State of California
DEPARTMENT OF TRANSPORTATION

Business, Transportation and Housing Agency

Memorandum

To: CHAIR AND COMMISSIONERS

CTC Meeting: April 2-3, 2003

Reference No.: 4.5
Information Item

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Ref: **PROPOSED AMENDMENTS TO THE GRANT ANTICIPATION REVENUE VEHICLE (GARVEE) PROGRAM GUIDELINES**

SUMMARY

Chapter 783, Statutes of 1999 (SB 928), authorized the State of California to issue Grant Anticipation Revenue Vehicles (GARVEEs) to accelerate the funding of transportation projects. On November 2, 2000, the California Transportation Commission (Commission) adopted guidelines for the GARVEE Program.

Chapter 113, Statutes of 2001 (AB 438), and Chapter 438, Statutes of 2002 (AB 3026), expanded the types of projects eligible for GARVEE financing to include projects under the State Transportation Improvement Program, State Highway Operation and Protection Program, Toll Bridge Seismic Retrofit Program, and Traffic Congestion Relief Program.

The proposed amendments to the GARVEE guidelines are consistent with the above legislation and are presented here as an information item.

BACKGROUND

GARVEEs are tax-exempt debt instrument financing mechanisms that are backed by annual federal appropriations for federal-aid transportation projects. Proceeds of the financing can be used for the costs of right of way and/or construction of highway or other transportation projects that are eligible under Title 23 of the United States Code, and that meet all federal requirements. Additionally, projects must have environmental clearance and completed project design, be designated for GARVEE financing by the Commission, and eligible for advance construction using GARVEE financing through

the Federal Highway Administration. Because GARVEE financing relies on future federal-aid funding for debt repayment, the project is subject to federal match requirements.

Government Code Section 14553.2 specifies that the Commission, in cooperation with the California Department of Transportation and regional agencies, shall establish guidelines for eligibility for funding allocations under this chapter. The guidelines shall be nondiscriminatory and shall be designed to allow as many counties as possible to establish eligibility for funding allocations under this chapter, regardless of the population or geographic location of the county. The Regional Transportation Planning Agencies' GARVEE Task Force members have reviewed these guidelines and provided input into the proposed amendments.

Attachment

CALIFORNIA TRANSPORTATION COMMISSION
GRANT ANTICIPATION REVENUE VEHICLE (GARVEE) GUIDELINES

1. AUTHORITY AND PURPOSE

GARVEE bonds are tax-exempt debt instrument financing mechanisms backed by annual federal appropriations for federal-aid transportation projects. They were authorized in federal law by Section 311 of the National Highway System Designation Act of 1995, which amended Section 122 of Title 23 of the United States Code (the Federal Aid Highway Act) to expand the eligibility of bond and other debt instrument financing costs for federal-aid reimbursement. The definition of construction was revised in Title 23, Section 101, to include a reference to bond-related costs eligible for reimbursement, including principal and interest payments, issuance costs, insurance, if needed, and other costs incidental to financing.

At the state level, Chapter 862 of the Statutes of 1999 (SB 928) added Chapter 4 (commencing with Section 14550) to Title 2, Division 3, Part 5.3 of California's Government Code, authorizing the State Treasurer to issue Federal Highway Grant Anticipation Revenue Vehicles (GARVEE bonds) and authorizing the California Transportation Commission (the Commission) to select and designate projects to be funded for accelerated construction from bond proceeds that are approved by the Federal Highway Administration (FHWA) and the regional transportation planning agency.

Chapter 113, Statutes of 2001 (AB 438) and Chapter 438, Statutes of 2002 (AB 3026), amended the Code to expand the definition of projects eligible for GARVEE financing to include those listed in the State Highway Operation and Protection Program (SHOPP), Toll Bridge Seismic Retrofit Program (TBSRP), and Traffic Congestion Relief Program (TCRP), as well as Interregional Transportation Improvement Program (ITIP) projects in the State Transportation Improvement Program (STIP). Regional Transportation Improvement Program (RTIP) projects in the STIP were made eligible for GARVEE financing under SB 928. It is recognized that many STIP projects are jointly funded with both Regional Improvement Program and Interregional Improvement Program (IIP) funding. It should also be noted that the guidelines address only those projects included in the STIP or SHOPP, since TBSRP and TCRP projects must be included in either the STIP or SHOPP, as appropriate, in order to be eligible for GARVEE financing.

