December 15, 2012

Mr. David Loya, Community Development Deputy Director
City of Arcata
736 F Street
Arcata, CA 95521

Dear Mr. Loya:

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 9, 2012. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Arcata Successor Agency (Agency) submitted an oversight board approved LMIHF DDR to the California Department of Finance (Finance) on October 11, 2012. Finance issued a LMIHF DDR determination letter on November 9, 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 November 28, 2012.

Based on a review of additional or clarifying information provided to Finance during the Meet and Confer process, Finance is revising an adjustment made in our previous DDR determination letter. Specifically, we are revising the following adjustment:

- Assets transferred in the amount of $1,858,432. Finance initially disallowed $753,570 of the $1,858,432 total cash transferred during March 2011 to the City of Arcata (City) because the amount was not supported by an enforceable obligation. Amounts allowed consisted of $600,000 for the Plaza Point Development (Plaza) and $504,862 for the Sandpiper Mobile Home Park (Sandpiper) projects. However, based on review of information and clarification provided by the Agency during the meet and confer, Finance is reversing its initial decision to allow $1,104,862 because the total transfer of $1,858,432 was not obligated by the redevelopment agency (RDA).

  The Sandpiper project's remaining obligation of $1,953,000 was not originally in the RDA's October 2010 agreement, in which City as the housing entity executed first and second amendments during September 2011 and June 2012, respectively. Additionally, the Plaza project's remaining obligation of $200,000 was not specified as being funded with LMIHF in the RDA's agreement executed in March 2011. Per HSC 34163 (c)(5), the RDA was not allowed to transfer funds out of the LMIHF, except to meet the minimum housing-related obligations that existed as of January 1, 2011. Therefore, the $1,858,432 transferred during March 2011 is not allowed.

Further, Finance continues to believe some of 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 reason:

- Balances retained for an enforceable obligation in the amount of $250,000. Our review indicated the amount retained for a housing replacement project did not qualify as an enforceable obligation. According to the Agency, because the RDA demolished two housing units, the Agency is required to make available two housing units in compliance with HSC section 33413 (a). The project was not listed on any of the Agency's Recognized Obligation Payment Schedules and no contract has been executed. The Sandpiper project, which created this replacement housing obligation, was transferred to the City in March 2011. Obligations associated with the former RDA's previous statutory housing obligations are not enforceable obligations. Upon the transfer of the former RDA's housing functions to the new housing entity, HSC section 34176 requires that, "all rights, powers, duties, obligations and housing assets, ...shall be transferred" to the new housing entity. This transfer of "duties and obligations" necessarily includes the transfer of statutory obligations to the extent any continue to be applicable. To allow such housing obligations as an on-going enforceable obligation of the Agency would require a transfer of tax increment for life, which directly is contrary to the wind down directive in ABx1-26/AB1484. Therefore, the amount is not allowed to be retained.

The Agency's LMIHF balance available for distribution to the affected taxing entities has been revised to $2,415,359 (see table below).

LMIHF Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	306,927
Finance Adjustments		
Add:		
Disallowed transfers		1,858,432
Retained balance not supported		250,000
Total LMIHF available to be distributed:	$	2,415,359

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, the successor agency is required to take diligent efforts to recover such funds. A 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 Beliz Chappuie, Supervisor or Cindie Lor, Lead Analyst at (916) 445-1546.

Sincerely,

for

STEVE SZALAY
Local Government Consultant

cc: Ms. Janet Luzzi, Finance Director, City of Arcata
Ms. Nancy Diamond, Attorney, Law Offices of Nancy Diamond
Mr. Joe Mellet, Auditor-Controller, County of Humboldt
California State Controller's Office