

## SAM - BUDGETING

### STATE PUBLIC WORKS BOARD (PWB) LEASE-REVENUE BOND PROGRAMS (New 5/1998)

6873

PWB is authorized to issue lease-revenue bonds to finance acquisition and construction projects when such projects are authorized by the Legislature.

In a typical project, the client department leases the site for a nominal fee to PWB, although for some projects the board may acquire the site directly. The client department then constructs the project as PWB's agent. The board leases the *completed facility* back to the client department for a rental fee equal to the amount needed to provide for the debt service on the revenue bonds and associated administrative expenses. Leases can be for periods up to 35 years, although 20 to 25 years is typical. The lease term cannot exceed the useful life of the capital asset.

Although there are limited exceptions, under federal tax laws arbitrage rebate penalties will be incurred or any arbitrage profits have to be rebated to the federal government if construction proceeds of revenue bond financing are not expended within two years. ("Arbitrage" refers to interest earnings on the investment of bond proceeds that result in a return in excess of borrowing costs.) To avoid this rebate, PWB may defer long-term bond sales and instead authorize loans from PMIA or the General Fund to cover interim financing needs, with a commitment to subsequently sell bonds (Section 6878). Long-term bonds are later sold in an amount sufficient to repay interim financing and to provide for the balance of construction costs, required debt service reserves, the capitalized interest account, and administrative expenses.

#### **PWB's lease-revenue programs:**

**Public Buildings Construction Fund.** Government Code Sections 15815 et seq. establish a financing program for the acquisition of sites and construction of public buildings. PWB issues lease-revenue bonds for acquisition of sites and construction of public buildings when such projects are specifically authorized by the Legislature. The fund contains a construction account for the project, and a revenue account from which principal and interest on the bonds are paid, and into which is deposited any revenue derived from the operation of the facility.

**New Prison Construction Revenue Fund.** Government Code Section [15819.3](#) authorizes PWB to finance prison facilities by the issuance of revenue bonds. Authorizations for specific prison projects have been enacted in legislation and codified in the Penal Code. These authorizations mirror those contained in the Government Code. Certain terms of the bonds must be reported to the appropriate legislative committees at least 20 days prior to bond sale (Government Code Section 15819.8).

**High Technology Educational and Research Facilities in Public Universities.** Government Code Section [15820](#) et seq. authorizes PWB to finance the construction or renovation, and the equipping of facilities for lease-purchase to the University of California, the California State University, and the California Community Colleges for educational and research purposes related to specific fields of high technology. This has been expanded to also be used for instructional or library purposes.

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**Energy and Water Conservation Revenue Bond Projects.** PWB may issue revenue bonds pursuant to Government Code Section 15814.15 to finance the cost of alternative energy equipment and for energy and water conservation measures in state public buildings, defined to include local school districts' (K-12) buildings. The total amount of revenue bonds authorized to be issued is \$500 million through January 1, 2000. The client department is responsible for payment of debt service on issued bonds under an energy service contract. Proposed energy service projects, agreements and leases must be reported to the appropriate legislative committees at least 30 days prior to PWB action. DGS implements this program on behalf of PWB.

#### Fiscal highlights:

1. PWB issues the bonds. The board adopts resolutions authorizing sales/interim financing and setting policy guidelines for the issuance, works with STO in preparing for the bond sale and sizing the bonds, executes sales documents, has responsibility for providing certain disclosure information on an initial and continuing basis, and periodically reviews balances in bond fund accounts to determine surplus status.
2. DOF has general powers of fiscal supervision pursuant to Government Code Section 13070, works with STO in preparing for the bond sale, may participate in rating agency meetings, prepares fund condition statements as required for the bond sale and for continuing disclosure, and evaluates (in conjunction with STO) the disposition of surplus bond funds, if any. In addition, DOF includes appropriations in the annual Budget Act for lease-revenue rental payments based on calculations of need provided by STO.
3. SCO and the State Auditor participate in the due diligence process and provide certain financial information necessary for General Fund disclosure.
4. The State Attorney General's Office also participates in the due diligence process and, together with bond counsel, provides a legal opinion required for the issuance of the bonds.
5. If the bond sale is for a DGS-managed project, DGS provides project time tables, makes recommendations to PWB/DOF on bond sizing, participates in due diligence meetings, and keeps PWB, DOF and STO informed of any events with material impact on project status or budget. If DGS manages the facility after construction, it is responsible for obtaining rental interruption, casualty (fire) and liability insurance. (Otherwise, the owning department is responsible for obtaining this insurance.)

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6. STO is the agent for sale and the trustee of PWB bonds, with all associated rights and responsibilities including appointment of the underwriting team, setting the bond sale date, organizing meetings and due diligence associated with the sale, securing ratings and bond insurance, and pricing. STO coordinates continuing disclosure for PWB issues. By policy, the board has delegated to STO the appointment of bond counsel and the selection of financial advisory services related to sales activities.
7. The client department has responsibilities as summarized in Section 6886.

Fiscal information generic to lease-revenue bonds is found in Section 6872. PWB oversight of lease-revenue projects is described in the portion of this chapter on project administration (Sections 6840–6869). Lease requirements for lease-revenue bonds are described in Section 6872 and in Section 6876 under the heading “financing leases.”