<u>Background Report</u>

Senate Transportation and Housing Committee

Informational Hearing

Build California Bonds and
Los Angeles METRO's 30/10 Initiative

July 8, 2011

10 a.m.

Metropolitan Water District

Headquarters' Building

700 N. Alameda Street

Los Angeles, California

Introduction

In April the Senate Transportation and Housing Committee heard SB 867 (Padilla), which authorizes an innovative debt financing mechanism for funding the construction of regional and local transportation projects. The committee held the bill pending holding an informational hearing in Los Angeles to examine the Los Angeles County Metropolitan Transportation Authority (METRO) transportation investment plans that the bill would aid in financing.

To learn about the implications of SB 867 for Los Angeles, witnesses will discuss the program that METRO intends to develop and the financing strategy proposed to fund the program. In addition, witnesses will explain the regional economic benefits of the investment program, the financing mechanism in SB 867, and the mechanics potential as a public finance tool. Finally, there will be witnesses who will discuss the impacts of the METRO program on the construction industry.

Los Angeles METRO's 30/10 Initiative

Typically, major urban transportation projects take up to thirty-years to complete. During the thirty-years, the project will go through various planning analyses, environmental reviews, and financing phases. In the interim, segments of the project may be opened for limited service providing some benefits, but the total project benefits are not realized until the full project is completely operational. The objective of the 30/10 Initiative is to compress that project development timeline so METRO may construct the twelve transit projects that constitutes it's high priority program in ten years. The key to this effort is a thirty-year local, voter-approved ½ percent sales tax referred to Measure R, which was approved by two-thirds of Los Angeles County voters in November 2008. Measure R is forecast to generate $40 billion over a thirty year period. Accelerating the construction program reduces the impact of inflation on the total cost of the program.

Key Regional Projects

Of the twelve transit projects in the 30/10 Initiative, two are essential for making the entire regional rail transit network operate as a system. The first is the Regional Connector, which is a 1.9-mile fully underground line that will close gaps in the existing light rail network by connecting Claremont, Pasadena, the Eastside, Long Beach, and western Los Angeles with the heavy rail lines that serve the Wilshire Corridor and Hollywood/North Hollywood. The Regional Connector will carry approximately 90,000 daily passengers. The cost of the Regional Connector is estimated to be $1.25 billion in 2009 dollars. Construction is expected to start in 2014 and be completed in 2019.

The second major regional project is the Westside Subway Extension. This will be a high-capacity, high-speed, subway linking such important destinations as downtown Los Angeles, the Miracle Mile, Beverly Hills, Century City, and Westwood, including the UCLA campus. This is a 9 mile extension from the current Wilshire/Western terminus to Westwood. The estimated cost of the project is $5.1 billion if it can be completed by 2022, which is the goal of the 30/10 Initiative. Under conventional project development practices this line will be completed in about 2040, and due to inflation its cost would be must higher. Ridership is estimated to be 50,000 daily boardings.

Funding Elements of the 30/10 Initiative

To date METRO has three primary funding components for the 30/10 Initiative. The first, of course, is the sales tax discussed above. The other two revenue components are federal initiatives: Transit Improvement Bonds (TIB) and Transportation Infrastructure Finance and Innovation Act (TIFIA) credit assistance.

METRO is proposing as a national debt financing program for accelerating transit investments of national significance. This concept proposes that the Secretary of the U.S. Department of Transportation authorize a state or local agency to issue bonds. The federal government would pay the interest on the bonds, and the issuer would be responsible for paying the principal from a dedicated revenue source such as Measure R. The federal government would be providing an interest subsidy. This is a new program that Congress must enact.

The second financing mechanism will require an amendment to the TIFIA law. TIFIA provides federal credit assistance in the form of direct loans, loan guarantees, and standby lines of credit to finance surface transportation projects of national and regional significance. TIFIA credit assistance provides improved access to capital markets, flexible repayment terms, and potentially more favorable interest rates than can be found in private capital markets for similar instruments. TIFIA can help advance qualified, large-scale projects that otherwise might be delayed or deferred because of size, complexity, or uncertainty over the timing of revenues. The existing TIFIA operates on a project by project basis. METRO is proposing that the federal government make an up-front commitment to a multi-project program, such as the twelve transit projects that comprise the 30/10 Initiative. METRO estimates that it requires a $2.3 billion federal TIFIA loan. This will require METRO to have a $200 million capital reserve and demonstrate that that the majority of non-federal funding is committed to the project and sufficient to repay the federal credit assistance.

SB 867—Build California Bonds

SB 867, sponsored by METRO, is essentially a proposal to create a state-local partnership program by allowing the Treasurer to issue tax credit bonds to fund the construction of local transportation projects. The bill authorizes the California Transportation Financing Authority in the Treasurer's office to issue up to $5 billion of thirty-year bonds for funding transportation projects. The bill allows a bond holder to claim annually a tax credit valued at five percent of the face value of the bond in lieu of an annual interest payment. The bill caps the total amount of annual tax credits at $250 million. The principal would be paid by a local agency, such as

METRO, for whom the Treasurer issues the bonds. (The Transportation and Housing Committee analysis of the bill is attached.)

The purpose of this bill is to add a state component to Metro's debt financing strategy. It allows a local transportation agency to accelerate the construction of projects. Usually, the cost of accelerating financing would be substantial to the agency; however, the tax credit bond removes the obligation to pay interest, thus reducing the cost of the bond to the local agency.

Benefits of the tax credit bonds

According to the Los Angeles Economic Development Corporation (LAEDC), the $12.6 billion 30/10 Initiative, which anticipates $10.8 billion in direct construction expenditures (the remaining $1.8 billion is for vehicle acquisition and right-of-way purchases) will generate $23.3 billion of regional economic output, 137,000 jobs, $8.7 billion of direct income to project workers, and federal, state, and local taxes of $962 million during the ten years of the program. These are important benefits which the 30/10 Initiative is trying to capture.

The summary of issues in this background report will be thoroughly discussed at the hearing.