DEPARTMENT OF FINANCE

EDMUND G. BROWN JR. • GOVERNOR

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April 13, 2013

Mr. Steve Valenzuela, Chief Financial Officer
CRA/LA – DLA, A Designated Local Authority
1200 West 7th Street, 2F
Los Angeles, CA 90017

Dear Mr. Valenzuela:

Subject: Other Funds and Accounts Due Diligence Review

The City of Los Angeles successor agency to the Community Redevelopment Agency (Agency) submitted an oversight board approved Other Funds and Accounts (OFA) Due Diligence Review (DDR) to the California Department of Finance (Finance) on January 29, 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 is not bound to completing its review and making a determination by the April 1, 2013 deadline pursuant to HSC section 34179.6 (d). However, 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:

- The Agency transferred $75.3 million in cash to the City between January 1, 2011 and January 31, 2012; of which $42.5 million are disallowed. Specifically, Finance noted the following:
    - Item No. 1, 4, 9, 20, 31, 32, 40, 41 and 58 totaling $30.5 million for the return of City AB 1290 pass-through funds is not allowed. It is our understanding the City passed resolutions allowing the Agency to retain their share of AB 1290 pass-through payments to conduct various projects. To the extent the Agency had not encumbered these funds through a third party agreement prior to June 28, 2011, they should be considered unencumbered funds of the Agency, not the City. Should a legal and binding agreement require the repayment of these funds, the Agency should request funding through the ROPS process.
    - Item No. 7 and 8 totaling $12 million for City loan repayments pursuant to Agreement No. 65464 is not allowed. HSC section 34171 (d) (2) states that agreements, contracts, or arrangements between the city that created the RDA and the former RDA are not enforceable, unless issued within two years of the RDA's creation date or for issuance of indebtedness to third-party investors or

bondholders. Upon receiving a Finding of Completion, these loans may become eligible for repayment pursuant to HSC section 34191.4 (b).

- Procedure 7 – Property located on 4020 Buckingham, identified on the Housing Assets Transfer form as Exhibit C1, Item 62 in the amount of $9,861,343.47 was denied in our Housing Assets Transfer (HAT) letter dated March 27, 2013. The non-liquid assets transferred to the City are subject to the California State Controller's Office review of asset transfers. To the extent these assets that transferred are not for a government purpose or pursuant to an enforceable obligation, these assets should be returned to the Agency and disposed of in a manner consistent to the Agency's Long Range Property Management Plan pursuant to HSC section 34191.5. As these are non-liquid assets, the OFA balance available for distribution to the taxing entities will not be adjusted.

- Your request to retain $90.1 million as legally restricted for the funding of an enforceable obligation is partially denied. Based on our review of your DDR, the Agency has not adequately proven there will be insufficient property tax revenues to pay for the $90.1 million in obligations. HSC section 34179.5 (c) (5) (D) states that a successor agency shall provide a listing of all approved enforceable obligations that includes a projection of annual spending requirements to satisfy each obligation and a projection of annual revenues available to fund those requirements. Included in the request to retain $90.1 million, Finance notes the following:

    - $54 million of Low and Moderate Income Housing Fund (LMIHF) equity in the Agency's investment pool as of June 30, 2012 is partially denied. After remitting $35.6 million to the County Auditor Controller for the LMIHF DDR process, a balance of $18.2 million remains. It is our understanding the remaining balance will be used for the scheduled payments on the Recognized Obligation Payment Schedule (ROPS) II and III obligations. However, Finance only approved $16.7 million for ROPS II and III LMIHF obligations. As such, the Agency is limited to spending Finance's approved ROPS II and III LMIHF amounts. Therefore, the OFA available for distribution to the taxing entities will be adjusted by $1.5 million.

    - The Agency's calculation of restricted balances includes administration and litigation in the amount of $8 million reserved for judgments and settlements. The CPA firm asserts the Agency did not provide legal documents with appropriate restricting language associated with this item. According to the legal analysis performed by the County Auditor Controller, the administration/litigation reserve, listed as Item No. 1575 on ROPS I is not an enforceable obligation under ABx1 26. Therefore; the OFA available for distribution to the taxing entities will be adjusted by $8 million.

