File Code No. 120.03

CITY OF SANTA BARBARA

FINANCE COMMITTEE AGENDA REPORT

AGENDA DATE: October 13, 2009

TO: Finance Committee

FROM: Administration Division, Finance Department

SUBJECT: Property Tax Securitization Program

RECOMMENDATION:

That the Finance Committee:

A. Hear a report from staff on the California Communities' Proposition 1A Securitization Program, which allows cities to receive upfront the property tax revenues being borrowed by the State of California in connection with the adoption of its Fiscal Year 2010 budget; and

B. Forward to City Council staff's recommendation to participate in the Securitization Program.

DISCUSSION:

On July 28, 2009, Governor Arnold Schwarzenegger signed the Fiscal Year 2010 California State budget, pursuant to which cities, counties, and special districts will be required to lend property tax revenues to the State. The amount being borrowed by the State is equal to 8% of the property taxes collected and allocated in Fiscal Year 2009. For the City of Santa Barbara, this amounts to an estimated $2.2 million. Repayment is due by the State in three years.

The borrowing by the State is authorized by Proposition 1A, a ballot measure approved by California voters in 2004. Proposition 1A amended the California Constitution and provided certain protections from State raids on local government revenues. It also provided that, in cases of fiscal emergencies as declared by the Governor and approved by 2/3's of the legislature, the State could "borrow" from local governments.

The State's budget bills included a provision allowing local governments to receive the monies being borrowed in advance through a securitization program. California Communities, a joint powers authority sponsored by the League of California Cities and California State Association of Counties is working to implement this program.

Some of the key features of the program include:

- Participating agencies will receive 100% of the amount of the property taxes being borrowed.

- California Communities will issue tax-exempt bonds and provide each local agency with the cash proceeds in two equal installments, on January 15, 2010 and May 3, 2010, coinciding with the dates that the State will be shifting property tax from local agencies.

- Participating local agencies will incur no costs of issuance and have no obligation on the bonds or credit exposure to the State.

Clean-up legislation is needed to implement the securitization program. Senate Bill 67, a clean-up bill recently failed; however, California Communities expects legislation to be approved prior to funding the program. However, if the clean-up legislation is not enacted in time, the program will collapse and all agencies will have to wait three years for repayment.

Local governments have the option of not participating in the securitization program offered by California Communities and thus simply waiting for the State to repay the loan. Some of the considerations for not participating in the securitization program include the impact on General Fund available reserves, the interest rate payable on the loan relative to the interest that would otherwise be earned by the City; and the risk of non-payment by the State.

Choosing to not participate in the securitization program would in fact reduce the amount of General Fund cash reserves available to respond to emergencies that may arise. However, cash reserves are available in other funds and, if necessary, could be used temporarily to respond to a natural disaster.

The loan would be repaid in approximately three years with interest calculated at 2% per year. By way of comparison, the interest rates on three-year investments typically purchased by the City currently range from approximately 1.5% to 1.7%. Therefore, the rate to be paid by the State is slightly better than what would be available in the current investment environment for the same term. However, it is likely that interest rates will increase over the next year, which would allow the City to invest the securitized funds at a higher rate if and when actually received.

Although the amounts borrowed by the State are legal obligations of the State and repayment is protected by the California Constitution, it is possible that the State may delay payment. There is still considerable uncertainty over the economy and the State has yet to completely address their budget shortfalls and structural imbalance.

Staff recommends participation in the securitization program primarily based on the fact that 100% of the funds will be received with no financial commitments or obligations associated with the bonds to be issued by California Communities. It also removes the risk of non-payment by the State.

On October 20, staff will be requesting that Council approve certain documents required for participation in the securitization in the program. These documents include the proposed Proposition 1A Receivables Sale Resolution, which essentially authorizes the sale of the City of Santa Barbara's Proposition 1A Receivable to California Communities for 100% of its receivable; and the Proposed Purchase and Sale Agreement, which spells out the terms and conditions for the sale of the Proposition 1A Receivable to California Communities.

SUBMITTED BY: Robert Samario, Interim Finance Director

APPROVED BY: City Administrator's Office