

# **HUNTINGTON BEACH REDEVELOPMENT AGENCY**

Review Report

## **ASSET TRANSFER REVIEW**

*January 1, 2011, through January 31, 2012*



**BETTY T. YEE**  
California State Controller

June 2015



**BETTY T. YEE**  
California State Controller

June 30, 2015

Fred Wilson, City Manager  
Huntington Beach Redevelopment/Successor Agency  
2000 Main Street  
Huntington Beach, CA 92648

Dear Mr. Wilson:

Pursuant to Health and Safety Code section 34167.5, the State Controller's Office reviewed all asset transfers made by the Huntington Beach Redevelopment Agency (RDA) to the City of Huntington Beach (City) or any other public agency after January 1, 2011. This statutory provision states, "The Legislature hereby finds that a transfer of assets by a redevelopment agency during the period covered in this section is deemed not to be in furtherance of the Community Redevelopment Law and is thereby unauthorized." Therefore, our review included an assessment of whether each asset transfer was allowable and whether it should be turned over to the Successor Agency.

Our review applied to all assets including, but not limited to, real and personal property, cash funds, accounts receivable, deeds of trust and mortgages, contract rights, and rights to payment of any kind. We also reviewed and determined whether any unallowable transfers of assets to the City or any other public agencies have been reversed.

Our review found that the RDA transferred \$60,218,918 in assets after January 1, 2011, including unallowable transfers to the City totaling \$26,237,108 or 43.57% of transferred assets.

However, the following corrective actions have taken place:

- On September 30, 2012, the City turned over \$21,011,462 in capital assets, land held for resale, and proceeds of property sold, to the Successor Agency.
- On September 29, 2013, the City turned over \$4,669,451 in cash to the Successor Agency.

Therefore, the remaining amount of unallowable transfers, totaling \$556,195, must be turned over to the Successor Agency.

If you have any questions, please contact Elizabeth González, Chief, Local Government Compliance Bureau, by telephone at (916) 324-0622 or by email at [egonzalez@sco.ca.gov](mailto:egonzalez@sco.ca.gov).

Sincerely,

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

JVB/ljs

cc: Lori Ann Farrell, Director of Finance  
Huntington Beach Redevelopment/Successor Agency  
Kellee Fritzal, Deputy Director  
Huntington Beach Redevelopment/Successor Agency  
Matthew M. Harper, Oversight Board Chair  
City of Huntington Beach Successor Agency  
Jan Grimes, CPA, Auditor-Controller  
County of Orange  
David Botelho, Program Budget Manager  
California Department of Finance  
Richard J. Chivaro, Chief Legal Counsel  
State Controller's Office  
Elizabeth González, Bureau Chief  
Division of Audits, State Controller's Office  
Betty Moya, Audit Manager  
Division of Audits, State Controller's Office  
Nesha Neycheva, Auditor-in-Charge  
Division of Audits, State Controller's Office

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# Asset Transfer Review Report

## Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the Huntington Beach Redevelopment Agency (RDA) after January 1, 2011. Our review included, but was not limited to, real and personal property, cash funds, accounts receivable, deeds of trust and mortgages, contract rights, and rights to payments of any kind from any source.

Our review found that the RDA transferred \$60,218,918 in assets after January 1, 2011, including unallowable transfers to the City of Huntington Beach (City) totaling \$26,237,108 or 43.57% of transferred assets.

However, the following corrective actions have taken place:

- On September 30, 2012, the City turned over \$21,011,462 in capital assets, land held for resale, and proceeds of property sold, to the Successor Agency.
- On September 29, 2013, the City turned over \$4,669,451 in cash to the Successor Agency.

Therefore, the remaining amount of unallowable transfers, totaling \$556,195, must be turned over to the Successor Agency.

## Background

In January of 2011, the Governor of the State of California proposed statewide elimination of redevelopment agencies (RDAs) beginning with the fiscal year (FY) 2011-12 State budget. The Governor's proposal was incorporated into Assembly Bill 26 (ABX1 26, Chapter 5, Statutes of 2011, First Extraordinary Session), which was passed by the Legislature, and signed into law by the Governor on June 28, 2011.

ABX1 26 prohibited RDAs from engaging in new business, established mechanisms and timelines for dissolution of the RDAs, and created RDA Successor Agencies to oversee dissolution of the RDAs and redistribution of RDA assets.

