



December 18, 2012

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

Dear Mr. Riper:

Subject: Recognized Obligation Payment Schedule

This letter supersedes Finance's Recognized Obligation Payment Schedule (ROPS) letter dated September 28, 2012. Pursuant to Health and Safety Code (HSC) section 34177 (m), the City of Morgan Hill Successor Agency (Agency) submitted a Recognized Obligation Payment Schedule (ROPS III) to the California Department of Finance (Finance) on August 16, 2012 for the period of January 1 through June 30, 2013. Finance issued its determination related to those enforceable obligations on September 28, 2012. Subsequently, the Agency requested a Meet and Confer session on one or more of the items denied by Finance. The Meet and Confer session was held on October 22, 2012.

Based on a review of additional information and documentation provided to Finance during the Meet and Confer process, Finance has completed its review of the specific item being disputed.

In regards to items that may have been reentered into, the Agency contends those items are enforceable obligations because the Agency was authorized to reenter into the agreements by resolution of the duly appointed Oversight Board. While HSC section 34178 (a) and 34180 (h) authorizes successor agencies to reenter into agreements, any agreement reentered into cannot conflict with the requirements set forth in HSC 34171 (d), as ABx1 26 did not specifically carve out an exception to the definition of an enforceable obligation nor did HSC section 34178 (a) or 34180 (h) notwithstanding HSC section 34171 (d). Therefore, the Oversight Board had no legal basis to approve an action that directly conflicted with and violated the definition of an enforceable obligation. Even if Finance did not object to the specific Oversight Board actions authorizing the Agency to reenter into agreements, the statute as a whole prohibits such an action from being validated if it conflicts with the definition of an enforceable obligation. Additionally, Finance has clearly defined authority under HSC section 34177 and 34179 (h) to review any items on ROPS to determine whether or not successor agencies are responsible for the obligation listed on their ROPS. Even if an Oversight Board approved an action that created an enforceable obligation, Finance has the authority to review the enforceable obligation for compliance with HSC section 34171 (d) or for compliance with any other statutory requirements contained in Chapter 26, statutes of 2012 (AB 1484). At no time can an Oversight Board action eliminate Finance's authority to review an enforceable obligation as part of a ROPS review.

- Item No. 1.2 – 2008 Tax Allocation Bonds Series A & B payment request of Redevelopment Property Tax Trust Fund (RPTTF) in the amount of \$1,950,500. These bonds are Variable Rate Tax Allocation Bonds; therefore, there is no fixed rate each

year. The original amount listed on ROPS III is the maximum interest rate the Agency could be charged. However, this amount is not realistic based on current rates and the Agency acknowledged this point during the Meet and Confer session. The Agency has instead proposed reducing this request down to \$150,000, which would provide a slightly larger cushion than that proposed by Finance in our original determination. Finance is amenable to providing a larger cushion than previously approved. As such this item will be reduced by \$1,800,500 from \$1,950,500 to \$150,000.

- Administrative cost claimed exceeds the allowance by \$303,730. HSC section 34171 (b) limits fiscal year 2012-13 administrative costs to three percent of property tax allocated to the successor agency or \$250,000, whichever is greater. As a result, the City is eligible for a \$250,000 administrative costs allowance. The Santa Clara Auditor Controller's Office distributed \$184,910 of administrative costs for the July through December 2012 period, thus leaving a balance of \$65,090 available for the January through June 2013 period. Although \$368,820 is claimed for administrative cost, only \$65,090 is available pursuant to the cap. Therefore, \$303,730 of excess administrative cost claimed is not allowed. The following line items continue to be and/or are now reclassified as an administrative cost following our review: 1.9, 1.10, 1.35, 1.36, 1.57, 1.65, and 1.66.
- Item Nos. 1.33 and 1.37 – Costs to deliver housing obligations and CIP property acquisition totaling \$44,727. Finance continues to deny the items. The contract provided related to Item 1.37 is between the City of Morgan Hill and a third party. The former RDA is not a party to the contract. As such, the Agency is not obligated to pay any costs associated with the contract. As it relates to Item 1.33 maintenance and/or administrative costs associated with the former RDA's previous housing functions are not enforceable obligations. Upon the transfer of the former RDA's housing functions to the new housing entity, HSC section 34176 requires that, "all rights, powers, duties, obligations and housing assets, ... shall be transferred" to the new housing entity. This transfer of "duties and obligations" necessarily includes the transfer of any on-going maintenance and administrative costs.
- Item No. D1.52 – A Morgan Hill Chamber of Commerce agreement totaling \$24,655. Finance continues to deny the item. HSC section 34163 (b) prohibits a redevelopment agency from entering into a contract with any entity after June 27, 2011. The contract was signed by the Agency on June 28, 2011; therefore, this line item is not an enforceable obligation and not eligible for RPTTF funding.
- Item Nos. 2.7, 2.17, and 2.18 – Various Butterfield Boulevard related contracts in the amount of \$152,455 funded by bond proceeds. Finance continues to deny the items. HSC section 34163 (b) prohibits a redevelopment agency from entering into a contract with any entity after June 27, 2011 and HSC section 34163 (c) prohibits a redevelopment agency from amending or modifying existing agreements, obligations or commitments with any entity for any purpose after June 27, 2011. The contract with MH Engineering Co. was signed on July 27, 2011; therefore, it is not an enforceable obligation. The contract with Mark Thomas & Company, Inc. is for the period between July 23, 2009 and December 22, 2011. The contract ended before ROPS III period and may not be extended. The original contract with Jarvis, Fay, and Doporto and Gibson covered services from March 1, 2011 through June 30, 2011. The first amendment to extend the contract term through June 30, 2012 was signed June 28, 2011. Assuming the excess bond proceeds requested for use were issued prior to January 1, 2011, upon receiving a Finding of Completion from Finance, HSC section 34191.4 (b) may cause these items to be enforceable in future ROPS periods.

