

CERRITOS REDEVELOPMENT AGENCY

ASSET TRANSFER REVIEW

Review Report

January 1, 2011, through January 31, 2012



JOHN CHIANG
California State Controller

October 2013



JOHN CHIANG
California State Controller

October 8, 2013

CERTIFIED MAIL—RETURN RECEIPT REQUESTED

Art Galluci, City Manager
City of Cerritos/Successor Agency
18125 Bloomfield Avenue
Cerritos, CA 90703

Dear Mr. Galluci:

Pursuant to Health and Safety (H&S) Code section 34167.5, the State Controller's Office (SCO) reviewed all asset transfers made by the Cerritos Redevelopment Agency to the City of Cerritos 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 of Cerritos or any other public agencies have been reversed.

Our review found that the Cerritos Redevelopment Agency (RDA) transferred \$210,774,198 in assets after January 1, 2011, including unallowable transfers of assets totaling \$170,836,440, or 81.05%, of the transferred assets. These assets must be returned to the Successor Agency.

If you have any questions, please contact Steven Mar, Bureau Chief, Local Government Audits Bureau by phone at (916) 324-7226.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/sk

Attachment

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Asset Transfer Review Report

Summary

The State Controller's Office (SCO) reviewed the asset transfers made by the Cerritos Redevelopment Agency 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 Cerritos Redevelopment Agency (RDA) transferred \$210,774,198 in assets after January 1, 2011, including unallowable transfers of assets totaling \$170,836,440, or 81.05%, of the transferred assets. These assets must be returned 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.

In accordance with the requirements of H&S Code section 34167.5, the State Controller is required to review the activities of RDAs, "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," and the date on which the RDA ceases to operate, or January 31, 2012, whichever is earlier.

The SCO has identified transfers of assets that occurred after January 1, 2011, between the Cerritos Redevelopment Agency, the City of Cerritos, 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 order 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 Cerritos City Council, the Cerritos Redevelopment Agency, and the Cerritos Housing Authority.
- 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 Cerritos Redevelopment Agency (RDA) transferred \$210,774,198 in assets after January 1, 2011, including unallowable transfers of assets totaling \$170,836,440, or 81.05%, of the transferred assets. These assets must be returned to the Successor Agency.

The city is ordered to immediately reverse the transfers of \$170,836,440 and to return the assets identified in this report to the Successor Agency.

Views of Responsible Officials

We issued a draft review report on August 21, 2013. Mark W. Steres, City Attorney, responded by letter dated September 13, 2013, disagreeing with the review results. The Cerritos Successor Agency and City of Cerritos' response is included in this final review report as an attachment.

Restricted Use

This report is solely for the information and use of the City of Cerritos, the Successor Agency, the Successor Agency Oversight Board, 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

October 8, 2013

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Findings and Orders of the Controller

FINDING 1— Unallowable repayment of advances from the City of Cerritos

During the review period the Cerritos Redevelopment Agency (RDA) transferred \$104,099,199 (\$75,329,199 in real property and \$28,770,000 in future ground rents) in assets for \$39,770,000 in offsets against the “Advance from the City of Cerritos” account. The RDA also made three different types of cash repayments to the City of Cerritos (City) totaling \$21,282,887.

Pursuant to Health and Safety (H&S) Code section 34167.5, any asset transfers by the RDA to a city, county, city and county, or any other local public agency after January 1, 2011, must be returned to the Successor Agency for disposition in accordance with H&S Code sections 34177(d) and (e). In addition, any rents received by the City for ground rents discussed in No. 2, below must also be returned to the Successor Agency.

