The local sewer pipes constitute the wastewater collection system, and are typically owned by the city in which they are located. The two regional wastewater systems—the City of Los Angeles and County Sanitation District—process almost all of the Los Angeles area wastewater. The regional systems own and maintain the larger sewer pipes, also known as trunk lines and outfalls, inside and outside the cities. The cities own the local sewers—the collection system of sewer pipes that connect into the trunk lines—and are responsible for maintaining local sewers, issuing sewer permits, and billing sewer customers. If the City of Los Angeles were to retain the local wastewater collection system in Hollywood, it would be a unique arrangement. However, the City has requested that it retain ownership of these local assets, and the Applicant is amenable to continued City of Los Angeles ownership of the wastewater collection system at least until the outstanding bonded indebtedness associated with the system is retired. The wastewater system and other public utility systems operated by the City of Los Angeles will be addressed in the Enterprises section of this Report.

¹⁰⁵ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁰⁶ Streets & Highways Code section 989, Government Code sections 57329, 57385.

Additional City of Los Angeles communications assets may also lie beneath the streets in Hollywood. Such assets may include fiber optic cabling for computer networking. The City has not adequately identified its “communications or other centralized systems” that the City proposes to retain.

The City of Los Angeles has proposed the following term and condition:

Upon incorporation the new city shall receive real property interests in roads and highways owned by the City within the incorporated area, except the City [of Los Angeles] shall retain title to all assets, property, rights of way, easements, and other property interests (including, but not limited to, those that may be on, under, or adjacent to those roads and highways) related to operation of the water system, power system, wastewater system, and communications or other centralized systems.¹⁰⁷

The Applicant has proposed the following term and condition:

All local physical assets...including streets, sidewalks, signage, land, infrastructure improvements...owned by the City of Los Angeles will be transferred to the new Hollywood City without adjustment as of the Effective Date.

Executive Officer’s Recommendation

Consistent with the Subcommittee’s recommendation, the Commission should impose the following term and condition:

Upon the effective date of incorporation, all right, title, interest and responsibility for any and all public roads, adjacent slopes, medians, sidewalks, trails, bikeways, landscaped areas, open space, street lights, signals, and bridges located within the boundaries of the special reorganization area shall vest in the new city, except that the City of Los Angeles shall retain title to all assets, property, rights of way, easements, and other property interests (including, but not limited to, those that may be on, under, or adjacent to those roads and highways) related to operation of the water system, power system, wastewater system, and communications or other centralized systems.¹⁰⁸

The wastewater system will be addressed in the Enterprises section of this Report.

STORM WATER FACILITIES

The Orange County LAFCO has transferred local storm drain facilities to new cities. In the Rancho Santa Margarita resolution, drainage devices, storm drain channels, and appurtenant facilities, site drainage and all storm drain facilities were transferred to the new city.

The City of Los Angeles has proposed the following term and condition:

Storm drains owned in fee by the City and storm drain easements owned by the City that are located in the incorporated area shall be transferred to the new city. The new city shall obtain its own MS4 permit or other necessary permit from the California

¹⁰⁷ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁰⁸ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

Regional Water Quality Control Board in order to discharge into the waters of the United States.¹⁰⁹

Executive Officer's Recommendation

Storm drain facilities in the Hollywood Special Reorganization area should transfer to the new city.

INTANGIBLE ASSETS

The Applicant has also proposed that:

The new Hollywood City will be entitled to a proportional and equitable share, a geographically relevant share, and/or duplicate copies of all intangible informational and intellectual assets or property maintained by the city including but not limited to databases, maps, records, GIS files, intellectual property and administrative methodologies. This shall include licenses, rights, and access to relevant records and files.

The Subcommittee recommended such a provision.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should impose Executive Officer recommends a provision that requires such transfers, if consistent with the City's contractual and licensing agreements.

MISCELLANEOUS ASSETS

Certain assets have not been explicitly addressed elsewhere by the parties or not identified, such as City passenger buses and sanitation equipment used to service the Hollywood Special Reorganization area, should be subject to transfer. The Valley proposed a catch-all provision that would transfer miscellaneous assets of this sort.

The City of Los Angeles proposed that specific assets that transfer should be listed in the resolution making determinations; however, the City has not provided any such listing for miscellaneous equipment, rolling stock, and databases. The Subcommittee recommended a miscellaneous asset provision.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should transfer easements on the basis of functional association with other transferred assets, and adopt a provision transferring, without compensation, all other assets owned by the City of Los Angeles and located within the Hollywood Special Reorganization area, but not transferred or excluded from transfer elsewhere in the resolution.¹¹⁰

¹⁰⁹ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹¹⁰ Minutes of the Meeting of the Local Agency Formation Commission of the County of Los Angeles Findings, Terms & Conditions Subcommittee, March 25, 2002.

ENTERPRISES

City of Los Angeles enterprises include the Department of Water and Power (“DWP”), the airport system (Los Angeles World Airports), and the Port of Los Angeles (the “Port”), in addition to the City’s wastewater treatment infrastructure.

In general, the City of Los Angeles has proposed that it retain the assets under the control of the Departments of Airports, Harbor, and Water and Power, along with ownership and control of the wastewater system.¹¹¹ The Applicant has proposed that the Commission transfer a proportional undivided interest in the Department of Water and Power, the wastewater system, airports, transit, Port of Los Angeles and the zoo.¹¹²

UTILITIES

The City of Los Angeles municipal utilities include water service, power service, and wastewater disposal and treatment service. The DWP provides both water and power service, while the City’s Department of Public Works provides wastewater services.

The City of Los Angeles has proposed that it retain ownership and control over the water, power and wastewater systems. Further, the City has proposed that it be explicitly allowed to impose wastewater fees and regulate industrial wastewater dischargers located in Hollywood.¹¹³ The Applicant has proposed that it receive an undivided proportional interest in these systems and, barring such an arrangement, that the City of Los Angeles be obligated to provide utility services to Hollywood residents at the same rates that the City charges its own residents.

The Commission lacks the authority to impose a joint powers authority arrangement for joint ownership of the utilities because a joint powers authority must be formed by at least two existing public entities, and the proposed city has not yet been formed. Joint ownership might also be achieved by forming a utility district encompassing the territory of the City of Los Angeles, as it now exists, including any cities to be formed pursuant to special reorganization. Depending on the type of district proposed, formation must be initiated by the public entities involved or it must be initiated by petition. For instance, pursuant to the Municipal Utility District Act, formation proceedings must be initiated by resolution of the public agencies involved or by petition signed by ten percent of the registered voters.¹¹⁴ The Applicant cannot comply with the first means of initiation because the proposed new city has not been formed and the City of Los Angeles has not agreed to the formation of such a district. Neither has the Applicant complied with the second means of initiation, because it has not submitted a petition for the formation of such a district signed by ten percent of the registered voters. Other types of districts would likely have similar initiation requirements.

It also appears that the Commission may not have the authority to transfer utility assets because the City has constitutional and statutory rights to own and operate public utilities, and any transfer of

¹¹¹ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹¹² Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

¹¹³ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹¹⁴ Public Utilities Code sections 11581, 11641.

such assets may be subject instead to the requirements of the Public Utilities Code.¹¹⁵ This would also include the wastewater collection system discussed under the Streets and Highways section of this Report.

The City of Los Angeles continues to object to a resolution provision that prevents the City of Los Angeles from charging higher utility rates to Hollywood customers than it would charge equivalent customers in the remaining City of Los Angeles. This provision does not involve utility rate-setting on the part of LAFCO and does not prevent the City from recouping its costs of providing utility service.

The City of Los Angeles objects to the resolution provision and alleges that it would require ratepayers in the remaining City to subsidize ratepayers in Hollywood through payment of a DWP franchise fee in Hollywood. The Executive Officer acknowledges that if Hollywood imposes a franchise fee on utility usage, that would limit the City of Los Angeles “Power Revenue Transfer” fee imposed on Hollywood ratepayers to no more than two percent less than the corresponding fee charged to ratepayers in the remaining City of Los Angeles. The Executive Officer does not concur with the City’s conclusion that ratepayers in the remaining City would subsidize Hollywood ratepayers. In fact, the provision does not prevent the City from continuing to impose “Power Revenue Transfer” charges on Hollywood ratepayers, thus Hollywood ratepayers would be effectively subsidizing the City of Los Angeles general fund.

