



May 2, 2013

Ms. Jan Davison, Redevelopment and Housing Director
City of Watsonville
250 Main Street
Watsonville, CA 95076

Dear Ms. Davison:

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 March 26, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Watsonville Successor Agency (Agency) submitted an oversight board approved OFA DDR to the Finance on January 14, 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 March 26, 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 April 16, 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:

- Total amount of assets held as of June 30, 2012 should be \$3,605,844, not \$3,779,920 as previously determined. Our review indicates the balance listed on the DDR did not include the June 1 distribution. The Agency concurred that June 1, 2012 Redevelopment Property Tax Trust Fund distribution of \$1,279,204 was not included in the beginning balance. This amount is offset below with the restriction of the funds to satisfy approved enforceable obligations on the July through December 2012 Recognized Obligations Payment Schedule. Therefore, the OFA beginning balance will be increased by \$1,279,204.

The remaining \$444,923 adjustment from the original determination should have reflected the difference between the adjusted beginning balance of \$3,606,844, as referenced above, and the total assets per the Comprehensive Annual Finance Report (CAFR). The actual difference is \$270,847. This amount offsets the negative cash balance of the Low and Moderate Income Housing Fund DDR; however, this is not permitted. Therefore, the beginning balance as stated in the DDR will be increased by \$270,847.

As such, the OFA beginning balance will be increased by \$1,550,051 (\$1,279,204 + \$270,847).

- Our review indicates that \$4,466,870 was transferred between January 2011 and June 2012 pursuant to two financing agreements and a cooperative agreement between the City of Watsonville (City) and the former Redevelopment Agency (RDA). Per HSC section 34179.5 (c) (2), the dollar value of assets and cash transferred by the former redevelopment agency or successor agency to the city, county, or city and county that formed the former RDA between 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. 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. These loans were issued after the first two years of the RDA's creation. However, we note that a payment totaling \$25,460 was included and approved on the January through June 2012 Recognized Obligation Payment Schedule; therefore, the transfer of \$25,460 will be permitted. The total increase to the OFA balance available for distribution is \$4,441,410 (\$4,466,870 - \$25,460).

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 for repayment. Refer to HSC section 34191.4 (b) for more guidance.

The Agency did not object to the following adjustment made by Finance during the Meet and Confer process. HSC section 34179.6 (d) authorizes Finance to make adjustments. We maintain that the following adjustment is appropriate:

- Balances needed to be retained for enforceable obligations to be paid in the fiscal year 2012-13 in the amount of \$1,279,204 will be added. These obligations were not listed on the DDR; however, Finance adjusted the beginning balance for the July through December 2012 period. The Agency stated the difference between the 2011-12 CAFR and the DDR was for the ROPS II distribution amount of \$1,279,204 which was RPTTF funds that were not part of the reviewed transaction period. Therefore, the OFA balances available for distribution to the taxing entities will be adjusted by \$1,279,204.

The Agency's OFA balance available for distribution to the affected taxing entities is \$4,611,017 (see table below).

OFA Balances Available For Distribution To Taxing Entities	
Available Balance per DDR:	\$ (101,240)
Finance Adjustments	
Add:	
Adjustment to the June 30, 2012 balance:	\$ 1,550,051
Disallowed transfers:	4,441,410
ROPS II retention:	<u>(1,279,204)</u>
Total OFA available to be distributed:	\$ 4,611,017

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 Evelyn Suess, Supervisor or Danielle Brandon, Analyst at (916) 445-1546.

Sincerely,



STEVE SZALAY
Local Government Consultant

cc: Mr. Ezequiel Vega, Administrative Service Director, City of Watsonville
Ms. Mary Jo Walker, Auditor-Controller, Santa Cruz County
Ms. Marianne Ellis, Property Tax Accounting Manager, Santa Cruz County
California State Controller's Office