1. On March 24, 2011, the City Council and the RDA approved the sale of real property assets with a book value of \$75,329,199 (Schedule 2) to the City in the amount of \$11,000,000. The remaining \$64,329,199 of book value was eliminated due to a decline in fair market value.
2. On January 26, 2012, the City Council and the RDA approved the sale of future ground rents (years 2012-2087) from certain Towne Center and Auto Mall properties to the City at the City’s calculated present value of \$28,770,000 (Schedule 3).
3. The City charged \$3,733,742 in interest expense derived from the outstanding balance of the “Advance from the City of Cerritos” account. The offsetting entries are negative entries against “Due from General Fund,” a receivable account of the RDA. The negative balance was subsequently cancelled by a cash payment of \$3,733,742. The cash payment is as follows:
 - o May 25, 2011, General Entry JV101 for \$3,733,742
4. On June 29, 2011, and January 31, 2012, the RDA made two cash payments for a total of \$11,916,550 to reduce the “Advance from the City of Cerritos” account. The payments are as follows:
 - o June 29, 2011, check No. 903852 for \$20,640,000. On July 15, 2011 the City returned \$16,066,000 to the RDA by check No. 903852. The net cash transfer was \$4,574,000.
 - o January 31, 2012, Journal Entry GJ120716 cash transfer for \$7,342,550

5. The City charged \$5,632,595 in interest expense to the RDA derived from the outstanding balance of the "Advance from the City of Cerritos" account. The cash payments are as follows:
 - o November 11, 2011, check No. 903929 for \$1,857,823
 - o January 14, 2012, check No. 903945 for \$3,774,772

Order of the Controller

Based on H&S Code section 34167.5 and 34163(d), the City of Cerritos is ordered to reverse the transfers of the above assets, restore the book value of the assets in the amount of \$104,099,199, and turn them over to the Successor Agency. The Successor Agency is directed to properly dispose of those assets in accordance with H&S Code sections 34177(d) and (e).

In addition, based on H&S Code section 34167.5 and 34163(c) (2), the City of Cerritos is ordered to reverse the transfers of cash in the amount \$21,282,887 to the Successor Agency. The Successor Agency is directed to properly dispose of these assets in accordance with H&S Code sections 34177(d) and (e).

City's Response

The City disagreed with Finding 1 for two reasons. First, the City believes that the loan repayments made by the Redevelopment Agency to the City were valid and believes that the loan fell within the definition of "enforceable obligation." Second, the City believes that the real properties listed in Finding 1, were contractually committed to "third parties" prior to June 28, 2011.

SCO Comments

SCO's authority under H&S Code section 34167.5 extends to all assets transferred after December 31, 2010, 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(f), which allowed the RDA to continue to make payments under enforceable obligations to private third parties.

Lease agreements between the RDA and third parties do not qualify as third-party exemptions under H&S Code section 34167.5. The exemption only applies to contractual commitments to a third party made by the City.

The Finding and Order of the Controller remain as stated.

**FINDING 2—
Unallowable asset
transfers (gift) to
the City of Cerritos**

On March 24, 2011, the City Council and the RDA approved the transfer of real property assets, construction in progress, and land held for resale to the City with a book value of \$45,454,354 for zero dollar value.

APN	Address	Description
7012-027-901	Adjacent to the 91 Freeway, North of Artesia Blvd	Freeway Slope Easement
7016-012-902	16733 Studebaker Road	Reservoir Hill Park
7030-011-910	12700 Center Court Drive	Cerritos Center for the Performing Arts
7030-002-902	12616 183 rd Street	Former Mullikin Medical Building
7034-016-910	17423-1501 Studebaker Road	Former ROP Building
7034-018-901	Adjacent to San Gabriel River Between Artesia Blvd and 183 rd Street	B&B Stables
7039-020-900	1880 Gridley Road	Parking Lot; Former ARCO Service Station
7049-014-907	19033 Studebaker Road	Liberty Park Annex
7054-001-904	19030 Pioneer Boulevard	Fire Station
7055-024-900	20101 Cabrillo Lane	C-5 Well
N/A	N/A	Construction in Progress
Total		\$ 45,454,354

Pursuant to H&S Code section 34167.5, any asset transfers by the RDA to a city, county, city and county, or any other public agency after January 1, 2011, must be returned to the Successor Agency for disposition in accordance with H&S Code sections 34177(d) and (e). However, it appears that these assets also may be subject to the provisions of H&S Code section 34181 (a).