- Item Nos. 2.36 and 2.37 – Underground Monterey project totaling \$253,000 funded with bond proceeds. Finance continues to deny the items. The original contract ended June 30, 2010, before the ROPS III period. HSC sections 34163 (b) and 34163 (c) prohibits an Agency from entering into and amending a contract with any entity after June 27, 2011. Assuming the excess bond proceeds requested for use were issued prior to January 1, 2011, upon receiving a Finding of Completion from Finance, HSC section 34191.4 (b) may cause these items to be enforceable in future ROPS periods.
- Item Nos. P2.39 through P2.42 and 2.43 – Downtown and Monterey project totaling \$14.3 million funded by bond proceeds. Finance continues to deny the items. Finance denied these items as there are no contracts in place to support these expenditures. The Agency indicates that it anticipates receiving a Finding of Completion during the ROPS period. Finance cannot approve the expenditure of funds based on a potential event or action that may or may not happen. Assuming the excess bond proceeds requested for use were issued prior to January 1, 2011, upon receiving a Finding of Completion from Finance, HSC section 34191.4 (b) may cause these items to be enforceable in future ROPS periods.
- Item Nos. A1.68 through A2.50 – Amendments to ROPS I in the amount of \$487,693 are identified as payments from the prior ROPS. Finance continues to deny the items. Successor agencies are prohibited from expending monies on items not listed or approved on a ROPS schedule. At no time should a successor agency expend money from any funding source that has not been approved. If a successor agency identifies a legitimate expense that it believes is an enforceable obligation it should list that item on the subsequent ROPS for approval and payment. For Items A1.68 through A1.72 and A2.46 through A2.50, none of the information provided demonstrates that the expenditure in the prior period was for an enforceable obligation as defined in statute. The documentation provided merely demonstrates invoices were sent to and paid by the City of Morgan Hill. However no documentation including contracts were provided to show how these payments are an obligation of the Agency. For Item A1.77 the documentation provided was two staff reports and the second amendment to the Owner Participation and Loan Agreement (OPLA). Unfortunately, the signed second amendment to the OPLA does not provide information related to the financial responsibility of the Agency and the staff report dated December 17, 2008 merely discusses what the Agency agreed to provide in the original OPLA. This is insufficient information, as it does not demonstrate the contractual obligation of the Agency. Without being provided all the necessary documentation Finance cannot determine when payment, if any, under the OPLA is due. Therefore, we are denying these items.
- Item Nos. D1.8 through D1.66, D2.31 and D2.43 in the amount of \$635,184. Finance continues to deny the items. The documentation provided during the Meet and Confer session was insufficient to overturn the previous decisions related to reclassifications or denials and does not support these items as an enforceable obligation on this ROPS. For example, two contracts provided were between the City of Morgan Hill and a third party. The former RDA is not a party to the contract and as such is not obligated for payments related to the contract. Another contract provided was between the former RDA and a third party, but was overly broad as to the services to be provided and the requested expenditure could not be tied to a specific project. As such, the reclassification to administrative costs was valid. Other items deal with advertising and marketing campaigns or graphic designs and were appropriately reclassified as an administrative cost.

