Attachment B

Introduced: 9/3/2021
Version: 1

Current Status: Agenda Ready
Matter Type: General Agenda Item

a. Receive a Status Report on the Board Referral 2020.12 “Consider funding options to increase the Pavement Condition Index of County roads to at least a “Fair” standard over the next ten years;
b. Consider adding the County Service Areas with activated services of road/street services into the plan; and
c. Provide appropriate direction to staff.

RECOMMENDATION:
It is recommended that the Capital Improvement Committee:
a. Receive a Status Report on the Board Referral 2020.12 “Consider funding options to increase the Pavement Condition Index of County roads to at least a “Fair” standard over the next ten years;
b. Consider adding the County Service Areas with activated services of road/street services into the plan; and
c. Provide appropriate direction to staff.

SUMMARY/DISCUSSION:
BOARD REFERRAL
The County Administrative Office (CAO) and the Public Works, Facilities, and Parks Department (PWFP) received Board Referral 2020.12 on March 3, 2020, to consider funding options to increase the Pavement Condition Index of County roads to at least a “Fair” standard over the next ten years. The Board Referral is attached as Attachment A. Upon receiving the Board Referral, staff began researching options and consulted with the County’s municipal advisor, KNN Public Finance. Staff began research of financing tools that the Board has mentioned in the past, starting with iBank, then the Total Road Improvement Program (TRIP), and lines of credit. These financing tools and their strengths/constraints are summarized later in this report. KNN Public Finance performed extensive research, and their summary is below.

Overview of Financing Options
KNN Public Finance evaluated potential financing options and security structures to leverage existing Road Fund revenues. The primary financing options available are:
1) revenue bonds;
2) certificates of participation (COPs)

The County could pursue one or both of these financing options.

The details and background are provided in Attachment B, prepared by KNN Public Finance. Please note that these structures use Measure X revenues and Maintenance of Effort (MOE, also known as the portion of Transient Occupancy Tax, provided to Road Fund), with the greatest lending capacities using the entire revenue stream of both sources as the pledge (payment to debt service). The COPs also require the County to identify an unencumbered asset with an insured asset value approximately equivalent to the par amount of the bonds as a pledge. The long-term debt capacity ranges from $87 million to $257 million. These projects do have a timeline associated. If the bonds are issued as tax-exempt then the proceeds of the bonds must be spent in 3 years. Thus, the strategy would be to issue bonds when the projects become “shovel ready". Further, you could issue bonds in multiple series over time rather than issuing upfront as a single series. This would help ensure that the bond proceeds are spent in a timely manner.

Please note that SB 1 revenue and Highway Users Tax Account (HUTA) revenue are not eligible for pledge purposes and could continue to be used for road and bridge purposes. State law prohibits the use of revenues generated from gas taxes to pay debt service on bonds without majority voter approval. Attachment B outlines other restrictions imposed on HUTA and SB 1 revenues. Hence, SB 1 and HUTA revenues could potentially amount to an additional $20 million annually to add to these lending combinations but could not be used as a security source or source of payment on bonds. It should also be noted that these two funding sources are used for funding ongoing maintenance services by Public Works crews and address other needs such as traffic engineering/safety improvements and bridge rehabilitation/repair needs.

In terms of other financing and funding options, the County could pursue other revenue measures such as tax initiatives (like Measure X) or voter-approved bonds; however, those require an affirmative 2/3-vote by voters. KNN Public Finance researched the maximum indebtedness obtainable that do not require another ballot initiative to be voted on by the voters. Further analysis could be conducted on potential revenue measures that would require voter approval.

Types of Financing Tools

iBank

The California Infrastructure & Economic Development Bank (IBank) is the state’s only general-purpose financing authority created to finance public infrastructure and private development.

- IBank has broad statutory authority to issue tax-exempt and taxable revenue bonds;
- The maximum allowable bond amount is $25 million for a single project or up to $50 million per entity;
- Pre-paying the loan would not be allowed until after the 13th year of the 30 year period;
- Projects must be completed within two years.

An issue is that iBank requires a specific list of projects to be completed in the two-year time period. It is an effective financing tool for an individual project but challenging to implement in the County Road network of approximately 1,260 miles of roads where priorities could change.

Total Road Improvement Program (TRIP)

Total Road Improvement Program (TRIP) allows counties to leverage a portion of their gas tax and/or local transportation sales tax (Measure X) to finance street and highway maintenance and reconstruction projects.

