Using General Obligation Debt to Finance Park and Recreation Public Improvements: the Case of San Jose, California

by
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Abstract

The purpose of this case study is two-fold. First, to provide an in-depth review of the General Obligation Bond issuance process adopted by the City of San Jose to issue the 2004 Series of the Parks and Recreation bonds. Second, to identify the lessons learned as a result of the bond issuance. The case study finds that these lessons include: 1) prepare detailed plans *prior* to the bond issuance; 2) be conservative in what you promise the residents; 3) anticipate changes in economic environment; 4) identify supplementary funding sources should the primary source not yield adequate funds; and 5) make sure that the jurisdiction is organizationally capable of handling the increased workload.

About the Author

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Table of Contents

Introduction

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The City of San Jose, California - heart of the world famous Silicon Valley - has grown significantly in the last five decades. The population has grown from 90,000 in 1950 to 920,000 in 2000 – more than a 10-fold increase! The city is projected to add 129,300 more people by the year 2020[1] - primarily through in-fill development and densification. Its land area during the same time period expanded from 17 square miles to 179 square miles – largely through annexation of surrounding agricultural land (San Jose 2004).

While the city has grown multiple times in size and population, its infrastructure and services have failed to keep pace. Parks, libraries, fire, police and transportation related departments, through their master or strategic plans and other needs assessment studies, have estimated their unfunded needs to be approximately $1.9 billion (City of San Jose 2000a).[2] San Jose is the single largest provider of housing in the region. However, the new residential development is unable to generate enough revenue to finance these needs. There are several reasons for the revenue shortfall. One, the ability of the local governments in California to raise property tax revenue is restricted by Proposition 13. Proposition 13 caps the property tax rate at 1% of the assessed value of all taxable property. Property is only assessed at the time of the sale or when major improvements are made to it. Hence if the property has not been recently sold or major improvements have not been made, a property may be assessed at substantially lower value than a comparable property that is recently sold or improved. Moreover, the annual increase in the property tax is capped at 2%. Second, while the City of San Jose has provided most of the housing, its neighboring cities have attracted most of the new jobs. Thus the City's sales tax revenue has not increased significantly. Third, federal and state funds for the construction of community facilities have become more limited. Fourth, the City's conveyance and construction taxes have proven insufficient. In this rather constrained fiscal scenario the City Council asked Del Borgsdorf, the City Manager, to examine the financing options before the city to cover the $2 billion funding shortfall.

[1] Source: Association of Bay Area Governments (ABAG)
[2] The following strategic or master plans were prepared - Parks and Community Facilities Strategic Plan, Library Branch Facilities Master Plan and Fire Strategic Plan. Need assessment studies were conducted for – traffic and street improvements; police facilities; cultural facilities capital rehabilitation; public safety driver training facility; and police and fire CAD system.

Financing Options

As per the direction of the Mayor and the City Council, a comprehensive report titled "Capital Facilities Financing Strategy" was prepared and provided to the Council on May 16, 2000. The report compiled a preliminary cost estimate of the capital facility needs for parks and recreational services, library facilities, fire protection services, police protection services, and traffic and street improvements. The total need amounted to $1.9 billion. Of this $1.156 billion were needed to provide parks and recreational facilities.

The report, among other things, presented four financing options - general obligation (G.O.) bonds, special tax bonds, special assessment bonds, and a community facilities district - that the city may use to meet its unfunded infrastructure and services needs. Each financing option's technical, financial, political and administrative feasibility is discussed below.[3] The analysis is followed by Table 1 that summarizes the financing options.

General Obligation (G.O.) Bonds

For the City of San Jose the advantages of financing long-term debt through G.O. bonds are: a) G.O. bonds do not require a reserve fund or funded interest (i.e. capitalized interest) during acquisition or construction of the project. This makes a G.O. bond smaller in size, and the debt lower, than any other long-term debt financing mechanism; b) as the bonds are backed by the full faith and credit of the city, the interest rate (coupon rate) payable on G.O. bonds is lower than on other kinds of municipal bonds; and c) the issuance of G.O. bonds will allow the city to take advantage of the significant increases in the property valuations in the redevelopment areas. The city of San Jose Redevelopment Agency is the largest redevelopment agency in California. Over decades, due to the efforts of the redevelopment agency and the normal economic growth, the property values within the redevelopment areas[4] have grown significantly. Properties were sold multiple times, thereby increasing their assessed value. The high assessed values will ensure that a small increase in property tax rate will yield funds sufficient to retire the G.O. bonds.