H&S Code section 34181 (a) states:

The oversight board shall direct the successor agency to do all of the following:

- (a) Dispose of all assets and properties of the former redevelopment agency; provided, however, that the oversight board may instead direct the successor agency to transfer ownership of those assets that were constructed and used for a governmental purpose, such as roads, school buildings, parks, police and fire stations, libraries, and local agency administrative buildings, to the appropriate public jurisdiction pursuant to any existing agreements relating to the construction or use of such an asset. Any compensation to be provided to the successor agency for the transfer of the asset shall be governed by the agreements relating to the construction or use

of that asset. Disposal shall be done expeditiously and in a manner aimed at maximizing value. Asset disposition may be accomplished by a distribution of income to taxing entities proportionate to their property tax share from one or more properties that may be transferred to a public or private agency for management pursuant to the direction of the oversight board.

Order of the Controller

Based on H&S Code section 34167.5, the City of Cerritos is ordered to reverse the transfer of the above assets, restore the book value of the assets in the amount of \$45,454,354, and turn them over to the Successor Agency. The Successor Agency is directed to properly dispose of those assets in accordance with H&S Code sections 34177(d) and (e) and 34181(a).

City's Response

The City indicated that "the Successor Agency and City intend to address this finding by pursuing ratification under Health and Safety Code section 34181 (a) of the government purpose properties listed in Finding 2."

SCO Comments

The Finding and Order of the Controller remain as stated.

**Schedule 1—
Unallowable RDA Assets Transferred to the City of Cerritos
January 1, 2011, through January 31, 2012**

Unallowable asset transfers to the City of Cerritos:	
Real properties sold to the City by the RDA (Finding 1, Schedule 2)	\$ 75,329,199 ¹
Future ground rents sold to the City by the RDA (Finding 1, Schedule 3)	<u>28,770,000 ¹</u>
Subtotal	104,099,199
Transfer of real property to the City by the RDA (Finding 2)	<u>45,454,354 ¹</u>
Subtotal	149,553,553
Payment of loans made to the City of Cerritos (Finding 1)	<u>21,282,887 ¹</u>
Total unallowable asset transfers to the City of Cerritos	<u>\$ 170,836,440</u>

¹ See the Findings and Orders of the Controller section.

**Schedule 2—
List of Real Properties Sold
to the City by the RDA**

APN	Address	Description
7030-001-020	17500 Bloomfield Avenue	Cerritos Towne Center
7030-001-021	17550 Bloomfield Avenue	Retail/Office/Hotel Area
7030-001-024	12701 Towne Center Drive	Group
7030-001-025	12721 Towne Center Drive	
7030-001-026	12727 Towne Center Drive	
7030-001-027	12731-12771 Towne Center Drive	
7030-001-029	12081 Towne Center Drive	Group
7030-001-030	N/A	
7030-001-031	N/A	
7030-001-033	12821 Town Center Drive	
7030-001-037	12601 Town Center Drive	Group
7030-001-038	12603 Towne Center Drive	
7030-001-040	12831-12865 Towne Center Drive	
7030-001-041	12875 Towne Center Drive	
7030-001-042	12989 Park Plaza Drive	
7030-011-004	12750 Center Court Drive	Group
7030-011-005	12610 Park Plaza Drive	
7030-011-006	12725 Center Court Drive	
7030-011-007	17785 Center Court Drive	
7030-011-008	12898 Towne Center Drive	Group
7030-011-009	17871 Park Plaza Drive	
7030-011-010	N/A	
7030-011-011	12900-12911 Park Plaza Drive	
7030-011-012	1777 Center Court Drive	
7030-011-915	12800 Center Court Drive	Group
7034-017-909	10861 183 rd Street	Jaguar/Land Rover Dealership
7034-017-910	18201 Studebaker Road	Kia Dealership
7054-024-060	11900 South Street	Lincoln Station
7054-024-061		
Total		<u>\$ 75,329,199</u>