- Can leverage up to $65 million in funding based on the estimated annual revenue through

Measure X (30 years);
- The interest rate is extremely high;
- Very short timelines (milestones) to complete the projects;
- No option to pre-pay the loan;
- All of the funded projects would need to be packaged and would be subject to short timelines.

The discrete, focused nature of TRIP is similar to the constraints of iBank.

Lines of Credit
Staff contacted a private lending institution about lines of credit.
- Credit ranges in the low millions
- Good for a smaller, finite range of projects
- Flexibility with use

This may be an avenue for individual County Service Area (CSA) needs.

<u>Other Funding Options</u>
Grants that are offered from time-to-time are another funding source but are generally for individual projects and have a short timeframe to construct.

COUNTY SERVICE AREA (CSA) NEEDS
The County Road network includes local, primarily residential streets in CSAs, many of which are in poor condition. There are 37 CSAs, of which 8 have street maintenance as an activated service and intended to be funded by the CSA. However, these streets are also generally in poor condition because funding mechanisms for those CSAs have been inadequate or non-existent to support proper road maintenance. Historically, local streets have not been eligible for Federal and State grant funding, as these programs have targeted highways and major arterial roads. Therefore, funding for repair of local streets is limited to the sources noted in the Financing Section below. With road repair needs that exceed available funding, local streets with relatively low vehicle volumes typically become a lesser priority for funding than higher-volume arterial roads and highways. However, the need for repair of local streets in CSAs is great and will increase over time, therefore, staff recommends that the CIC consider adding CSA roads into the overall financing plan for improving the condition of County roads.

<u>OTHER AGENCY INVOLVEMENT</u>:
PWFP staff continues to coordinate with the County Administrative Office Budget & Analysis Division. This item is scheduled for the Board of Supervisors' consideration at its regularly scheduled meeting on September 28, 2021.
<u>FINANCING</u>:
Road Fund revenue varies depending on sales and gas tax revenues. The Road Fund is projected to receive $33.4 million in FY 2021-22:
- <u>Highway Users Tax Account (HUTA)</u>. Annual allocation based on maintained mileage, vehicle registration, population, amongst other factors. FY 2021-22 revenue allocation is

estimated at $11.43 million. There currently is no sunset date for these funds.

- SB 1 (the Road Maintenance and Rehabilitation Account, or RMRA). Annual allocation based similar to HUTA. FY 2021-22 revenue allocation is estimated at $8.83 million. There currently is no sunset date for these funds.
- Measure X. Annual allocation based on 50% population/50% lane miles. FY 2021-22 revenue allocation is estimated at $7.65 million. The tax sunsets in FY 2047.
- Transient Occupancy Tax (TOT). Board policy to allocate 25% of TOT for road maintenance that is part of the County's Maintenance of Effort (MOE) obligation through SB1 and Measure X. Additionally, TAMC amended the minimum MOE requirement to be the amount of local resources spent for the fiscal year calculated as the annual average of its expenditures from its general fund during the 2009-10, 2010-11, and 2011-12 fiscal years, but not less than what was expended in 2016-17 (when Measure X passed), as reported to the Controller pursuant to Streets and Highways Code section 2151. This baseline amount will be indexed annually to the Engineering News Record construction index. In FY2021-22, the revenue allocation is estimated at $5.49 million.

Additionally, there are potential grant opportunities and other funding avenues possible through the federal infrastructure bill. Because the bill's details have not been released to the public as of this report, staff will continue to research and explore these potential opportunities when they are released. Technology and construction methods are also evolving, so staff will look into more efficient methods that achieve the desired performance at a reduced cost to constituents.

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Reviewed by: Tom Bonigut, P.E., Interim Assistant Director of Public Works, Facilities and Parks
Approved by: Randell Ishii, MS, PE, TE, PTOE, Director of Public Works, Facilities and Parks

DocuSigned by:
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Attachments:
Attachment A - Board Referral 2020.12
Attachment B - Financial Analysis Memorandum prepared by KNN

Monterey County Board of Supervisors
Referral Submittal Form

Referral No. 2020.12
Assignment Date: 03/03/2020
(Completed by CAO's Office)

SUBMITTAL - Completed by referring Board office and returned to CAO no later than noon on Thursday prior to Board meeting:

