December 8, 2012

Mr. Jerry Schwartz, Economic Development Manager
City of Arcadia
240 West Huntington Drive
Arcadia, CA 91065

Dear Mr. Schwartz:

Subject: Low and Moderate Income Housing Fund Due Diligence Review

This letter supersedes Finance's original Low and Moderate Income Housing Fund (LMIHF) Due Diligence Review (DDR) determination letter dated November 6, 2012. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Arcadia successor agency (Agency) submitted an oversight board approved LMIHF DDR to the California Department of Finance (Finance) on October 10, 2012. Finance issued a LMIHF DDR determination letter on November 6, 2012. Subsequently, the Agency requested a Meet and Confer session on one or more items adjusted by Finance. The Meet and Confer Session was held on December 4, 2012.

Based on a review of additional or clarifying information provided to Finance during the Meet and Confer process, Finance continues to believe the adjustments made to the DDR's stated balance of LMIHF available for distribution to the taxing entities is appropriate. HSC section 34179.6 (d) authorizes Finance to make these adjustments. We maintain the adjustment continues to be necessary for the following reasons:

- The Agency contends the retention of $3.35 million for a required loan payment in January 2015 related to the Arcadia Campus project is necessary. This expense associated with the Arcadia Campus project was listed as an enforceable obligation on the Recognized Obligation Payment Schedules (ROPS) periods of January through June 2012, July through December 2012, and Janaury through June 2013, although no funding was requested.

  Finance originally denied the Agency's request to retain $3.35 million due to a lack of evidence there would be insufficient property taxes to pay the specified obligation. During the Meet and Confer process, the Agency provided a projection of annual revenue and spending requirements suggesting there will be insufficient tax increment to cover this expense when it comes due in January 2015. The Agency contends they must retain the funds to honor the loan.

  The Agency's cash flow analysis indicates HSC section 34186 will affect tax increment available for current enforceable obligations. However, HSC section 34186 is intended to adjust for differences between estimated and actual expenditures from prior periods and should not contribute to current cash deficiencies. Further, the cash flow analysis suggests the available tax increment will experience an annual decrease of approximately 6 percent. A more likely scenario is that the available tax increment will increase.

The loan agreement requires a $3.4 million payment in January 2015 only if all conditions outlined in Section 2.7 of the loan agreement have been met. Therefore, there is a possibility this payment will never materialize. Further, it is not evident in the loan agreement that retention of these balances is a specific requirement

Should this payment materialize and should a deficit occur, HSC provides successor agencies with various methods to address short term cash flow issues. These may include requesting a loan from the city pursuant to HSC section 34173 (h), or requesting the accumulation of reserves on the ROPS when a future balloon or uneven payment is expected. The Agency should seek counsel from their oversight board to determine the solution most appropriate for their situation. Since the Agency has alternatives to address short term cash flow shortages, Finance deems it is not necessary for Agency to retain the requested funds.

The Agency's LMIHF balance available for distribution to the affected taxing entities continues to be $6,784,469 (see table below).

| LMIHF Balances Available For Distribution To Taxing Entities | | |
|---|---|---|
| Available Balance per DDR: | $ | 3,428,904 |
| Finance Adjustments | | |
| Add: | | |
| Requested retained balance not supported: | | 3,355,565 |
| **Total LMIHF available to be distributed:** | $ | 6,784,469 |

This is Finance's final determination of the LMIHF balances available for distribution to the taxing entities. HSC section 34179.6 (f) requires successor agencies to transmit to the county auditor-controller the amount of funds identified in the above table within five working days, plus any interest those sums accumulated while in the possession of the recipient.

If funds identified for transmission are in the possession of the successor agency, and if the successor agency is operated by the city or county that created the former redevelopment agency, then failure to transmit the identified funds may result in offsets to the city's or the county's sales and use tax allocation, as well as its property tax allocation. If funds identified for transmission are in the possession of another taxing entity, that Agency's failure to recover and remit those funds may result in offsets to the other taxing entity's sales and use tax allocation or to its property tax allocation. If funds identified for transmission are in the possession of a private entity, HSC 34179.6 (h) (1) (B) states that any remittance related to unallowable transfers to a private party may also be subject to a 10 percent penalty if not remitted within 60 days.

Failure to transmit the identified funds will also prevent the Agency from being able to receive a finding of completion from Finance. Without a finding of completion, the Agency will be unable to take advantage of the provisions detailed in HSC section 34191.4. Specifically, these provisions allow certain loan agreements between the former redevelopment agency (RDA) and the city, county, or city and county that created the RDA to be considered enforceable obligations. These provisions also allow certain bond proceeds to be used for the purposes in which they were sold and allows for the transfer of real property and interests into the Community Redevelopment Property Trust Fund once Finance approves the Agency's long-range property management plan.

In addition to the consequences above, willful failure to return assets that were deemed an unallowable transfer or failure to remit the funds identified above could expose certain individuals to criminal penalties under existing law.

Pursuant to HSC section 34167.5 and 34178.8, the California State Controller's Office (Controller) has the authority to claw back assets that were inappropriately transferred to the city, county, or any other public agency. Determinations outlined in this letter and Finance's Housing Assets Transfer letter dated August 31, 2012 do not in any way eliminate the Controller's authority.

Please direct inquiries to Kylie Le, Supervisor or Michael Barr, Lead Analyst at (916) 445-1546.

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Mr. Jason Kruckeberg, Assistant City Manager/Development Services Director, City of Arcadia
Ms. Elizabeth Hull, Agency Counsel, BBK Law
Ms. Shannon Huang, Financial Services Director and City Treasurer, City of Arcadia
Ms. Kristina Burns, Manager, Los Angeles County Auditor-Controller's Office
California State Controller's Office