The intent of the Legislature in authorizing the use of GARVEE financing in California is to accelerate the funding and construction of critical transportation infrastructure projects in order to provide congestion relief benefits to the public significantly sooner than would be possible using traditional funding mechanisms. GARVEE financing of a project is appropriate only when the additional public benefits resulting from early construction exceed financing costs. Other considerations for the use of GARVEE financing include the availability of other funding mechanisms and whether GARVEE financing for a project would be the best commitment of future federal aid funds.

Legislation related to GARVEE bond issuance specifies that:

- the bonds shall not constitute a debt or liability of the state and bond repayments are to be made only from the funds and revenues pledged;

- funds allocated to a STIP project that utilizes GARVEE financing, including cost overruns and financing costs, shall be counted against the interregional share in the case of a project in the ITIP, and the county share for the county in which the project is located in the case of a project in the RTIP; and

- state transportation funds that are subject to the constraints of Section 1 or 2 of Article XIX of the California Constitution may be programmed in the STIP or SHOPP as the principal matching share for any project that is funded pursuant to this program.

Government Code Section 14553.2 specifies that the Commission, in cooperation with the California Department of Transportation (the Department) and regional agencies, "shall establish guidelines for eligibility for funding allocations under this chapter. The guidelines shall be nondiscriminatory and shall be designed to allow as many counties as possible to establish eligibility for funding allocations under this chapter, regardless of the population or geographic location of the county."

The Commission intends to re-evaluate these adopted guidelines and criteria for approving GARVEE financing at such time as one-half of the statutorily-allowable federal apportionment (15%) has been allocated to annual GARVEE debt service, or within twenty-four months of the first debt issuance, whichever occurs first. The guidelines will be further evaluated every two years thereafter, consistent with the timing of the Department's biennial Fund Estimate.

2. PROJECT ELIGIBILITY

The Commission will consider GARVEE bond financing only for right of way and/or construction costs of highway or other transportation projects that meet the following eligibility requirements. The projects must:

- be eligible under Title 23 of the United States Code (USC) and all other federal law pertaining to federal transportation funds apportioned to the state;

- comply with state laws, as well as any guidelines related to the STIP or SHOPP;

- have environmental clearance and completed project design prior to allocation;

- be eligible for advance construction using GARVEE financing by the FHWA;

- meet all federal requirements, including compliance with the National Environmental Policy Act (NEPA) for preliminary engineering, right of way, and construction activities; and

- have sufficient non-federal matching funds available. Unless otherwise exempted, the matching funds must be expended for costs incurred outside of the debt service payment, and after approval of federal aid for the project by the FHWA has been obtained. The costs of financing, including interest and issuance costs, must be included in determining the amount of the required match.

3. PROGRAMMING OF STIP OR SHOPP PROJECTS FOR GARVEE FINANCING

The Commission's designation of projects for accelerated construction with GARVEE bond financing will be through programming in the STIP or SHOPP. Except as otherwise provided in these guidelines, the Commission will program and allocate GARVEE bond financing for STIP projects in accordance with the Commission's STIP Guidelines. The Department will recommend the rejection of projects proposed for GARVEE financing that do not meet eligibility requirements or that are not financially feasible.

GARVEE bond project programming will be accomplished in the same manner as it is for other projects programmed in the STIP or SHOPP. The programming of the project will establish the term over which the bonds are to be repaid and will include an estimate of the annual debt service. GARVEE bond financing relies on future federal-aid funding for debt repayment, and is, therefore, subject to federal match requirements. Project proposals for GARVEE bond financing will specify the source of match, which may be from current STIP or SHOPP programming as appropriate to the type of project (subject to limitations on state-only funding), or from any other non-federal sources. Additionally, the federal government does not permit tapered match on debt-related reimbursements; therefore, this type of match cannot be utilized in conjunction with any GARVEE financing. However, other flexible matches, including donations, value of publicly-owned right of way, and toll credits, if available, might be applicable.

Metropolitan Planning Organizations (MPOs) may start the federal programming process for their GARVEE-financed project(s) prior to Commission approval of the GARVEE financing. However, the MPOs are cautioned that the FHWA and/or the Federal Transit Administration may not approve inclusion of the project(s) in the FSTIP until after Commission approval of the GARVEE financing and programming of the project(s) in the appropriate state document. In contrast to GARVEE programming in the STIP or SHOPP, which is based on the annual amount of debt service over the term of the bond repayment, the FSTIP will reflect the total amount of funds needed to be authorized for the right of way and construction components of the project in the federal fiscal year(s) wherein the authorization would be sought, as well as the annual debt service payments. The debt service payments must be programmed separately in the FTIP, with the project description clearly identifying that the programming is for the debt service payment. The description must also identify the GARVEE-financed capital improvement for which the debt service is being programmed. Until bond repayment is complete, the MPOs must address the apportionments set aside for the debt service in their Financial Plan.