Executive Officer’s Recommendation

Consistent with the Subcommittee’s recommendation, the Commission should not transfer any public utility assets to the new city.¹¹⁶ It is recommended that these integrated systems remain under single ownership and that the Commission, instead, fashion terms and conditions that will ensure that Hollywood customers continue to be provided the same level of service at the same rates as City of Los Angeles customers.

In addition, it is recommended that the Commission adopt the City’s proposed condition authorizing the City to continue to impose fees and charges related to operation of the wastewater system and to regulate industrial dischargers.

Utility Service

As the owner of these public utility systems, the City of Los Angeles would be obligated to continue to provide public utility services to Hollywood in the event of special reorganization. The City of Los Angeles has proposed that utility customers in the new city be required to remain customers of the City of Los Angeles until the existing utility debt has been repaid. The City of Los Angeles currently has long-term debt that is scheduled to reach maturity in 2042 for water service¹¹⁷ and 2028 for wastewater service.¹¹⁸ The long-term debt for power service is scheduled to reach maturity in 2032¹¹⁹ after the termination of existing take-or-pay obligations.¹²⁰

¹¹⁵ Cal. Const., Art. XI, § 9(a), Public Utilities Code section 10052, *et seq.*

¹¹⁶ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹¹⁷ Water Services, Department of Water and Power, City of Los Angeles, *Report and Financial Statements*, June 30, 2001.

¹¹⁸ Official Statement, Los Angeles Wastewater System Revenue Bonds, Refunding Series 1999-A, January 26, 1999.

¹¹⁹ Energy Services, Department of Water and Power, City of Los Angeles, *Report and Financial Statements*, June 30, 2001.

¹²⁰ City of Los Angeles, Office of Administrative and Research Services, *City Response to LAFCO Regarding Valley Secession Proposal and Initial Fiscal Analysis*, June 13, 2001.

As part of the transfer of streets and highways, the rights of way in the Hollywood Special Reorganization area would be transferred to the new city. With control of the rights of way, the new city may grant a franchise to utility providers to use those rights of way for the purpose of providing utility service.

Local governments typically grant utility franchises for fixed terms of 15 to 60 years. The local government agency typically negotiates a franchise agreement whereby a utility company is authorized to use its rights of way in exchange for franchise fees. The County of Los Angeles has 20 separate water franchise agreements for its unincorporated areas, most of which are 25-year non-exclusive agreements. In the case of power, Sempra (Southern California Edison) has non-exclusive franchise agreements with the County of Los Angeles and the City of Long Beach for 50 and 60-year terms respectively. Within the County of Los Angeles, an exclusive franchise agreement may only be granted subsequent to a competitive bid process.

Executive Officer's Recommendations

Consistent with the Subcommittee's recommendation, the Commission should require that the City of Los Angeles continue to provide water and power public utility service to customers located in the new city and require that the new city protect the rights of DWP bond-holders by adopting agreements for water and power with the City of Los Angeles for terms that end no sooner than the latest maturity date of bonded indebtedness for debt issued prior to the effective date.¹²¹

Consistent with the Subcommittee's recommendation, the Commission should also require that the City of Los Angeles continue to provide wastewater collection and treatment service to customers located in the new city and that the new city protect the rights of wastewater system bond-holders by adopting an agreement for wastewater services with the City of Los Angeles for a term that ends no sooner than the latest maturity date of bonded indebtedness for debt issued prior to the effective date.¹²²

Utility Rates

The City of Los Angeles has indicated that it could charge customers in the new city a premium for water usage that reflects the differential between the cost of water purchased from the Metropolitan Water District and the cost of Los Angeles Aqueduct water.¹²³ The City contends that it should be permitted to set justifiable rate differentials restricted only by the legal standards set forth in case law. Legal Counsel has advised, however, that Commission has the authority to impose terms and conditions regarding rates.¹²⁴ Given that it is recommended that the City of Los Angeles retain full ownership of its public utility assets and that the new city's residents remain customers of the DWP at least until the latest maturity date of the DWP's bonded indebtedness, those customers should be provided some rate protection. The Commission may do so without restricting the City's ability to raise rates to meet changing circumstances by requiring that the DWP charge the same rates within both cities, as it does presently in those territories.

¹²¹ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹²² *Id.*

¹²³ City of Los Angeles, Office of Administrative and Research Services, *City Response to LAFCO Regarding Valley Secession Proposal and Initial Fiscal Analysis*, June 13, 2001, page 674.

¹²⁴ County of Los Angeles, Office of the County Counsel, *Commission Authority to Set Terms and Conditions Regarding Public Utilities*, February 7, 2002.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the City of Los Angeles to provide the same level of service as is provided to each particular type of customer within the City of Los Angeles to customers of the corresponding type within the new city, and to charge the same utility rates as are charged to each particular type of customer within the City of Los Angeles to customers of the corresponding type in the new city, with no rate differential based upon the location of the customer within one city or the other, such that while the City of Los Angeles may adjust rates and differentiate between different types of customers based on usage or cost of service, the rates charged to a particular type of customer in the remaining City will always be the same as the rate charged to the corresponding type of customer in the new city, and to the extent that there are additional costs associated with the provision of utility services to a particular type of customer in either area, those additional costs shall be borne uniformly across the two cities by that type of customer, without any differentials based upon the location of the customer within one city or the other. Should this rate protection condition be found unlawful, the Executive Officer recommends that the new city be relieved of its obligations to enter into franchise agreements with the City of Los Angeles.

Other Enterprises

The Applicant proposes to hold a proportionate, undivided interest in the airports, Port and zoo. The City of Los Angeles proposes to retain ownership of the airports, Port, and public utilities. The Executive Officer recommends that the airports, the Port and the public utilities remain under the ownership and control of the City of Los Angeles.

LIABILITIES

Government Code section 56886(c) authorizes the Commission to set terms and conditions related to the imposition, exemption, transfer, division or apportionment, as among affected agencies, of liability for payment of all or any principal, interest, and any other amounts which shall become due on account of all or any part of any outstanding or then authorized but thereafter issued bonds, including revenue bonds, or other contracts or obligations of any city, county, district or improvement district.

Government Code section 56121 provides that no change of organization or reorganization, or any term or condition thereof “shall impair the rights of any bondholder or other creditor of any county, city or district.” It also provides that any bondholder or creditor may enforce his or her rights in the same manner and to the same extent as if the change of organization, reorganization or term or condition had not been made. Thus, the Commission should not impose terms and conditions relating the apportionment of liabilities that adversely impact the rights of bondholders or creditors; however, the Commission should also be aware of the fact that pursuant to Government Code section 56121, the rights of bondholders and creditors are protected should the special reorganization or a term and condition of the special reorganization ultimately have an unforeseen adverse impact on their rights.

The City of Los Angeles has proposed in general that the [new] city pay its portion of the City debt on a monthly basis until the debt is extinguished.¹²⁵

The Applicant has proposed:

The new Hollywood City will be allocated a proportional and equitable share of liabilities. Outstanding liens and obligations associated with the Geographic area defined as Hollywood’s portion of the distributed infrastructure will become the responsibility of the new Hollywood City. The new Hollywood City will also be allocated liens or debt that can be attributed directly to all other assets transferred to the new Hollywood City. The new Hollywood City will participate proportionally and equitably in any liability attaching to prospectively shared assets, infrastructure or other assets.

TAX AND REVENUE ANTICIPATION NOTES

The City of Los Angeles has raised concerns about its ability to issue and reimburse fiscal year 2002-03 tax and revenue anticipation notes so long as the Commission imposes a mid fiscal year effective date. The City’s Controller has indicated that the City is contemplating issuance of approximately \$250 million in short-term debt for the upcoming fiscal year. The City is expected to issue the debt in June 2002, and to repay the debt in July 2003.

