

City of Imperial Beach, California

OFFICE OF THE CITY CLERK _____

August 22, 2013

The Honorable Robert J. Trentacosta
Presiding Judge
San Diego County Superior Court
220 W. Broadway
San Diego, CA 92101

Dear Judge Trentacosta:

At the City Council meeting of August 21, 2013, the Imperial Beach City Council took action to adopt Resolution No. 2013-7375, approving a response to a report by the San Diego County Grand Jury filed May 28, 2013 entitled "Imperial Beach Finances – A City Under Stress." Enclosed please find a certified copy of the resolution, along with the City's response letter.

If you have any questions regarding this matter, please contact Greg Wade, Assistant City Manager, at (619)628-1354 or gwade@ImperialBeachCA.gov.

Sincerely,


Jacqueline M. Hald, MMC
City Clerk

Enclosures (2)

cc: Mayor
City Council



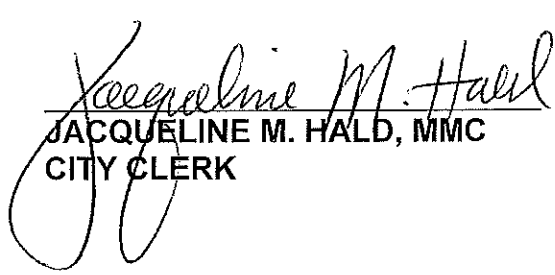
City of Imperial Beach, California

OFFICE OF THE CITY CLERK _____

STATE OF CALIFORNIA)
COUNTY OF SAN DIEGO) ss.
CITY OF IMPERIAL BEACH)

I, Jacqueline M. Hald, City Clerk of the City of Imperial Beach, do hereby certify that the attached is a true and exact copy of Resolution No. 2013-7375 – **A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF IMPERIAL BEACH, CALIFORNIA, APPROVING A RESPONSE TO A REPORT BY THE SAN DIEGO COUNTY GRAND JURY FILED MAY 28, 2013 ENTITLED “IMPERIAL BEACH FINANCES – A CITY UNDER STRESS.”**

DATED: August 23, 2013


JACQUELINE M. HALD, MMC
CITY CLERK

RESOLUTION NO. 2013-7375

A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF IMPERIAL BEACH, CALIFORNIA, APPROVING A RESPONSE TO A REPORT BY THE SAN DIEGO COUNTY GRAND JURY FILED MAY 28, 2013 ENTITLED "IMPERIAL BEACH FINANCES – A CITY UNDER STRESS"

WHEREAS, on May 28, 2013, the San Diego County Grand Jury issued a report entitled "Imperial Beach Finances," which made various findings and recommendations pertaining to the City of Imperial Beach; and

WHEREAS, the City Council is obligated per Penal Code section 933(c) to respond to these recommendations in accordance with Penal Code section 933.05(a) and (b).

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Imperial Beach as follows:

- Section 1. That the City Council adopts the response to the Grand Jury's report accompanying this resolution, and the Mayor is authorized to sign such response.
- Section 2. That the City Clerk is authorized to send a signed copy of the response to the Presiding Judge of the San Diego County Superior Court as required by Penal Code section 933(c).

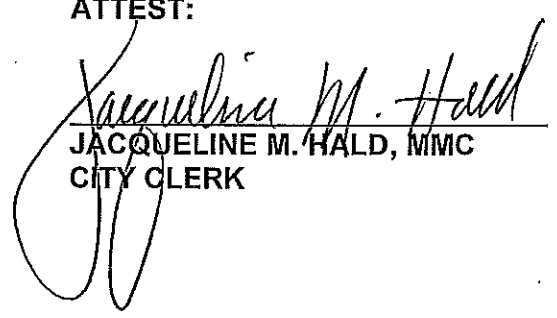
PASSED, APPROVED, AND ADOPTED by the City Council of the City of Imperial Beach at its meeting held on the 21st day of August 2013, by the following vote:

AYES: COUNCILMEMBERS: SPRIGGS, BILBRAY, PATTON, BRAGG, JANNEY
NOES: COUNCILMEMBERS: NONE
ABSENT: COUNCILMEMBERS: NONE



JAMES C. JANNEY, MAYOR

ATTEST:



JACQUELINE M. HALD, MMC
CITY CLERK



City of Imperial Beach, California

OFFICE OF THE MAYOR

825 Imperial Beach Blvd., Imperial Beach, CA 91932 Tel: (619) 423-8303 Fax: (619) 628-1395

August 21, 2013

The Honorable Robert J. Trentacosta
Presiding Judge
San Diego County Superior Court
220 W. Broadway
San Diego, CA 92101

SUBJECT: RESPONSE TO MAY 28, 2013 GRAND JURY REPORT ENTITLED "IMPERIAL BEACH FINANCES – A CITY UNDER STRESS"

Dear Presiding Judge Trentacosta:

The City respectfully submits this letter as its response to the above-referenced Grand Jury report (the "Grand Jury Report") on behalf of the Mayor, City Council, and City Manager for the City of Imperial Beach (referred to collectively as the "City"). Pursuant to California Penal Code (the "Penal Code") Section 933(c) and in compliance with Penal Code Section 933.05(a) and (b), the response discusses each of the Findings and Recommendations set forth in the Grand Jury Report.

As part of the Grand Jury Report, the Grand Jury requested that the San Diego County Office of Audits & Advisory Services (OAAS) conduct a formal audit (the "OAAS Audit") of the City's financial records. Although the stated purpose of the audit "was to examine potential financial irregularities in the specific areas of outsourced attorney charges and employee time allocations related to RDA activities," the City believes that the OAAS Audit and Grand Jury Report extend well beyond this stated purpose. Despite this belief, the City appreciates and concurs with the determination of the Grand Jury that there has been no fraud on behalf of the City or the Imperial Beach Redevelopment Agency Successor Agency (the "Successor Agency"). Further, although the Grand Jury Report accurately points out that City and Successor Agency staff has had to navigate "a ROPS process that involved arbitrary deadlines, changing submission requirements, and evolving definitions of Enforceable Obligations," it incorrectly suggests that the City and Successor Agency have been "struggling" with this process. Rather, to date, every Recognized Obligation Payment Schedule (the "ROPS") has been submitted on time by the statutory deadlines and as directed by the California Department of Finance (the "DOF"), with most of the listed enforceable obligations approved by the DOF and all available Redevelopment Property Tax Trust Fund (the "RPTTF") monies approved by the DOF for distribution to the Successor Agency to pay such approved enforceable obligations. It should also be noted that the challenges presented by the redevelopment dissolution process have been experienced by virtually every successor agency throughout the state and that the Successor Agency has experienced a very high DOF approval rate of all required submittals made pursuant to the Dissolution Act.

