DEPARTMENT OF FINANCE

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May 5, 2013

Mr. John B. Bahorski, City Manager
City of Cypress
5275 Orange Avenue
Cypress, CA 90630

Dear Mr. Bahorski:

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 April 1, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Cypress Successor Agency (Agency) submitted an oversight board approved OFA DDR to Finance on January 9, 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 April 1, 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 23, 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:

- The Agency's request to retain $62,739 for administrative costs is allowed. The Agency contends that $9,520 in administrative costs were incurred on the Recognized Obligation Payment Schedule (ROPS) for the January through June 2012 ROPS (ROPS I) period, but paid after June 30, 2012. Finance verified these costs were approved on the ROPS I form and that the costs were actually incurred during the ROPS I period, but paid after June 30, 2012. Due to the timing of ROPS I and the July through December 2012 ROPS (ROPS II) submittals, the $9,520 was not included on the ROPS II form. The remaining $53,219 was to cover administrative costs in the ROPS II period. Since no funds were received from the Redevelopment Property Tax Trust Fund in the ROPS II period, the Agency may retain OFA balances to cover the administrative costs. Therefore, the Agency may retain $62,739 to cover the ROPS I expenditures paid after June 30, 2012, and administrative costs in the ROPS II period.

  Finance notes that amounts requested and approved in a ROPS are effective only for the six-month period covered. To the extent the Agency does not expend funds approved and received on a ROPS until a subsequent period, the Agency should relist the unexpended amounts that need to be retained for those enforceable obligations on the subsequent ROPS with the funding source as "Reserves" or "Other" and an entry in the Notes section indicating the funds were received in a prior ROPS period.

- Our review indicates that $2,048,839 was transferred to the City of Cypress (City) and was previously disallowed by Finance. The amount consists of $1,196,000 for an interest payment made by the former Redevelopment Agency (RDA) to the City on outstanding loans and two payments totaling $852,839 in accordance with a 2001 reimbursement agreement for debt service payments on the 2001 Lease Revenue Bonds. Per HSC section 34179.5 (c) (2), the dollar value of assets and cash transferred by the former RDA or successor agency to the city, county, or city and county that formed the former RDA between January 1, 2011 through June 30, 2012 must be evidenced by documentation of the enforceable obligation that required the transfer. 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; however, written agreements entered into at the time of issuance, but in no event later than December 31, 2010, and solely for the purpose of securing or repaying indebtedness obligations may be deemed enforceable obligations.

  The former RDA entered into a reimbursement agreement with the City on July 1, 2001, to use tax increment to pay debt service payments for Lease Revenue Bonds issued July 1, 2001. Therefore, the reimbursement agreement meets the exception in HSC section 34171 (d) (2) and is an enforceable obligation. The $852,839 transfer is permitted. However, the $1,196,000 transfer was made for interest payments on outstanding promissory notes between the City and the former RDA; therefore, the transfer was not made pursuant to an enforceable obligation and the OFA balance available will be increased by $1,196,000.

  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 ROPS for repayment. Refer to HSC section 34191.4 (b) for more guidance.

- Transfer of $18,580,000 in land to the City is disallowed. The Agency claims the transferred land was purchased in 2006 with advances received from the City's General Fund. The Agency also claims that the transfer to the City was to repay this loan and was recorded at fair market value consideration. However, HSC section 34167.5 states asset transfers after January 1, 2011, between the city or county, or city and county that created a RDA for which an enforceable obligation does not exist is not permitted. HSC section 34179.5 states "enforceable obligation" includes any of the items listed in subdivision (d) of section 34171. Further, 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. The loan was issued after the first two years of the RDA's creation; therefore, the transfer of property to repay the loan was not permitted. Since property is not considered cash or cash-equivalent asset, Finance has made no adjustment to the available balance to the affecting taxing entities.

  This non-liquid asset transferred to the City is subject to the California State Controller's Office review of asset transfers. To the extent these properties do not meet criteria outlined in HSC section 34181 (a), they should be returned to the Agency and disposed of in a manner consistent with the Agency's Long Range Property Management Plan pursuant to HSC section 34191.5.

Finance notes, however, that to the extent the City would like to retain these parcels, HSC section 34191.5 (c) (2) states that one of the property disposition options available to the successor agency of the former RDA is the retention of property for future development purposes pursuant to an approved LRPMP. If this option is selected, HSC section 34180 (f) (1) states that the city, county, or city and county must reach a compensation agreement with the other taxing entities to provide payments to them in proportion to their shares of the base property tax, as determined pursuant to HSC section 34188, for the value of the property retained.

The Agency's OFA balance available for distribution to the affected taxing entities is $156,637 (see table below).

OFA Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	(1,039,363)
Finance Adjustments		
Add:		
Disallowed transfers	$	1,196,000
Total OFA available to be distributed:	$	156,637

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. Matt Burton, Assistant Director of Finance & Administrative Services
Mr. Frank Davies, Property Tax Manager, Orange County
California State Controller's Office