The Comprehensive Fiscal Analysis allocated \$7 million in short-term debt costs to the new city.

Executive Officer’s Recommendation

Should the Commission impose an effective date other than July 1, 2003, it is recommended that the fiscal agent be required to set aside the new city’s share of tax and revenue anticipation note debt outstanding prior to the effective date of incorporation on the dates and in the proportions dictated

¹²⁵ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

by the pledge schedule in the City's bond covenant. For the pension portion of the debt, the new city's share of debt service should be proportional to its contribution to the City's general fund (4.90%), and then reduced by half. For the cash flow portion of the debt, the new city's share should be zero (0%). The fiscal agent should be required to remit the debt payment to the City of Los Angeles in a timely fashion for repayment of the bondholders, with appropriate deductions for interest earned by the City on any pledged funds paid by Hollywood prior to the City's actual payment of debt service. For the 2003-04 fiscal year and subsequent years, each party should be responsible for its own tax and revenue anticipation notes.

GENERAL OBLIGATION BONDS

General obligation (GO) bonds are voter-approved loans from bondholders for the acquisition and improvement of real property, and are repaid through increased property taxes. The City of Los Angeles had \$766 million (as of February 2002) in outstanding debt in the form of general obligation bonds, the proceeds of which have been used to fund library, zoo, fire, helicopter and animal shelter facilities. The existing debt should be repaid with interest in 2022.

The general obligation bonds are secured by tax liens on property in the City of Los Angeles. The City of Los Angeles determines the GO property tax rate, the County collects the taxes from the property owners, and the City of Los Angeles pays debt service to the bondholders.

Given that property owners throughout the City of Los Angeles approved the GO bonds by a two-thirds vote, the property owners in Hollywood and the remaining City of Los Angeles should continue to be liable for the payment of ad valorem GO property taxes.

The City of Los Angeles has also proposed allocating the unissued authorization for general obligation bonds previously approved by the voters. This would not carry any financial obligation unless the new city issued the bonds. Unissued bonds include the recently approved Proposition Q, and Proposition F.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the new city to pass an ordinance by August 1 of each year adopting the GO property tax rate established by the City of Los Angeles for repayment of GO debt issued as of the election date and outstanding on the effective date, and require the new city to authorize the Los Angeles County Tax Collector to remit to the City of Los Angeles all Hollywood property owners' payments for GO debt outstanding on the effective date. The City of Los Angeles should continue to be responsible for repaying the bondholders.¹²⁶ The Executive Officer also recommends allocating the unissued authorization for general obligation bonds previously approved by the voters.

ASSESSMENT BONDS AND SPECIAL TAX BONDS

The City of Los Angeles has \$212 million in outstanding special tax bonds. This debt primarily consists of voter-approved bonds for a police emergency communications system. In addition, the City has issued about \$13 million in Proposition K parcel tax bonds for parks, recreation facilities, and childcare centers in a citywide assessment district. Further, there are two Mello-Roos bonds approved by voters in small assessment districts within the City, with \$8 million in outstanding debt

¹²⁶ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

approved by a Pershing Square Park district and \$11 million in outstanding debt approved by Cascades Business Park district in Sylmar.

So long as the Hollywood parcels that are currently encumbered would remain encumbered until the bonds are paid in full, there should not be a negative impact on bondholders or the remainder of the City of Los Angeles.¹²⁷

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the parcels that are currently encumbered with such assessments to remain encumbered until the bonds are paid in full, including parcels within the Hollywood Special Reorganization area that are currently encumbered. Property owners in the new city would not bear liability for outstanding Pershing Square Park Project and Cascades Business Park debt. Property owners in the new city would continue to bear liability for assessments related to the police emergency communications system and Proposition K.¹²⁸

JUDGMENT OBLIGATION BONDS

The City of Los Angeles currently has \$75 million in outstanding debt financed by judgment obligation (JO) bonds. The debt has been issued to pay business tax refunds and other claims resulting from past legal claims against the City of Los Angeles. Most of this debt is related to business tax refunds to financial institutions, and will be fully defeased before the recommended effective date. However, a portion of the debt will not reach maturity until the year 2011.

The City of Los Angeles has proposed that:

For these forms of indebtedness, the new city shall pay its share of existing debt...to the City on a monthly basis until the debt is extinguished. If the new city does not make this payment, the County Auditor-Controller shall pay the City the sums due for the new city's share of debt service using the property tax otherwise payable to the new city. This payment to the City from either the new city or the Auditor-Controller shall occur monthly.¹²⁹

The Executive Officer estimates that Hollywood's contribution to the general fund is 4.90 percent, based on adjustments for boundary changes and use of the most recent fiscal year data. The Subcommittee recommended that the Commission require the new city to make monthly debt service payments to the City of Los Angeles for the debt until the new city pays the City of Los Angeles for its share of the outstanding debt.¹³⁰

Executive Officer's Recommendation

Similar to the Subcommittee's recommendation, the Commission should require the new city to pay 4.90 percent of City of Los Angeles debt service for the debt outstanding on the effective date consistent with the payment schedule in the bond covenant, unless and until the new city pays the

¹²⁷ Public Financial Management, San Fernando Valley Proposal for Special Reorganization Comprehensive Fiscal Analysis, January 9, 2002.

¹²⁸ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹²⁹ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹³⁰ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

City of Los Angeles for its share of the outstanding debt. The fiscal agent should be required to remit the debt payment to the City of Los Angeles in a timely fashion for repayment of the bondholders, with appropriate deductions for interest earned by the City on any pledged funds paid by Hollywood to the City prior to the City's actual payment of debt service.

GENERAL FUND LEASE OBLIGATIONS AND CERTIFICATES OF PARTICIPATION

The City of Los Angeles has approximately \$1.1 billion in outstanding debt in the form of lease bonds or certificates of participation (COPs). These bonds have been used to purchase real property and equipment anticipated to have a useful life of six years or more. In addition to real estate, the bonds have financed a central library cataloguing system, heavy-duty equipment, fire trucks, helicopters and major computer systems. The bonds are secured on the assets that have been financed in this manner, or in some cases related assets. The "lease payments" for these assets include debt service, and are paid out of the City of Los Angeles general fund.

The Comprehensive Fiscal Analysis estimated that 4 percent of debt service unrelated to the Convention Center would be borne by the new city. The CFA approach is as follows:

In order to comply with state constitutional debt limit provisions (Art. XVI, Section 18), the apportionment of obligations represented by COPs generally should be based on where the leased property is located. This should not raise impairment problems so long as the market value and credit ratings of the COPs are not adversely affected by such apportionment.... To ensure that the rights of bondholders are not negatively impacted as a result of a special reorganization...it is assumed the new city would make payment for a portion of the City's outstanding lease obligations according to the proportion of assets financed, which would continue to provide service to the new city upon a special reorganization.¹³¹

The City is prohibited from assigning its lease obligations by the terms of the lease bonds and COPs, but the City may sublease the financed assets. The City of Los Angeles must be able to demonstrate that it has beneficial use of the property. The City of Los Angeles has concluded that "this will likely require any MICLA obligation concerning property to be transferred to a seceding entity to be defeased." The City of Los Angeles has proposed that:

For these forms of indebtedness, the new city shall pay its share of existing debt... to the City on a monthly basis until the debt is extinguished. If the new city does not make this payment, the County Auditor-Controller shall pay the City the sums due for the new city's share of debt service using the property tax otherwise payable to the new city. This payment to the City from either the new city or the Auditor-Controller shall occur monthly.¹³²

The Executive Officer estimates that Hollywood's contribution to the general fund is 4.90 percent, based on adjustments for boundary changes and use of the most recent fiscal year data.

The Subcommittee recommended that the Commission should require the new city to make monthly debt service payments to the City of Los Angeles for the debt that is secured and paid by

¹³¹ Public Financial Management, Hollywood Proposal for Special Reorganization Comprehensive Fiscal Analysis, March 6, 2002.

