DEPARTMENT OF FINANCE

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April 25, 2013

Ms. Colleen O'Donoghue, Assistant Finance Director
City of Costa Mesa
77 Fair Drive, 1st Floor
Costa Mesa, CA 92626

Dear Ms. O'Donoghue:

Subject: Other Funds and Accounts Due Diligence Review

This letter supersedes the California Department of Finance's (Finance) original Other Funds and Accounts (OFA) Due Diligence Review (DDR) determination letter dated March 20, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Costa Mesa Successor Agency (Agency) submitted an oversight board approved OFA DDR to the California Department of Finance (Finance) on January 11, 2013. The purpose of the review was to determine the amount of cash and cash equivalents available for distribution to the affected taxing entities. Finance issued an OFA DDR determination letter on March 20, 2013. 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 April 4, 2013.

Based on a review of additional information and documentation provided to Finance during the Meet and Confer process, Finance has completed its review of those specific items being disputed. Specifically, the following adjustments were made:

- Our review indicates that $2,609,617 was transferred to the City of Costa Mesa (City) to pay for a series of loans the City made to the Agency between 1971 and 1993. The Agency was created in 1972. HSC section 34179.5 states "enforceable obligation" includes any of the items listed in subdivision (d) of section 34171. HSC section 34171 (d) (2) states "enforceable obligation" does not include any agreements, contracts, or arrangements between the city that created the RDA and the former RDA unless issued within the two years of the Agency's creation or at the same time and solely for the purpose of issuing debt. The Agency claims the loan, issued one year prior to the Agency's creation is within two years of the Agency's creation.

  The Agency issued a new promissory note each time new funds were loaned by the City. Each promissory note between 1971 and 1978 was either paid or refinanced by a subsequent loan. Per the documentation provided by the Agency, the amounts loaned within the first two years were fully paid back to the City by January 1980; therefore the amounts transferred to the City in 2011 were for loans not made within two years of the Agency's creation. Therefore, the transfer was not made pursuant to an enforceable obligation and is not permitted. The OFA balance available for distribution will be increased by $2,609,614.

Finance notes the repayment of these loans may become enforceable obligations after the Agency receives a finding of completion from Finance. If the oversight board makes a finding that the loans were for legitimate redevelopment purposes, these loans should be placed on future Recognized Obligation Payment Schedules (ROPS) for repayment. Refer to HSC section 34191.4 (b) for more guidance.

- The DDR includes $13,661 needed to pay for approved enforceable obligations incurred during the January through June 2012 ROPS (ROPS I) period. Our review indicates these costs were approved on the ROPS I and incurred during the ROPS I period; however, they were paid after June 30, 2012. As such, the Agency will be permitted to retain these funds.

- The Agency requested to retain $2,090,874 in balances needed to satisfy ROPS for the 2012-13 fiscal year. Our review indicates the Agency did not receive all Redevelopment Property Tax Trust Funds (RPTTF) approved for the July through December 2012 ROPS (ROPS II) period. Therefore, the Agency will be permitted to retain the funds to satisfy ROPS II obligations.

  Should a deficit occur in the future, 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), requesting the accumulation of reserves on the ROPS when a future balloon or uneven payment is expected, or subordinating pass-through payments pursuant to HSC section 34183 (b). The Agency should seek counsel from their oversight board to determine the solution most appropriate for their situation if a deficiency were to occur.

The Agency's OFA balance available for distribution to the affected taxing entities is $2,492,747 (see table below).

OFA Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	(116,867)
Finance Adjustments		
Add:		
Disallowed transfers	$	2,609,614
Requested retained balance not supported		0
Total OFA available to be distributed:	$	2,492,747

This is Finance's final determination of the OFA 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. Upon submission of payment, it is requested you provide proof of payment to Finance within five business days.

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 sections 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 do not in any way eliminate the Controller's authority.

Please direct inquiries to Evelyn Suess, Supervisor or Danielle Brandon, Analyst at (916) 445-1546.

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Mr. Bobby Young, Finance Director, City of Costa Mesa
Ms. Willa Bouwens-Killeen, Principal Planner, City of Costa Mesa
Mr. Frank Davies, Property Tax Manager, Orange County
California State Controller's Office