**Schedule 3—
List of Future Ground Rents Sold
to the City by the RDA**

Valuation of Share of Base (Minimum) Ground Rents Allocated to the RDA		
	Base Rent Available for RDA Share	Share to RDA
2012	\$ 5,135,130	\$ 1,651,282
2013	5,135,130	1,651,282
2014	5,135,130	1,651,282
2015	5,152,280	1,668,432
2016	5,164,530	1,680,682
2017	5,164,530	1,680,682
2018	5,164,530	1,680,682
2019	5,164,530	1,680,682
2020	5,182,708	1,698,861
2021	5,195,693	1,711,845
2022	5,195,693	1,711,845
2023	5,195,693	1,711,845
2024	5,195,693	1,711,845
2025	4,874,531	1,390,684
2026	4,645,130	1,161,282
2027	4,645,130	1,161,282
2028	4,645,130	1,161,282
2029	4,645,130	1,161,282
2030	4,645,130	1,161,282
↓	↓	↓
2087	<u>2,222,963</u>	<u>555,741</u>
2012-Expiration	<u>\$ 339,416,700</u>	<u>90,122,161</u>
Present Value of RDA Share-5.0%		<u>\$ 28,770,000</u>

**Attachment—
Cerritos Successor Agency and City of Cerritos
Response to Draft Review Report**

In addition to the attached letter, the city provided two additional documents. Due to their size we are not including them as an attachment to this report. Please contact the City of Cerritos for copies of the following documents:

- Cerritos Legal Brief Regarding Loan Payments Made by the Cerritos Redevelopment Agency to the City of Cerritos
- Supplemental Reponse to April 24, 2013 Exit Conference

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September 13, 2013

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Via E-mail and Overnight Mail

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Re: Cerritos Redevelopment Agency Asset Transfer Review Report (the "Review Report")

Dear Mr. Mar:

The Cerritos Successor Agency and the City of Cerritos have reviewed the Review Report, including the findings, conclusion and order. Both the Successor Agency and the City of Cerritos appreciate and thank you for the opportunity to comment and respond to the draft Review Report. The Review Report provided two findings – Finding 1 (unallowable repayment of advances from the City of Cerritos) and Finding 2 (unallowable asset transfers (gift) to the City of Cerritos). This is the Successor Agency's and the City's response to the Review Report.

The Successor Agency and City object to Finding 1. Finding 1 on pages 4 and 5 of the Review Report sets forth five (5) categories of payments made by the Cerritos Redevelopment Agency ("Agency") to the City of Cerritos ("City") with the first payment made on March 24, 2011 and the last payment made on January 31, 2012. All of these payments represent payments for enforceable obligations of the Agency to the City at the time of payment. All of these payments represent payment of principal or interest due and owing from the Agency to the City pursuant to a valid and legal loan between the Agency and the City. The subject loan fell within the definition of "enforceable obligation" at the time of payment. Health & Safety Code section 34167(f) mandated

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that the Agency continue to make payments due for enforceable obligations. The loan between the Agency and the City was an enforceable obligation under the express terms of AB 1484 at the time of the payments made between March 24, 2011 and January 31, 2012, and the payments made were due under the terms of the loan. Although the State Controller has authority under Health & Safety Code section 34167.5 to review asset transfers made between January 1, 2011 and January 31, 2012, and to order the unwinding of asset transfers in the proper case, the State Controller has no authority nor jurisdiction to order the unwinding of an agency's performance of its enforceable obligations, such as the loan payments made in Finding 1 of the Review Report.

The Agency/City loan was created in 1969. For 42 years, pursuant to this loan agreement, the City has loaned money to the Agency for redevelopment activities and the Agency has made quarterly interest payments to the City and principal payments at times when redevelopment funds have been available. The payments made by the Agency to the City between March 24, 2011 to January 31, 2012 were all consistent with payments made by the Agency to the City over the past several decades and reflect a long-standing course of conduct between the Agency and City with respect to administration and implementation of the loan. The adoption of AB 26 did not change the authority nor the obligation of the Agency to make such payments. Under AB 26 the loan between the Agency and the City continued to be an enforceable obligation of the Agency. See Health & Safety Code section 34167(d)(2) and (d)(5). By making the payments on the loan, the Agency was simply complying with AB 26 as required by Health & Safety Code section 34167(f) [redevelopment agency shall make payments due, and shall perform its obligations] and section 34169(a) and (f) [redevelopment agency shall continue to make all scheduled payments for enforceable obligations, and avoid triggering an event of default under enforceable obligations].