¹³² City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

the general fund, on the basis of the new city's contribution to the general fund (4.90%) unless and until the new city pays the City of Los Angeles for its share of the outstanding debt.²¹²

Executive Officer's Recommendation

Similar to the Subcommittee's recommendation, the Commission should require the new city to make debt service payments to the City of Los Angeles, consistent with the payment schedule for the bond covenant, for the debt that is secured and paid by the general fund, on the basis of the new city's contribution to the general fund (4.90%) unless and until the new city pays the City of Los Angeles for its share of the outstanding debt. The fiscal agent should be required to remit the debt payment to the City of Los Angeles in a timely fashion for repayment of the bondholders, with appropriate deductions for interest earned by the City on any pledged funds paid by Hollywood to the City prior to the City's actual payment of debt service.

Consistent with the Subcommittee's recommendation, if the debt-financed equipment cannot be transferred to the new city, the Commission should require the City of Los Angeles to provide the new city with access to, and use of, an equitable share of this debt-financed equipment during its useful life. The new city should not bear responsibility for debt paid by special funds, in particular, the portion of debt paid by Convention Center revenues, the Staples Arena developer or the Pershing Square special taxes.¹³³

SANITATION EQUIPMENT CHARGE REVENUE BONDS

Sanitation equipment charge revenue bonds have been used to purchase garbage containers and trucks throughout the City of Los Angeles. As of February 2002, the City had \$173 million in outstanding sanitation equipment debt. These bonds are secured on revenues from the sanitation equipment charge. The City of Los Angeles estimated that 5.92 percent of current sanitation equipment charges are generated in the originally proposed special reorganization area; this allocation was estimated by the City of Los Angeles and has not been reviewed by staff¹³⁴ The Executive Officer estimates that the 5.11 percent of sanitation equipment charges are generated in the recommended boundaries for the Hollywood special reorganization area.

The Subcommittee recommended that the Commission should require the new city to make monthly debt service payments to the City of Los Angeles for its portion of the sanitation equipment charge revenue bonds debt on the basis proposed by the City unless and until the new city pays the City of Los Angeles for its share of the outstanding debt.¹³⁵

Executive Officer's Recommendation

The Executive Officer has recommended that the City of Los Angeles retain the sanitation charges collected in Hollywood during the transition period and credit those charges toward the transition period service payment. Consistent with that recommendation, the City of Los Angeles should be required to pay the new city's share of the outstanding sanitation equipment charge revenue bonds debt from the sanitation charges collected in Hollywood during the transition period. After the

²¹² *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹³³ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹³⁴ City of Los Angeles, *Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions*, April 2, 2002.

¹³⁵ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

transition period, the Commission should require the new city to make debt service payments to the City of Los Angeles, consistent with the payment schedule in the bond covenant, for a 5.1 percent share of the sanitation equipment charge revenue bonds debt unless and until the new city pays the City of Los Angeles for its share of the outstanding debt. The fiscal agent should be required to remit the debt payment to the City of Los Angeles in a timely fashion for repayment of the bondholders, with appropriate deductions for interest earned by the City on any pledged funds paid by Hollywood to the City prior to the City's actual payment of debt service.

PARKING REVENUE BONDS

The City of Los Angeles has \$80 million in outstanding debt in the form of parking revenue bonds. These bonds are secured on revenues from parking meters and City-owned parking lots, of which about 8.7 percent is generated in Hollywood. This allocation was estimated by the City of Los Angeles and has not been reviewed by staff. The City's bond covenant requires that parking revenues net of operating costs equal at least 125 percent of annual debt service.

The City of Los Angeles has proposed that:

For these forms of indebtedness, the new city shall pay its share of existing debt ...to the City on a monthly basis until the debt is extinguished. If the new city does not make this payment, the County Auditor-Controller shall pay the City the sums due for the new city's share of debt service using the property tax otherwise payable to the new city. This payment to the City from either the new city or the Auditor-Controller shall occur monthly.¹³⁶

The Subcommittee recommended that the Commission should require the new city to make monthly debt service payments to the City of Los Angeles for its portion of the parking revenue bonds debt on the basis proposed by the City unless and until the new city pays the City of Los Angeles for its share of the outstanding debt.¹³⁷

Executive Officer's Recommendation

The Executive Officer has recommended that the City of Los Angeles retain the parking fees collected in Hollywood during the transition period and credit those charges toward the transition period service payment. Consistent with that recommendation, the City of Los Angeles should be required to pay the new city's share of the outstanding parking revenue bond debt from the parking fees collected in Hollywood during the transition period. After the transition period, the Commission should require the new city to make debt service payments to the City of Los Angeles, consistent with the payment schedule in the bond covenant, for its 8.7 percent portion of the parking revenue bonds debt unless and until the new city pays the City of Los Angeles for its share of the outstanding debt. The fiscal agent should be required to remit the debt payment to the City of Los Angeles in a timely fashion for repayment of the bondholders, with appropriate deductions for interest earned by the City on any pledged funds paid by Hollywood to the City prior to the City's actual payment of debt service.

¹³⁶ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹³⁷ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

NON-DEBT LIABILITIES

Non-debt liabilities include workers' compensation liability resulting from litigation against the City, and arguably salary-related liability.

Workers Compensation

The City of Los Angeles is self-insured for purposes of workers' compensation, and pays out approximately \$100 million annually for doctors' bills, temporary and permanent disability income support payments, and vocational training costs. Ninety seven percent of the payments are for currently inactive employees, with only 3 percent of payments for active employees.

The City of Los Angeles has proposed that the new city pay on a monthly basis the City of Los Angeles for a proportionate share of workers' compensation costs.¹³⁸ The City has proposed that the allocation factor be Hollywood city's share of general fund revenues that, according to the most recent estimate, would be 4.90 percent.¹³⁹

The City of Los Angeles has proposed that Hollywood's obligation includes claims that were filed prior to the effective date of incorporation as well as claims filed subsequently for injuries that "at least some of which" occurred prior to the effective date.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the new city to pay on a monthly basis a share of the City of Los Angeles workers' compensation attributable to workplace injuries that occurred prior to the effective date, as well as all claims filed prior to the effective date, where Hollywood's share of these costs is equivalent to the percentage Hollywood contributed to the City of Los Angeles general fund in the most recent fiscal year.¹⁴⁰

Salary-related Liability

The City of Los Angeles has raised the issue of liability relating to accrued vacation, overtime and sick leave of City of Los Angeles employees. In particular, the City is concerned that when employees transfer to the new city, they will en masse seek payouts for the accrued leave.¹⁴¹

The Executive Officer concludes that the accrued leave of employees need not be cashed out when employees transfer, and recommends that the new city honor all accrued leave of employees who transfer to the new city as part of a transfer in service responsibility.

Liability Claims

Liability claims are filed against the City for numerous reasons, including personal injury, property damage, discrimination complaints, employee actions, inverse condemnations, and employee actions. The City pays liability claims from its general fund, through judgment obligation bonds, and from special funds such as the Sewer Construction and Maintenance Fund.

¹³⁸ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹³⁹ Public Financial Management, San Fernando Valley Proposal for Special Reorganization Supplemental Report, February 19, 2002.

¹⁴⁰ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

¹⁴¹ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

The City of Los Angeles has proposed that Hollywood be liable for a share of these liability claims based on the percent of general fund revenues attributable to Hollywood, which is estimated by staff as approximately 4.90 percent.

The City of Los Angeles has proposed that Hollywood's obligation include claims that were filed prior to the effective date of incorporation as well as claims filed subsequently for injuries that "at least some of which" occurred prior to the effective date.

Both the City and the Applicant have agreed that the City shall consult with Hollywood on the status and progress of claims and lawsuits involving the payment of \$500,000 or more.¹⁴²

Consistent with the Subcommittee's recommendation, the Commission should require Hollywood to pay on a monthly basis a share of the City of Los Angeles liability claims attributable to injuries that occurred prior to the effective date, as well as all claims filed prior to the effective date, where Hollywood's share of these costs is equivalent to the percentage Hollywood contributed to the City of Los Angeles general fund in the most recent fiscal year.¹⁴³ It is further recommended that the City be required to consult with the new city on lawsuits involving settlements of \$500,000 or more.