A California Supreme Court decision on December 28, 2011 (*California Redevelopment Association et al. v. Matosantos*), upheld ABX1 26 and the Legislature's constitutional authority to dissolve the RDAs.

ABX1 26 was codified in the Health and Safety (H&S) Code beginning with section 34161.

H&S Code section 34167.5, states in part, ". . . the Controller shall review the activities of redevelopment agencies in the state to determine whether an asset transfer has occurred after January 1, 2011, between the city or county, or city and county that created a redevelopment agency or any other public agency, and the redevelopment agency."

The SCO has identified transfers of assets that occurred after January 1, 2011, between the RDA, the City, and/or other public agencies. By law, the SCO is required to order that such assets, except those that already had been committed to a third party prior to June 28, 2011, the effective date of ABX1 26, be turned over to the Successor Agency. In addition, the SCO may file a legal action to ensure compliance with this order.

## **Objective, Scope, and Methodology**

Our review objective was to determine whether asset transfers that occurred after January 1, 2011, and the date upon which the RDA ceased to operate, or January 31, 2012, whichever was earlier, between the city or county, or city and county that created an RDA, or any other public agency, and the RDA, were appropriate.

We performed the following procedures:

- Interviewed Successor Agency personnel to gain an understanding of the Successor Agency operations and procedures.
- Reviewed meeting minutes, resolutions, and ordinances of the RDA, the City, and the Successor Agency, and the Oversight Board.
- Reviewed accounting records relating to the recording of assets.
- Verified the accuracy of the Asset Transfer Assessment Form. This form was sent to all former RDAs to provide a list of all assets transferred between January 1, 2011, and January 31, 2012.
- Reviewed applicable financial reports to verify assets (capital, cash, property, etc.).

## **Conclusion**

Our review found that the Huntington Beach Redevelopment Agency transferred \$60,218,918 in assets after January 1, 2011, including unallowable transfers to the City of Huntington Beach (City) totaling \$26,237,108 or 43.57% of transferred assets.

However, the following corrective actions have taken place:

- On September 30, 2012, the City turned over \$21,011,462 in capital assets, land held for resale, and proceeds of property sold, to the Successor Agency.
- On September 29, 2013, the City turned over \$4,669,451 in cash to the Successor Agency.

Therefore, the remaining amount of unallowable transfers, totaling \$556,195, must be turned over to the Successor Agency.

Details of our findings are in the Findings and Orders of the Controller section of this report.

**Views of  
Responsible  
Officials**

We issued a draft review report on July 22, 2014. Fred Wilson, City Manager, responded by letter dated July 30, 2014, disagreeing with the review results. The City's response is included in this final review report as an attachment.

**Restricted Use**

This report is solely for the information and use of the Successor Agency, the City, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record when issued final.

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

June 30, 2015

# Finding and Order of the Controller

## **FINDING— Unallowable asset transfers to the City of Huntington Beach**

The Huntington Beach Redevelopment Agency (RDA) made unallowable asset transfers of \$26,237,108 to the City of Huntington Beach (City). The transfers occurred after January 1, 2011, and were not contractually committed to a third party prior to June 28, 2011.

Unallowable asset transfers were as follows:

- On various dates after January 1, 2011, the RDA transferred a total of \$5,225,646 in cash to the City to pay outstanding loans for various projects and for land acquisition (See Schedule 1). To accomplish those transfers, the City and the RDA entered into agreements under RDA and City Resolution Nos. 2011-17 and 388.
- On March 7, 2011, the RDA transferred \$21,011,462 in assets (\$14,853,064 in capital assets and \$6,158,398 in land held for resale) to the City.

Pursuant to Health and Safety (H&S) Code section 34167.5, any cash asset transfers by the RDA to the City after January 1, 2011, that were not contractually committed to a third party prior to June 28, 2011, must be turned over to the Successor Agency for disposition in accordance with H&S Code section 34177(d) and (e).

### Order of the Controller

Pursuant to H&S Code section 34167.5, the City is ordered to turn over cash assets in the amount of \$26,237,108 to the Successor Agency.

However, on September 30, 2012, the City turned over \$21,011,462 (\$14,853,064 in capital assets and \$5,978,103 in land held for resale, plus the proceeds of the property sold for \$180,295) to the Successor Agency. Also, on September 29, 2013, the City turned over \$4,669,451 in cash to the Successor Agency. Therefore, the remaining amount of unallowable transfers, totaling \$556,195, must be turned over to the Successor Agency.