Although the City and Successor Agency strongly believe that each entity has successfully carried out their responsibilities as required by Assembly Bill X1 26, Assembly Bill No. 1484, and Assembly Bill No. 1585 (collectively, the "Dissolution Act") for dissolution of the former Imperial Beach Redevelopment Agency (the "Former RDA"), the City and Successor Agency nevertheless take very seriously the Grand Jury Report and, therefore, the City respectfully offers the following responses to the Findings and Recommendations as required under Penal Code Section 933(c). In connection with each Finding, the City discusses its belief of inaccuracies in connection with certain Facts stated to support such Finding.

SUMMARY OF FACTS AND FINDINGS:

Fact: The City pays just over 10% of its personnel labor costs from redevelopment funds.

The City believes this "fact" is incorrect. First, both the OAAS Audit and the Grand Jury Report do not acknowledge that their period of reviews cover a span of time during which the Former RDA operated and redevelopment existed pursuant to the California Community Redevelopment Law (California Health and Safety Code Section 33000 et seq.) and then was later suspended and subsequently dissolved pursuant to the Dissolution Act. It is incorrect, therefore, to state this "fact" in the present tense as 1) redevelopment and redevelopment funds no longer exist and 2) the Successor Agency (not the City) is now responsible for payment of labor costs associated with redevelopment activities funded with former redevelopment tax increment funds (now called the Redevelopment Agency Property Tax Trust Fund or "RPTTF", which receives and holds property tax funds for distribution by the County of San Diego in accordance with the Dissolution Act). However, as with the Former RDA, the Successor Agency does not directly employ its own staff to perform its operations and functions. Rather, the Successor Agency relies on City staff to perform its operations and functions and lawfully compensates the City for such actions. Although, prior to dissolution, the Former RDA funded much of its labor costs through project-related tax allocation bond proceeds and tax increment funds, as discussed in detail below, since redevelopment dissolution, the labor costs performed by City staff on behalf of the Successor Agency are capped at \$250,000 per year pursuant to the Dissolution Act which equates to only 4% of the City's labor costs in the recently approved operating budget.

Fact: The City's redevelopment budget is equivalent to slightly more than 50% of its General Fund.

The City believes this "fact" is incorrect. This statement seems to apply to pre-redevelopment dissolution and, therefore, it is misleading to state it in the present tense. There is no longer a redevelopment budget and the Successor Agency's "budget" is far less than 50% of that of the General Fund as further discussed below.

FINDING 01: THE CITY CONTINUES TO BE DEPENDENT ON TAX INCREMENT REDEVELOPMENT FUNDS FOR A SUBSTANTIAL AMOUNT OF ITS OPERATING BUDGET.

Response

The City respectfully **disagrees** with this Finding as the City believes that the "facts" offered to support such Finding are incorrect.

The City and the Successor Agency have successfully completed the primary part of the redevelopment wind-down process in compliance with the requirements of the Dissolution Act. In this regard, on April 12, 2013, the Successor Agency received its Finding of Completion (the "FOC") from the DOF – which is one of the first FOC's issued by the DOF in the County of San Diego. This FOC was issued well in advance of both the OAAS Audit and the issuance of the Grand Jury Report. Issuance of the FOC means that the Successor Agency has satisfactorily performed certain of its obligations required by the Dissolution Act and is a sign of approval by the DOF that the Successor Agency is properly winding down the affairs of the Former RDA consistent with the Dissolution Act. Additionally, as of February 1, 2012, all assets and outstanding obligations of the Former RDA were transferred by operation of law to the Successor Agency pursuant to the Dissolution Act for the wind-down process. Upon the enactment of the Dissolution Act on June 28, 2011, there is no longer any "tax increment" provided to the Former RDA or the Successor Agency. Rather, a limited amount of property tax is allocated to the Successor Agency from the RPTTF

administered by the San Diego County Auditor and Controller (the "CAC") to pay DOF approved "enforceable obligations" of the Former RDA and Successor Agency. Further, as noted above, the Former RDA did not have separate employees performing solely redevelopment operations and functions and, instead, relied on City staff to perform all such actions. Therefore, the City staff currently performs all operations and functions of the Successor Agency for the redevelopment wind-down process. Pursuant to the Dissolution Act, other than pass-through payments to taxing entities (which include the City and the County of San Diego among other taxing entities), as mandated by State law, the only portion of RPTTF that benefits the City's operating budget is the Administrative Cost Allowance which is capped at \$250,000 per year pursuant to the Dissolution Act and paid to the Successor Agency from the RPTTF to fund the administrative costs of the Successor Agency for its operations and functions. This amount represents only 1.4% of the City's current operating budget making it impossible for the City to depend upon RPTTF for its on-going operational needs. As the wind-down of redevelopment progresses and the Former RDA's and Successor Agency's enforceable obligations are reduced, the City, like every other affected taxing entity including the County of San Diego, will also receive a portion of the "residual" balance of RPTTF, if available, for each six-month period which is the balance of funds in the RPTTF after the payment of the County's administrative costs, pass-through payments to the taxing entities, enforceable obligations of the Former RDA and Successor Agency, and the Administrative Cost Allowance. To date, however, there has been no residual balance of RPTTF for distribution to any taxing entities including the City.