- Item Nos. D2.11 through D2.30 and D2.33 – Bond proceeds in the amount of \$1,289,987. Finance continues to deny the items. There were no contracts or agreements in place for these line items by June 27, 2011. Additionally, HSC section 34171 (d) (2) states that agreements, contracts, or arrangements between the city, county, or city and county that created the RDA and the former RDA are not enforceable obligations. Assuming the excess bond proceeds requested for use were issued prior to January 1, 2011, upon receiving a Finding of Completion from Finance, HSC section 34191.4 (b) may cause these items to be enforceable in future ROPS periods.
- Item Nos. P1.75 and P1.76 – General bond counsel costs totaling \$100,000. Finance continues to deny the items. Finance denied these items as there are no signed contracts to support the amount. The Agency indicated that they plan on entering into contracts within the ROPS period. However, Finance cannot approve these items solely based on the intent of the Agency to conduct a transaction that may or may not take place. Without an executed contract to review there is no choice but to deny the item as an enforceable obligation.
- Item No. P2.52 – Property Acquisition costs in the amount of \$30,000 funded by bond proceeds. Finance continues to deny this item. There are no contracts or agreements in place for this line item signed by June 27, 2011; therefore this line item is not an enforceable obligation. The Agency indicates that it anticipates receiving a Finding of Completion during the ROPS period, which would make this an enforceable obligation. Finance cannot approve the expenditure of funds based on a potential event or action that may or may not happen. Assuming the excess bond proceeds requested for use were issued prior to January 1, 2011, upon receiving a Finding of Completion from Finance, HSC section 34191.4 (b) may cause these items to be enforceable in future ROPS periods.

The Agency's maximum approved Redevelopment Property Tax Trust Fund (RPTTF) distribution for the reporting period is: \$403,608 as summarized below:

Approved RPTTF Distribution Amount For the period of January through June 2013	
Total RPTTF funding requested for obligations	\$ 3,571,657
Less: Six-month total for item(s) denied or reclassified as administrative cost	
Item No. 1.2 (Portion denied)	1,800,500
Items reclassified as administrative costs (1.9, 1.10, 1.35, 1.36, 1.57, 1.65, 1.66)	261,670
Item No. 1.33	23,950
Item No. 1.52	24,655
Item No. 1.37	20,777
Item No. A1.68 through A1.77	366,403
Item No. D1.10 through D1.66	529,764
Item No. D2.31	3,732
Item No. D2.43	101,688
Item No. P1.75 and P1.76	100,000
Total approved RPTTF for enforceable obligations	\$ 338,518
Plus: Allowable RPTTF distribution for administrative cost for ROPS III	65,090
Total RPTTF approved:	\$ 403,608

Administrative Cost Calculation	
Total RPTTF for the period July through December 2012	\$ 6,348,577
Total RPTTF for the period January through June 2013	338,518
Total RPTTF for fiscal year 2012-13:	\$ 6,687,095
Allowable administrative cost for fiscal year 2012-13 (Greater of 3% or \$250,000)	250,000
Administrative allowance for the period of July through December 2012	184,910
Allowable RPTTF distribution for administrative cost for ROPS III:	\$ 65,090

Pursuant to HSC section 34186 (a), successor agencies were required to report on the ROPS III form the estimated obligations and actual payments associated with the January through June 2012 period. The amount of RPTTF approved in the above table will be adjusted by the county auditor-controller to account for differences between actual payments and past estimated obligations. Additionally, these estimates and accounts are subject to audit by the county auditor-controller and the State Controller.

The amount available from the RPTTF is the same as the property tax increment that was available prior to enactment of ABx1 26 and AB 1484. This amount is not and never was an unlimited funding source. Therefore, as a practical matter, the ability to fund the items on the ROPS with property tax is limited to the amount of funding available to the successor agency in the RPTTF.

Except for items disallowed as noted above, Finance is not objecting to the remaining items listed in your ROPS III. Obligations deemed not to be enforceable shall be removed from your ROPS. This is Finance's final determination related to the enforceable obligations reported on your ROPS for January 1 through June 30, 2013. Finance's determination is effective for this time period only and should not be conclusively relied upon for future periods. All items listed on a future ROPS are subject to a subsequent review and may be denied even if it was or was not questioned on this ROPS or a preceding ROPS.

Please direct inquiries to Evelyn Suess, Dispute Resolution Supervisor or Danielle Brandon, 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