

April 1, 2013

Gilbert Rojas, Director of Finance
City of Escondido
201 North Broadway
Escondido, CA 92025

Dear Mr. Rojas:

Subject: Other Funds and Accounts Due Diligence Review

Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Escondido (Agency) submitted an oversight board approved Other Funds and Accounts (OFA) Due Diligence Review (DDR) to the California Department of Finance (Finance) on January 10, 2013. The purpose of the review was to determine the amount of cash and cash equivalents available for distribution to the affected taxing entities. Pursuant to HSC section 34179.6 (d), Finance has completed its review of your DDR, which may have included obtaining clarification for various items.

HSC section 34179.6 (d) authorizes Finance to adjust the DDR's stated balance of OFA available for distribution to the taxing entities. Based on our review of your DDR, the following adjustments were made:

- Assets transferred in the amount of \$20 million. The former Community Development Commission of Escondido transferred cash in the amount of \$20 million to the City of Escondido (City) on February 16, 2011. The transfer was to accelerate a City loan repayment. However, HSC section 34171 (d) (2) states agreements, contracts, or arrangements between the city, county, or city and county that created the redevelopment agency (RDA) and the former RDA are not enforceable obligations.

It is our understanding that upon receiving the July True-Up Demand Letter from the county auditor controller (CAC), the City Council via Resolution 2012-132R ordered this transfer reversed. However, instead of transferring back \$20 million in cash, the Agency received \$13.2 million in cash as well as property purchased with the funds valued at \$6.7 million. HSC section 34163 (b) prohibits an Agency from entering into contracts with any entity for any purpose after June 28, 2011. Since the return of inappropriate asset transfers occurred in or around July 2012, the Agency was unauthorized to accept property in lieu of the liquid asset that was originally transferred.

To protect assets of the former RDAs, HSC section 34167.5 gives the California State Controller's Office (Controller) the authority to claw back assets that were inappropriately transferred to the city, county, or any other public agency after January 1, 2011. In addition, HSC section 34179.6 (d) authorizes Finance to adjust the DDR in order to

protect balances due to the affected taxing entities. As such, the amount available for distribution to taxing entities will be adjusted by \$20 million.

After the Agency receives a Finding of Completion from Finance, these loans may become enforceable and eligible to be repaid through the Recognized Obligation Payment Schedule (ROPS) process.

- Balances requested to be retained in the amount of \$4.8 million for fiscal year 2012-13 obligations are partially denied. The Agency has demonstrated an immediate need to retain some of these funds to meet approved bond debt payments in the ROPS II and III periods. Specifically, the Agency has proven that \$2.8 million for the ROPS II period and \$792,716 for the ROPS III period is needed to ensure adequate funding for debt service, when combined with RPTTF distributions. This retention will also allow for a \$2 million reserve to ensure adequate funding for upcoming bond payments in the ROPS 13-14A period. Therefore, Finance is adjusting the \$4.8 million by \$1.2 million to allow retention of \$3.6 million.

Finance is only allowing the retention of funds that are sufficient to meet the Agency's bond debt obligations. Although Finance may have approved more obligations to be funded with Redevelopment Property Tax Trust Fund (RPTTF) than was available for distribution, the Agency is limited to retaining the amount of RPTTF distributed by the CAC. However, as stated, Finance is allowing the retention of additional funds to ensure adequate funding for bond payments.

To the extent there were other unfunded items that constitute enforceable obligations, the Agency should request funding for these in a future ROPS. In addition, 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 Recognized Obligation Payment Schedule (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.

If you disagree with Finance's adjusted amount of OFA balances available for distribution to the taxing entities, you may request a Meet and Confer within five business days of the date of this letter. The Meet and Confer process and guidelines are available at Finance's website below:

http://www.dof.ca.gov/redevelopment/meet_and_confer/

The Agency's OFA balance available for distribution to the affected taxing entities is \$6,534,396 (see table on the next page).

OFA Balances Available For Distribution To Taxing Entities	
Available Balance per DDR:	\$ (14,675,543)
Finance Adjustments	
Add:	
Disallowed cash transfer	\$ 20,000,000
Requested retained balance not supported:	\$ 1,209,939
Total OFA available to be distributed:	\$ 6,534,396

Absent a Meet and Confer request, 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 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 do not in any way eliminate the Controller's authority.

Mr. Gilbert Rojas
April 1, 2013
Page 4

Please direct inquiries to Wendy Griffe, Supervisor or Derk Symons, Lead Analyst at (916) 445-1546.

Sincerely,

A handwritten signature in black ink, appearing to read 'Steve Szalay', with a long horizontal stroke extending to the left.

STEVE SZALAY
Local Government Consultant

cc: Ms. Joan Ryan, Finance Manager, City of Escondido
Mr. Juan Perez, Senior Auditor and Controller Manager, County of San Diego
California State Controller's Office