Successor Agency activities related to redevelopment dissolution are handled in a fund separate from the City's operational fund. The City's operations are funded directly from the City's General Fund. While significant time was previously spent by the City Manager and other City staff on redevelopment activities prior to redevelopment dissolution, and significant time has also been spent by the same staff since dissolution, City activities unrelated to redevelopment are paid from the City's General Fund. The City's Fiscal Year 2013-2015 General Fund budget was approved by the City Council on May 15, 2013. This two-year budget is balanced and shows fund surplus in both fiscal years. In addition, the City has strong unrestricted reserves of approximately 30% of General Fund expenditures, and an economic uncertainty reserve of 10% of General Fund expenditures. These reserves well exceed the minimum standards (Government Finance Officers' Association ("GFOA")) of 10% of General Fund expenditures recommended by the GFOA. The Successor Agency's use of RPTTF funds is correctly and solely for payment of debt service for tax allocation bonds issued by the Former RDA and used for public and private projects within the Redevelopment Project Area, and for payment of other enforceable obligations of the Former RDA and the Successor Agency approved by the DOF. With the dissolution of the Former RDA, City staff has been reduced by nine (9) positions previously required to support the Former RDA's redevelopment activities. City staffing is very lean and, in spite of the additional responsibilities resulting from redevelopment dissolution and obligations of the Successor Agency by the Dissolution Act, City staff continues to carry out the responsibilities of the City and also those of the Successor Agency including the several important projects funded through tax allocation bonds issued by the Former RDA as required by the Dissolution Act. Overall, the City is on stable financial footing without the use of Former RDA tax increment funds.

Fact: The City does not record outsourced legal services costs in a manner required by ROPS reporting requirements.

The City believes this "fact" is incorrect, as discussed in great detail below under Finding 02. The Dissolution Act does not contain requirements as to how a Successor Agency (and certainly not a City) independently records its legal costs. Rather, the Dissolution Act simply provides that legal costs associated with litigation may be considered and separately listed as an enforceable obligation payable from RPTTF and distinguishes such costs from other legal services paid from the Administrative Cost Allowance.

FINDING 02: THE CITY OFTEN RECORDS LEGAL SERVICES COSTS INCORRECTLY TO THE RDA, THE SUCCESSOR AGENCY, AND/OR CITY ACCOUNTS.

Response

The City respectfully **disagrees** with this Finding and the City believes that one of the "facts" offered to support such Finding is incorrect.

The City had been recording some legal costs, as noted in the Grand Jury Report, to professional services and some to legal services accounts (which is neither improper nor illegal); however, the City has not charged the funds incorrectly. All legal costs have been and are recorded to the specific fund for which the services are provided. The legal invoices provided to the OAAS auditors clearly identify the purposes for which the legal services were rendered and were recorded to the appropriate account accordingly. Although there is no statutory requirement to do so, subsequent to the OAAS Audit, staff has segregated and retitled four accounts that had been charged to professional services and is now charging the legal expenditures to the legal services account and not the professional services account. Finally, it is inaccurate to state that the City does not record legal services costs "in a manner required by ROPS reporting requirements." First, the Dissolution Act does not contain requirements as to how a Successor Agency (and certainly not a City) independently records its legal costs. Rather, the Dissolution Act simply provides that legal costs associated with litigation may be considered and separately listed as an enforceable obligation payable from RPTTF and distinguishes such costs from the legal services paid from the Administrative Cost Allowance. In order to obtain RPPTF, separate from the Administrative Cost Allowance, with which to pay legal litigation costs, such legal litigation costs must be separately reported on a ROPS. However, this distinction was only adopted with AB 1484 on June 27, 2012 **after** the preparation and submittal of ROPS I and II. Therefore, in connection with certain legal litigation costs invoiced to the Successor Agency in July 2012, the Successor Agency was forced to seek payment from RPTTF through the ROPS II prior period reconciliation process since costs for litigation were incurred during the ROPS II period, but after the ROPS II had been prepared by the Successor Agency and approved by the DOF. In the Successor Agency's most recent ROPS 13-14A approval letter from the DOF, the DOF not only approved the payment of other litigation expenses from RPTTF as reported and requested on the ROPS 13-14A, but the DOF also indicated that the Successor Agency can seek reimbursement from RPTTF for the subject legal litigation costs incurred during ROPS II on a future ROPS. This clearly indicates that the Successor Agency is fully complying with ROPS reporting requirements and appropriately receiving funds to pay its legal costs.

FINDING 03: THE RDA'S ADMINISTRATIVE COSTS FOR SHARED LABOR ARE INACCURATE.

Response

The City respectfully **disagrees** with this Finding.

Although the Former RDA no longer exists, prior to its dissolution, the City acknowledges that the manner in which costs were allocated was based on a percentage of actual time spent by individual staff members. Understanding that the entire City is located within the Redevelopment Project Area and, therefore, that almost every employee of the City performed work on behalf of the Former RDA, this was the most effective and efficient way to account for administrative costs of the Former RDA. Regardless of this fact, it is entirely incorrect to conclude that the administrative costs for shared labor are inaccurate because the percentage of time spent on Former RDA costs allocated to each employee was based on an historic analysis of actual time spent.

Since dissolution of the Former RDA, the City has established project codes for each project, including all of those related to the Successor Agency. All labor costs related to projects are charged directly to the correct project in order to segregate labor costs between the City and the Successor Agency. In the payroll process, the labor is charged accordingly based on the electronic timesheet approvals by each department head. As an additional payroll control, the payroll clerk validates the approved departmental payroll against employee time sheets. The Administrative Services Director has final review and approval of each payroll. This system of checks and balances ensures that Successor Agency costs continue to be accurately recorded.

Fact: The DOF mistakenly approved some Enforceable Obligations in ROPS I and ROPS II that were subsequently funded by the CAC. The DOF later denied these obligations in ROPS III.

The City believes this "fact" is incorrect. The DOF approved both the ROPS I and ROPS II in their entirety without qualification as indicated in the DOF's approval letter dated May 29, 2012, as well as in subsequent court filings submitted on behalf of the DOF. Although the CAC and the OAAS may disagree with the DOF's approval of ROPS I and II in their entirety, it is the DOF that has the ultimate authority for approval or denial of obligations listed on a ROPS and for their funding from RPTTF. Additionally, as with many other ROPS submitted by other successor agencies, the DOF did deny some obligations listed on ROPS III that were approved on ROPS I and II; however, the DOF also either approved or "reclassified" as administrative costs other obligations listed on ROPS III – and thus the DOF did not deny most of the obligations listed on ROPS III.

Fact: The City has understated its RDA expenses in FY2010-11 by \$1.7M.