### City's Response to the Draft Report

The City disputes the SCO's conclusions. The City believes that the remaining unallowable transfers of \$556,195 in payments to the City were lawful and valid, and cannot be reversed by the SCO's Asset Transfer Review.

The City believes that the total unallowable cash transfer should be \$4,408,468. The difference between the SCO's stated finding amount of \$5,225,646 and the City's amount of \$4,408,468, is comprised of two transfers (\$409,483 for a loan payment, and \$407,695 for a bond payment) that the SCO included in its unallowable cash transfer calculation.



- \$409,483 transfer of cash to the City for repayment of an outstanding loan on January 1, 2011. The City says that the transfer should be excluded because the transaction was outside of the period for H&S Code section 34167.5, which states, in part, that the Controller shall determine whether an asset transfer has occurred **after January 1, 2011**. In addition, the transfer was an automated electronic recurring journal entry and was processed by the Accounting Department staff on the first business day, which was January 3, 2011. Lastly, transactions scheduled and automated to be posted on a specific date are widely recognized as having posted on that day, even when a holiday schedule delays recording of such a transaction.
- \$407,695 transfer of cash to the City for repayment of the Emerald Cove bond payment. The City says the transfer was for the express purpose of the City's payment of bonded indebtedness that was issued to pay the cost of the Emerald Cove affordable senior housing project. Furthermore, the Emerald Cove bond repayment of \$407,695 was a valid transfer that was contractually committed to the bondholders and is exempt from being ordered returned to the Successor Agency. Lastly, Huntington Beach notes that the Department of Finance (DOF) determined that the bond payments were enforceable obligations on the Enforceable Obligation Payment Schedule (EOPS), and the Recognized Obligation Payment Schedule (ROPS) for the January-June 2012 and July-December 2012 periods.

See attachment for details of the City's response.

#### SCO's Comment

- The SCO disagrees with the City that the loan repayment in the amount of \$409,483 is outside the period of H&S Code section 34167.5. Based on additional documentation provided by the City, the transaction was entered on January 3, 2011, however, it was back-dated to January 1, 2011. Therefore, it still falls under the authority of the State Controller Office's Asset Transfer Review.
- Regarding the transfer of \$407,695, the Emerald Cove bond payment was an obligation of the City, not the former RDA. The assets could not be contractually committed to a third party when the bond payments were already a debt of the City. The asset transfer was a repayment/reimbursement of debt that the City was obligated to pay. Furthermore, the City states that the DOF has approved this as an enforceable obligation on the EOPS and the following two ROPS cycles. However, in the subsequent ROPS beginning January 2013, the DOF denied these payments as enforceable obligations and the obligations were removed. SCO's authority under H&S Code section 34167.5 extends to all assets transferred after January 1, 2011, by the RDA to the city or county, or city and county that created the RDA, or any other public agency. This responsibility is not limited by the other provisions of the RDA dissolution legislation, including H&S Code section 34167(d), which allowed the RDA to continue to make payment under enforceable obligations to private third parties.

The asset transfer review performed by the SCO is a different and separate review from the DOF's Due Diligence Review (DDR). As such, transfers not identified through the DDR process may be identified in the asset transfer review. The RDA transferred assets to the City after January 1, 2011; therefore, the transfers are unallowable under H&S Code section 34167.5.

On May 13, 2014, the Successor Agency received a Finding of Completion from the DOF. Pursuant to H&S Code section 34191.4, the Successor Agency may place payments for loan agreements between the RDA and the City on the ROPS as an enforceable obligation, provided that the Oversight Board finds that the loans were for legitimate redevelopment purposes.

The Finding and Order of the Controller remain as stated.

