DEPARTMENT OF FINANCE
EDMUND G. BROWN JR. ▪ GOVERNOR
915 L STREET ▪ SACRAMENTO CA ▪ 95814-3706 ▪ WWW.DOF.CA.GOV

September 20, 2013

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

Dear Ms. Fritzal:

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 August 15, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Huntington Beach Successor Agency (Agency) submitted an oversight board approved OFA DDR to Finance on June 3, 2013. The purpose of the review was to determine the amount of cash and cash equivalents available for distribution to the affected taxing entities. Since the Agency did not meet the January 15, 2013 submittal deadline pursuant to HSC section 34179.6 (c), Finance was not bound to completing its review and making a determination by the April 1, 2013 deadline pursuant to HSC section 34179.6 (d). Finance issued an OFA DDR determination letter on August 15, 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 September 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:

- Transfers in the amount of $5,078,834 to the City of Huntington Beach (City) were not allowed. The former redevelopment agency (RDA) transferred a total of $5,485,765 in cash to the City during the period January 1, 2011 to September 30, 2011. Of the total cash transferred, $406,931 was supported by an enforceable obligation for payments for the 2010 Series A Lease Revenue Refunding Bond. Based on further review during the Meet and Confer process, the Agency provided supporting documents showing that an additional transfer of $409,483 occurred on January 1, 2011, which is outside of the period for disallowed transfers per HSC section 34179.5 (c) (2).

  The remaining transfers represent payments to the City in relation to multiple cooperative agreements between the City and the former RDA entered into between 1983 through 2003 and amended annually from 2004 through 2011. However, 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 created the former RDA after 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, contracts detailing specific work that were entered into by the former RDA prior to June 28, 2011, with a third party other than the city, county, or city and county that created the former RDA. 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. Therefore, the transfers were not made pursuant to an enforceable obligation and are not permitted. The OFA balance available will be increased by $4,669,451 ($5,485,765 - $406,931 - $409,383).

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 request to retain balances totaling $12,241,970 to satisfy future enforceable obligations was originally decreased by $8,813,384. Based on further review during the Meet and Confer process, the Agency may retain a total of $5,179,470 for enforceable obligations, as further discussed below. Accordingly, the OFA balance available for distribution will be increased by $7,062,500 ($12,241,970 - $5,179,470).

  For the July through December 2012 ROPS (ROPS II) period, Finance approved $5,747,947 to be distributed from the Redevelopment Property Tax Trust Fund (RPTTF). The County Auditor Controller only distributed $3,428,586 from the RPTTF. On the Estimated Obligations vs. Actual Payments tab of the July through December 2013 ROPS (ROPS 13-14A) form, the Agency reported $5,513,899 in expenditures for the ROPS II period, which consisted of $3,428,586 paid from the RPTTF and $2,085,313 paid from Reserves. However, based on the expenditure report provided for the period July 1 through December 31, 2012, only $5,179,470 in approved expenditures was supported. Therefore, the Agency may retain $5,179,470 ($3,428,586 in RPTTF + $1,750,884 in Reserves) for ROPS II approved enforceable obligations.

  Finance notes that HSC section 34177 (a) (3) states that only those payments listed in the approved ROPS may be made from the funding source specified in the ROPS. However, HSC section 34177 (a) (4) goes on to state that with prior approval from the oversight board, the successor agency can make payments for enforceable obligations from sources other than those listed in the ROPS. In the future, the Agency should obtain prior oversight board approval when making payments for enforceable obligations from a funding source other than those approved by Finance.

  For both the January through June 2013 (ROPS III) and ROPS 13-14A periods, the Agency received the full amount approved from the RPTTF. Therefore, the Agency is not allowed to retain any additional funds for the ROPS III and ROPS 13-14A periods. Although the Agency contends it will experience a shortfall of RPTTF for the ROPS 13-14A and subsequent periods, the cash flow analysis provided does not adequately incorporate all the requirements detailed in HSC section 34179.5 (c) (5) (D). HSC section 34179.5 (c) (5) (D) requires an extensive analysis before retention of current unencumbered balances can be contemplated. This includes, but is not limited to, providing a detail of the projected property tax revenues and other general purpose revenues to be received by the Agency, together with both the amount and timing of the bond debt service payments, for the period in which the oversight board anticipates the

Agency will have insufficient property tax revenue to pay the specified obligations. The cash flow analysis provided only identified one period (July through December 2014) in which there may be insufficient funding from the RPTTF; however, the period prior to this estimates excess funding from the RPTTF would be available to cover this shortfall, should it be needed to cover bond debt service. As such, it is not evident that future property tax revenue will be insufficient or that there is an immediate need to retain these balances.

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 pursuant to HSC section 34177 (d) (1) (A), 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.

Since the Agency has not met the requirements detailed in HSC section 34179.5 (c) (5) (D) and possesses alternatives to address any short-term cash flow shortages, Finance deems it is not necessary for the Agency to retain any additional OFA unencumbered balances.

The Agency's OFA balance available for distribution to the affected taxing entities is $11,071,092 (see table below).

OFA Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	(660,859)
Finance Adjustments		
Add:		
Disallowed transfers	$	4,669,451
Requested retained balance not supported		7,062,500
Total OFA available to be distributed:	$	11,071,092

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 section 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, Dispute Resolution Supervisor, or Mary Halterman, Analyst, at (916) 445-1546.

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Ms. Lori Ann Farrell, Director of Finance, City of Huntington Beach
Mr. Frank Davies, Property Tax Manager, Orange County
Mr. Steven Mar, Bureau Chief, Local Government Audit Bureau, California State Controller's Office