November 14, 2001

Larry J. Calemine
Executive Officer
Los Angeles Local Agency Formation Commission
500 West Temple Street, Room 383
Los Angeles, CA 90012

Re: Special Reorganization in the San Fernando Valley

Dear Larry:

This letter addresses the question of asset allocation asked by the Commission and by LAFCO staff regarding the simultaneous detachment of the San Fernando Valley from the City of Los Angeles and the incorporation of the detached area as a new city. The basic purpose of this letter is to emphasize the enormous power that LAFCO has to structure the proposed special reorganization through use of its terms and conditions authority.

1. LAFCO's Powers: Generally

It is important to remember that LAFCO’s powers are constitutionally based, and are legislatively mandated. The Legislature is vested with all legislative power of the State of California pursuant to the provisions of California Constitution Article IV, Section 1, subject only to the powers of initiative and referendum. Further, California Constitution Article XI, Section 2 (a) requires the Legislature to “prescribe uniform procedure for city formation and provide for city powers.” Pursuant to authority granted to it, the Legislature has adopted a comprehensive statutory scheme to address the formation, organization and reorganization of cities and local public agencies within
the state. That statutory scheme, the one applicable to the special reorganization at hand, is the Cortese-Knox Local Government Reorganization Act of 1985.\(^1\)

The provisions of the Act expressly state the Legislature’s intention that the Act serve as the “sole and exclusive authority and procedure for the initiation, conduct, and completion of changes of organization and reorganization for cities and districts. On and after January 1, 1986, all changes of organization and reorganizations shall be initiated, conducted and completed in accordance with, and as provided in, this division.” (Gov. Code § 56100 (emphasis added).) Further, the Legislature made clear that the powers of LAFCO to affect the purpose of the Act were broad in nature:

This division shall be liberally construed to effectuate its purposes. No change of organization or reorganization ordered under this division and no resolution adopted by the commission making determinations upon a proposal shall be invalidated because of any defect, error, irregularity, or omission in any act, determination or procedure which does not adversely and substantially affect the rights of any person, city, county, district, the state or any agency or subdivision of the state. All determinations made by a commission under, and pursuant to, this division shall be final and conclusive in the absence of fraud or prejudicial abuse of discretion. Prejudicial abuse of discretion is established if the court finds that any determination or a commission or a legislative body was not supported by substantial evidence in light of the whole record. (Gov. Code § 56107 (emphasis added).)\(^2\)

California courts have determined that the Cortese-Knox Local Government Reorganization Act of 1985 preempts local laws regarding municipal reorganizations or changes or organizations because such matters are matters of statewide concern. (Ferrini v. City of San Luis Obispo (1983) 150 Cal.App.3d 239.)

For example, in Friends of Mount Diablo v. County of Contra Costa (1977) 72 Cal.App.3d 1006, the court stated that “LAFCO is a public entity created by legislative fiat, is a body

\(^1\)As you know, the recently enacted Cortese-Knox-Hertzberg Local Agency Reorganization Act of 2000 is inapplicable to the Valley’s special reorganization application because it was filed prior to the effective date of the 2000 version of the Act. Accordingly, all further references to the Act are to the 1985 version of the Act unless otherwise noted.

\(^2\)In other words, it is very difficult to overturn a LAFCO decision. If there is substantial evidence to support LAFCOs decision, the court must rule in its favor.
of special and limited jurisdiction, exercising the function of achieving the fundamental policies which have been determined by the Legislature.” (Friends of Mount Diablo, 72 Cal.App.3d at 1011.) The court further found that District Reorganization Act (“DRA”), one of the predecessors to LAFCO’s current statutory scheme, was “an encompassing regulation over such a statewide concern.” (Friends of Mount Diablo, 72 Cal.App.3d at 1010.)

