



REVISED

August 19, 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

This letter supersedes the California Department of Finance's (Finance) Other Funds and Accounts (OFA) Due Diligence Review (DDR) Meet and Confer determination letter dated May 17, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Los Angeles Successor Agency to the Community Redevelopment Agency (Agency) submitted an oversight board approved OFA DDR to 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. Finance issued an OFA DDR determination letter on April 13, 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 May 6, 2013 and an OFA DDR Meet and Confer determination letter was issued on May 17, 2013.

A revised OFA DDR determination letter is necessary to account for changes authorized in Finance's revised July through December 2013 Recognized Obligation Payment Schedule (ROPS 13-14A) determination letter dated August 19, 2013. Finance's revised ROPS 13-14A determination letter addresses technical adjustments requiring the reclassification of certain administrative items from a funding source of Redevelopment Property Tax Trust Fund (RPTTF) to a funding source of Other. As a result of these reclassifications, Finance's previous OFA DDR determination that \$77,262,410 is unencumbered and available for distribution to the taxing entities will be reduced by \$1,611,303.

All the adjustments identified in our May 17, 2013 OFA DDR determination letter continue to be upheld. Specifically, Finance's May 17, 2013 OFA DDR determination letter identified the following necessary adjustments:

- The Agency transferred \$75,349,198 in cash to the City of Los Angeles (City) between January 1, 2011 and January 31, 2012, of which \$42,473,209 was disallowed. Based on further documentation provided during the Meet and Confer process, Finance is reversing its adjustment of \$42,473,209, as further discussed below.
 - Exhibit B-1 in the DDR, Item Nos. 1, 4, 9, 20, 31, 32, 40, 41, and 58 totaling \$30,457,626 for the return of City AB 1290 pass-through funds had been disallowed. During the Meet and Confer process, the Agency provided additional

information showing that the AB 1290 pass-through payments were being held by the former Redevelopment Agency (RDA) based on a Policy adopted by the City Council in 2003. The Agency provided documents showing that the former RDA did not expend the funds without prior approval from the City Council. The Agency also provided audited reports related to the funds in question that demonstrate the amounts belong to the City. As such, these are City funds and may be returned to the City. Finance is reversing its adjustment of \$30,457,626.

- Item Nos. 7 and 8 totaling \$12,015,853 for City loan repayments pursuant to Agreement Nos. 65464 and 68887 was not allowed. During the Meet and Confer process, the Agency provided additional documents demonstrating that the City advanced federal Community Development Block Grant (CDBG) funds to the former RDA. 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. The promissory notes were entered into at the time of the agreements and for the purpose of repaying the loans from the CDBG program. Therefore, these payments were for enforceable obligations pursuant to HSC section 34171 (d) (2). Finance is reversing its adjustment of \$12,015,853.
- 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 was denied in our Housing Assets Transfer (HAT) letter dated March 27, 2013. The City, as housing successor, has submitted a HAT Meet and Confer request and this item will be addressed through the HAT Meet and Confer process. 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.
- The Agency's request to retain \$90,125,123 as legally restricted for the funding of an enforceable obligation was partially denied in the amount of \$32,382,453. During the Meet and Confer process, the Agency provided additional information showing that \$5,557,459 of this amount is allowed to be retained. Therefore, Finance is reversing \$5,557,459 of its adjustment and continues to increase the OFA balance available by \$26,824,994 (\$735,552 + \$3,255,593 + \$22,833,849), as further discussed below.
 - \$53,867,883 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 \$35,644,416 to the County Auditor Controller for the LMIHF DDR process, a balance of \$18,223,467 remains. The remaining balance was used to fund the following Recognized Obligation Payment Schedule (ROPS) obligations:
 - \$5,632,361 in approved obligations from the January through June 2012 (ROPS I) period was paid after June 30, 2012.
 - \$3,504,830 in approved obligations from the July through December 2012 (ROPS II) period was reported as expended on the July through December 2013 (ROPS 13-14A) form.

- \$8,350,724 was approved for obligations in the January through June 2013 (ROPS III) period.

Therefore, the Agency may retain \$17,487,915 (\$5,632,361 + \$3,504,830 + \$8,350,724) for approved obligations in the ROPS I, II, and III periods. The OFA balance available for distribution to the taxing entities will be increased by the remaining \$735,552 (\$18,223,467 - \$17,487,915).

