City of Santa Rosa

Financing Alternatives for Capital Projects

September 22, 2015

The PFM Group
Public Financial Management, Inc.
PFM Asset Management, LLC
PFM Advisors

San Francisco
50 California Street, Suite 2300
San Francisco, CA 94111
p. 415-982-5544

City Infrastructure Projects

- **City has identified the following various types of unfunded infrastructure projects:**
  - Courthouse Square project
  - City facilities improvements
  - Stormwater infrastructure
  - Streets improvements
    - *Pavement preservation*
    - *Sidewalk construction/reconstruction*
    - *Highway 101 crossings*
    - *Capacity enhancements*
    - *Circulation improvements*
- **With the potential exception of the stormwater projects, the contemplated projects are not anticipated to be revenue-generating**

Traditional Tax-Exempt Financing Alternatives – Overview

- **The City has access to a number of tax-exempt public financing methods that typically offer lower borrowing costs than private capital, including:**
  - General Obligation Bonds
  - Lease Revenue Bonds or Certificates of Participation (COPs)
  - Revenue Bonds
  - Community Facilities District (CFD) Special Tax Bonds
  - Assessment District Bonds
  - Enhanced Infrastructure Financing District

- **The City has utilized several of these forms of financing previously**

Traditional Tax-Exempt Financing Alternatives

- **General Obligation Bonds**
  - Secured by a pledge of the issuer's taxing powers paid from ad valorem property taxes
  - Considered the most secure of all municipal debt
  - Limited in California by Proposition 13 to debt authorized by a vote of two thirds of voters in the case of local governments
- **Lease Revenue Bonds/Certificates of Participation**
  - Form of lease revenue bond that permits the investor to participate in a stream of lease payments relating to the acquisition or construction of specific equipment, land or facilities
  - Issuance does not require voter approval
  - COPs are not viewed legally as "debt" because payment is tied to an annual appropriation
  - As a result, COPs are seen by investors as providing weaker security and often carry ratings that are a notch or two below an issuer’s general obligation rating
- **Revenue Bonds**
  - Debt service is payable solely from the revenues derived from operating the facilities acquired or constructed with the proceeds of the bonds
  - Credit quality of a Revenue Bond, and its associated rating, depends on the strength of the particular revenues pledged and thus can vary widely

Traditional Tax-Exempt Financing Alternatives – Continued

- **Community Facilities District ("CFD") Special Tax Bonds**
  - Pursuant to 1982 Mello-Roos CFD Act, CFDs can be formed and bond issuance authorized by a 2/3 vote of the property owners in the special district
  - Debt service is paid from special taxes levied on property within the district
  - The property within the district secured the bonds and can be foreclosed upon if special taxes are unpaid
- **Assessment District Bonds**
  - Secured by special assessments, as opposed to property taxes, levied on properties within the district
  - The assessment levy represents the specific benefit to the property owner derived from the improvement
- **Enhanced Infrastructure Financing District ("EIFD")**
  - Authorized by SB628 in September 2014, EIFDs may be created within a city or county to finance the construction or rehabilitation of public infrastructure and private facilities
  - EIFD may fund infrastructure with the property tax increment of those taxing agencies that consent and a variety of other sources
  - City or county must prepare an Infrastructure Financing Plan detailing proposed infrastructure and funding
  - Bonds may be issued with 55% voter approval
  - EIFD creation requires that the Successor Agency has received a finding of completion from the DOF and certain other dissolution-related actions

Traditional Tax-Exempt Financing Alternatives

Financing	Funding Source	Typical Uses	Applicable For
General Obligation Bonds	Secured by a pledge of ad valorem property taxes approved by a 2/3 vote.	Projects that create a City-wide benefit.	-Courthouse Square -Streets Projects -City Facilities -Stormwater
Certificates of Participation	Secured by a pledge of lease payments in respect of an essential asset that is owned by the City, the General Fund is usually pledged to make the lease payments, though other revenues can be identified internally as the budgetary source for the payments.	Public capital facilities.	-Courthouse Square -Streets Projects -City Facilities -Stormwater
Revenue Bonds	Secured by a pledge of revenues from a specific source, such as a tax or fees (revenues from water system, storm drainage fees, etc.)	Enterprise infrastructure; could be area-specific using a local rate surcharge.	-Stormwater
CFD Special Tax Bonds	Secured by a Special Tax levied on each parcel in the District; requires 2/3 approval by voters in the District.	CFD area-specific improvements.	-Courthouse Square -Streets Projects -Stormwater
Assessment District Bonds	Secured by a Special Assessment Lien under which each parcel in the District pays a fixed portion of associated debt service; requires majority approval by property owners from the District.	AD area-specific improvements.	-Courthouse Square -Streets Projects -Stormwater
EIFD Bonds	Secured by an allocation of the local jurisdiction's property tax increment from the area; requires a 55% vote (IFDs were "enhanced" by SB 628, reducing vote requirement from 2/3).	Public capital facilities or other specified projects of communitywide significance that provide significant benefits to the EIFD or the surrounding community.	-Courthouse Square -Streets Projects -Stormwater

Traditional Tax-Exempt Financing Alternatives

- **A comparison of the credit, cost, and procedural characteristics of these options is presented below**

Financing Mechanism	Expected Credit Ratings	Expected Borrowing Cost	Process Length / Complexity
General Obligation Bonds	Strongest	Lowest	Medium
Certificates of Participation	Strong	Low	Low
Revenue Bonds	Medium	Medium	Low
Community Facilities District	Varies	Varies	High
Assessment District	Varies	Varies	High
Enhanced Infrastructure Financing District	Varies	Varies	High