Date: 3/2/2020	Submitted By: Supervisors John Phillips and Mary Adams	District #: 2 and 5
Referral Title: Consider funding options to increase the Pavement Condition Index of County roads to at least a "Fair" standard over the next ten years.		
Referral Purpose: Establish funding for a program to increase the condition of our county roads over the next ten years that will reduce long term capital expenses.		
Brief Referral Description: Even with the added funding received through Measures X and SB1, the 1250 miles of our county roads continue to degrade at an increasing rate such that the repairs that are made can't keep up with the pace of decay, and each year of maintenance deferral will ultimately cost the county more in future years. This referral requests the Budget Office to work with RMA on funding options to implement a program that will repair and replace roads at an accelerated level over a 10-year period, which would ultimately require less annual funding commitment in future years. Advanced funding and repairs will lower the long-term funding requirements for our roads. One option includes leveraging dedicated self-help road repair funding allocation such as TOT commitments, Measure X funds, and maintenance of efforts requirements to seek bonding which would fund improvements to improve the overall Pavement Condition Index (PCI) of county roads. In the past decade our county has made capital infrastructure improvements a priority evidenced by our new jail addition, new juvenile hall, East West building renovation, new Government Center, Schilling building acquisition and occupancy and other capital investments. Implementation of this referral would satisfy our necessary road funding levels over the next decade and make road quality a top priority countywide.		

Classification - Implication	**Mode of Response**
☐ Ministerial / Minor X Land Use Policy X Social Policy X Budget Policy ☐ Other: ______________________________	☐ Memo ☐ Board Report X Presentation **Requested Response Timeline** ☐ 2 weeks X 1 month ☐ 6 weeks ☐ Status reports until completed ☐ Other: _____________ ☐ Specific Date: _______

ASSIGNMENT – Provided by CAO at Board Meeting. Copied to Board Offices and Department Head(s) Completed by CAO's Office:

Department(s): CAO/RMA	Referral Lead: Ezequiel Vega/Carl Holm	Board Date: 03/03/2020

REASSIGNMENT – Provided by CAO. Copied to Board Offices and Department Head(s). Completed by CAO's Office:

Department(s):	Referral Lead:	Date:

ANALYSIS - Completed by Department and copied to Board Offices and CAO:

Department analysis of resources required/impact on existing department priorities to complete referral:	
Analysis Completed By:	**Department's Recommended Response Timeline**

____ Date: _______________	☐ By requested date ☐ 2 weeks ☐ 1 month ☐ 6 weeks ☐ 6 months ☐ 1 year ☐ Other/Specific Date: ______________

REFERRAL RESPONSE/COMPLETION - Provided by Department to Board Offices and CAO:

Referral Response Date:	Board Item No.:	Referrals List Deletion:

Note: Please cc Karina Bokanovich, Rocio Quezada and Maegan Ruiz-Ignacio on all CAO correspondence relating to referrals.

Date: July 20, 2021

To: Monterey County Department of Public Works, Facilities, and Parks
Randy Ishii, Director
Jessica Cordiero-Martinez, Finance Manager II
Shawne Ellerbee

Cc: Monterey County Administrative Office
Dewayne Woods, Assistant County Administrative Office
Juan Pablo Lopez, Principal Administrative Analyst

From: KNN Public Finance
David Leifer and Melissa Shick

Re: Road Fund: Road and Bridge Capital Improvement Needs
Financing Alternatives and Debt Capacity Analysis

Monterey County's Public Works, Facilities, and Parks Department (Public Works) provides transportation infrastructure needs and improvements countywide. The County's road and bridge network connects the cities within Monterey County to the Caltrans expressways and freeways, allowing commuters and tourists to travel to the Monterey Peninsula and agricultural products to access the broader markets.

As with other well-traveled, high-traffic regions across the state, the County's road conditions are declining and need to be rehabilitated. Public Works has received a pavement condition report suggesting various rehabilitation cost scenarios and associated road condition improvement results.

You have indicated that the Board desires to pursue road rehabilitation on an accelerated schedule, if feasible. Under this objective, staff of Public Works in partnership with the County Administrative Office, has asked KNN Public Finance (Municipal Advisor to the County) to evaluate the ability to advance road and bridge projects through bonding. The following memorandum and accompanying summary presentation discuss financing options for the County's road and bridge projects within the context of the Road Fund's existing financial framework and available revenue sources.