ADVANCE PAYMENTS

The resolution includes a provision that prevents the City of Los Angeles from demanding advance payments for the City's debt, as the City had originally proposed to do. The provision would require the City of Los Angeles to credit the new city for interest on payments made more than one week in advance.

The City of Los Angeles has proposed that it should be allowed to require advance payments from the new city if the new city does not pay in a timely manner. The Executive Officer notes that the resolution authorizes the City of Los Angeles to reduce service levels in the new city if the new city is more than 30 days late in making a transition period service payment. There is no risk of late payments for City of Los Angeles debt as those payments receive top priority in the payment scheme.

The City of Los Angeles has asked that reasonable interest expenses be more specifically defined based upon the City of Los Angeles general pool investment yield. The Executive Officer has accommodated this proposal.

The Executive Officer continues to recommend that advance payments require compensation for lost interest.

¹⁴² City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁴³ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

MISCELLANEOUS PROVISIONS

REDEVELOPMENT AREAS

The City of Los Angeles has proposed that any transfer of the administration of any redevelopment area located in the detached territory be in accordance with the California Health and Safety Code sections 33214-33217.¹⁴⁴ The Applicant has proposed that the Hollywood redevelopment projects along with associated assets and liabilities transfer to the new city. The Commission has no role in the transfer of redevelopment projects. In the San Fernando Valley special reorganization, however, the Subcommittee adopted a recommendation that the City of Los Angeles shall not expand the boundaries of any redevelopment project area within Hollywood nor shall it establish any new redevelopment project area during the transition period without official consent of the Hollywood City Council.¹⁴⁵

Executive Officer's Recommendation

The parties are required by law to comply with the provisions of Health and Safety Code sections 33214-33217 to effectuate a transfer of responsibility for redevelopment areas, and the Commission has no role in that process; therefore, it is not recommended that the Commission adopt a term and condition with respect to the transfer of redevelopment areas. The Executive Officer does recommend requiring the City of Los Angeles to obtain the consent of the new city's city council before it expands or establishes a redevelopment area within the new city during the transition period.

PROPOSITION K ASSESSMENT DISTRICT

In 1996, the voters citywide approved Proposition K—a \$25 million annual assessment for parks and related improvements. Proposition K funds can only be used for improving, constructing, and maintaining City parks, recreation facilities, childcare centers, and acquiring land for open space purposes. Land acquired for open space purposes must be owned by the City. Eighty-two percent of the assessment funds are reserved for capitol improvement projects, 15 percent for maintenance of completed acquisitions and improvements and 3 percent for incidental costs.

The assessment district is a citywide district, formally organized as a landscaping and street lighting district. The legal authority for the Proposition K assessments is the California Streets and Highways Code, Section 22500, *et seq.*, otherwise known as the Landscaping and Lighting Act of 1972. The Act requires that an annual engineer's report estimate the net amount assessable and apportion that amount among the parcels in proportion to the estimated benefits to be received by each parcel from the improvements. The engineer's report allocates benefit points to all parcels within the citywide district.

Assessments are levied annually by the City and collected by the County along with general property taxes. The rate and method of apportionment is based on the size and use of each parcel. The benefits associated with the park improvements vary depending on the land use category for a particular parcel.

¹⁴⁴ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁴⁵ Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.

Proposition K funding is designated for both specified projects and competitive grant projects. Under Proposition K, \$298.85 million of the total amount generated over 30 years is allocated to 183 specified projects. Should any project become infeasible for any reason or there are project savings, the City Council is authorized to reprogram the applicable funds during the annual assessment proceedings to other projects. Many of the specified projects are located within the Hollywood Special Reorganization area, including neighborhood park, recreational and athletic facilities. Proposition K also allocates \$143.65 million of the total amount generated over 30 years competitive grants for public agencies, City departments and nonprofit organizations.

The City of Los Angeles issued a \$14.4 million assessment bond in 2000 for ten of the Proposition K projects, several of which are located in the special reorganization areas. The debt is scheduled to be paid off in fiscal year 2026-27.

The City and the Applicant have agreed that Hollywood property owners would continue to pay for existing debt. The Applicant has proposed that the district be separated into two districts. The City of Los Angeles has proposed that the assessment district be maintained under its existing boundaries. The draft resolution provides that the City's proposed term be the fall-back in the event that the division of the Proposition K district is deemed unlawful.¹⁴⁶

Government Code section 56886(u) provides the Commission with authority to transfer authority and responsibility among any cities, counties, or districts for the administration of special tax and assessment districts, including the determination of annual tax rates within authorized limits, the management of funds, the issuance of authorized bonds, the supervision of construction, etc. Section 56886(e) provides authority for the formation of a new improvement district, and section 56886(t) provides authority for the extension and continuation of any previously authorized tax or assessment. Section 56125 provides that the Commission need not comply with the principal act when the formation of a new improvement district is pursuant to a reorganization.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should detach Hollywood from the Proposition K assessment district, authorize the continuation of the assessment with a limit on the total amount assessed, and form a separate district in Hollywood consistent with the responsibilities, powers and limitations of the current district.¹⁴⁷ The Hollywood Proposition K district would continue to be liable for a pro rata share of the outstanding bonds of the former district, and should be obligated to carry out those specified projects in Hollywood, unless the new City Council determines that they are infeasible, consistent with Proposition K. Since this is a previously authorized assessment that has been and is being collected in Hollywood, and no increase in the assessment limitation is contemplated, the requirements of Proposition 218 should not be triggered. The Executive Officer further recommends that the Commission adopt the format of the City's proposed term and condition, with an appropriate clarification that the voters in Hollywood Special Reorganization election will not be determining fund limits and project allocations for the Harbor and Hollywood, but only for Hollywood and the remaining City of Los Angeles.

¹⁴⁶ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002. Excludes reference to the pending other special reorganization areas.

¹⁴⁷ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

OTHER ASSESSMENT DISTRICTS

The City of Los Angeles has proposed that control of assessment districts other than Landscaping and Street Lighting District number 96-1 (Proposition K) located wholly within the new cities be transferred to the new city councils after the effective date of incorporation, and that assessment districts that are partially within the new cities be detached and the portion within the new city shall become the responsibility of the new city.¹⁴⁸ The City of Los Angeles has indicated that it does not believe that there are any assessment districts only partially in the Hollywood Special Reorganization area.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require the transfer of districts located in Hollywood to the new city.¹⁴⁹

BUSINESS IMPROVEMENT DISTRICTS

Business improvements districts (BIDs) are geographic areas where special assessments are paid either by the property owners or the business owners for purposes of services such as maintenance, security and marketing programs. The assessment funds must be spent in the BID, and the funds for each BID are segregated into separate City trust accounts. The City of Los Angeles has thirty BIDs, of which several are located in the proposed Hollywood city. The proposed North Hollywood Transit BID is located on the border of the proposed Valley and Hollywood special reorganization areas.

With respect to BIDs, the City of Los Angeles has proposed the following condition:

The administration of any Business Improvement District located entirely within the detached territory shall be transferred to the new city's legislative body after the effective date of incorporation. To the extent that any Business Improvement District is located partially within the new city and partially within the remaining City, that portion located within the new city shall be detached and become the responsibility of the new city.

Executive Officer's Recommendation

The Commission should require the transfer of BIDs located within Hollywood to the new city. Given that the City maintains trust funds for the BIDs, it is also recommended that the City be required to transfer any unexpended BID fund balances for BIDs located within Hollywood territory to the new city or its fiscal agent.

AUDIT RIGHTS

Due to the financial and service obligations contemplated by the recommended terms and conditions, the City of Los Angeles and the new city will have a financial relationship that will last for decades. Incidental to the ongoing financial obligations placed upon the new city, the new city

¹⁴⁸ Hollywood Vote, Inc. Hollywood Proposal for Special Reorganization Preliminary Comprehensive Fiscal Analysis, October 1, 2001.; City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁴⁹ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

should be entitled to audit rights to ensure the City is properly allocating to the new city its share of financial obligations.

The City of Los Angeles requested reciprocal audit rights of the new city and its fiscal agent. The draft resolution accommodates this request.