The City believes this "fact" is incorrect. This amount was reviewed and subsequently approved by the DOF as an authorized transfer of Former RDA tax increment to the City for services performed by the City on behalf of the Former RDA subject to a valid and approved reimbursement agreement between the Former RDA and the City dated July 1, 2007.

FINDING 04: THE CITY'S ROPS I AND ROPS II SUBMISSIONS WERE INACCURATE.

Response

The City respectfully **disagrees** with this Finding and the City believes that some of the "facts" offered to support such Finding are incorrect.

The DOF is the ultimate authority for and approval of the Successor Agency's ROPS' submissions and for funding of obligations from RPTTF. Under the Dissolution Act, ROPS submittals are estimates of Successor Agency expenditures of an up-coming six-month period. The statement that the DOF "mistakenly approved" and then denied some enforceable obligations is simply not accurate. In fact, the DOF approved both the ROPS I and ROPS II in their entirety as indicated in DOF's ROPS I and II approval letter dated May 29, 2012, as well as in subsequent court filings submitted on behalf of the DOF. While the CAC subsequently disagreed with the payment of RPTTF for some of the items approved on both ROPS I and II in connection with their reconciliations on ROPS III and ROPS 13-14A respectfully, the DOF ultimately disagreed with the CAC and specifically approved the use of RPTTF for each and every item requested on both ROPS I and ROPS II per the DOF's approval letter issued on December 18, 2012. Although the CAC had disagreed and formally recommended to the DOF reductions in RPTTF to be distributed to the Successor Agency for payment of enforceable obligations on ROPS III based on the payment of obligations approved by the DOF on ROPS I, which reduction would have withheld more than \$2.3 million of RPTTF requested for ROPS III obligations, the DOF specifically directed the CAC not to make any such reduction to RPTTF and, rather, to distribute all available RPTTF to the Successor Agency

for payment of DOF approved enforceable obligations. In doing so, the DOF also increased the amount of RPTTF requested by the Successor Agency to make up for the deficit of RPTTF received by the Successor Agency for the ROPS II period. Since the Successor Agency has received all available RPTTF since dissolution of the Former RDA, it is clear that all ROPS prepared and submitted to the CAC and DOF have not only been accurate but have also been substantially approved by the DOF (including approval of ROPS I and ROPS II in their entirety). Although the DOF did deny some items on ROPS III that were approved on both ROPS I and II, the DOF's approval of these items on ROPS I and II and the subsequent approval by the DOF and payment of RPTTF to the Successor Agency for these items speaks for itself.

Finally, a transfer from the Former RDA of \$1.7 million to the City, which was made in a timely manner to reimburse the General Fund for costs incurred on behalf of the Former RDA and reimbursed as part of a properly executed reimbursement agreement, was initially denied by the DOF during its review of the Successor Agency's Non-Housing Due Diligence Review Audit. However, after meeting and conferring with the DOF on this matter, the DOF reversed its initial determination and this transfer was subsequently approved by the DOF per the DOF's approval letter issued on April 8, 2013.

FINDING 05: INADEQUATE ACCOUNTING, AND ESPECIALLY INCORRECT REPORTING OF SHARED LABOR COSTS, PREVENTED THE CITY FROM PREPARING ACCURATE AND TIMELY ROPS SUBMISSIONS.

Response

The City respectfully **disagrees** with this Finding.

As stated above, the Successor Agency's (not the City's) ROPS I and ROPS II submissions were approved in their entirety by the DOF. Additionally, for both ROPS III and ROPS 13-14A, all available RPTTF was approved by the DOF and paid to the Successor Agency to fund enforceable obligations approved by the DOF on each respective ROPS. The statement that the "incorrect reporting of shared labor costs prevented the City [sic] from preparing accurate and timely ROPS submissions," therefore, is absolutely incorrect given that all of the Successor Agency's ROPS have been prepared and submitted in a timely manner and prior to every statutory deadline in the Dissolution Act and further that all available RPTTF for the enforceable obligations approved by the DOF on every ROPS has been paid to the Successor Agency.

Fact: The City's timekeeping system does not currently allow employee time sheets to be electronically approved by a supervisor.

The City believes this "fact" is incorrect. The City's payroll system does, in fact, provide for electronic timesheet entry **and** electronic supervisor approval.

Fact: Employees may make unauthorized adjustments to time sheets after supervisor's approval, but prior to payroll processing.

The City believes this "fact" is incorrect. Employees do not have access to the time sheet entry module after the supervisor has given approval.

FINDING 06: THE CITY TIMEKEEPING SYSTEM AND PROCEDURES ARE FLAWED AND THEY ARE OPEN TO ALTERED ENTRIES.

Response

The City respectfully **disagrees** with this Finding as the City believes that the "facts" offered to support such Finding are incorrect.

Contrary to the above stated "Facts," the City's payroll system provides both for electronic timesheet entry and electronic supervisor approval. Although the system did allow for a two-hour time frame providing sufficient time for the supervisor to review the time sheet before approval, that window has since been narrowed and employees do not have access to the time sheet entry module after the supervisor has given approval. Additionally, as noted above, time sheets are compared to time entered and against approved leave and overtime slips before processing the pay by the payroll technician. A supervisor and the Administrative Services Director then approve the final payroll schedule before any checks/check stubs are created. As such, timesheets are not open to altered entries.

FINDING 07: THE CITY'S ACCOUNTING PROCEDURES REGARDING RDA FUNDS WERE FLAWED.

Response

The City **partially agrees** with this Finding, although the City respectfully disagrees with the use of the word 'flawed' which the City believes conveys an unnecessarily harsh connotation that is unwarranted.

The City has always received an unqualified audit opinion for its annual financial audits. The City agrees that there is always room for improvement and, as a result of an audit recommendation, reconciliation of the City's bank accounts has been adjusted to agree to the actual cash in the funds and not to the pooled cash account. All bank reconciliations must be reviewed and approved by the Administrative Services Director.

The fund balance adjustment to the Project Fund referred to in the independent audit for the period ending January 31, 2012, was in fact accurate. The amount of the adjustment was \$8,118. In their January 31, 2012 report, the auditors stated, "None of the misstatements detected as a result of audit procedures and corrected by management were material."

