DEPARTMENT OF FINANCE

EDMUND G. BROWN JR. • GOVERNOR
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April 6, 2013

Mr. Kevin Riper, Finance Director
City of Morgan Hill
17575 Peak Avenue
Morgan Hill, CA 95037

Dear Mr. Riper:

Subject: Other Funds and Accounts Due Diligence Review

The City of Morgan Hill Successor 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 24, 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 total amount of assets held as of June 30, 2012 should be $121,805,048. As such, the amount has been increased by $3,901. This amount was adjusted by the Oversight Board for expenses paid on rental properties. These expenses were not listed on any Recognized Obligation Payment Schedule (ROPS) approved by Finance; therefore, are not approved. The OFA balances available for distribution to the taxing entities will be adjusted by $3,901.

- Balances legally restricted totaling $60,338,858 should be adjusted by $5,374,274. Included in this amount is $1,126,242 for items that were denied in ROPS III. The Agency requested a Meet and Confer session regarding the disputed items. Based on the Meet and Confer session held on October 22, 2012, Finance continues to object to this project.

  Also included in this amount is $4,245,032 due to pending litigations, which is also denied. The Agency cannot hold onto funds for future obligations that may or may not materialize. In the event that the Agency anticipates a need for litigation funding, the Agency may place this obligation on future ROPS for funding from Redevelopment

Property Trust Fund (RPTTF). Therefore, the OFA balances available for distribution to the taxing entities will be adjusted by a total of $5,371,274 ($1,126,242 +$4,245,032).

- The Agency's request to retain $6,804,176 for fiscal year 2012-13 obligations is partially denied. Included in this amount is $455,599 which is the administrative costs on ROPS II and III in excess of the statutory administrative cost cap. HSC section 34171(b) limits administrative costs to three percent of property tax allocated to the successor agency or $250,000, whichever is greater for the fiscal year. As a result, the Agency is eligible for a $250,000 administrative cost allowance. Therefore, the OFA balances available for distribution to the taxing entities will be adjusted by $455,599.

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 $9,947,155 plus the ongoing lease revenues received after June 30, 2012 associated with the non-cash assets identified in the California State Controller's August 28, 2012 Asset Transfer Review Report. (see table below).

OFA Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	4,116,381
Finance Adjustments		
Add:		
Adjustment to the June 30, 2012 balance:	$	3,901
Request to retain legally restricted balance not supported:		5,371,274
Request to retain balance not supported:		455,599
Total OFA available to be distributed:	$	9,947,155

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.

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

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Mr. Ed Tewes, City Manager, City of Morgan Hill
Mr. Danny Wan, City Attorney, City of Morgan Hill
Mr. John Guthrie, Director of Finance Agency, County of Santa Clara
Ms. Irene Lui, Controller-Treasurer, County of Santa Clara
California State Controller's Office