**Schedule 1—  
Unallowable RDA Asset Transfers to  
the City of Huntington Beach  
January 1, 2011, through January 31, 2012**

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Cash transfer to the City of Huntington Beach (various dates after January 1, 2011)	\$ 5,225,646
Capital Asset transfers to the City of Huntington Beach (March 7, 2011)	<u>21,011,462</u>
Total unallowable transfers to the City of Huntington Beach	26,237,108
Less:	
Assets turned over to the Successor Agency (September 30, 2012)	
Capital Assets	(14,853,064)
Land held for resale	(5,978,103)
Proceeds from property sold (cash)	(180,295)
Cash turned over to the Successor Agency (September 29, 2013)	<u>(4,669,451)</u>
Total transfers subject to Health and Safety Code section 34167.5	<u><u>\$ 556,195</u></u>

**Attachment—  
City's Response to  
Draft Review Report**

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ATTACHMENT A

EDMUND G. BROWN JR. • GOVERNOR

915 L STREET ■ SACRAMENTO CA ■ 95814-3706 ■ WWW.DOF.CA.GOV

September 20, 2013

Ms. Kellee Fritzel, Deputy Director  
City of Huntington Beach  
2000 Main Street  
Huntington Beach, CA 92648-2702

Dear Ms. Fritzel:

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 August 15, 2013. Pursuant to Health and Safety Code (HSC) section 34179.6 (c), the City of Huntington Beach Successor Agency (Agency) submitted an oversight board approved OFA DDR to Finance on June 3, 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 was not bound to completing its review and making a determination by the April 1, 2013 deadline pursuant to HSC section 34179.6 (d). Finance issued an OFA DDR determination letter on August 15, 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 September 4, 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:

- Transfers in the amount of \$5,078,834 to the City of Huntington Beach (City) were not allowed. The former redevelopment agency (RDA) transferred a total of \$5,485,765 in cash to the City during the period January 1, 2011 to September 30, 2011. Of the total cash transferred, \$406,931 was supported by an enforceable obligation for payments for the 2010 Series A Lease Revenue Refunding Bond. Based on further review during the Meet and Confer process, the Agency provided supporting documents showing that an additional transfer of \$409,483 occurred on January 1, 2011, which is outside of the period for disallowed transfers per HSC section 34179.5 (c) (2).

The remaining transfers represent payments to the City in relation to multiple cooperative agreements between the City and the former RDA entered into between 1983 through 2003 and amended annually from 2004 through 2011. However, per HSC section 34179.5 (c) (2), the dollar value of assets and cash transferred by the former RDA or successor agency to the city, county, or city and county that created the former RDA after 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

**ATTACHMENT A**

enforceable obligation includes any of the items listed in subdivision (d) of section 34171, contracts detailing specific work that were entered into by the former RDA prior to June 28, 2011, with a third party other than the city, county, or city and county that created the former RDA. 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. Therefore, the transfers were not made pursuant to an enforceable obligation and are not permitted. The OFA balance available will be increased by \$4,669,451 (\$5,485,765 - \$406,931 - \$409,383).

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.

- The request to retain balances totaling \$12,241,970 to satisfy future enforceable obligations was originally decreased by \$8,813,384. Based on further review during the Meet and Confer process, the Agency may retain a total of \$5,179,470 for enforceable obligations, as further discussed below. Accordingly, the OFA balance available for distribution will be increased by \$7,062,500 (\$12,241,970 - \$5,179,470).

For the July through December 2012 ROPS (ROPS II) period, Finance approved \$5,747,947 to be distributed from the Redevelopment Property Tax Trust Fund (RPTTF). The County Auditor Controller only distributed \$3,428,586 from the RPTTF. On the Estimated Obligations vs. Actual Payments tab of the July through December 2013 ROPS (ROPS 13-14A) form, the Agency reported \$5,513,899 in expenditures for the ROPS II period, which consisted of \$3,428,586 paid from the RPTTF and \$2,085,313 paid from Reserves. However, based on the expenditure report provided for the period July 1 through December 31, 2012, only \$5,179,470 in approved expenditures was supported. Therefore, the Agency may retain \$5,179,470 (\$3,428,586 in RPTTF + \$1,750,884 in Reserves) for ROPS II approved enforceable obligations.