In Ferrini v. City of San Luis Obispo (1983) 150 Cal. App. 3d 239, the court was asked to evaluate the constitutionality of a San Luis Obispo City Charter provision that allowed its electorate to reject an annexation already approved by LAFCO. The court found that the charter provision was unconstitutional despite the fact that it was enacted pursuant to the City’s home rule powers under California Constitution Article XI, Section 5 (a) because it conflicted with the Municipal Organization Act of 1977 (“MORGA”). The court noted that while charter cities, such as San Luis Obispo, have the power to enforce all “ordinances and regulation in respect to municipal affairs, subject only to restrictions and limitations” in its charter,” they lack the authority to legislate regarding matters of statewide concern. (Ferrini, 150 Cal. App. 3d at 246.) The court concluded that “the municipal charter may not contain provisions pertaining to annexation which are contrary to the general laws of statewide application. ‘The annexation of territory to a city is governed by the general laws of the state and is not a municipal affair, and where a city council proceeds under legislative requirements relating to annexation, such requirements constitute the measure of power to be exercised.’” (Ferrini, 150 Cal App. 3d at 274, citing County of Los Angeles v. City Council (1962) 202 Cal. App.2d 20, 25.) Similarly, in L.I.F.E. Committee v. City of Lodi (1989) 213 Cal.App.3d 1139, the court once again confirmed its position that matters concerning the reorganization of public agencies are matters of statewide concern.

2. **LAFCO’s Powers Over Special Reorganizations**

   The Legislature in 1997 adopted AB 62 which expressly authorized LAFCO to process a special reorganization, such as the one at hand. The term special reorganization is defined as “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.” (Gov. Code §56075.5.) The Legislature could have adopted legislation, outside the parameters of the Cortese-Knox Act that provided specific

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3 The Municipal Organization Act of 1977 is a predecessor to the Cortese-Knox Act.

4 “Proceedings for a special reorganization shall be conducted in accordance with the procedures otherwise prescribed for incorporation of a city, including, but not limited to, the provisions specified in sections 56720, 56800, 56810, and 56815. Notwithstanding any other provision of this division, an election, if required, shall be conducted in accordance with sections 57119 and 57132.5.” (New Gov. Code § 56730). While the provisions of new Government Code section 56730 are not applicable to the current special reorganization proposal, it indicates the Legislature’s intent as to the manner in which such proposals should be processed.

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procedures for the processing of a special reorganization, but it did not. Instead, the Legislature, by adoption of AB 62, granted LAFCO the authority to utilize the already existing provisions of the Cortese-Knox Act to process a special reorganization. The Legislature was aware that each future special reorganization proposal would present unique facts and circumstances, just as each future annexation or detachment processed under the Cortese-Knox Act presents unique facts and circumstances. By charging LAFCO with the duty to process a special reorganization, the Legislature was aware that the provisions of the Cortese-Knox Act would provide the proper procedural structure that LAFCO needed to facilitate navigating and deciding the substantive issues required.

There can be no doubt that the Legislature has expressed its intent that this special reorganization is a matter of statewide concern. In fact, the Legislature has appropriated state funds to aid in determining whether this special reorganization is feasible. (see, S.B. 160, item 92101-119-0001 (1999).) What this means is that the provisions of the Cortese-Knox Act were intended by the California Legislature to preempt the field and supersede the provisions of a general law or a charter city covering the same subject matter as this special reorganization.

We think it is important at this point to clearly look at the current special reorganization proposal. This proposal is not about the creation of a new city from county territory resulting in two distinct different levels of government between a county and the city. As you know, a county and a city generally provide different types of services, with the county providing predominately municipal court services, health and social services, jails and in some cases offering and providing county municipal services to a newly formed city. However, the newly formed city, as a distinct different level of government, does not provide county services. For example, a new city would not operate its own county sheriff’s department, thus, in such an instance it would not be appropriate to transfer a sheriff station to the new city. This proposal, in contrast, is a special reorganization that takes an existing city with existing infrastructure and existing services, revenues, assets and liabilities and creates two cities. In a special reorganization one existing city is reorganized into two resulting cities that will be responsible to provide to their respective residents with the same services. Some of the existing residents of the existing city will become residents of the new city. Similarly, a proportionate share of the existing assets and existing liabilities of the old city will become assets and liabilities of the new city.

3. Transfer of Assets and Liabilities

Government Code Section 56844 gives LAFCO the authority to proportionately allocate the assets and liabilities from the original city to the two or more resulting cities without payment. The Applicant and the City of Los Angeles, in negotiation sessions facilitated by you and your staff, have identified the following categories of assets: a) Cash and other liquid assets and liabilities; b) Municipal service-supporting assets and liabilities; c) Regional utility assets and liabilities; and d) Municipal enterprise assets and liabilities. It is our experience that assets are generally transferred to the new city without payment. Typically liabilities associated with particular
assets follow the transferred assets and visa versa