Conduit Issuance

- **The City can also issue tax-exempt debt through various conduit financing authorities**
  - Examples include CSCDA and CMFA
- **Local governments can and typically do issue tax-exempt bonds on their own**
  - Governmental entities typically pursue conduit debt when participation in a pooled financing program offers a benefit, such as reduced issuance costs or favorable interest rates
  - One such program is a pooled financing program that enables local governments to leverage their State Motor Vehicle Fuel Tax (the “Gas Excise Tax”) to finance road improvement projects
- **Conduit issuers charge initial and ongoing fees**
  - Initial fee paid at issuance, typically based upon the size of the borrowing
  - Annual fees typically based on either the original or the outstanding par amount

Public Private Partnerships

- **Public-Private Partnerships (“P3s”) can be structured using various models that represent a range of public- and private-sector involvement and varying levels of public and private risk**
  - Basic characteristic is reliance on a private organization for a range of services which the private sector may do more cost effectively or with less risk to the public sector
  - Many P3 transactions entail a more limited private role (design-build only) but the relationships of the public and private parties can vary greatly
- **Unlike a public debt-funded projects, P3 projects may be funded through equity contributed by private partners**
  - Any debt issued to finance the project is often payable solely by the private partner
  - Private capital carries a higher cost of borrowing than tax-exempt financing
- **Whether a project is funded publicly or using a P3, payment for the project and any associated debt will ultimately come from public sources (e.g., taxes, assessments, user fees)**

Financing Options for Courthouse Square - COPs

- **A number of the financing options could be considered for the Courthouse Square project**
  - General Obligation bonds, COPs, CFDs, and EIFDs all are potentially applicable
  - Non-revenue generating nature of the project makes revenue bonds and private financing through a P3 structure a poor fit
- **COPs are the simplest to execute and the process is entirely within the City's control**
  - Tradeoff is their reliance on City's existing financial resources – the General Fund – to pay for the project
  - Takes 3-4 months to complete, requires approval from City Council and a financing authority
  - Requires unencumbered assets as valuable as the borrowed amount to serve as the subject of the lease
  - Assuming comparable essentiality of the leased asset(s), a COP financing for Courthouse Square expected to achieve the rating on the 2007 COPs (AA-/A1), resulting in a low borrowing cost
  - California Infrastructure and Economic Development Bank ("I-Bank") loan is a variation on a COP, but the I-Bank subsidizes the interest rates based on demographic characteristics (income, unemployment, etc.)

Financing Options for Courthouse Square – GO Bonds

- **GO Bond offers lowest borrowing cost but requires a 2/3 super-majority vote of the electorate**
  - Polling conducted to determine voter support
  - City Council must pass a resolution to place the measure on the ballot months before the election
  - If passed, financing process can then begin and lasts 3-4 months
  - Unlike COPs, GO bonds are repaid from taxes levied on all property within the City based on AV
  - Credit ratings on a GO bond are the highest, and the borrowing cost the lowest, of all financing options

Financing Options for Courthouse Square – CFDs

- **Formation of a CFD requires a 2/3 vote of property owners in the proposed District and enables the City to levy a tax to pay debt service on the project**
- **CFD boundaries can be drawn as desired – a District could encompass the entire City or any portion thereof**
  - Design of the special tax formula is also flexible: all properties can pay the same tax, different types of properties can pay different levels of tax, be exempted, etc.
- **Process to form a CFD is more complex and involves more steps than that to place a GO bond measure on the ballot**
  - Typically takes 3 to 4 months, including drafting of district boundary map and tax formula, election, public hearing, and other actions by the City Council
  - Once the District is formed, the process to issue the bonds generally takes about 2-3 more months
- **Depending on the nature of the District, CFD bonds can have varying credit quality and borrowing costs**
  - A citywide CFD would be highly rated and carry low borrowing cost
  - A district with high taxpayer concentration and low property value relative to the amount of the bonds would be unrated and carry a high borrowing cost

Financing Options for Courthouse Square – EIFDs

- **Enhanced Infrastructure Financing Districts are a new form of financing that have not yet been utilized since their authorization by SB628 in September 2014**
  - Courthouse Square may not be an eligible infrastructure project
- **An EIFD harnesses the property tax increment of affected taxing agencies (county and special districts, but not schools) that consent to pay for improvements**
  - Tax increment increases over time as the Assessed Value of property in the EIFD increases, so the ability to repay debt service in the near term is limited
  - Negotiation of agreements with other taxing entities would be challenging
- **City would have to prepare an Infrastructure Financing Plan detailing of the Courthouse Square project and any other improvements contemplated within the EIFD**
- **Creation of an EIFD requires that the Successor Agency has received a finding of completion from DOF and certain other dissolution-related actions**
- **Issuance of EIFD Bonds requires 55% approval by voters within the District**

Project Cost and Debt Service

- **The City has estimated the cost of the Courthouse Square project between $10 million and $17 million**

- **A borrowing to fund the cost of the project will be repaid over many years**

- **The borrowing rate and amortization depend on the financing technique used, but we conservatively assume a 30 year amortization with a borrowing rate of 5%**
  - A $10 million project generates debt service of approximately $20 million ($665,000 annually)
  - A $17 million project generates debt service of approximately $34 million ($1.12 million annually)

- **These estimates include fixed costs of issuance (such as bond counsel fees) and the per-bond cost of a bank or underwriter**

Next Steps

- Determine the size of the project – is it $10 million or $17 million
- With a goal of construction next season (late May to October) staff recommends Certificates of Participation
- Upon determination of the financing method, staff will return to Council for approval of the financing proposal and timing
- During the October to December timeframe, staff will conduct public outreach through the Downtown Subcommittee and at downtown events in concert with the Chamber of Commerce.

Questions / Comments