Background and Approach

Road Fund Financial Resources

The Road Fund is a special revenue fund established per State law to account for revenues that are legally restricted for County road and bridge construction and related maintenance projects. The Road Fund's primary funding sources for construction and maintenance projects include:

- Gas Taxes: State Highway User Tax Allocation (HUTA)
- Gas Taxes and Fees: Road Maintenance & Rehabilitation Account (RMRA)/(SB-1)
- Local Sales Taxes: Transportation Agency for Monterey County (TAMC) Measure X

The County's General Fund also transfers a portion of annual transient occupancy tax (TOT) revenues to the Road Fund. While TOT represents a meaningful portion of the Road Fund resources, this revenue source serves as the County's Maintenance of Effort (MOE) requirement for each of the above primary revenue sources – HUTA, SB-1, and Measure X.

To the right we summarize actual financial results of the Road Fund for the last three Fiscal Years. Measure X revenues are reported within the "Taxes" line item, HUTA and RMRA/SB-1 revenues are reported within the "Aid from other Governmental Agencies" line item, and TOT is reported within the "Transfers In" line item – each highlighted in the summary table.

	Actual FY 2018	Actual FY 2019	Actual FY 2020
Revenues			
Taxes	$6,647,661	$9,525,367	$7,284,754
Licenses, Permits, and Franchises	$168,873	$380,277	$623,020
Revenue from Use of Money and Property	($24,630)	$179,775	$400,666
Aid from other Governmental Agencies	$27,310,083	$23,796,359	$24,731,882
Charges for Services	$1,833,178	$1,064,534	$1,271,839
Miscellaneous Revenues	$57,801	$311,794	$403,097
Total Revenues	**$35,992,966**	**$35,258,106**	**$34,715,258**
Expenditures			
Public Ways and Facilities	$33,912,689	$33,279,939	$33,870,221
Total Expenditures	**$33,912,689**	**$33,279,939**	**$33,870,221**
Revenues Less Expenditures	**$2,080,277**	**$1,978,167**	**$845,037**
Other Financing Sources			
Transfers In (General Fund)	$10,738,857	$5,397,106	$6,275,833
Other	$41,499	$23,202	$6,300
Net Change in Fund Balance	**$12,860,633**	**$7,398,475**	**$7,127,170**
Beginning Fund Balance	**($2,707,005)**	**$10,153,628**	**$17,552,103**
Ending Fund Balance	**$10,153,628**	**$17,552,103**	**$24,679,273**

For Fiscal Year 2022, staff estimates these primary revenue sources to provide the following resources:

- HUTA: $11,433,663
- RMRA/SB-1: $8,828,207
- TAMC Measure X: $7,652,168
- General Fund Transfer of TOT: $5,486,766

Analysis Approach

KNN conducted a detailed review of the Road Fund's primary revenues through dialogue and background information from staff and study of audited financial results and budget data. Our review was primarily focused on the nature of the revenue source to determine:

1) Can the revenue source legally support a borrowing?
   - Pursuant to the California constitutional debt limit and statutory limitations.
2) What credit structures are available for a borrowing?
   - Special fund obligation in the form of a Revenue Bond obligation or Installment Sale Revenue Certificates of Participation
   - Contingent obligation in the form of a General Fund lease obligation or Certificates of Participation

In the discussion that follows we highlight our preliminary conclusions to these questions for each of the Road Fund's primary revenue sources. If the revenue source is determined to be legally available to support a borrowing, we then quantify estimated bonding proceeds that could be generated assuming Fiscal Year 2022 estimated revenues. While this approach is instructive as it provides an initial approximation of upfront resources that could be directed toward project delivery and the advancement of the County's road rehabilitation under an accelerated schedule, we note that this "maximum upfront proceeds" analysis would require shovel-ready projects if implemented today. Often, bonding for road projects is phased over multiple issuances to align with construction readiness and expenditure requirements for tax-exempt bonds.

Upon further exploration of the leveraging opportunities outlined below, KNN would expect to work with Public Works and CAO staff to develop a plan of finance based on actual project costs and construction schedules. Such approach would likely involve multiple bond series driven by the size and timing of specific road and bridge projects. We would therefore not necessarily expect that the County would leverage 100% of resources available for bonding as a single issuance but rather time its issuances more closely to expected project expenditure needs.

Additionally, it is assumed that any bond issuance would be financed with tax-exempt bond proceeds. This adds further consideration to the amount and timing of a bond offering for Road Fund projects. Specifically, the spend down of bond proceeds must meet IRS requirements and, broadly speaking, the County must reasonably expect to spend 85% of the proceeds of any issuance within 3 years.

Road Fund Revenues Available for Bonding

Gas Tax and Legal Constraints for Bonding

While HUTA and RMRA/SB-1 revenues represent the most significant portion of the Road Fund's revenue resources, these funding streams are the most restrictive with regard to bonding opportunities.