We believe that LAFCO has the authority to allocate the assets between the resulting cities. Assets to be allocated by LAFCO would include, but are not limited to, public roads, adjacent slopes, medians, sidewalks, bikeways, streetlights, traffic signals, bridges, open space, local and community recreation facilities, local drainage devices, storm drain channels, easements and dedications, surplus land designated for local municipal uses, applicable trust funds, cash on hand, monies due but not collected, benefits and rights of applicable developer agreements, equipment appurtenant to a transferred facility, rolling stock, copy of all applicable records and files, local redevelopment agency assets, local municipal service facilities including fire stations, police stations, libraries, local municipal meeting and office facilities, rights to use of water, and any other property or assets directly associated with the provision of local municipal services.

Dan Miller will provide a matrix of specific assets transferred in past incorporations for your reference. The fact that there is no history of special reorganizations to refer to by way of example, does not limit the authority granted to LAFCO under the Cortese-Knox Act to provide an equitable allocation of the assets between the resulting cities. Nothing in the Cortese-Knox Act limits in any way the classes or specific types of assets that LAFCO may allocate as part of this proposal. We believe LAFCO should use its discretion and authority as granted to it by the Legislature to create an equitable proposal for the residents of the resulting cities.

It has been suggested that the Valley city pay the resulting City of Los Angeles for an assets that are allocated to it. To make either resulting city pay for allocated assets results in multiple payment for those assets. This is especially true where, in this instance the proposed Valley city has been contributing over $60 million more each year to the City of Los Angeles than it receives in return from the City of Los Angeles. All of the assets have already been purchased by all of the residents. If one were to require that all assets transferred to the resulting Valley city be paid for by the resulting Valley city to the resulting City of Los Angeles, then under the same logic, the resulting City of Los Angeles should pay to the resulting Valley city the cost of all of the assets not transferred to the resulting Valley city.

For example, suppose that you transfer an existing local park in the valley to the new Valley city. That park already exists. The resulting Valley city would then pick up the maintenance costs of the park and the capital costs of any improvements to the park. This would relieve the resulting City of Los Angeles of those costs. The residents of the entire city paid for the park. At the same time, a park remaining in the resulting City of Los Angeles serving the resulting City of Los Angeles, but paid for in part by residents of the resulting Valley city, would not be charged against the resulting City of Los Angeles. In other words, the resulting Valley city is going to leave assets that it has partially paid for with the resulting City of Los Angeles without compensation. It is not equitable to charge the resulting Valley city for the assets that provide local services to the resulting Valley city that already exist.
It is clear that assets such as streets and highways statutorily flow to the new city upon incorporation. (Gov. Code § 57385.) The distribution of other assets and liabilities, we believe, are within LAFCO’s discretion to determine. In an analogous situation, the court found that it was within the discretion of the Legislature to determine the manner in which the assets and liabilities of an existing county were distributed to a new county. In County of Tulare v. County of Kings (1897) 117 Cal. 195, the court noted that while the Constitution provided that newly created counties shall be liable for a “just proportion of the existing debts and liabilities of the county of counties from which such territory shall be taken,” it concluded that it was up to the Legislature to determine “what that just proportion may be.” (County of Tulare, 117 Cal. at 196-197.)

Similarly, the California Constitution provides the authority for the Legislature to “prescribe uniform procedure for city formation and provide for city powers.” (Cal. Const. art. XI, § 2 (a).) The Legislature has the discretion to determine exactly what this “procedure” entails. By adoption of procedures in the Cortese-Knox Act the Legislature authorized LAFCO to utilize its discretion to process special reorganizations within the provisions of the Act. As we stated above, this is not the typical incorporation. Rather, it is a special reorganization that includes the division of an existing city into two resulting cities.

The fact that proprietary departments of the City of Los Angeles are involved has no impact on LAFCO’s ability to transfer assets to the proposed Valley city. We believe that pursuant to the authority granted to the Legislature under California Constitution, Article XI, Section 2, and delegated by the Legislature to LAFCO, LAFCO has the authority to distribute such assets. This is so despite the provisions of Constitution, Article XI, Section 9 which permits municipalities to own and operate municipal utilities.

General rules of constitutional construction require that:

Constitutional provisions adopted by the People are to be interpreted so as to effectuate the voters’ intent, and if the intent is clear from the language used, there is no room for further judicial interpretation.

