County of Monterey

Item No.3

Board of Supervisors Chambers
168 W. Alisal St., 1st Floor
Salinas, CA 93901

Board Report

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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. Support implementation of a financing plan for the local road repair pilot program;
c. Approve the initial local road repair plan; and
d. Provide appropriate direction to staff.

RECOMMENDATION:
It is recommended 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. Support implementation of a financing plan for the local road repair pilot program;
c. Approve the initial local road repair plan; and
d. Provide appropriate direction to staff.

SUMMARY:
This report provides an update to the Capital Improvement Committee (CIC) on the status of the proposed local road repair pilot program and a financing plan for the proposed initial 10-year plan.

DISCUSSION:
Background
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. Upon receiving the Board Referral, staff began researching options and consulted with the County’s municipal advisor, KNN Public Finance (KNN), to identify funding/financing strategies within the context of the Road Fund existing revenue sources. Staff reviewed financing tools that the Board has mentioned in the past, starting with iBank, then the Total Road Improvement Program (TRIP), and lines of credit. KNN performed extensive research and analysis of potential financing options and security structures to leverage existing Road Fund revenues. Based on this collective research and evaluation, the primary financing options available are: 1) Revenue Bonds, non-General Fund backed; and 2) Certificates of Participation (COPs), General Fund backed.

At the September 13, 2021 CIC meeting, staff and KNN presented their findings and options to the CIC. The road financing evaluation concluded that the clearest path forward is a borrowing approach that leverages the Measure X transaction and use tax revenues, either directly as a revenue bond structure or indirectly as a General Fund COP structure. It was estimated that this approach could generate approximately $87 million to $257 million. This would be much less than the $600 million needed to increase Pavement Condition Index of County roads to at least a "Fair" standard over the next ten years. The CIC provided direction to staff to review and return with implementation strategies to gain a more comprehensive understanding of the internal County impacts of employing an augmented funding mechanism for the Road Fund, with the goal of commensurate increased delivery of road treatment projects.

At the November 8, 2021 CIC meeting, staff presented three implementation options consisting of: 1) increased County staffing levels; 2) increased use of contracted support (consultants and contractors); and 3) Design-Build contracting. Staff recommended a combination of the first two options, which would provide a measured approach for increasing staff levels while relying on consultant/contractor support as much as practicable to be able to make timely progress on delivery of an increased number of road improvement projects. The CIC concurred, and recommended staff to present this proposed program to the Budget Committee.

At the November 18, 2021 Budget Committee (BC), staff presented the financing options and the implementation plan. BC discussion included questions about staffing level, use of Road Fund balance, long term plan after the bond proceeds have been expended, financing approach, and additional potential funding sources. Key points from the discussion included the following:

- For Road Fund balance, follow the County's General Financial Policies which recommend major funds create reserves for operational contingencies equal to one percent (1%) of estimated annual revenue and a strategic reserve equal to ten percent (10%) of estimated annual revenue. This would result in maintaining at least a minimum of approximately $3 million in unprogrammed Road Fund balance to account for unanticipated events such as winter storm damage response and repair, fire response, other emergencies, etc.
- Staffing increase to implement the bond financed repair program and make greater use of existing Road Fund balance will be measured and modest, and also rely on increased consultant support (i.e., the "hybrid" approach discussed with the CIC).
- If a bond program is approved, then future Measure X revenues and Maintenance of Effort (the portion of Transient Occupancy Tax provided to Road Fund) would be programmed and used for the bond debt service, and thus no longer available for future road projects and services. That would leave the Gas Tax (Highway User Tax Account [HUTA]) and SB1 revenues as the only ongoing funding sources for future road repair and maintenance services (and possibly other Federal/State infrastructure allocations and/or grants which are not guaranteed).
- Bonds could be issued as multiple offerings over time to best match funding requirements with the delivery levels.
- Revenue bonds and certificates of participation (COPs) are the two viable financing vehicles to advance Road Fund capital projects. Revenue bonds could leverage 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 assets or other sources of funds. Or, Measure X funds could be used to offset debt service on a General Fund COP issuance. This approach requires the pledge of a County asset(s). Thus,

the County would need to identify an unencumbered asset(s) with an insured asset value approximately equivalent to the par amount of the bonds.

