January 17, 2013

Ms. Kellee Fritzal, Deputy Director
City of Huntington Beach
2000 Main Street
Huntington Beach, CA 92648-2702

Dear Ms. Fritzal:

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 19, 2012. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Huntington Beach Successor Agency (Agency) submitted an oversight board approved LMIHF DDR to the California Department of Finance (Finance) on November 1, 2012. Finance issued a LMIHF DDR determination letter on December 12, 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 7, 2012.

Based on a review of additional or clarifying information provided to Finance during the Meet and Confer process, Finance is revising some of the adjustments made in our previous DDR determination letter. Specifically, we are revising the following adjustments because these items were not properly classified in the DDR:

- Transfer in the amount of $6,500,000 made pursuant to an Owner's Participation Agreement (OPA) with Makallon Atlanta Huntington Beach, LLC (Makar). Finance originally determined the transfer was ineligible because the OPA was never implemented by Makar. Based on information provided during the Meet and Confer session, it was determined no cash was transferred to the Housing Successor.

  It was noted that Finance denied the Makar OPA during the Housing Asset Transfer (HAT) review in our letter dated August 31, 2012. Because the Meet and Confer process for the HAT has not been completed, the item is still denied for transfer to the Housing Successor and may still be questioned in current and future Recognized Obligation Payment Schedule (ROPS) reviews.

- Lease Revenue Refunding Bonds in the amount of $4,054,198. Finance originally denied this item because repayment of the bonds is secured by lease payments, and not Redevelopment Property Tax Trust Funds (RPTTF) or LMIHF. Based on information provided during the Meet and Confer session, it was determined that this item was identified in the DDR as an obligation, and should not have been classified as an asset transfer.

- Loan repayments to BTDJM Phase II Associates, LLC, in the amount of $15,722,100. Finance originally denied this item because the Agency requested RPTTF to fund this obligation during the ROPS submitted for the periods covering January 2012 through June 30, 2013. Based on information provided during the Meet and Confer session, it was determined that this item was identified in the DDR as an obligation, and should not have been classified as an asset transfer.

However, 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 adjustments continue to be necessary for the following reason:

- The Agency requested the retention of $4,860,535 to help pay for the above-mentioned housing obligations. According to information provided by the Agency, $4,959,145 in cash was transferred to the Housing Successor. However, the ROPS covering the January 2012 through June 2013 periods only requested $98,610 in LMIHF obligations; therefore, Finance continues to object to the transfer of $4,860,535.

The Agency's LMIHF balance available for distribution to the affected taxing entities has been revised to $4,860,535 (see table below).

| **LMIHF Balances Available For Distribution To Taxing Entities** | | |
|---|---|---|
| Available Balance per DDR: | $ | - |
| Finance Adjustments | | |
| Add: | | |
| Disallowed transfers | $ | 31,136,833 |
| Revised adjustments | $ | (26,276,298) |
| **Total LMIHF available to be distributed:** | $ | 4,860,535 |

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 Nichelle Thomas, Supervisor or Alex Watt, Lead Analyst at (916) 445-1546.

Sincerely,

For

STEVE SZALAY
Local Government Consultant

cc: Lori Ann Farrell, Director of Finance, City of Huntington Beach
Frank Davies, Property Tax Manager, Orange County
California State Controller's Office