DEPARTMENT OF FINANCE

EDMUND G. BROWN JR. ▪ GOVERNOR

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May 8, 2013

Ms. Jessica Hurst, Accounting Manager
City of Colton
650 North La Cadena Drive
Colton, CA 92324

Dear Ms. Hurst:

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 April 1, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Colton Successor Agency (Agency) submitted an oversight board approved OFA DDR to Finance on December 27, 2012. 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 1, 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 24, 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:

- Our initial review indicated the total cash and investments held as of June 30, 2012, should be $21,355,725. This amount is listed in the Comprehensive Annual Financial Report (CAFR) and is greater than the amount listed on the DDR. As such, the total amount of assets held as of June 30, 2012, had been increased by $1,819,013. However, based on further review during the Meet and Confer process, part of the adjustment included $48,208 from the City of Colton's (City) Cemetery Endowment Fund. Therefore, Finance is reversing $48,208 of the adjustment.

  The remaining $1,770,805 was funds received by the Agency for enforceable obligations in the July through December 2012 Recognized Obligation Payment Schedule period (ROPS II) from the Redevelopment Property Tax Trust Fund (RPTTF). Since the Agency elected not to include the ROPS II distribution in the beginning balance and did not restrict the funds in Procedure 9, Finance is reversing $1,770,805 of the adjustment.

- A transfer in the amount of $1,650,000 is not allowed. The Agency transferred funds for the Colton Crossing project; the resolution provided states the former redevelopment agency (RDA) was to reimburse the City for their share of the project costs. However, the City did not enter into a funding agreement with a third party until October 2011. Per HSC section 34179.5 (c) (2), the dollar value of assets and cash transferred by the RDA 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. Furthermore, as of June 28, 2011, an agency is prohibited from entering into contracts with any entity for any purpose. Therefore, the transfer was not made pursuant to an enforceable obligation and is not permitted. Finance continues to increase the OFA balance available by $1,650,000.

- Transfers for repayments of loans provided from the City to the former RDA totaling $1,753,860 are not allowed. The Agency transferred $1,554,033 to the City for the Fly Mitigation Land in West Valley and $199,827 for the Rancho Mill Project. 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. Therefore, the transfer was not made pursuant to an enforceable obligation and is not permitted. Finance continues to increase the OFA balance available by $1,753,860.

  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.

- In Procedure 8a of the DDR, the Agency's request to retain balances in the amount of $5,955,818 for the January through June 2012 (ROPS I) obligations paid after June 30, 2012, is partially denied. Based upon further review during the Meet and Confer process, the Agency may retain $3,235,625 ($1,892,522 + $1,054,927 + $288,176) for the ROPS I obligations paid after June 30, 2012. The OFA balance available will be increased by $2,720,193 ($5,955,818 - $3,235,625), as further discussed below.

  - For the ROPS I period, Finance approved $8,307,967 and the County Auditor Controller (CAC) distributed $6,598,532 to from the RPPTF. The Agency had requested bond debt service payments for the entire year on the ROPS I form due to a concern about receiving insufficient RPPTF distributions. HSC section 34171 allows an agency to hold a reserve when the next property tax allocation will be insufficient to pay the next payment due in the following half of the calendar year. On the ROPS I Estimated vs. Actual Payments Report (Estimated vs. Actual), the Agency reported actual expenditures of $7,591,380 ($7,268,193 + $323,187) from the RPTTF. The reported expenditures included all debt service payments, even though $3,173,546 ($2,352,648 + $283,944 + $373,464 + $128,679 + $34,811) was being held for the July through December 2012 (ROPS II) period and was expended in the ROPS II period. Therefore, the Agency actually expended $4,417,834 ($7,591,380 - $3,173,546) for the ROPS I period and can retain the remaining $1,892,522 ($6,598,532 - $4,417,834 - $288,176) for the ROPS II debt service payments and enforceable obligations.

During the Meet and Confer process, the Agency provided supporting documents showing \$50,761 and \$1,004,166 of ROPS I accruals for enforceable obligations and pass though payments, respectively, were paid during the ROPS II period. Therefore, the Agency may retain \$1,054,927 to cover the ROPS I expenditures that were paid during the ROPS II period.

Finance notes that amounts requested and approved in a Recognized Obligation Payment Schedule (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.

Furthermore, the CAC made a \$288,176 adjustment for the ROPS I period on the January through June 2013 ROPS (ROPS III) distribution pursuant to HSC section 34186 (a). Therefore, the Agency may retain \$288,176 for the ROPS III period.

- In Procedure 9 of the DDR, the Agency requested to retain balances in the amount of \$1,900,170 to pay for approved ROPS II obligations. Based upon further review of documents provided during the Meet and Confer process, the Agency may not retain any balances for the ROPS II obligations. Therefore, the OFA balance available for distribution will be increased by \$3,391,192 (\$1,900,170 + \$1,491,022), as further discussed below.

  - During the Meet and Confer process, the Agency requested to retain \$2,071,248 to cover a shortfall in available RPTTF for the ROPS II period. For the ROPS II period, Finance approved \$5,059,897 and the CAC distributed \$2,838,477 from the RPTTF. As previously discussed above, the Agency retained \$1,892,522 of the RPTTF funding received in the ROPS I period for ROPS II debt service. On the ROPS II Estimated vs. Actual, the Agency reported expenditures of \$3,239,977 (\$3,114,977 + \$125,000). Therefore, the Agency had received excess RPTTF funding in the amount of \$1,491,022 (\$3,239,977 - \$2,838,477 - \$1,892,522). Since the Agency received excess RPTTF funding and the CAC did not make a prior period adjustment for the ROPS II period pursuant to HSC section 34186 (a), OFA balances available will be increased by an additional \$1,491,022.

  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 34171 (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.

- In Procedure 8b of the DDR, the Agency requested to retain \$10,019,712 in balances for negotiated pass-through payments to the taxing entities. However, the documents provided by the Agency do not validate what amounts, if any, are owed for the pass through payments that the former RDA had alledgedly failed to pay pursuant to the agreements. To the extent the Agency can provide documentation that substantiates the payments, if any, that are owed to the applicable taxing entities, the Agency should list these payments on future ROPS for consideration. Since that documentation has not been provided as part of this review the amounts listed are considered unencumbered and should be remitted to the taxing entities. Therefore, the OFA balance available for distribution will be increased by $10,019,712.

We note that the documentation, which was provided by the agency, had discrepancies that could not be reconciled to the amount listed in the DDR. Therefore, Finance is utilized the amount as reported in the DDR for this adjustment.

The Agency's OFA balance available for distribution to the affected taxing entities is $21,332,452 (see table next page).

OFA Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	1,797,495
Finance Adjustments		
Add:		
Disallowed transfers	$	3,403,860
Requested retained balance not supported ROPS I	$	2,720,193
Requested retained balance not supported ROPS II	$	3,391,192
Requested retained balance not supported for pass through payments	$	10,019,712
Total OFA available to be distributed:	$	21,332,452

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 Mary Halterman, Analyst, at (916) 445-1546.

Sincerely,

STEVE SZALAY
Local Government Consultant

cc: Ms. Bonnie Johnson, Management Services Director, City of Colton
Ms. Vanessa Doyle, Auditor Controller Manager, San Bernardino County
California State Controller's Office