- There are potential grant opportunities and other funding avenues possible through the new Federal infrastructure bill, the "Bipartisan Infrastructure Law." Staff will continue to research and explore these potential opportunities when they are released.
- The BC supported pursuing a bond-funded program to repair local roads, using the "hybrid" model involving a measured increase in County staffing levels and increased reliance on consultant assistance.

Staff presented information discussed at the CIC and BC meetings to the Board of Supervisors at the February 8, 2022 meeting. The Board directed staff to pursue a hybrid implementation approach as was discussed with the CIC and BC. This hybrid approach would implement a pilot road repair program with a smaller bond amount on the lower end of the $87 to $267 million range discussed with the CIC and BC. The bond would be backed by existing Road Fund revenue sources, and the repair program would address County roads in Community Service Areas and small communities such as Aromas, Spreckels, San Ardo, and Bradley.

Proposed Financing Approach

Based on the prior analysis and feedback discussed above, County staff and its legal and financial advisors focused on two possible bond financing approaches, a Revenue Bond or General Fund COP, to leverage Measure X revenues to advance road repair projects under the pilot road repair program. One approach would use Measure X revenues as a budgetary offset to debt service on a General Fund Certificate of Participation (COP) issuance, and the other approach would use Measure X revenues as a pledge to a Revenue COP issuance. A General Fund COP issuance appears to be more favorable because the County's lease credit rating offers debt issuance advantages (e.g., lower interest rates), provides sufficient capacity to help fund the proposed local road repair program, and would only add a modest amount of General Fund obligations so that projected General Fund debt ratios are estimated to remain strong. Revenue COP present some legal limitations that may be challenging to overcome. To minimize the size of bond issuances to support this program, the approach includes maximizing use of available funding to help implement the program and then using bonds only to address future funding needs.

The County's Debt Management Policy requires that the County's Debt Advisory Committee (DAC) advise the CIC, BC and Board of Supervisors regarding any proposed debt issuances. Therefore, staff presented the proposed financing approach to the DAC on November 21, 2022. After discussion, the DAC concluded that if the County were to implement bond financing to support the local road program, the General Fund COP approach appeared to make more sense. That said, the DAC had the following concerns that should be considered and evaluated:

- Debt service difference between General Fund COP and Revenue bond.
- Asset capacity if the BOS wanted to bond for other major capital projects.
- Clarify and ensure that any bonds have terms not exceeding the Measure X sunset date, and that the road improvement useful life is 20 years or more.
- Recognize that the Measure X County allocation is set by ordinance (by TAMC) and could technically change in the future.

- Acknowledge concerns about future SB1/HUTA revenues/trends due to changes in fuel use.

The DAC also noted that staff should pursue releases of currently pledged assets to the extent allowable under existing debt issuances.

Following the DAC meeting summarized above, staff presented the proposed road repair plan and financing approach to the BC at its meeting of November 30, 2022. The BC did not make a recommendation, and instead offered the following key issues that the BC felt should be further considered:

- Ensure that this program focusing on local roads does not impact on going efforts to rehabilitate higher-volume County roads that serve as important agriculture and tourism links.
- Concern about funding road repair in those County Services Areas (CSAs) that are responsible for and should be funding road repairs, and desire to understand how much of this program is directed to these CSAs.
- Cost of the program, specifically, the high cost of debt service and suggestion to pursue local road repair to the extent existing revenue sources allow.
- Ability to deliver projects in a timely manner and provide adequate inspection and oversight given current staffing levels.
- Provide information on potential upcoming large projects that the County might issue bonds for and ensure that the proposed road bond program does not preclude the County's ability to pursue other large bond-financed projects.

The proposed financing approach relies on maximizing available Road Fund balance to fund local road repairs until Fiscal Year (FY) 2025, at which time a General Fund COP of approximately $43 million would be issued to continue funding the program, followed by another issuance of about $23 million in FY 2028. The estimated total debt service for these two issuances is about $109 million, with a total interest cost of $43.3 million. The alternative Revenue COP issuance is projected to cost the Road Fund about $4.9 million in higher interest costs. These are current preliminary estimates, which would be refined and further detailed at the time the BOS would be asked to approve the first debt issuance.

PWFP continues to work with the County Administrative Office on the financing plan to address the future costs of this plan. Alternatives to bond-issuance include borrowing from county funds and reducing the scope of the 10-year plan to allow the Road Fund to use ongoing revenues and fund balance to fund the projects.