The payment made as set forth in Item #3 of Finding 1 on page 4 of the Review Report is a scheduled quarterly interest payment for January-March 2011; the payments made as set forth in Item #4 of Finding 1 on page 4 of the Review Report are a scheduled end of the fiscal year principal payment and an end of the redevelopment agency principal payment; and the payments made as set forth in Item #5 of Finding 1 on page 5 of the Review Report are scheduled quarterly interest payments for April-June 2011, July-September 2011, and October-December 2011. The payments made as set forth in Items #1 and #2 of Finding 1 on page 4 of the Review Report are principal payments made upon demand of the City to the Agency for repayment of the Agency loan as required in the loan agreement.

The Successor Agency and City have briefed these arguments, with legal citation and evidence attached, and have provided these briefs to the State Controller's Office. The two briefs submitted are entitled "Legal Brief Regarding Loan Payments Made by the Cerritos Redevelopment Agency to the City of Cerritos", and "Supplemental Response to April 24, 2013 Exit Conference: Discussion of Scope and Historical Implementation of Cooperation Agreement". We are attaching these legal briefs to this response and request that this letter, along with the attached briefs, be a part of the Agency/City response to the draft report and be included in the final report.

Mr. Steven Mar
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Page 3

In addition to above, the real property assets identified in Item #1 of Finding 1 were committed to third parties both at the time of the transfer and for many years prior to June 28, 2011. As the State Controller has acknowledged in the Review Report, the Controller has no authority to order the reversal of a transfer pursuant to Health & Safety Code section 34167.5 if the real property is committed to a third party prior to June 28, 2011. All of the real property assets listed in Item #1 of Finding 1 are subject to long term leases that extend for years into the future and obligate the City to contractual commitments to such third parties. All of these long term leases were entered into many years prior to 2011. The State Controller has no jurisdiction over these real property assets.

In regards to Finding 2, as previously indicated the Successor Agency and City intend to address this finding by pursuing ratification under Health & Safety Code section 34181(a) for the governmental purpose properties listed in Finding 2. We also note that the operation of Health & Safety Code section 34177(e) referenced in your order has been suspended until January 1, 2015, pending approval of a long-range property management plan, pursuant to Health & Safety Code section 34191.3.

Without waiver of the general objections and observations set forth above with respect to Findings 1 and 2, we further note that (i) clarification is requested to the reference in the Review Report to the transfer of \$288,192,359 in assets when as set forth in Schedule 1 to the Review Report the cumulative total of identified book value transfers appears to be \$170,836,440 at most, and (ii) in the event any transfers for consideration are unwound for any reason, there would, of course, be a corresponding increase to the outstanding balance of the City/Agency loan in order to reverse the prior credit applied to that loan.

The response provided herein does not waive the right of the Successor Agency and the City to later provide additional information or statements as part of the review process. The Successor Agency and the City retain the right to raise new material or positions as required. These responses and objections are made without prejudice to, and are not a waiver of, the City's and the Successor Agency's right to rely on other facts, documents, responses or information in the State Controller review process or at a later proceeding. By making the accompanying responses and objections, the City and the Successor Agency do not waive, and hereby expressly reserve, its right to assert any and all objections as to the State Controller findings and statements in this review, or in any other proceedings, on any and all grounds including, but not limited to, jurisdiction, scope, competency, relevancy, and materiality. Further, the City and the Successor Agency make the responses herein without in any way implying that they consider all of the State Controller findings and statements to be legally valid or within the scope of AB 26, or relevant or material to the subject matter of this action. The City and the Successor Agency reserve the right to supplement, clarify, revise, or correct

Mr. Steven Mar
September 13, 2013
Page 4

any and all of the responses and statements herein, and to assert additional information or arguments, in one or more subsequent supplemental responses.

Sincerely,



Mark W. Steres
City Attorney, City of Cerritos
Agency Counsel, Cerritos Successor Agency

MWS/cp
Encls.

cc: Jeffrey V. Brownfield, Chief, Division of Audits, State Controller's Office (via e-mail)
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Bruce Barrows, Mayor, City of Cerritos (via e-mail)
Denise Manoogian, Director Administrative Services, City of Cerritos (via e-mail)
Torrey Contreras, Director Community Development, City of Cerritos (via e-mail)

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