Fact: On June 14, 2012, the Tax Allocation Bonds insured rating was downgraded from A3 to Ba1.

The City believes this "fact" is incorrect. Neither the 2003 Tax Allocation Bonds nor the 2010 Tax Allocation Bonds issued by the Former RDA have ever been downgraded, and the 2010 Bonds retain their A rating today.

Fact: The DOF has continued to deny RPTTF funding for many items claimed by the Successor Agency on its ROPS.

The City believes that this fact, though somewhat true, is misleading and primarily inaccurate. Not only has the DOF approved the majority of items included on all ROPS submitted thus far, but the DOF has also approved **all available RPTTF** with which to fund the DOF approved enforceable obligations. Although, on occasion, the DOF has denied some items listed on a ROPS seeking RPTTF funding, this is not unique to the Successor Agency and, in fact, is commonly experienced by most successor agencies throughout the State in the redevelopment wind down process. Additionally, most of the items denied for funding from RPTTF were not denied outright but were reclassified as administrative costs payable with the Administrative Cost Allowance.

FINDING 08: THERE IS NO GUARANTEE THAT RPTTF FUNDS WILL BE SUFFICIENT TO REPAY THE SUCCESSOR AGENCY'S DEBT.

Response

The City respectfully **disagrees** with this Finding as the City believes that the "facts" offered to support such Finding are both incorrect and misleading.

Specifically, the proposed "fact" that on June 14, 2012, the Tax Allocation Bonds insured rating was downgraded from A3 to Ba1 is plainly inaccurate and an untrue statement. There is no record that the bond rating has been changed at all. Indeed, in the Successor Agency's review of the 2010 Continuing Bond Disclosure completed at the end of 2012, there was no bond rating change which would have been disclosed as a 'Significant Event' in the Bond Disclosure. Going forward, the Former RDA's and now the Successor Agency's obligation to make bond debt service payments for the two bonds issued to complete redevelopment projects remains a continuing obligation of the Successor Agency. Pursuant to the Dissolution Act, the servicing and/or repayment of this bond debt receives the highest priority of all Successor Agency enforceable obligations. Given the history of tax increment generation in the Redevelopment Project Area, even during the recent economic recession, there is no reason whatsoever to doubt that continued generation of and required distributions from the RPTTF will be more than sufficient to pay all outstanding debt service. Additionally, the Successor Agency is currently proceeding with a proposed refunding/refinancing of the 2003 bonds that will reduce the interest component thereby freeing additional property tax in the RPTTF for payment to the taxing entities (including the County of San Diego) as residual payments – a primary goal of the Dissolution Act. The Successor Agency's Financial Advisor indicates that the Successor Agency's 2010 bonds have retained their A rating and preliminary analysis of the City's property tax generation indicates that tax revenues will be more than sufficient to service the debt on the 2003 refunding/refinancing bonds, including continued debt service on the 2010 bonds, and that the new refunding bonds would also have an A rating.

Additionally, while every successor agency in the State, including the Successor Agency, continues to have some enforceable obligations included on a ROPS denied by the DOF and a corresponding denial of RPTTF funding for such obligations, this only means that more RPTTF will be available to service the Successor Agency's bond debt obligations. Additionally, the DOF has continued to approve RPTTF for bond debt service and, in fact, has been approving the use of RPTTF to fund bond debt reserves, thereby making any default on these bonds all the more unlikely. Likewise, most other enforceable obligations listed on the ROPS' by the Successor Agency have been approved by the DOF for funding from the RPTTF. Therefore, while there is no guarantee that the law will not substantially change again with respect to the redevelopment wind down process and RPTTF distribution to successor agencies throughout the State, a default on any of the Successor Agency's enforceable obligations is highly unlikely.

Fact: The City, under protest, made a payment in July 2012 of \$372,115 to the CAC as part of the clawback of unqualified Enforceable Obligations in ROPS I.

The City believes this "fact" is inaccurate and misleading. It is true that this payment was made and was made under protest by the Successor Agency (not the City). However, the reason for the protest was that, in June 2012, the CAC and DOF improperly questioned certain items included on the ROPS I which had already been approved by the DOF in its entirety on May 29, 2012. This subsequent questioning and "disapproval" of already-DOF-approved enforceable obligations (not "unqualified") on the ROPS I resulted in the \$372,115 "true-up" payment demand and the Successor Agency's subsequent payment of such amount. As further discussed below, this payment was made under protest due to the threat of significant penalties provided in the Dissolution Act to both the Successor Agency and the City if payment was not made by July 12, 2012. The DOF subsequently acknowledged the improper questioning of items on both the ROPS I and

ROPS II and allowed the Successor Agency's use of RPTTF distributed on June 1, 2012 to pay the improperly imposed \$372,115 true-up payment.

Fact: The City, using bond proceeds, made a Housing Authority debt service payment in November 2012 of \$533,092.

The City believes this "fact" is incorrect and misleading. Although the Successor Agency (not the City) was forced to use housing bond proceeds to make a 2003 bond debt service payment, it was not a "Housing Authority" debt service payment as the Housing Authority is not obligated to service debt on either the 2003 or 2010 tax allocation bonds. The true facts regarding this payment are discussed below.

Fact: The City's ROPS III submission shows an outstanding debt for redevelopment activities of \$111M and a payment deficit of \$2.6M.

The City believes this "fact" is misleading. Though it is true that \$111 million of outstanding Successor Agency debt was indicated in the Successor Agency's ROPS III, it was actually a clear error in which the outstanding 2003 Tax Allocation Bond Debt of \$32.5 million was entered and automatically counted twice by the DOF's ROPS spreadsheet under line item 1 (2003 Bond Debt) and line item 17 (the aforementioned \$533,092 2003 Bond debt payment from the above-referenced bond proceeds). The actual outstanding debt for the ROPS III submittal, therefore, was \$78.5 million. Of that amount, \$77 million was for the outstanding bond debt for both the 2003 and 2010 tax allocation bonds. As mentioned above, under the Dissolution Act, this outstanding bond debt has the highest priority for RPTTF funding of all Successor Agency enforceable obligations.