5The California Streets and Highways Code defines the terms “highways” as follows:

“highway” includes bridges, culverts, curbs, drains, and all works incidental to highway construction, improvement, and maintenance. (Sts. & Hy. Code § 23.)
If there is a seeming conflict between two constitutional provisions, rules of constitutional construction require harmonization or reconciliation of the provisions. (State Board of Education v. Honig (1993) 13 Cal.App.4th 720, 758-59.)

Here, it is clear that the language of Article XI, Section 2 mandates that the Legislature prescribe uniform procedures for the formation of cities and provide for the powers of cities. The language of Article XI, Section 9, on the other hand, merely permits municipalities to "establish, purchase, and operate public works to furnish its inhabitants with light, water, power, heat, transportation, or means of communication." We believe that an appropriate reading of these two constitutional provisions allows the Legislature to proscribe procedures for the formation of cities which can include the distribution of assets owned by a municipal utility to a portion of the constituency that currently owns and is served by that utility. To conclude otherwise could result in limiting the ability of the Legislature to proscribe procedures for city formation in any instance where a municipal utility is involved. This interpretation furthers the rules of constitutional construction by not limiting the Legislature's constitutional authority under Article XI, Section 2, or precluding municipalities from choosing to operate public utilities under Article XI, Section 9.

a. There is no "Taking"

The concept of a division of the existing city into two cities is important in our understanding of the possible payment for transferred assets. It has been argued that a forced division of assets without compensation is similar to an eminent domain action where property cannot be taken without just compensation. We believe this is a flawed analysis.

6 It is interesting to note that while such utilities are formed pursuant to the California Constitution, the Legislature retains the authority to take action to regulate municipal utilities. (See, Polk v. Los Angeles (1945) 26 Cal.2d 519 (holding that California Public Utility Commission safety rules related to electric power line maintenance apply to municipal utilities); Harbor Carriers, Inc. v. Sausalito (1975) 46 Cal.App.3d 773 (holding that orders adopted by the California Public Utilities Commission trump conflicting municipal actions). See also, County of Inyo v. Los Angeles Department of Water and Power (1980) 26 Cal.3d 154 (holding that there was no constitutional barrier to regulation of municipal utility rates by the California Public Utilities, but that the Legislature had not exercised its authority under Article XII to confer it such jurisdiction).
The provisions of the California Constitution related to eminent domain are inapplicable to the division of assets involved in the present special reorganization. Stated another way, there is no "taking" involved. Article I, Section 19 of the California Constitution provides:

Private property may be taken or damaged for public use only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner.

This Constitutional provision deals with the taking of property without just compensation as opposed to the division of ownership rights of the property currently owned by two parties. A "taking" in its distilled form involves a situation where A, who has no interest in the subject property, takes property owned by B, for A's purposes. The Constitution mandates that A must pay B for taking away B's ownership interest in the property. Here, we have an "A" and "B," both of which hold an ownership interest in the subject property. The division of the ownership interests between A and B do not constitute a taking under the Constitution. The law of eminent domain simply has no application to this matter of municipal law.

This special reorganization is similar to a partition action or to a dissolution of marriage. If there is no agreement upon the division of assets and liabilities, the court (or, in this case, LAFCO), can divide them between the parties. It is again important to note that the Valley consists of 1.4 million people who each year contribute $60 million more to the rest of the city than they receive in return from the city. This is not a taking of assets of one entity to give to another entity. These assets belong to the people who will form the new entity.

Further, the assets (and liabilities) are not being taken by a LAFCO term or condition; LAFCO cannot make this special reorganization happen. The most it can do is approve it and send it on to the voters for a decision. As an additional measure of fairness, the Legislature required that the proposal pass in the territory proposed for the special reorganization and in the entire city. This is clearly not a taking.

Our consulting team has had extensive experience in evaluating asset transfers in incorporations throughout the state. We pledge to work with you to develop an efficient procedure to provide for such an asset transfer. It is our desire to assist you in developing a record that shows that there is substantial evidence for the types of transfers of assets that occur. Nothing precludes you from transferring assets without compensation as we propose.
We urge you to exercise your authority to generally transfer assets located in the valley to the new city without compensation. We will work with you to make sure that this process works to the benefit of all the citizens of the new Valley city without harm to the remaining citizens of the City of Los Angeles.

Very truly yours,

Clark H. Alsop
of BEST BEST & KRIEGER LLP

cc: Jeff Brain, Valley Study Foundation, Inc.
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