Executive Officer's Recommendation

Consistent with the Subcommittee's recommendation, the Commission should require that the new city have audit rights with respect to the City of Los Angeles' fiscal management of all outstanding debt service and other liabilities for which the new city shall be proportionately liable as provided for in the terms and conditions, including but not limited to workers' compensation claims and legal liability claims.¹⁵⁰ The City of Los Angeles should be required to maintain all records related to the outstanding debt service and other liabilities for a period of at least three years from the date of retirement of a debt or payment of a liability claim. The new city's right to audit shall terminate two years after the date of retirement of a debt or payment of a liability claim. The new city shall bear all expenses related to any audits. The Executive Officer further recommends that the Commission fix all percentages to be used for allocation of any outstanding debt or liabilities to alleviate the need for audit rights with respect to the percentages. Any objections to the percentage allocations should be raised with the Commission before it makes its final determinations.

The Executive Officer recommends that the Commission also require that the new city have audit rights with respect to transition period service costs and any revenue collected by the City of Los Angeles within Hollywood during fiscal year 2002-2003 and during the remainder of the transition period. The City of Los Angeles should be required to maintain all records of such revenues for a period of at least three years from the date when the transition period ends. The new city's right to audit shall terminate two years after the last day of the transition period. The new city shall bear all expenses related to any audits.

Similarly, the City of Los Angeles should have the right to audit the new city or the third party fiscal agent during or soon after the transition period.

¹⁵⁰ *Special Reorganization of Hollywood Staff Report on Terms and Conditions*, approved by the Subcommittee on Findings, Terms and Conditions on March 25, 2002.

STANDARD PROVISIONS

ELECTED REPRESENTATIVES

In its preliminary comprehensive fiscal analysis, the Applicant originally proposed a city council of seven members elected by district. Due to time constraints and the cost associated with creating council district boundaries, staff has recommended that the proposed Hollywood City have a five-member city council elected at large, the format followed by most general law cities. The city council will appoint a mayor from among its members. The Applicant has agreed to this form of government. The new city would have the option of changing its form of government after incorporation by majority vote of the electorate.

Government Code section 57377 generally provides that, at the first election, the three members elected receiving the lowest number of votes only hold office until the next succeeding general municipal election, and the two members elected receiving the highest number of votes hold office until the second succeeding general municipal election.

Since the Applicant has not requested postponement of the election for city council members, the holding of city council elections will be at the same time as the election on the question of special reorganization.¹⁵¹

The Subcommittee recommended the following condition:

The legislative body of the Hollywood City shall consist of five city council members, elected in accordance with Government Code section 57377. The first election of city council members shall be held concurrently with the election on the question of special reorganization.

Executive Officer's Recommendation

The Commission should follow the Subcommittee's recommendation.

APPOINTIVE POSITIONS

In California incorporations, it is standard practice for the resolution making determinations to list certain officials of the new city as being appointive rather than elected positions. Such a provision appears necessary in the case of the City Clerk and Treasurer, as the law provides that these positions be either appointive or elective.¹⁵² The resolutions of other LAFCOs frequently list the City Manager and City Attorney positions as appointive rather than elective.

It is not necessary to list all appointive positions at the new city, as many of these positions are required by statute to be appointive rather than elective. For example, in a general law city, the statute authorizes the city council to appoint a city attorney, a chief of police, a superintendent of streets or other subordinate officers.¹⁵³

Executive Officer's Recommendation

The Commission should specify that the City Manager, City Clerk and City Treasurer will be appointed by the City Council of the new city.

¹⁵¹ Government Code section 56724.

¹⁵² Government Code section 36511.

¹⁵³ Government Code section 36505.

ORDINANCE ADOPTION

The default provisions of the Hertzberg Act require that a newly incorporated city comprised of territory formerly unincorporated adopt all previously applicable county ordinances of the City of Los Angeles for the first 120 days of the new city's existence or until the city council adopts its own ordinances.¹⁵⁴ The code requires that enforcement of these laws be provided by the new city, but may be provided by the county during the transition period if enforcement services are provided by the county during that period.¹⁵⁵

In some past incorporation cases, the resolution making determinations has specifically required the new city to adhere to the existing general plan and zoning ordinances of the county until the new city has adopted its own general plan.

Since the proposed Hollywood Special Reorganization area is not unincorporated territory, adoption of the county's ordinances would not make sense. The Applicant and the City agree that that Commission should require the new city to adopt the relevant ordinances of the City of Los Angeles for this time period.

Executive Officer's Recommendation

The Commission should require the new City Council to adopt, immediately following its organization and prior to performing any other official act, an ordinance providing that all City of Los Angeles ordinances remain in full force and effect as city ordinances for a period of 120 days or until the City Council enacts ordinances superceding them, whichever occurs first.

DEVELOPMENT PERMITS

The City of Los Angeles has proposed the following term relating to development permits:

Any conditions of approval (including, without limitation, mitigation measures adopted pursuant to the California Environmental Quality Act) imposed by the City on any discretionary project approved prior to the effective date of incorporation shall be valid and enforceable between the applicant and the new city in which the development is located. The new city shall indemnify and hold the City harmless from any claims or actions based on the new city's failure to fulfill or enforce any of the terms of the permit or conditions of its approval, including, without limitation, terms or conditions related to environmental mitigation.¹⁵⁶

Executive Officer's Recommendation

The Executive Officer recommends against imposing this condition. The Commission's terms and conditions should not directly regulate land use, property development or subdivision requirements.¹⁵⁷ The validity of permits issued by the City of Los Angeles, and the responsibility of the parties in relation thereto are determinable by statutes and case law.

¹⁵⁴ Government Code section 57376(a).

¹⁵⁵ Government Code sections 57376(a), 57384.

¹⁵⁶ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁵⁷ Government Code section 56886.

TAX AUTHORIZATION

It is standard practice in California incorporations for the resolution making determinations to authorize the new city to continue levying the same taxes and fees. The Commission has the discretion to impose such a term and condition, however, the statute granting that authority pre-dates Proposition 218.¹⁵⁸

In 1996, California voters approved Proposition 218, which requires local governments to obtain voter approval (majority or two-thirds) for all general and special taxes. In addition, Proposition 218 places stricter requirements on the approval and use of assessments and fees.

The Legislative Counsel has issued two opinions that conclude that the provisions of Proposition 218 would prevail over the provisions of the former Cortese-Knox Act with regard to the proposed imposition of a tax, assessment or fee as a condition of annexation. In the opinion of the Legislative Counsel, the imposition of a City's local taxes, assessments, fees, and charges to a territory approved for annexation must first be approved by a vote of those in the annexed territory because the tax, assessment or fee had not been previously imposed in that territory.¹⁵⁹ Proposition 218 requires that the voters must approve any increases in general taxes by a majority vote and special taxes by a two-thirds vote.¹⁶⁰ To impose a benefit assessment, a public agency must prepare an engineer's report which demonstrates the special benefits derived by the properties proposed to be assessed and conduct a protest hearing in which the votes of property-owners are weighted in accordance with the proportional financial obligation of the affected properties.¹⁶¹ Most fees and charges must also survive a protest hearing and be approved by either a majority of the property owners affected or a two-thirds vote of the electorate.¹⁶²

Subsequently, the Attorney General released a formal opinion which concluded that "if LAFCO conditions approval of a change of organization or reorganization upon a requirement that the subject agency levy or fix and collect a previously established and collected tax, assessment or fee on parcels being annexed to the agency, the voter approval requirements of Proposition 218 do not apply."¹⁶³ The opinion reasoned that the protest procedures in the former Cortese-Knox Act provide for voter approval, and Proposition 218 was not intended to apply to LAFCO actions.

Seven California incorporations have been processed since the passage of Proposition 218, all of which have conditioned approval on the imposition of previously established and collected taxes, fees and assessments without requiring further compliance with Proposition 218. None has been challenged on the legal grounds of violation of Proposition 218. These incorporations have included authorization in the resolution making determinations of both general and special taxes. The annexations discussed in the Legislative Counsel and Attorney General opinions differ from the incorporations, however, because annexations involve the imposition of these taxes, fees and assessment in territory where they were not previously imposed and the property owners and/or voters had not previously approved their imposition. In the case of incorporations or the proposed Hollywood Special Reorganization, the taxes, fees and assessments have already been approved by and imposed upon the subject territory. Thus, it could be argued that they are not new taxes, fees or assessments, and not subject to Proposition 218.