The STIP guidelines specify that the Commission shall approve or disapprove a region's RTIP in its entirety for inclusion in the STIP. However, if the Commission does not approve a GARVEE bond proposal that is part of an RTIP, any portion of the county share that is thereby left unprogrammed will be made available during the next county share period. This action will not require the rejection of the entire RTIP.

The Commission's approval of projects for accelerated construction with GARVEE bond proceeds is subject to the statewide GARVEE bonding capacity limit and the appropriateness of bonding. Project nominations (either at the time of STIP adoption or SHOPP approval or through subsequent related amendments) should include an explanation of the benefits derived

from GARVEE financing compared to the use of other possible funding that may be available for the project.

Statewide GARVEE Bonding Capacity and Other Program Limits - Government Code Sections 14553(b) and 14553.4 require the Commission and the State Treasurer to annually determine the statewide GARVEE bonding capacity limit (generally, annual bond repayments may not exceed 30% of annual federal transportation fund deposits in the State Highway Account). The Commission will not program or allocate GARVEE bond funding in excess of this limit, and the Treasurer is not permitted to issue bonds if this limit would be exceeded. Furthermore, the Commission will set an annual limit on the amount of obligation authority and related advance construction commitment that may be available for each fiscal year of programming. This limit will be incorporated into each biennial Fund Estimate prepared by the Department.

Projects financed with GARVEE bond proceeds are subject to the requirements of the STIP or SHOPP, as appropriate, including any prioritization requirements established for these programs. However, whenever the Commission determines that the sum of all GARVEE bond proposals received, or likely to be received, will exceed the greater of one-half of either the bonding capacity or annual obligation authority limits, the Commission will set priorities for the use of the remaining capacity. After prioritization, the Commission may decline to approve any or all new programming proposals or allocation requests for GARVEE bond financing. In addition, the Commission may also, in consultation with the applicant, regional agency, and the Department, reduce the amount of bonding or lengthen the term of bond repayment to be approved for a project. The term of any proposed financing may also be limited by the Commission to ensure the most efficient and effective use of state resources.

Appropriateness of Bonding - Before approving the allocation of GARVEE bond financing, the Commission, in cooperation with the Department and the Department of Finance, will consider and determine the appropriateness of GARVEE bonding for the project in comparison to other appropriate funding mechanisms including, but not limited to using a STIP advance, the State Highway Account Loan Program or other innovative financing mechanisms, or non-STIP funds. This consideration and determination will include, but not be limited to (1) the availability of various funding mechanisms, (2) the anticipated economic, safety, and other benefits of the project and its early construction, and (3) the anticipated useful life of the project.

4. DEBT SERVICE

All GARVEE bond-financed STIP project programming will be counted against respective county or interregional shares in the same manner as for other STIP projects, except that the programming will be for the debt service by fiscal year rather than for right of way or construction costs by fiscal year. SHOPP projects will also be programmed in the amount of annual debt service. The amount programmed will thus be spread over the period of debt service, normally well beyond the current STIP or SHOPP period. Debt service includes all costs and expenses incurred by the state (including the State Treasurer) for interest payments, the retirement of principal, the cost of issuing bonds, the cost of insurance for the bonds, if needed, and any other cost incidental to the sale of the bonds. In addition, the Department will charge a fee of 1/20 of 1% of the principal amount financed to recover administrative costs incurred in the course of issuing GARVEE bonds. This fee will be included in the debt service payment repaid

through federal STIP shares or SHOPP funding and will reimburse the Department for the costs of coordinating the work of the financial advisor, bond counsel and other members of the financing team, presentations to rating agencies, ongoing reporting requirements, and other related costs of financing.

Each STIP or SHOPP proposal for GARVEE bond financing will include the term and amount of annual debt service, as well as the amount of bond proceeds to be allocated. For future STIPs, until bond repayment is complete, the amount needed to meet the debt service in each fiscal year within those STIPs will be treated as already programmed in that fiscal year and deducted from the county or interregional share as appropriate, before such share is made available for other programming. Future SHOPPs will also reflect the amount of debt service committed to GARVEE financing in each fiscal year prior to programming any other projects. The initial estimates of debt service programmed by the Commission for the project will be adjusted by the Department for any revisions at the time of allocation, and ultimately, with actual debt service payments as structured in the financing by the Treasurer. The adjustments will be reflected in the county and/or interregional share or SHOPP programming, as appropriate. The Department will notify the Commission on a bi-annual basis of any adjustments made to the debt service programming.