Stating that the Successor Agency has a "payment deficit" of \$2.6 million is both incorrect and misleading as this amount is simply an estimate on the ROPS Summary page, being the difference between the anticipated or estimated amount of RPTTF to be received by the Successor Agency and the amount of requested RPTTF to fund enforceable obligations for the applicable six-month period. Given this expected deficiency, and pursuant to applicable procedures of the Dissolution Act, the Successor Agency did notify the CAC that it would have insufficient RPTTF for the ROPS III period with which to pay all of its enforceable obligations. In a letter dated January 29, 2013, the CAC concurred with the Successor Agency and identified insufficient RPTTF in the amount of \$964,696 for the ROPS III period. However, the Successor Agency simply decreased the DOF-approved 2003 and 2010 bond debt reserve amounts to account for this deficit. These bond reserves were simply a protective measure sought by the Successor Agency and approved by the DOF and were still partially funded during the ROPS III period. Notwithstanding this deficit, and along with the reclassification and denial of some items on the ROPS III, the amount of RPTTF provided to the Successor Agency was sufficient to pay all bond debt service and certain other enforceable obligations during the ROPS III period.

Fact: The City's ROPS 13-14A submission shows an outstanding debt for redevelopment activities of \$40M and a payment deficit of \$1.5M.

The City believes this "fact" is incorrect and misleading. Though it is true that the ROPS 13-14A shows an outstanding debt of \$40 million, stating that the Successor Agency has a "payment deficit" of \$1.5 million is incorrect and misleading as this amount is simply an estimate on the ROPS Summary page, being the difference between the anticipated or estimated amount of RPTTF to be received by the Successor Agency and the amount of requested RPTTF to fund enforceable obligations for the applicable six-month period. Additionally, the actual amount of RPTTF distributed on June 1, 2013, was \$3,265,673, which was \$1,529,810 more than the estimate of RPTTF, which estimate was based on the June 1, 2012 RPTTF distribution. The DOF approved all \$3,265,673 of RPTTF available to fund the Successor Agency's enforceable obligations, which, combined with the reclassification of some items on the ROPS III to

administrative costs, should be sufficient to pay all enforceable obligations approved on the ROPS 13-14A for this six-month period.

FINDING 09: THE CITY'S REDEVELOPMENT DEFICITS, SHOWN IN THE ROPS SUBMISSIONS AND AUDITED FINANCIAL STATEMENTS, ARE EVIDENCE OF THE CITY'S GROWING FISCAL STRESS.

Response

The City respectfully **disagrees with** this Finding and the City believes that the "facts" offered to support such Finding are both incorrect and misleading.

Not only is the City's fiscal condition quite sound, the City's General Fund is, in fact, not responsible for the obligations of the Successor Agency, including its bond debt. Notwithstanding these facts, and as noted above, there is absolutely no reason at this time to doubt that there will be sufficient RPTTF every six months with which to pay all outstanding bond debt and other enforceable obligations of the Successor Agency. As for the statement that "the City, under protest, made a payment in July 2012 of \$372,115 to the CAC as part of the clawback of unqualified Enforceable Obligations in ROPS I," this is only partially true. This "true-up" payment (imposed under the Dissolution Act on many successor agencies and intended to represent unused or improperly used tax increment funds paid to the Former RDA for ROPS I obligations) was, in fact, made under protest by the Successor Agency because this "true-up" payment of \$372,115 was the result of the CAC and DOF making unauthorized and improper adjustments to the DOF-approved enforceable obligations listed on the ROPS I after the DOF had already approved all obligations listed on the ROPS I by its letter dated May 29, 2012. Further, because the Successor Agency had no available funds with which to make this payment, it was forced to use RPTTF distributed on June 1, 2013, which was intended for the ROPS II period. This statutorily unauthorized adjustment to the ROPS I was included as part of the ROPS II reconciliation included in ROPS 13-14A and discussed with the DOF during the ROPS 13-14A "Meet and Confer" meeting on April 30, 2013. Given the facts presented by the Successor Agency, the use of RPTTF to make the improper "true-up" payment was approved by the DOF as stated in its approval letter dated May 17, 2013. As such, the Successor Agency was reimbursed \$372,115 from RPTTF for having to make the improper "true-up" payment demand. The DOF's determinations outlined in its letter dated May 17, 2013 rejected the CAC's recommended reductions in RPTTF to be paid to the Successor Agency on June 1, 2013 that would have reduced the payment of RPTTF to the Successor Agency on June 1, 2013 by \$747,238. If the OAAS and Grand Jury are truly concerned about the ability of the Successor Agency to adequately fund its bond debt service and other debt obligations, it is both perplexing and contradictory that the CAC has consistently sought to significantly reduce and/or minimize the amount of RPTTF due to the Successor Agency, which efforts have been rejected by the DOF.

The Successor Agency's (not the City's) use of \$533,092 of affordable housing bond proceeds to make a bond debt service payment was necessary as there was no available RPTTF with which to make this payment and pursuant to the Dissolution Act and other laws and contractual obligations, the Successor Agency was required to avoid a default on these bonds. The lack of funding was due to the improper "true-up" payment required by the CAC as discussed above, along with the prior depletion of all Former RDA assets by prior Supplemental Education Revenue Augmentation Fund ("SERAF") payments imposed by the State, and an on-going cash-flow deficiency of the Former RDA. This bond debt service payment, an approved enforceable obligation on all ROPS submitted thus far, was subsequently approved by the DOF for reimbursement from RPTTF received by the Successor Agency on January 2, 2013. Finally, having successfully navigated the first four ROPS submittals and having been approved for all available RPTTF with which to fund the DOF-approved enforceable obligations of the Successor Agency, it appears that, as expected, the number of Successor Agency enforceable obligations on ROPS 13-14B for which RPTTF will be needed has decreased to the point that, for the January 2, 2014 RPTTF distribution, residual RPTTF will

be available for distribution to the other affected taxing entities including the City. This, therefore, will actually serve to improve the City's fiscal stability and will continue to do so as the wind down process continues and the number of enforceable obligations is reduced.

SUMMARY OF RECOMMENDATIONS AND RESPONSES:

13-83: Update the City's timekeeping system and approval procedure to allow required segregation of labor costs to the Successor Agency.