- 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. Additionally, according to the legal analysis performed by the County Auditor Controller, the administration/litigation reserve, listed as Item 1575 on ROPS I, is not an enforceable obligation under ABx1 26. However, Finance did not deny the request to use reserve funding on ROPS III in the amount of \$3,294,407 for Item 263 – Administration/Litigation. Furthermore, the Agency listed \$1.45 million for Items 250, 252, 253, and 255 through 259 on the July through December 2013 (ROPS 13-14A) form with a funding source of "Other," which was identified as "Restricted liability account for legal services." Finance did not deny the items or change the funding source for the items. Therefore, the OFA balance available for distribution to the taxing entities will be increased by \$3,255,593 (\$8,000,000 - \$3,294,407 - \$1,450,000).

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 by HSC section 34171 are not subject to the administrative cap.

- Obligations totaling \$5,423,391 pertains to expenditures for the January through June 2012 ROPS I period. Per Exhibit H-1 of the DDR, \$5,423,391 was paid subsequent to the ROPS I period. Therefore, due to the timing of when the obligations were actually paid, the Agency's request to retain \$5,423,391 is allowed.

During the Meet and Confer process, the Agency stated the amount should be increased by \$750,000 for Item 984 on ROPS I. However, on the Finance approved ROPS I formed dated May 24, 2012, no funds were requested for expenditure for this item during the ROPS I period. Therefore, the Agency did not have authority to expend OFA balances on the item. To the extent the item is an enforceable obligation, it should be listed on a subsequent ROPS for review by Finance.

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.

- For the remaining \$22,833,849 balance requested to be retained, it is not evident that future property tax revenues will be insufficient. The Agency requested to retain \$3.45 million for legal services, \$7,418,004 for employee salaries and benefits, and \$11,965,845 for various administrative costs.

Since Finance has only approved funding through the ROPS III period, the Agency's fund balances are only encumbered to the extent they have been approved on a ROPS through June 30, 2013. The Agency did not provide a cash flow analysis demonstrating an immediate need to retain these unencumbered OFA balances, nor did the Agency 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 \$22,833,849 in OFA unencumbered balances. Therefore, the OFA balances available will be increased by \$22,833,849.

- During the Meet and Confer process, the Agency stated that the Restricted Balances – Grant Proceeds and Program Income (Exhibit F-2 in the DDR) should be increased by \$465,554 for restricted program income related to the Contract #C-92080. The contract is related to a federal loan program, which requires principal repayments to be remitted to the City. Therefore, the OFA balance available will be decreased by \$465,554.
- Balances requested to be retained for fiscal year 2012-13 in the amount of \$76,755,992 is being decreased by \$3,936,772 (\$4,698,149 - \$761,377), as further discussed below.

For the ROPS II period, the Agency requested to retain \$60,362,102 for approved obligations. The items listed in Exhibit I-1 in the DDR were reported as paid on the ROPS 13-14A form from Reserves, RPTTF, and "Other" funding sources. Therefore, the Agency may retain \$60,362,102 for ROPS II approved expenditures.

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 the ROPS III period, 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 unnecessary for the Agency to retain current OFA balances for obligations that have already been funded through a separate process. However, of the \$16,393,890 requested for ROPS III, Finance did not deny \$11,695,741 to be funded from Reserves or "Other" funding sources. Therefore, the Agency may retain \$11,695,741 for the ROPS III period and the OFA balances available will be increased by \$4,698,149 (\$16,393,890 - \$11,695,741).

For the ROPS 13-14A, Finance did not deny \$761,377 from Reserves or "Other" funds for Item 395 – Employees and Item 132 – PAYPRO Administrators that had been previously reclassified as administrative costs during the ROPS III period. Therefore, the Agency may retain \$761,377 for the ROPS 13-14A period.

- Finance noted the CAC adjusted the ROPS III January 2, 2013 distribution by \$21,967,236 pursuant to HSC section 34186 (a). Therefore, the Agency may retain \$21,967,236 in order to adequately fund approved ROPS III expenditures.
- In addition to the above adjustments, Finance is authorizing an additional retention of \$1,611,303 to conform to the technical adjustments detailed in our August 19, 2013 ROPS 13-14 A revised determination letter.

The Agency's revised OFA balance available for distribution to the affected taxing entities is \$75,651,107 (see table below).

OFA Balances Available For Distribution To Taxing Entities	
Available Balance per DDR:	\$ 68,933,434
Finance Adjustments	
Add:	
Requested restricted balance not supported:	26,359,440
Requested retained balance for fiscal year 2012-13 not supported:	3,936,772
HSC Section 34186 (a) retention:	(21,967,236)
Authorized retention for ROPS 13-14A	(1,611,303)
Total LMIHF available to be distributed to taxing entities:	\$ 75,651,107

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 Zachary Stacy, Manager 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