Legislative Framework. California law prohibits the use of revenues generated from gas taxes for the payment of debt service on bonds without majority voter approval.

- **Legislation restricting the use of HUTA revenues for bonding:**

STREETS AND HIGHWAYS CODE – SHC
DIVISION 3. APPORTIONMENT AND EXPENDITURE OF HIGHWAY FUNDS [2004.5 - 2704.78]
(Heading of Division 3 amended by Stats. 1953, Ch. 192.)
CHAPTER 3. Highway Users Tax Account [2100 - 2127]
(Heading of Chapter 3 amended by Stats. 2013, Ch. 359, Sec. 12.)

Section 2101.

Notwithstanding Section 13340 of the Government Code, all moneys in the Highway Users Tax Account in the Transportation Tax Fund and hereafter received in the account are appropriated for all of the following:

(a) The research, planning, construction, improvement, maintenance, and operation of public streets and highways, including their related public facilities for nonmotorized traffic, the mitigation of their environmental effects, the payment for property taken or damaged for those purposes, and the administrative costs necessarily incurred in the foregoing purposes. For purposes of this subdivision, "maintenance of public streets and highways" shall include maintenance or removal of cattle guards within the right-of-way of a county highway.

(b) The research and planning for exclusive public mass transit guideways, their related fixed facilities, the payment for property taken or damaged for those purposes, and the administrative costs necessarily incurred in the foregoing purposes.

(c) The construction and improvement of exclusive public mass transit guideways, including their related fixed facilities, the mitigation of their environmental effects, the payment for property taken or damaged for those purposes, the administrative costs necessarily incurred in the foregoing purposes, and the maintenance of the structures and the immediate right-of-way for the public mass transit guideways, but excluding the maintenance and operating costs for mass transit power systems and mass transit passenger facilities, vehicles, equipment, and services, in any area where the voters have approved a proposition pursuant to Section 4 of Article XIX of the California Constitution.

(d) The payment of principal and interest on voter-approved bonds issued for the purposes specified in subdivision (c).

(Amended by Stats. 2019, Ch. 636, Sec. 5. (AB 1810) Effective January 1, 2020.)

- **Legislation restricting the use of RMRA/SB-1 revenues for bonding:**

  Article XIX section 6 (b) of the California Constitution allows "[u]p to 25 percent of the revenues allocated to any city or county" from revenues imposed by the State on motor vehicles to be used "for the payment of principal and interest on voter-approved bonds issued by that city or county" for purposes specified in Article XIX section 2 of the California Constitution.

ARTICLE XIX MOTOR VEHICLE REVENUES [SECTION 1 - SEC. 10]
(Article 19 heading renumbered from Art. 26 on June 8, 1976, by Prop. 14. Res.Ch. 5, 1976.)

Section 2.
Revenues from taxes imposed by the State on motor vehicle fuels for use in motor vehicles upon public streets and highways, over and above the costs of collection and any refunds authorized by law, shall be deposited into the Highway Users Tax Account (Section 2100 of the Streets and Highways Code) or its successor, which is hereby declared to be a trust fund, and shall be allocated monthly in accordance with Section 4, and shall be used solely for the following purposes:

(a) The research, planning, construction, improvement, maintenance, and operation of public streets and highways (and their related public facilities for nonmotorized traffic), including the mitigation of their environmental effects, the payment for property taken or damaged for such purposes, and the administrative costs necessarily incurred in the foregoing purposes.

(b) The research, planning, construction, and improvement of exclusive public mass transit guideways (and their related fixed facilities), including the mitigation of their environmental effects, the payment for property taken or damaged for such purposes, the administrative costs necessarily incurred in the foregoing purposes, and the maintenance of the structures and the immediate right-of-way for the public mass transit guideways, but excluding the maintenance and operating costs for mass transit power systems and mass transit passenger facilities, vehicles, equipment, and services.

(Sec. 2 renumbered from Sec. 1 on Nov. 2, 2010, by Prop. 22. Initiative measure.)