Response

The City **has already implemented** this recommendation. The City agrees that it is a recommended practice that labor costs relative to work performed on behalf of the Successor Agency be segregated from the labor costs of the City, although we note that the Dissolution Act does not specifically require such segregation in the accounting system. In support of this recommended practice, however, a project code (SP1306) within the Successor Agency's financial system's general ledger was created with a start date of February 1, 2012 (the creation date of the Successor Agency), to segregate Successor Agency administrative costs, including labor costs. General use of this project code was not fully utilized during the ROPS I period because AB 1484, which imposed new tasks on county auditor-controllers and reporting requirements on successor agencies had not yet been enacted into law. As a result, uncertainty existed regarding the ROPS reporting among all former redevelopment agencies and their successor agencies across the State during the ROPS 1 period. Additionally, the Successor Agency has also created other project-related codes to more accurately account for costs incurred by the Successor Agency, as opposed to costs incurred by the City.

13-84: Immediately implement accounting procedures that accurately segregate all cost types (notably labor and outsourced legal expenses) between the General Fund, Successor Agency funds, and other City funds.

Response

The City **has already implemented** this recommendation. The City agrees it is a recommended practice that labor costs relative to work performed on behalf of the Successor Agency be segregated from the costs of the City. In support of this recommended practice, not only was the project code referenced above (SP1306) created within the Successor Agency's financial system's general ledger, but several other project codes segregating other Successor Agency costs from City costs have also been created and utilized during the OAAS audited period and the current period. Further, enforceable obligation expenses incurred during ROPS I and ROPS II period by the Successor Agency were specifically reviewed and approved by the DOF during the ROPS I and ROPS II reconciliation process. The support documentation of enforceable obligation transactions submitted by the Successor Agency adequately met the DOF's standards, to the extent that a significant majority of the listed obligations were approved by the DOF with all available RPTTF paid to the Successor Agency for every ROPS period thus far:

A significant number of project codes exist in each of the City and Successor Agency general ledgers that specifically segregate costs associated with legal work on projects and other activities. Such information was provided to the OAAS auditors but was apparently overlooked during the auditors' review. Indeed, the legal invoices provided to the OAAS auditors are quite detailed regarding the specific projects and cases for which the work was provided.

Since the OAAS auditors' visit to the City of Imperial Beach, several more project codes have been created in the general ledger for the Successor Agency including R13102 (Oversight Board Costs), R13103 (SA Litigation Costs), RDA Property Management (R13104), the Pier South Hotel (R13105), Bikeway Village (S11106) and the 2003 Tax Allocation Bond Refunding/Refinancing (SP1311). Additionally, the Successor Agency is continually pursuing procedures to improve the ROPS reporting and reconciliation process.

13-85: By the end of the Calendar Year (CY) 2013, institute a time study that should be performed on a periodic basis, to allocate time spent on RDA activities.

Response

The City **does not intend to implement** this Recommendation as the City believes it is unwarranted. To accurately allocate time spent on Successor Agency (not Former RDA) activities, the City has been and will continue to record actual time spent by each staff member through its payroll timesheets, rather than implement this recommendation.

City and Successor Agency staff had already implemented the practice of recording the actual hours worked on Successor Agency activities on the payroll time sheets and by the use of the specific Successor Agency's Administrative Allowance Cost project code (SP1306) at the time of the OAAS Audit and have also begun using the other project codes discussed above. The City believes that this will be a more cost effective and efficient way to accurately allocate time than a time study. Additionally, legal services are also specifically recorded to specific project codes as the invoices provided are very specific as to the projects for which the services have been performed and billed separately under specific project titles. These hours are journalized throughout the pay period by referencing notes of the employee, meeting appointments, and correspondence regarding Successor Agency activities and projects. Further, the support documentation of staff hours dedicated to Successor Agency activities were reviewed and approved by the DOF. A time study not only fails to achieve the OAAS auditors' goal, but would be a needless use of taxpayer resources.

13-86: By the end of CY 2013, improve the City accounting system for legal expenses as follows:

- **Make an adjusting journal entry to reclassify legal cost related to the RDA dissolution and the Successor Agency operations from the Professional Services Account to the Attorney Services account.**

Response: This Recommendation **has been implemented**. Staff has reclassified the attorney services to the Legal Services account from the Professional Services account, and journals have been created to correct previous entries.

- **Make an adjusting journal entry to reclassify legal costs related to City operations from the RDA and Successor Agency's accounts to City accounts.**

Response: The City **does not intend to implement** this Recommendation as the City believes it is unwarranted. As specifically detailed in all legal invoices provided to the OAAS auditors and subsequently provided to the Grand Jury, legal costs were and are correctly classified according to the appropriate fund for which the services were and are provided. In the case of one particular invoice specified by the OAAS auditors relating to legal services performed on behalf of the Housing Authority, these services were appropriately paid for by Former RDA tax increment pursuant to the CRL as the Former RDA was, at that time, legally authorized to pay for Housing Authority costs relating to the

Housing Authority's aid and cooperation to the Former RDA in implementation of the Former RDA's affordable housing obligations. After redevelopment dissolution, certain legal services relating to projects provided on behalf of the Housing Authority acting in its capacity as the "Successor Housing Entity" of the Former RDA were funded in part by RPTTF as specifically approved by the DOF. Additionally, as noted in the foregoing responses, the City and Successor Agency have taken additional measures to ensure that all legal costs are appropriately recorded and funded. The City and the Successor Agency intend to continue to specifically classify and correctly record all legal services to their appropriate funding sources.

- **Implement two accounts for recording legal services, one for legal services related to litigation and another for legal services related to general legal representation.**

Response: This Recommendation **had already been implemented** and in practice at the time of the OAAS Audit was conducted. In addition to the legal services account, all legal services are coded to sub account project accounts: one for litigation and a second one for operations. For example, all legal services are coded to their own account and, in addition, legal services related to litigation are also coded to a separate project code. This process segregates legal services between those for operations and those for litigation and provides the means to properly report information on a submitted ROPS.

- **Develop a process to ensure that legal services are recorded correctly.**

Response: This Recommendation **has been implemented**. Although legal services have always been correctly recorded under previous procedures, all legal services are now recorded to a Legal Services account and all purchase orders have been changed to reflect the correct coding.

13-87: By the end of CY 2013, restate financial statements for FY 2010-11.