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 both the January through June 2013 (ROPS III) and ROPS 13-14A periods, the Agency received the full amount approved from the RPTTF. Therefore, the Agency is not allowed to retain any additional funds for the ROPS III and ROPS 13-14A periods. Although the Agency contends it will experience a shortfall of RPTTF for the ROPS 13-14A and subsequent periods, the cash flow analysis provided does not adequately incorporate all the requirements detailed in HSC section 34179.5 (c) (5) (D). HSC section 34179.5 (c) (5) (D) requires an extensive analysis before retention of current unencumbered balances can be contemplated. This includes, but is not limited to, providing a detail of the projected property tax revenues and other general purpose revenues to be received by the Agency, together with both the amount and timing of the bond debt service payments, for the period in which the oversight board anticipates the

## ATTACHMENT A

Agency will have insufficient property tax revenue to pay the specified obligations. The cash flow analysis provided only identified one period (July through December 2014) in which there may be insufficient funding from the RPTTF; however, the period prior to this estimates excess funding from the RPTTF would be available to cover this shortfall, should it be needed to cover bond debt service. As such, it is not evident that future property tax revenue will be insufficient or that there is an immediate need to retain these balances.

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 34177 (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.

Since the Agency has not met the requirements detailed in HSC section 34179.5 (c) (5) (D) and possesses alternatives to address any short-term cash flow shortages, Finance deems it is not necessary for the Agency to retain any additional OFA unencumbered balances.

The Agency's OFA balance available for distribution to the affected taxing entities is \$11,071,092 (see table below).

<b>OFA Balances Available For Distribution To Taxing Entities</b>	
Available Balance per DDR:	\$ (660,859)
Finance Adjustments	
Add:	
Disallowed transfers	\$ 4,669,451
Requested retained balance not supported	7,062,500
<b>Total OFA available to be distributed:</b>	<b>\$ 11,071,092</b>

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 section 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.

## ATTACHMENT A

Ms. Fritzal  
September 20, 2013  
Page 4

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, Dispute Resolution Supervisor, or Mary Halterman, Analyst, at (916) 445-1546.

Sincerely,



STEVE SZALAY  
Local Government Consultant

cc: Ms. Lori Ann Farrell, Director of Finance, City of Huntington Beach  
Mr. Frank Davies, Property Tax Manager, Orange County  
Mr. Steven Mar, Bureau Chief, Local Government Audit Bureau, California State  
Controller's Office

**ATTACHMENT A**





# CITY OF HUNTINGTON BEACH

## SUCCESSOR AGENCY

to the former Redevelopment Agency

Fred A. Wilson  
Executive Director

July 30, 2014

Elizabeth Gonzalez  
Chief, Local Government Compliance Bureau  
Division of Audits  
Office of John Chiang  
California State Controller

Street Address:

3301 C Street, Suite 700  
Sacramento, CA 95816

Mailing Address:

P.O. Box 942850  
Sacramento, CA 94250-5874

RE: City of Huntington Beach and Huntington Beach Successor Agency's Response to SCO's Draft Asset Transfer Review Audit Transmitted and Received by Huntington Beach via email July 22, 2014

Dear Ms. Gonzalez:

I serve as City Manager for the City of Huntington Beach ("City") and Executive Director of the City of Huntington Beach as Successor Agency to the Huntington Beach Redevelopment Agency ("Successor Agency"). I am in receipt of Jeffrey V. Brownfield's letter dated July 22, 2014, sent by email. I received his letter on July 22, 2014.

Enclosed with Mr. Brownfield's letter was a draft Asset Transfer Review Report of the review the State Controller's Office ("SCO") conducted pursuant to Health and Safety Code Section 34167.5 of all "asset transfers" made by the former Huntington Beach Redevelopment Agency ("RDA") to the City or any other public agency after January 1, 2011.

The draft report identifies certain transfers from the RDA to the City between January 1, 2011, and January 31, 2012, the majority of which have been reversed and require no further action. However, the SCO asserts that the remaining cash transfers totaling \$556,195 were also unauthorized and must be remitted to the Successor Agency. The City and Successor Agency (collectively, "Huntington Beach") dispute the SCO's conclusions.

We are compelled to note that the draft Report bases its conclusions on a simple mathematical formula that subtracts reversed transfers from total transfers and concludes that the remaining amount is, therefore, unauthorized and must be returned. The draft Report makes no attempt to identify the specific transfers that make up the disputed amount. Neither does it make any attempt to provide a rationale for determining that the transfers were unauthorized. This omission places Huntington Beach in the difficult position of responding to bare conclusions. However, in spite of the cursory nature of the Report, we have been able to identify certain factual and legal errors that undermine its conclusions and Huntington Beach strongly urges the SCO to correct these errors and findings before the issuance of the final report.