¹⁵⁸ Government Code section 56886(t).

¹⁵⁹ Legislative Counsel Opinion Nos. 11267 (May 15, 1997), 25418 (March 17, 1998).

¹⁶⁰ Cal. Const., Art. XIII C.

¹⁶¹ Cal. Const. Art. XIII D, § 4.

¹⁶² Cal. Const., Art. XIII D § 6.

¹⁶³ 82 Ops. Cal. Atty. Gen 180.

Executive Officer's Recommendation

The Commission should authorize the new city to continue to levy all previously authorized and collected charges, fees, assessments and general or special taxes previously collected by the City of Los Angeles, except as prohibited by law.

DEVELOPMENT AGREEMENTS

Most California incorporation resolutions include a provision requiring the new city to abide by existing development agreements in the territory. This is a statutory requirement for incorporations of previously unincorporated territory,¹⁶⁴ but there is no similar statutory requirement for special reorganization. Nonetheless, such a provision protects the public, and real estate and business owners in areas subject to development agreements.

The City of Los Angeles has proposed that the resolution making determinations include a provision requiring the new city to abide by existing development agreements:

The new city shall succeed to the benefits and be bound by the obligations and duties of the City with respect to the Development Agreements listed below, and the City shall be relieved of any obligation under those Agreements. The new city shall indemnify and hold the City harmless from any claims or actions based on the new city's failure to fulfill or enforce any of the terms of the Development Agreement or conditions of its approval, including, without limitation, terms or conditions related to environmental mitigation.¹⁶⁵

Executive Officer's Recommendation

The Commission should adopt the City's proposed condition.

PROVISIONAL APPROPRIATIONS LIMIT

The Commission must establish a provisional appropriations limit for the new city. This limit is temporary, and will only affect the new city during its first two years. The new city is required by statute to submit to its voters a permanent appropriations limit in the first municipal election following the first full fiscal year of operation.¹⁶⁶

According to Government Code section 56812, the Commission may consider anticipated revenues, population growth and cost of living growth forecasts in setting the provisional appropriations limit. The CFA estimated that the Hollywood area would receive \$180 million in general and special purpose fund revenues in the fiscal year 2000-01. The objective is to set a provisional appropriations limit that should accommodate the new city through the 2004-05 fiscal year.

The Executive Officer has calculated the provisional appropriations limit of the new city as \$215.4 million. This provisional limit is based upon the new city's projected revenues of \$187 million in the base year, as well as inflation and population growth that is expected to occur between the base year and fiscal year 2004-05. The California Department of Finance has forecast 4.7 percent population

¹⁶⁴ Government Code section 65865.3.

¹⁶⁵ City of Los Angeles, Special Reorganization of the San Fernando Valley, Harbor, and Hollywood—Objections to Recommendations of the LAFCO Subcommittee on Terms and Conditions, April 2, 2002.

¹⁶⁶ Government Code section 56812.

growth in Los Angeles County will occur between year 2000 and 2005.¹⁶⁷ Given that the Hollywood population estimate is based on 2000 Census data, this forecast adjusts for population growth through fiscal year 2004-05. Based on a combination of empirical data from the U.S. Bureau of Labor Statistics and inflation forecasts issued by the California Department of Finance, inflation between January 2001 and January 2005 is estimated at 10 percent. Given that the base year is fiscal year 2000-01, this inflation figure adjusts for inflation between the base year and the middle of fiscal year 2004-05.

Executive Officer's Recommendation

The Commission should set a provisional appropriations limit of \$215.4 million.

NAME OF THE NEW CITY

The Applicant has proposed that the name of the new city be "Hollywood.". The draft resolution accommodates this proposal.

GEOGRAPHIC BOUNDARIES

The Commission is charged with the task of reviewing the proposed geographic boundaries to ensure that the boundaries are definitive and certain.¹⁶⁸

Several property owners and homeowners associations have requested that the Commission exclude their community or property from the special reorganization area. These include the Farmer's Market, the Beverly Center mall, the Melrose Neighborhood Association, the Hancock Park Neighborhood Association, the Larchmont Village Homeowners Association, the Mid-Wilshire Neighborhood Council, the Wilshire Homeowners Alliance, the Beverly/Wilshire Homeowners Association, and the East Hollywood Community Association.

On January 23, 2002, the Commission adopted a motion for staff to analyze two additional Hollywood boundary scenarios. The recommended scenario would exclude the area south of Melrose Avenue where the following are located: the Farmer's Market, the Beverly Center mall, the southern half of the Melrose Neighborhood Association area, the Hancock Park Neighborhood Association area, the Larchmont Village Homeowners Association area, part of the Mid-Wilshire Neighborhood Council area and the Beverly/Wilshire Homeowners Association area.

Subsequent to that action, the Valley and Hollywood proponents have jointly proposed to divide the Cahuenga Pass neighborhood in the northwestern portion of the Hollywood territory. This area had also been included in the San Fernando Valley special reorganization proposal. Removing the western Cahuenga Pass area from the proposed Hollywood Special Reorganization area had only a marginal effect on the fiscal mitigation payment estimate for Hollywood.

The Commission has also received a request from Universal Studios to exclude two parcels from the Hollywood Special Reorganization area and include those parcels in the Valley Special Reorganization area.¹⁶⁹ Universal Studios has requested this modest boundary change in order to have all of its non-county properties under the jurisdiction of one municipality. Universal Studios is currently within County unincorporated territory and City of Los Angeles territory. As the special reorganization boundaries were originally drawn, portions of Universal Studios were in both the Valley and Hollywood, as well as unincorporated County territory. The subject parcels are

¹⁶⁷ State of California, Department of Finance, *Interim County Population Projections*. Sacramento, California, June 2001

¹⁶⁸ Government Code section 56375(n).

¹⁶⁹ Latham & Watkins, Universal Studios, Inc.'s Request to Modify New City Boundary Lines, February 6, 2002.

uninhabited. Modification of the boundary had a negligible effect on the fiscal mitigation payment estimate.

A request for exclusion has also been submitted by Mount Sinai and Forest Lawn Memorial Parks, the cemeteries located near the northern most boundary of the original special reorganization proposal. The City of Los Angeles has requested exclusion of all portions of Griffith Park from the proposed boundary of Hollywood.

Executive Officer's Recommendation

The Commission should approve the boundaries of the Hollywood Special Reorganization area as generally set forth in the map on page 9 of this Report, which excludes the western portion of the Cahuenga Pass area from the Hollywood territory, the two Universal Studios parcels, the two cemeteries, and the Fern Dell Drive portion of Griffith Park. The full legal description of the Hollywood Special Reorganization boundaries is set forth in the resolution making determinations.

SPHERE OF INFLUENCE

The Commission has the option of defining the new city's sphere of influence in the resolution making determinations, or deferring the decision until the new city incorporates. If the Commission chooses to defer this decision, it must determine the sphere of influence within the first year following incorporation of the new city.¹⁷⁰

The City of Los Angeles sphere of influence does not currently extend beyond the city limits.

Executive Officer's Recommendation

The Commission should defer consideration of the sphere of influence until after a successful incorporation.

¹⁷⁰ Government Code section 56426.5

APPENDICES

EXHIBIT A: PROPOSED HOLLYWOOD CITY LEGAL DESCRIPTION¹⁷¹

¹⁷¹ The above legal description was submitted to LAFCO by Valley Vote. This description does not meet the State Board of Equalization requirements. Once the Valley boundary is finalized by the Commission, Valley Vote will submit a legal description that meets the State Board requirements.