A General Fund COP will require the County to pledge one or more assets to support the debt issuances. As discussed with the DAC, staff is pursuing releases of County assets that are currently pledged for prior bond issues to the extent allowable. Currently, there are assets with a value of at least $131 million that could be pledged for future General Fund COPs, plus numerous additional assets for which valuations could be developed if needed to support other large capital projects that the BOS might want to implement with debt financing. Staff is only aware of two potential future projects which include a possible downtown parking garage and a potential multi-use facility in the City of Seaside to support Social Services, Health and Library Departments.

Initial Road Repair Plan

PWFP engaged a consultant to help develop a proposed 10-year plan to show how and where bond financing proceeds would be applied to improve local County roads. Local roads in need of repair were selected in areas to make meaningful improvements to entire communities or neighborhoods and address needed deferred maintenance. The proposed plan assumed that approximately $100 million would be available over the 10-year period, which results in about 124 centerline miles of roads that would be improved. The plan is intended to be a living document that will be periodically updated, therefore, roads could be added or deleted depending on funding availability over the life of this program. The plan focuses on pavement repair and rehabilitation, and other road related repair needs such as drainage features, sidewalks, etc., will be addressed via other road maintenance funding programs. There are no County roads in District 1 (which is entirely comprised of the City of Salinas) and the relatively few County roads in District 4 are not local roads targeted under this program. Therefore, the road sections in this proposed program are contained only in Supervisorial Districts 2, 3, and 5.

Many of the targeted roads are in County Service Areas (CSAs) because these form distinct, residential neighborhood areas, and District 5 has many large CSAs. Therefore, District 5 has the highest percentage of roads targeted under this bond-financed program. Some CSAs include road maintenance services, and after the condition of those roads is improved by this program, those CSAs will be solely responsible for funding future road maintenance per discussion during prior meetings. Roads included in the program were grouped into neighborhoods, so that roads located in relatively close geographic proximity were included in the same neighborhood. This was done to complete repairs on selected roads in the same geographic area to avoid returning to the same area multiple times over the life of the program. This will create cost efficiencies as contractors working on this program can address multiple roads in the same area at the same time and minimize disruption to residents by impacting them with construction activity only once.

The proposed program will have a meaningful impact on the quality of roads, improving the condition of these local roads from an overall “Poor” condition rating to an overall “Very Good” condition. Without this program, these roads would continue to decline to a “Very Poor/Failed” condition. The table in Attachment A lists the neighborhoods selected for each year of the 10-year program, along with estimated cost. Maps depicting the roads included within each neighborhood and additional details on the proposed program are included in the report provided in Attachment B.

OTHER AGENCY INVOLVEMENT:

PWFP staff continues to coordinate with the County Administrative Office Budget & Analysis Division. The proposed bond-funded local road repair program has been discussed at the Capital Improvement Committee meetings of September 13, 2021 and November 8, 2021, the Budget Committee meeting of November 18, 2021 and the Board of Supervisors meeting of February 8, 2022. This most recent update was provided to the Debt Advisory Committee on November 21, 2022, where the expressed feedback and concerns. This was also presented to the Budget Committee at its November 30, 2022 meeting, where the members also provided feedback and concerns. Staff intends to bring this item to the Board on March 28, 2023.

FINANCING:

Public Works, Facilities, & Parks supports leveraging the Road Fund's Measure X transaction and use tax revenues to support either a General Fund COP or Revenue COP bond issuance to pay for the proposed local road and repair program. The General Fund COP is preferable to the Revenue COP, as the former would be secured by the General Fund which carries a higher credit rating resulting in reduced borrowing costs and interest rates. Issuing bonds, with the security of the County's General Fund, would also eliminate certain structural requirements, significantly increasing bond proceeds. Only the General Fund COP can meet the projected costs of the 10-year program. If a Revenue COP were chosen, additional financing options would need to be considered. Under both bond financing structures, Measure X revenues would be used to pay the annual debt service payment, which means there would be no impact to the General Fund revenues. The proposed bonding approach is structured so that the General Fund will not be impacted and a new tax on ratepayers will not be required. Based on feedback from the Budget Committee, the Public Works, Facilities & Parks and the County Administrative Office are reviewing alternatives.

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Attachments:

Attachment A - Initial Local Road Repair Program Summary Table

Attachment B - Initial Local Road Repair Program Complete Report