While we believe the County would be better served seeking voter approval for a more effective and efficient revenue solution specific to its road rehabilitation projects, <u>**if**</u> Monterey desired and received the necessary voter approval to use gas tax revenues to make principal and interest payments on bonds the borrowing would remain restricted:

- HUTA revenues are limited by uses of proceeds – projects financed with bond proceeds must be for the purpose of mass transit. Under this criteria, Monterey road and bridge projects would not be an eligible use of bond proceeds generated by the voter-approved gas tax borrowing.
- RMRA/SB-1 Revenues are limited by percentage of revenues that could be applied to debt service on voter-approved bonds. Only 25% of total RMRA/SB-1 revenues could be allocated to debt service. Depending on structure of a borrowing, assuming Fiscal Year 2022 estimated RMRA/SB-1 revenues of $8.8M estimated bond proceeds could range from $22M - $45M.

Overall, revenues generated from the gas tax do not provide an ideal leveraging solution for the County. The upside of potential bond proceeds is not meaningful enough given the effort required to seek voter approval.

Possible Non-Voter Approval Solution. The RMRA/SB-1 revenue stream is comprised of both gas tax components and a Transportation Improvement Fee (TIF) generated from the Vehicle License Fee (VLF). Upon the enactment of SB-1 (and subsequent voter disapproval of its repeal), the public finance legal community pursued avenues to leverage the TIF. As this portion of the SB-1 revenue stream is not gas tax generated, the general belief of bond counsels that we surveyed is that the TIF component of SB-1 could potentially be leveraged. However, five sources of revenues comprise RMRA/SB-1 funding, which creates complexities for this potential approach in that it could be challenging for the County to secure a financing with one source of revenue that is deposited into a comingled fund with four other sources of funds (that are gas tax generated).

We are not aware of any local governments that have leveraged the TIF as a repayment source for bonds. However, in tandem with the County's bond counsel, we could further pursue and analyze this alternative, which would require staff to research the internal accounting of RMRA/SB-1 revenues and whether or the TIF component could be accounted for separately from total RMRA/SB-1 revenues.

TAMC Measure X Revenues and Bonding Opportunities

The Measure X sales tax revenues received by the County from TAMC provide a clearer path forward for leveraging opportunities. There are two ways in which a local agency could leverage TAMC Measure X revenues as we discuss below.

Installment Sale Revenue Certificates of Participation (COPs). As a starting point, we consider an approach that directly leverages the Measure X sales tax revenues allocated to the County. This approach relies solely on the availability of Measure X revenues to secure and repay the bonds and does not commit the County's General Fund or other sources of funds. Under this structure, the bonds would be an obligation of the Road Fund (special fund) and would be secured solely by the Measure X annual direct allocation to the County. Because TAMC may also issue bonds secured by the Measure X sales tax for regional purposes, the County's pledge of Measure X would have to be subordinate in payment priority to sales tax revenue bonds issued by the TAMC.

Under this approach, there are several bond structuring factors that determine the amount of proceeds available for projects. Again, assuming a simplistic single issuance approach maximizing total estimated Fiscal Year 2022 Measure X revenues of $7.65 million, we calculate total proceeds that could be available to the County while considering specific structuring features:

- Debt Service Coverage: Bonds are sized such that sales tax revenues exceed debt service to protect against fluctuations in revenues (i.e. $7.65 million of annual sales tax revenues and $5.10 million of debt service equates to 1.5x debt service coverage). Revenues not used for debt service in any given year could be available for pay-go, cash-funded projects. Additionally, as revenues grow over the term of the tax, there could be more bonding capacity for future leverage.

Example Debt Service Coverage		$ Amount
A	Measure X Revenues	$7,650,000
B	Debt Service	$5,100,000
C = A/B	**Debt Service Coverage Ratio**	**1.50x**
D = A-B	**Residual Measure X Revenues**	**$2,550,000**

- Time Remaining on Tax: The final term of the bonds should be structured consistent with the term of the Measure X tax – April 1, 2047. This finite term impacts total resources available to generate bond proceeds and repay debt service on outstanding bonds.

- Interest Rates at the Time of Issuance: Lower interest rates lead to lower debt service and therefore create greater bonding capacity. On the flip side, higher interest rates increase debt service obligations and result in lower bonding capacity. Therefore, in lower interest rate environments, such as the present, the County will benefit from greater bonding capacity.

- Other Structure Features: With the direct pledge of a revenue stream (which can experience volatility) rating agencies and municipal bond investors may require the establishment of a debt service reserve fund – sized equal to one annual debt service payment. This provides additional security that the bonds will be repaid when due even amid declining revenue scenarios.

Taking the above bond structuring factors into account, **we approximate "maximum upfront proceeds" to be $86.5 million under this approach**. After the repayment of debt service, the County would have approximately $2.55 million of annual residual revenues to contribute to pay-as-you-go rehabilitation projects.

