January 7, 2013

Mr. Allen Jones, Deputy Chief of Staff
City of San Diego
202 C Street 11th Floor
San Diego, CA 92010

Dear Mr. Jones:

Subject: Low and Moderate Income Housing Fund Due Diligence Review

The City of San Diego Success Agency (Agency) submitted an oversight board approved Low and Moderate Income Housing Fund (LMIHF) Due Diligence Review (DDR) to the California Department of Finance (Finance) on December 12, 2012. 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 October 15, 2012 submittal deadline pursuant to HSC section 34179.6 (c), Finance is not bound to completing its review and making a determination by the November 9, 2012 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 LMIHF available for distribution to the taxing entities. Based on our review of your DDR, the following adjustments were made:

- The DDR notes various assets that transferred to the Housing Successor Agency as of February 1, 2012 including $49 million in cash and investments, $39 million of investments held with third party fiscal agents, and $70 million in working capital advances. These assets are not eligible for transfer to the Housing Successor Agency and should be returned to the Agency. HSC section 34177.3 (c) states that the Agency lacks the authority to transfer any revenues to any other party except pursuant to an enforceable obligation on a Recognized Obligation Payment Schedule (ROPS) approved by Finance. Since Finance has only approved funding through the January through June 2013 ROPS period, the Agency's fund balances, including the balances of the LMIHF, are only encumbered to the extent they have been approved on a ROPS through the June 30, 2013 period. All future housing obligations that were liabilities of the former redevelopment agency will need to be placed and approved on a future ROPS pursuant to HSC section 34176 (g) (1) (B) before expenditure authority can be achieved.

  The investments held with third party fiscal agents will not be disbursed to the taxing entities as this is not a liquid cash item. The remaining cash and working capital advances are addressed below.

- The June 30, 2011 transfer of cash out of the LMIHF to the City of San Diego in the amount of $74 million pursuant to a Cooperation Agreement is not a valid transfer. HSC section 34177.3 (c) states that the Agency lacks the authority to transfer any revenues to any other party except pursuant to an enforceable obligation on a ROPS approved by Finance. To date, Finance has only approved expenditures through the June 30, 2013 period. Exhibit A1 and A2 of the DDR provides support that $33 million of the original $74 million transfer has been reversed and is accounted for in the DDR's beginning cash balance as of June 30, 2012.

  The Agency contends approximately $39 million of the original $74 million transfer consisted of bond proceeds. However, restricted unspent bond proceeds totaling $49 million is already accounted for in Exhibit D of the DDR. The Agency has not provided adequate documentation to determine what portion, if any of the $74 million transfer is actually unspent bond proceeds. Therefore, $41 million ($74 million - $33 million) must be returned to the Agency and remitted to the county to be disbursed to the taxing entities.

- The Agency contends that the retention of $14 million is needed to fund enforceable obligations due to insufficient future Redevelopment Property Tax Trust Fund (RPTTF). HSC section 34179.5 (c)(5)(D) not only requires the Agency to submit a list of the enforceable obligations required for this amount, but to also include an analysis on the projection of annual revenues expected to be available in the future. This analysis shall include all future revenues received and demonstrate obligations being paid off over time. The Agency did provide a list of the enforceable obligations but did not provide an analysis on the projection of future revenues. Therefore, Finance is unable to determine whether future tax increment will be insufficient to meet future enforceable housing obligations. Therefore, the Agency's request retain $14 million is denied.

- The Agency's request to retain balances needed to satisfy enforceable obligations through June 2013 in the amount of $46 million is based on the total of all outstanding obligations. After further review, it was determined that the approved amount was incorrectly calculated. Based on the recalculation, Finance approves the retention of $22 million for fiscal year 2012-13 LMIHF approved obligations ($8 million identified in the July through December 2012 ROPS period and $14 million for the January through June 2013 ROPS period). The Agency's request to retain the remaining amount, $24 million ($46 million - $22 million) is denied.

If you disagree with Finance's adjusted amount of LMIHF 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 LMIHF balance available for distribution to the affected taxing entities is $68,083,203 (see table below).

LMIHF Balances Available For Distribution To Taxing Entities		
Available Balance per DDR:	$	(10,194,909)
Finance Adjustments		
Add:		
Disallowed transfers:		40,716,538
Requested retained balance not supported:		
Retention for 2012-13 fiscal year		23,520,730
Retention for future enforceable obligations		14,040,844
Total LMIHF available to be distributed:	$	68,083,203

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.

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 and Finance's Housing Assets Transfer letter dated January 4, 2013 do not in any way eliminate the Controller's authority.

Please direct inquiries to Zach Stacy, Manager or Jenny DeAngelis, Lead Analyst at (916) 445-1546.

Sincerely,

for

STEVE SZALAY
Local Government Consultant

cc: Mr. Jeff Graham, President of Civic San Diego, City of San Diego
Mr. Andrew Phillips, Chief Financial Officer of Civic San Diego, City of San Diego
Mr. Juan Perez, Senior Auditor and Controller Manager, San Diego County
Ms. Nenita DeJesus, Senior Auditor and Controller Accountant, San Diego County