As stated above, any state expense for debt service will be counted against the county or interregional share for STIP projects and the debt service will continue to be counted against the county share or IIP until the debt service is repaid in full. For SHOPP projects, the debt service will continue to be charged against the state's SHOPP allocation until repaid. If a STIP or SHOPP project is not advanced after GARVEE bonds have been issued, the debt service must still be repaid, and an early refunding of the bonds may be required under any call provisions incorporated into the bond indenture. If a determination is made that a project cannot be advanced, and bonds have not yet been issued, expenses incurred by the state relative to the financing of that project will be charged against STIP county or interregional shares or the SHOPP, as appropriate. Any payment due will be made through any available unprogrammed balance, or through an equivalent reduction in future county shares, until expenses have been paid in full.

5. ALLOCATION OF FUNDS

The Commission will consider allocating funds for a STIP or SHOPP project designated for GARVEE bond financing when it receives an allocation request and recommendation from the Department, consistent with:

- the STIP Guidelines or Government Code Section 14526.5 relative to SHOPP allocations,
- Section 14553.8 relative to the appropriate use of GARVEEs, and
- Section 14553.4 subject to the statewide bonding capacity referenced in Section 3.

The Commission's allocation of GARVEE bond financing for a project will approve a specific amount of bond proceeds to be applied to the project.

6. ISSUANCE OF GARVEE BONDS BY THE TREASURER

Pursuant to Government Code Section 14553.7, in order to provide security for repayment of the bonds, the Commission must adopt a resolution dedicating and pledging any future receipts of federal transportation funds received by the state to the payment of principal, interest and premium on the bonds, for as long as any debt remains outstanding.

The State Treasurer will issue GARVEE bonds in accordance with the provisions of Division 3, Part 5.3, Chapter 4, Article 4 (commencing with Section 14554) of the Government Code. Proceeds from the sale of bonds are deposited in the Transportation Financing Subaccount, a special trust fund in the State Highway Account. They are available for use as directed by the Commission and administered by the Department.

To the extent it is possible, the issuance of GARVEE debt will be scheduled to occur shortly after the acquisition of right of way or the award of the construction contract to ensure that sufficient resources will be available through GARVEE financing for the full amount of a project's funding shortfall. Under this process, bond proceeds may not be available for a few months following the acquisition of right of way or beginning of construction; therefore, the applicant will be required to provide other funds until the bond proceeds are available for reimbursement purposes.

7. PROJECT REIMBURSEMENTS

The Department will transmit funds on a reimbursement basis directly to the applicant after the bond proceeds are deposited in the Transportation Financing Subaccount and the applicant submits an invoice for an initial advance payment or a monthly invoice that demonstrates payment has been made.

8. PROJECT COST CHANGES

Certain project eligibility requirements, such as having environmental clearance and completed project design, are important elements in mitigating risk resulting from delays; however, it should be noted that delays in construction could potentially increase the cost of the project by the differential amount between the interest earned on the bond proceeds during this period and the amount of interest paid to the bondholders for use of the proceeds. Interest earned on the bond proceeds will be used to offset the cost of the project, including financing costs. Any additional costs incurred relative to the financing of the project under GARVEE programming will be counted against regional or interregional shares or SHOPP programming, as appropriate.

GARVEE bonds provide a fixed amount of funds for a given project. If the project costs increase above the amount of the bonds issued, it will be necessary to provide funds other than bond proceeds for the increase. These funds could be local funds, STIP and/or SHOPP funds. If the funds are proposed to be STIP or SHOPP funds, it will be necessary to have them approved by the Commission using a supplemental funds allocation. The supplemental funds allocation will count against the appropriate STIP regional share, interregional share and/or the SHOPP. In the event that the work is being funded with a combination of GARVEE and regular STIP or

SHOPP funds, Commission Resolution #G-02-12, "Delegation of Authority to Adjust Project Allocations and Modify Project Descriptions" (known as G-12 Authority), is limited to adjustments of the regular STIP or SHOPP funds. It is not possible to increase the amount of the GARVEE bond proceeds available through the financing after those bonds have been issued.

Projects financed under the GARVEE Program are subject to all federal tax laws governing the use of bond proceeds.