Case Study: Installment Sale Revenue COPs and Measure X. The issuance of bonds under an Installment Sale Revenue Certificates of Participation structure to accelerate future Measure X sales taxes has been executed by the City of Salinas. In 2018, Salinas funded approximately $40 million of road projects by leveraging its share of Measure X sales tax revenues with sales tax revenues serving as the direct security and repayment source. Annual debt service requirements equate to $2.34 million through the term of the Measure X tax – April 1, 2047. Required debt service coverage of the borrowing is 1.50x maximum annual debt service. For more details, please find the final offering document at: https://emma.msrb.org/ES1177197-EP799552-EP1201054.pdf.

General Fund Lease Revenue Bonds/COPs. Rather than directly pledging the Measure X tax as a repayment source on a bonds, the County could indirectly use Measure X revenues to offset debt service on a General Fund COP issuance. The County has traditionally used this form of borrowing to finance other capital improvement projects of the County, including the Natividad Medical Center, Schilling Place, and the Jail Complex. Because the bonds would utilize the security of the County's General Fund, this approach would not require the legal covenants of a debt service coverage target or a debt service reserve fund. By eliminating these structure requirements, the County could significantly increase upfront bond proceeds; however, the General Fund ultimately would be obligated to make debt service payments even if sales tax revenue collections were insufficient to backfill fully. Further, as the County is familiar, a General Fund COP security requires the pledge of a

County asset. Thus, the County would need to identify an unencumbered asset with an insured asset value approximately equivalent to the par amount of the bonds.

Under a General Fund COP structure, **we approximate "maximum upfront proceeds" to be $143.6 million under this approach**. This assumes that the County sizes a borrowing such that annual debt service is approximately equivalent to the estimated Fiscal Year 2022 Measure X revenues of $7.65 million. The term of the borrowing would remain consistent with the term of the Measure X tax – April 1, 2047 – to ensure General Fund debt service does not extend beyond the annual receipt of sales tax revenues.

Case Study: General Fund COPs and Measure X. The issuance of bonds under a General Fund Certificates of Participation structure to accelerate future Measure X sales taxes has been executed by the City of Seaside. In 2018, Seaside funded approximately $11 million of road projects by pledging its City Hall, Fire Station, and Community Center. The City's share of Measure X sales tax revenues serves as an indirect offset to the General Fund debt service obligation. Annual debt service requirements equate to $640,000 through the term of the Measure X tax – April 1, 2047. For more details, please find the final offering document at: https://emma.msrb.org/ER1153664-ER902443-ER1302941.pdf.

Comparison of Measure X Bonding Alternatives. The issuance of Installment Sale Revenue COPs provides an approach that has the value of insulating the General Fud from the obligation to make debt service payments and thereby protect the General Fund's future debt capacity for other capital improvement projects of the County. However, the tradeoff is that the Installment Sale Revenue COP structure does not generate as much upfront bond proceeds as a General Fund COPs issuance would given its superior credit quality and the eliminated requirement of additional structuring features. Below we summarize the tradeoffs of each Measure X bonding approach.

	Installment Sale Revenue COP	General Fund COP
PRO	▪ Aligns debt obligation with associated revenues ▪ Protects General Fund ▪ No asset pledge	▪ High credit rating ▪ Established credit in the market ▪ Lower interest costs ▪ Higher amount of project proceeds
CON	▪ Likely lower rating for financing ▪ Not an established credit; inaugural offering ▪ More complex credit structure ▪ Higher interest costs ▪ Lower amount of project proceeds	▪ General Fund obligation ▪ Impact on General Fund debt burden and/or capacity ▪ Requires asset pledge

Potential Additional Bonding with Transient Occupancy Tax

Overview: Since leveraging a bulk of the Road Fund's primary revenue sources (HUTA and RMRA/SB-1) would be challenging, we have also explored the use of TOT transfer funds as an offset to debt service on a General Fund COP issuance. As with the Measure X alternative discussed above, the bonds would be sized such that the resulting debt service is approximately equal to the annual