      To the extent funding becomes necessary for these administration and litigation expenses, they should be placed on the ROPS. Administrative expenses are subject to the administration cap pursuant to HSC section 34171 (b). However, settlements, judgments, and litigation as defined HSC section 34171 are not subject to the administrative cap.

    - Obligations totaling $5.4 million pertains to expenditures for the January through June 2012 ROPS I period. Per Exhibit H-1 of the DDR, $5.4 million was paid subsequent to ROPS I. Therefore, because of the timing of when the obligation was actually paid, the Agency's request will be adjusted to allow for the retention of $5.4 million.

- For the remaining $22.8 million balance requested to be retained, it is not evident that future property tax revenues will be insufficient. Since Finance has only approved funding through the January through June 2013 ROPS III period, the Agency's fund balances are only encumbered to the extent they have been approved on a ROPS through the June 30, 2013 period. The cash flow analysis provided by the Agency does not demonstrate an immediate need to retain these unencumbered OFA balances, nor does it suggest available funding will be insufficient to service the Agency's bond debt.

  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.

  Since the Agency has not demonstrated an immediate need to retain unencumbered OFA balances and possesses alternatives to address short term cash flow shortages, Finance deems it is not necessary for the Agency to retain the remaining $22.8 million in OFA unencumbered balances.

Therefore, your request to retain $90.1 million in OFA balances is partially denied and the OFA available for distribution to the taxing entities will be adjusted by a total of $32.4 million.

- Balances requested to be retained for fiscal year 2012-13 in the amount of $77 million is partially denied. Of this amount requested to be retained, the County Auditor Controller distributed $23.6 million to be funded with RPTTF for the July through December 2012 ROPS II period. Further, Finance approved obligations totaling $11.6 million to be funded with reserves and other funding for the January through June 2013 ROPS III period. Therefore, Finance is adjusting the balance to reflect $35.2 million in approved ROPS II and III expenditures.

  With the exception of $11.6 million approved in reserves and other funding, Finance approved LMIHF and RPTTF funding for other enforceable obligations on ROPS III. Since the County Auditor Controller distributed RPTTF for approved ROPS III obligations on January 2, 2013, after the June 30, 2012 OFA balances delineated in the DDR, it is inappropriate for the Agency to retain current OFA balances for obligations that have already been funded through a separate process.

  Pursuant to HSC 34177 (a) (3), expenditures approved in the ROPS can only be made from the funds identified. However, HSC 34177 (a) (4) allows Agencies, with prior approval from the oversight board, to pay enforceable obligations from sources other than those listed on the ROPS. It is our understanding prior oversight board approval was not obtained and therefore, the Agency did not have the authority to use funding sources other than those identified and approved on the ROPS. Since the law prohibits the use of funds other than what was approved on a ROPS unless prior approval from the oversight board is obtained, a portion of the Agency's request to retain $77 million in OFA balances is not allowed.

- Finance noted the county auditor controller adjusted the ROPS III January 2, 2013 distribution by $22 million pursuant to HSC section 34186 (a). Therefore, Finance is allowing the retention of these funds in order to adequately fund approved ROPS III expenditures.

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 $163,318,826 (see table below).

OFA Balances Available For Distribution To Taxing Entities	
Available Balance per DDR:	$ 68,933,434
Finance Adjustments	
Add:	
Disallowed transfers:	42,473,209
Requested restricted balance not supported:	32,382,453
Requested retained balance for fiscal year 2012-13 not supported:	76,755,992
Approved OFA expenditures for ROPS II and III:	(35,259,026)
HSC Section 34186 (a) retention:	(21,967,236)
Total LMIHF available to be distributed to taxing entities:	$ 163,318,826

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, please 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.

Please direct inquiries to Kylie Le, Supervisor or Michael Barr, Lead Analyst at (916) 445-1546.

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Ms. Daisy Pan, Special Projects Officer, CRA/LA – Designated Local Authority
Ms. Kristina Burns, Manager, Los Angeles County Department of Auditor-Controller
California State Controller's Office