**SCO Finding – Unallowable Asset Transfers to the City of Huntington Beach**

The draft report, on page 4 (and summarized in Mr. Brownfield’s letter), asserts the RDA transferred \$556,195 in cash to the City after January 1, 2011, identified below:

“...on September 30, 2012, the City turned over \$21,011,462 (\$14,853,064 in capital assets and \$5,978,103 in land held for resale, plus the proceeds of the property sold for \$180,295) to the Successor Agency, Also on September 29, 2013, the City turned over \$4,669,451 in cash to the Successor Agency. Therefore, the remaining amount of unallowable transfers, totaling \$556,195, must be turned over to the Successor Agency.”

**Huntington Beach Response:**

**The RDA’s \$556,195 Payments to the City were Lawful and Valid Payments and Cannot Lawfully be Reversed by the SCO’s Asset Transfer Review Audit.**

The total transfer amount listed on page 5 of the draft report lists unauthorized cash transfers of \$5,225,646 made on various dates after January 1, 2011. This amount is incorrect, and should be \$4,408,468, as calculated below:

Cash transfer to the City after January 1, 2011, per SCO	\$5,225,646
Less:	
Transfer to City made on January 1, 2011	(409,483)
Allowable payments for Emerald Cove bonds	<u>(407,695)</u>
<b>Cash transfer to the City after January 1, 2011, per Huntington Beach</b>	<b>\$4,408,468</b>

**January 1, 2011 Transfer of \$409,483**

The January 1, 2011, transfer of \$409,483 should **not** be included in the total unallowed transfer amount. This amount was transferred on January 1, 2011, which is outside of the period for the SCO review per Health and Safety Code Section 34167.5 which states in part:

“[T]he Controller shall review the activities of redevelopment agencies in the state to determine whether an asset transfer has occurred **after January 1, 2011**, between the city or county, or city and county that created a redevelopment agency or any other public agency, and the redevelopment agency ... .” (emphasis added).

The disputed transfer is made on a monthly basis through an automated electronic recurring journal entry. In 2011, January 1 fell on a Saturday. The entry was processed in the accounting system on January 1<sup>st</sup> and the Accounting Department staff recorded the transaction on the first business day, which was January 3<sup>rd</sup>. Because the transfer was processed on January 1<sup>st</sup>, it falls outside of the scope of the Asset Transfer Review. The automatic electronic posting of recurring financial transactions is common and standard accounting practice that is widely recognized by Certified Public Accounting firms nationwide. Accounting transactions that are automatically scheduled to post to certain, specific days (i.e., the first of the month) are recognized as having posted on that day by all CPA firms including the City’s auditing firms. It is customary for an auditor to deem this type of transaction as having occurred on the scheduled day, even in those cases where a holiday schedule delays administrative recording of the transaction.

#### Emerald Cove Bond Payment of \$407,695

It is Huntington Beach’s position that the SCO has no authority to order the return of the \$407,695 transfer to the City, relating to the Emerald Cove bond payment. Based on Health and Safety Code Section 34167.5, the SCO asset transfer review process is intended to determine assets transferred by the former redevelopment agency for no legitimate redevelopment purpose; for example, a situation where an asset was transferred to the host city for the sole purpose of transferring title, with the intent to insulate the asset from the requirements of ABx1 26. In the case of the \$407,695 transfer, the funds were transferred to the City for the express purpose of the City’s payment of bonded indebtedness that was issued to pay the cost of the Emerald Cove affordable senior housing project. Not only was this a legitimate redevelopment purpose, but the City was contractually committed to the bondholders for the expenditure of those funds, (i.e., the payment of bonded indebtedness). Health and Safety Code Section 34167.5 expressly states in part:

“If such an asset transfer did occur during that period **and the government agency that received the assets is not contractually committed to a third party for the expenditure or encumbrance of those assets**, to the extent not prohibited by state and federal law, the Controller’s shall order the available assets to be returned to the Redevelopment Agency or, on or after [February 1, 2012], to the Successor Agency...” (emphasis added).

The Emerald Cove bond repayment of \$407,695 was a valid transfer that was contractually committed to the bondholders and is exempt from being ordered returned to the Successor Agency. This is supported by the fact that Emerald Cove bond repayments are for debt service on bonds related to eligible housing activities. It is worth noting that the Department of Finance determined that the Emerald Cove bond payments were valid enforceable obligations on both the Enforceable Obligation Payment Schedule (EOPS) and Recognized Obligation Payment Schedule (ROPS) for both the January-June 2012 and July-December 2012 periods.