EXHIBIT B: HOLLYWOOD FACILITY-RELATED ASSETS

This asset compilation includes local service-related facility assets, and does not include assets that are not related to a facility such as streets, storm drains, and databases. The facilities, except as otherwise indicated, along with all furnishings, fixtures, rolling stock and other equipment contained therein, shall vest in the new city. In addition, all other property and facilities not specified below located within the new city that are local serving assets or facilities discovered after the effective date shall be transferred to the new city. Intangible assets to be transferred to the new city are addressed in the resolution.

Facilities Retained by the City of Los Angeles

The City of Los Angeles shall continue to own the following assets; however, the City of Los Angeles shall provide Transition Period services to the new city with these facilities.

Miscellaneous Municipal Facilities

Mount Lee Communication Facility

Assets Transferred to the City of Hollywood

These assets shall transfer to the new city as of the Effective Date. The City of Los Angeles shall be entitled to use these assets, at no cost, for the provision of services to the new city during the Transition Period. No assets of the proprietary departments of the City of Los Angeles shall transfer as a result of the Hollywood Special Reorganization. Should it later be determined that any asset listed herein was, as of the date of this Resolution, under the ownership and control of one of the proprietary departments, that asset(s) shall not transfer.

If any of the following assets are identified by the City of Los Angeles as facilities that are used under a lease or permitting arrangement, then if the terms of the lease permit, these leases shall transfer to the new city.

If any of the following assets are debt-financed with debt outstanding, the asset shall not transfer until the associated debt has been defeased or accepted by and transferred to the new city.

Hollywood Police Stations:

Hollywood Community Police Station 1358 N. Wilcox Avenue, 90028

Hollywood Fire Stations:

Fire Station #27 1327 N. Cole Avenue, 90028

Fire Station #35 1601 N. Hillhurst Avenue, 90027

Fire Station #41 1439 N. Gardner Street, 90046

Fire Station #52 4957 Melrose Avenue, 90029

Fire Station #82 1800 N. Bronson Avenue, 90028

Hollywood Public Libraries

Cahuenga Branch, 4591 Santa Monica Boulevard 90029

Frances Howard Goldwyn/Hollywood Regional Branch, 1623 N. Ivar Avenue 90028

John C. Fremont Branch, 6121 Melrose Avenue 90038

Los Feliz Branch, 1874 Hillhurst Avenue 90027

Will and Ariel Durant Branch, 1403 N. Gardner Street 90046 (replacement facility address is 7140 W. Sunset Boulevard, 90046)

Hollywood Public Parks

Barnsdall Art Park, 4800 Hollywood Boulevard 90027-5390
De Longpre Park, 1350 N. Cherokee Avenue 90025
Dorothy & Benjamin Smith Park, 7020 Franklin Avenue 90028
Lexington Park, Lexington Ave and Western Avenue, 90038
Runyon Canyon Park, 2000 N. Fuller Avenue 90046
Selma Park, Schrader Boulevard and Selma (under construction)
Wattles Garden Park, 1850 N. Curson Avenue 90046
William S. Hart Park, 8341 DeLongpre Avenue, 90028
Yucca Park, 6671 Yucca Street 90028

Hollywood Recreation Centers

Howard Recreation Center, 1122 Cole Avenue 90038
Lemon Grove Recreation Center, 4959 Lemon Grove Avenue 90029
Poinsettia Recreation Center, 7341 Willoughby Avenue 90046

Miscellaneous Hollywood Municipal Facilities

Tax and Permit Division Office, 6501 Fountain Avenue, 90028
Las Palmas Senior Citizen Center, 1820 N. Las Palmas Avenue 90028
Parking Lot #619 Sunset-Gardner, 1453 N. Gardner Street, 90046
Parking Lot #675 Vermont-Hollywood, 4642 Russell Avenue, 90027
Parking Lot #670 Hollywood-Vine, 1718 Cherokee Avenue, 90028
Parking Lot #702 Hollywood-Vine, 1623 N. Vine Street, 90028
Hollywood Sign

EXECUTIVE OFFICER FISCAL ALLOCATIONS: TECHNICAL NOTES

Revenues

In general, the Executive Officer's revenue estimates took the Comprehensive Fiscal Analysis as a starting point. The Executive Officer adjusted the CFA revenue estimates to account for the removal of several areas.

1. **Population Based Revenues:** Population-based revenues such as the Proposition A Local Transit Assistance Fund were allocated based on the Hollywood population share of 4.99 percent estimated by the County of Los Angeles Urban Research Division (URD) on the basis of the 2000 Census of Population and Housing.
2. **Property Tax:** The property tax was allocated using a fiscal year 2000-01 allocation factor prepared by the County of Los Angeles Auditor-Controller, with a minor adjustment. The allocation factor was estimated by the Auditor-Controller for the Hollywood area. Subsequently, the Executive Officer has recommended various minor boundary adjustments be made to the Hollywood special reorganization area. The Executive Officer estimate adjusts the Auditor-Controller estimate to include estimated property tax in the recommended boundaries. The current property tax estimate is based on the fiscal year 2000-01 tax roll, with reductions for the Community Redevelopment Agency (CRA) revenues associated with the major redevelopment projects located in the Hollywood territory.
3. **Vehicle License Fee:** The vehicle license fee was allocated under the City of Los Angeles current revenues to Hollywood based on the Hollywood population share of 4.99 percent estimated by the County of Los Angeles Urban Research Division (URD). The vehicle license fee boost is additional revenue that would accrue to Hollywood during its first eight years due to a funding formula that provides that new cities' population is calculated based on the number of registered voters. The formula estimates population by multiplying the number of Hollywood registered voters by a factor of three. In the case of Hollywood, this estimate exceeds the URD population estimate resulting in additional vehicle license fee revenues. The CFA calculations were based on March 1999 data on the number of registered voters, whereas the Executive Officer estimate is based on March 2001 data on the number of registered voters (77,723). This results in an increase in the Hollywood vehicle license fee boost to \$12.5 million.
4. **Gas Tax:** The gas tax is special fund revenue allocated similarly to the vehicle license fee. The Executive Officer's estimates reflect the updated population share and most recent count of registered voters in the proposed territory.
5. **Reserve Transfers:** The draws off the reserve fund were allocated in accordance with the recommended term and condition transferring 4.90 percent of the City of Los Angeles general fund reserves to Hollywood. The City's 2000-01 budget envisioned depleting the City's reserve fund balance by \$37 million, but due to revenue windfalls not anticipated in the budget, the City ended up adding \$144 million to its reserves that year. The CFA used the adopted 2000-01 budget figures as its numeric basis. Consistent with its assumption that fund balances would not transfer, the CFA did not allocate the City's draw from its reserve fund to the proposed Hollywood city revenues.
6. **Special Fund Balances:** The terms and conditions recommended by the Subcommittee and Executive Officer allocate a pro-rata share of special fund balances to Hollywood. In the City's adopted FY 2000-01 budget, the City budgeted all available special fund balances as revenues

and did not make explicit allocations for replenishing those fund balances. The actual revenues for past fiscal years have been presented in the City's budget to exclude the fund balances. The Executive Officer has based all fiscal estimates on actual revenues which do not include special fund balances.

Expenditures

In general, the Executive Officer's expenditure estimates took the Comprehensive Fiscal Analysis a starting point. The Executive Officer adjusted the SC3 expenditure estimates to account for various minor boundary adjustments.

1. **Transition Costs:** The Executive Officer followed the numeric recommendations of the State Controller in allocating transition costs and contract administration costs to the proposed new city for purposes of the fiscal viability calculations.
2. **Hollywood City Personnel and Non-Departmental Costs:** The Executive Officer used the CFA estimates of Hollywood city personnel and non-departmental costs for purposes of the fiscal viability calculations.
3. **Fiscal Agent:** The Executive Officer estimates that the fiscal agent responsibilities would occupy at least one full-time experienced accountant, with related costs estimated at \$250,000 annually for purposes of the fiscal viability calculations.
4. **Debt Allocations:** The Executive Officer's debt allocations are based on the recommended terms and conditions.

EXECUTIVE OFFICER FISCAL ALLOCATIONS: TABLES

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TERMS PROPOSED BY THE CITY OF LOS ANGELES AND THE APPLICANT

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