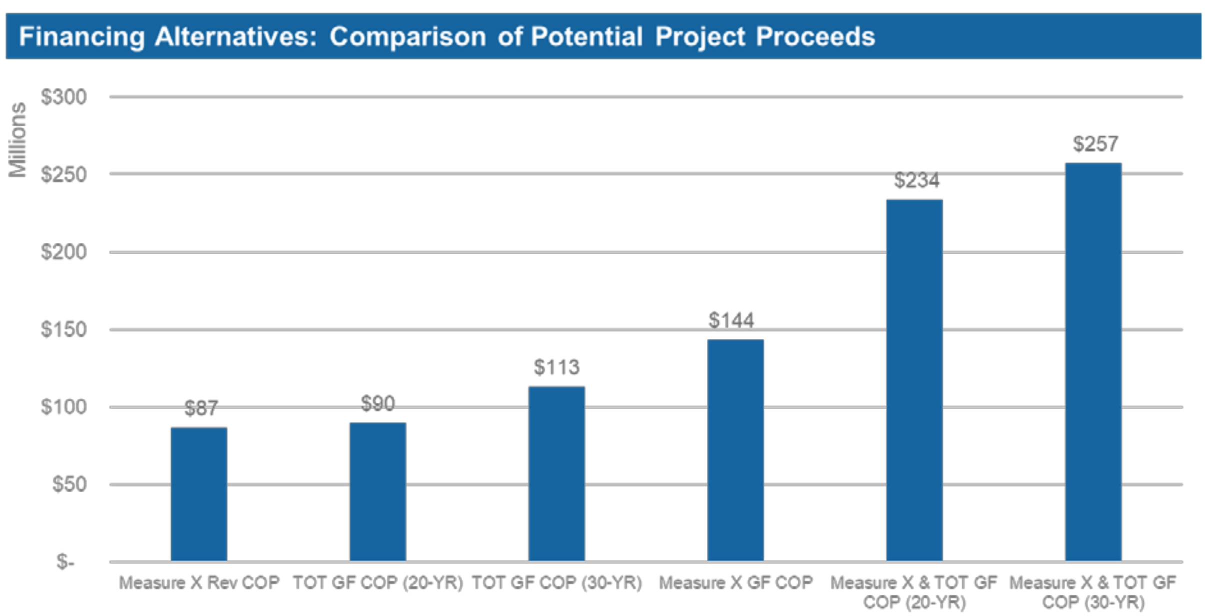
General Fund transfer of TOT to the Road Fund. Thus, the General Fund would absorb the cost of the debt service on a borrowing and the TOT that was otherwise transferred to the Road Fund would be used to offset debt service. An Installment Sale Revenue COP structure would not be feasible under this strategy as TOT is a general tax and does not carry the requisite voter-approval threshold to serve as a special tax revenue bond.

Under a General Fund COP structure, **we approximate "maximum upfront proceeds" to range from $90.0 million to $113.3 million under this approach**. This assumes that the County sizes a borrowing such that annual debt service is approximately equivalent to the estimated Fiscal Year 2022 TOT transfer revenues of $5.49 million. The proceeds range would be dependent on the term of the borrowing – the lower end equates to a 20-year borrowing and the higher end equates to a 30-year borrowing.

This approach should be noted as preliminary and subject to further consideration and analysis. The General Fund transfer of TOT to the Road Fund is used for MOE requirements for HUTA, SB1, and Measure X. Thus, the approval of the State Controller's Office and TAMC would be required to consider debt service as an allowable use of MOE funds. We would anticipate that the interest component of debt service would be problematic in meeting MOE requirements. KNN will continue to research and evaluate such approach with staff.

Summary and Conclusion

Subject to the political will to utilize the General Fund credit and available County assets to finance the Road Fund projects, the approach that produces the greatest amount of proceeds would be the General Fund COP approach. The chart below summarizes approximate bond proceeds that could be achieved through the alternatives discussed above, with the caveat that the TOT approach is still very much preliminary.



Overall, the clearest path forward is a borrowing approach that leverages the TAMC Measure X sales tax revenues – either directly as a revenue bond structure or indirectly as a General Fund COP structure. If the Road Fund had shovel ready projects, a borrowing under either of these approaches could be executed in approximately four months.

With direction from the Board and staff on borrowing preferences, the next step would be to develop a detailed plan of finance based on actual Road Fund project costs and anticipated construction schedules.

Finally, in closing, we note that the discussion and analyses provided herein focus on the Road Fund's current resources only; additional analyses could be prepared based on new revenue measures that require voter approval (i.e. sales taxes, property taxes; special taxes; special assessments). Again, with Board and staff direction, KNN could assist with the analysis of bonding capacity based on potential new, voter-approved revenue streams.

It has been a pleasure working with Public Works on this assignment. Should you have any questions or request additional information, please do not hesitate to contact David (dleifer@knninc.com) or Melissa (mshick@knninc.com).