The Department of Finance Has Final Authority to Determine Whether Successor Agencies Have Recovered All Amounts Wrongfully Transferred

The above transfers, which the SCO considers unauthorized, were reviewed by the Department of Finance as part of the Other Funds Due Diligence Review. The Department's final determination letter dated September 20, 2013 (see Attachment A) concluded that: (1) the January 1, 2011 transfer of \$409,483 was outside the scope of the Department's review (which only covered transfers made after January 1, 2011); and (2) the transfer of funds to pay the Emerald Cove bonds was supported by an enforceable obligation. The same facts that supported the Department's determination call for the SCO's reversal of its draft findings.

The SCO's review authority is contained in HSC 34167.5, which became effective on June 28, 2011. "Commencing on the effective date of the act adding this part, the Controller shall review the activities of redevelopment agencies in the state ...." (emphasis added). It has been over three years since the SCO was first authorized to conduct its review but it is only now issuing its draft report for Huntington Beach. In the meantime, the Department of Finance completed its Low and Moderate Income Housing Funds and Other Funds Due Diligence Reviews and verified that Huntington Beach has made full repayment of all unauthorized transfers of funds. Accordingly, the Department issued a Finding of Completion on May 13, 2014 under HSC 34179.7 (see Attachment B). The SCO's failure to timely review Huntington Beach's asset transfers has waived any right it might have had to issue findings that contradict the Department's determinations.

It was the apparent intent of the Legislature that the SCO's review of redevelopment agency transfers would occur prior to the Department's Due Diligence Reviews and the SCO's findings would be taken into account in the Department's review. In fact, specific provision was made for the SCO to receive a copy of the Due Diligence Reviews (HSC 34179.6(a)) and for the Department to consider comments from the SCO (HSC 34179.6(d)). Huntington Beach has no record of the SCO submitting any comments during the Due Diligence Review process. We contend, therefore, that the SCO has waived any right it had to participate in the Department's determinations or to attempt to overturn those determinations, after the fact.

In fact, the SCO apparently concedes in its draft Report that its findings are of no effect after a successor agency receives its Finding of Completion. The "Finding and Order of the Controller" on page 4 of the draft Report states that "[p]ursuant to Health & Safety (H&S) Code section 34167.5, any cash asset transfers by the RDA to the City after January 1, 2011, that were not contractually committed to a third party prior to June 28, 2011, must be turned over to the Successor Agency for disposition in accordance with H&S Code section 34177(e)." The "Order of the Controller" also directs the Oversight Board "to dispose of these assets in accordance with H&S Code section 34177(e)." However, H&S Code section 34177(e) expressly states: "The requirements of this subdivision shall not apply to a successor agency that has been issued a finding of completion by the Department of Finance pursuant to Section 34179.7" (emphasis added).

The SCO has had since June 28, 2011 to conduct its review of the RDA transfers and was also given statutory authority to comment on the Due Diligence Review process. Huntington Beach contends that the SCO, through its failure to comment during the Due Diligence Review process and through its unreasonable delay in conducting the asset transfer review, has waived any right it may have had to question transfers that were included in the Due Diligence Review and approved by the Department of Finance.

For the reasons set forth above, Huntington Beach respectfully submits that the Draft Report is in error both factually and legally, the Department of Finance's previous approvals of the disputed transfers must stand, and the draft Report must be revised and corrected to show that the only unallowable transfers that occurred have already been reversed and therefore no further action is required.

Please contact Lori Ann Farrell, Director of Finance, or Kellee Fritzal, Deputy Director of Business Development, with any questions or requests for additional documents.

Thank you for your cooperation.

Respectfully,



Fred Wilson  
City Manager, City of Huntington Beach  
Executive Director, Huntington Beach Successor Agency

Attachment

cc: Lori Ann Farrell, Director of Finance, City of Huntington Beach  
Kellee Fritzal, Deputy Director of Business Development, City of Huntington Beach  
Deborah Roads, Kane Ballmer & Berkman  
Jennifer McGrath, City Attorney  
Jeffrey W. Brownfield, Chief, Division of Audits, SCO

**State Controller's Office  
Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250-5874**

**<http://www.sco.ca.gov>**