Response

The City **does not intend to implement** this Recommendation as the City believes it is unwarranted. Although it is unclear to the City on what basis this Recommendation is provided, the issue with regard to the \$1.7 million transfer to the General Fund was successfully resolved with the DOF which found that the transfer was not an unauthorized transfer and, therefore, was approved. If the \$1.7 million transfer is the basis for this Recommendation, it is important to note that actions of the Former RDA were governed by the California Community Redevelopment Law during the period in question and which allowed for the aid and cooperation among cities and redevelopment agencies toward redevelopment activities and permitted the transfer of funds and other arrangements among the Former RDA and the City for redevelopment purposes. Additionally, both the City and the Former RDA received an unqualified audit report for FY 2010-11.

13-88: By the end of CY 2013, identify labor costs related to RDA activities for the period of February 1 through June 30, 2012 and make an adjusting journal entry to transfer this cost from the City's General Fund to the Successor Agency fund.

Response

The City **does not intend to implement** this Recommendation as the City believes it is neither reasonable nor warranted. First, there were no RDA costs incurred during the period mentioned as the Former RDA was dissolved on February 1, 2012. Secondly, the Dissolution Act allows for payment of labor costs related to Successor Agency activities. As previously noted above, the Successor Agency does not have independent staff or employees separate and apart from the City and, therefore, the Successor Agency fully relies upon City staff to perform all operations and functions of the Successor Agency. Additionally, once audited financial statements have been published, changes in the categorization of expenses on the income statement are not allowed. A restatement of financial statements for prior period adjustments is only done if the adjustments change the balance sheet. The implementation of this Recommendation would have no net effect to the balance sheets of the respective funds. Finally, the Due Diligence Reviews conducted pursuant to the Dissolution Act were a thorough audit of the Successor Agency's assets and accounts inclusive of the period identified which have been reviewed and approved by the DOF. Therefore, we cannot simply change or modify the assets and accounts of the Successor Agency at this time.

13-89: Develop a timekeeping system or work with the current vendor's system support to automate the timesheet approval process and to implement automated controls that prevent employees from adjusting time sheets after supervisor's approval.

Response

This Recommendation **had already been implemented** at the time of the OAAS Audit and it bears noting that there have been no instances of breaches of the City's internal control. The City's current electronic time keeping process is automated and payroll processing procedures are in place and strictly followed to protect against employees adjusting time sheets after submittal. The OAAS auditors noted that there exists a two-hour window when employees still have access to the time keeping system while department managers and directors are reviewing and approving submitted timesheets. This window is in place in order to give department directors access to make adjustments to submitted hours made in error. Once access to the payroll time keeping system is closed for the pay period, the Finance Department follows an additional internal control procedure of auditing the submitted approved timesheets against the timekeeping hours existing in the system. The report used for this internal control procedure is the "Hours Entry Report". This additional internal control procedure was discussed and demonstrated to the OAAS auditors but apparently was not recognized or acknowledged by the OAAS auditors in presenting their findings to the Grand Jury.

13-90: Begin immediately to increase the accuracy of their ROPS submission procedures to comply with DOF requirements.

Response

This Recommendation **has been implemented and will continue to be implemented**. Although all past ROPS submittals have been accurate inasmuch as estimate of funding needs for enforceable obligations can be, the Successor Agency is constantly pursuing procedures to improve the accuracy and compliance with the Dissolution Act. Although this Recommendation implies that past ROPS submittals have been inaccurate, as noted above, the Successor Agency's consistent approval rate by the DOF of the enforceable obligations and requested RPTTF funding for every ROPS submitted thus far clearly demonstrates both the accuracy and the appropriateness of the Successor Agency's ROPS submittals. Therefore, although this

Recommendation appears unwarranted based on the true facts, the Successor Agency will continue to provide accurate information on all ROPS submittals and the City will take steps to ensure this.

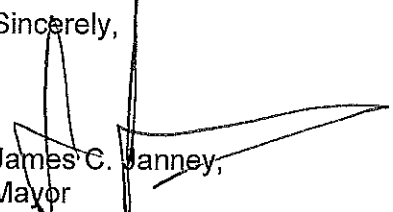
13-91: Consider getting help from the State representatives or County resources in the ROPS submission and settlement process.

Response

The Successor Agency **has implemented this Recommendation and will continue to implement** this Recommendation. As demonstrated by the foregoing responses, however, the City believes this Recommendation is not necessarily warranted based on the true facts. The Successor Agency has highly skilled and experienced staff who have successfully negotiated the challenges of redevelopment dissolution and compliance with the Dissolution Act including, without limitation, compliance with all applicable requirements, submittals, deadlines and procedures imposed to date on the Successor Agency, the City and successor housing entity (the Imperial Beach Housing Authority). The timely submittal of all ROPS, the approval by the DOF of most of the enforceable obligations included on each ROPS, the approval by the DOF and payment of all available RPTTF to the Successor Agency to fund approved enforceable obligations, the successful approval by the DOF of the Successor Agency's Due Diligence Review Audits (both Housing and Non-Housing funds and assets) with zero dollars owed, the approval of the State Controller's Asset Transfer Review, and the issuance of the Successor Agency's Finding of Completion on April 12, 2013 by the DOF, are absolute and irrefutable evidence of the Successor Agency staff's knowledge and understanding of the redevelopment dissolution process and the Dissolution Act, and the adequacy of the Successor Agency's ROPS preparation, submission, and review process. Beyond that, the City's, the Former RDA's and the Successor Agency's audit reports have always been unqualified and, while there is always room for improvement, staff continues to improve and refine its audit procedures. Finally, in connection with the myriad ambiguities and inconsistencies contained in the Dissolution Act (as acknowledged by both the OAAS auditors and the Grand Jury), the Successor Agency has sought and received assistance from State representatives and/or County resources in the preparation, submission and review process of submitted ROPS.

On behalf of the City, I thank you for the opportunity to respond to the Findings and Recommendations set forth in the Grand Jury Report. The City takes the Grand Jury investigative and reporting process very seriously, and we hope that the above responses provide additional helpful information in connection with each of the Findings and Recommendations discussed.

Sincerely,


James C. Janney,
Mayor

cc: City Council