Challenges of issuing G.O. bonds are: a) the City has not issued G.O. bonds in last three decades and hence would need to learn the details of the bond issuance process; b) the issuance of G.O. bonds will create inequities among the property owners in the City. Long-term property owners will pay substantially lower taxes than the recent property-owners because, due to Proposition 13, the assessed value of property owned by the former would be substantially lower than the assessed value of a similar property owned by the latter; c) the issuance of G.O. bonds will require 2/3 voter approval which in a state that pioneered property tax revolt may not be easy; and d) the G.O. bonds will not fund any operations and maintenance needs.

[3] The analysis of the financing option is conducted as if done in the year 2000. The analysis is a combination of the views of the author and the "Capital Facilities Financing Strategy" Report.
[4] They cover over a quarter of the City's area.

Special Tax Bonds
Special Tax bonds can be financed through several means including a parcel tax, or increases to such General Fund taxes as the Transient Occupancy Tax (TOT)[5] and Utility Users Tax (UUT).[6]

The advantage of the parcel tax is that the actual amount levied is reflective of the benefit derived from the improvement or service. This is in contrast to the G.O. bond, where the assessed value of the property is the only measure of the amount of tax payable by a property owner. A possible barrier to using a parcel tax is the need to gain approval by two-thirds of the voters. Moreover, facilities like parks and libraries have a positive spill over effect. Hence it may be difficult to accurately put a monetary value on the benefit an individual parcel may derive from the provision of such facilities.

Use of other General Fund taxes has the advantage of restricted impact. For example, the Business Tax will only impact businesses, and the TOT will only impact visitors. However the UTT will impact all residents. Like the issuance of G.O. bonds and the imposition of a parcel tax, General Fund taxes also need 2/3 voter approval.

Special Assessment Bonds
Special assessments on the parcels within a special assessment district can finance special assessment bonds. The assessment per parcel must be directly related to the benefit the parcel derives from the public improvements.

Advantages of using special assessments are: a) the assessments will be in proportion to the benefit derived; and b) voter approval requires a simple majority of property owners based on the amount of assessment. However, special assessment financing is predominantly used in the case of new land development where allocation of benefit is relatively easy. A majority of the improvements in San Jose will be in the already developed areas of the city. Moreover, special assessment bonds have the same drawback as the parcel tax bonds when it come to financing facilities like parks and libraries that have a positive spill over effect.

Community Facility Districts
The City can create separate public agencies known as community facilities districts to finance certain public facilities and services. The public facilities must directly serve the district. The community facility district can levy a special tax to finance capital and operating costs. The tax should be based on the benefit derived by the parcels, or on the cost of making the facilities or services available, or on any other reasonable basis. The tax cannot be ad valorem or related to the value of the property. The challenges in using this financing mechanism are: a) it requires 2/3 voter approval; b) the methodology of levying the tax may be politically complicated; and c) several districts would need to be created - which may be organizationally and politically complicated.

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[5] Usually levied for occupying lodging in a hotel, motel, inn or tourist home.
[6] Can be levied on such utilities as electricity, gas, water, and telephone.

TABLE 1: FINANCING OPTIONS

Financing Options	General Obligation Bonds	Special Tax Bonds/ Lease Obligations	Special Assessment Bonds	Community Facilities District
Eligible Projects	Property Acquisition and Construction Improvements. No Maintenance or Equipment.	Property Acquisition and Construction Improvements and Equipment. No Maintenance.	Infrastructure Improvements Assignable to Particular Property Owners. Limited Equipment. No Maintenance.	Property Acquisition, Construction of Improvements, Equipment and Maintenance Within a Localized Area.
Revenue Source	Property Tax	Parcel Tax, TOT, Utility Tax, Construction Taxes	Special Assessment on Property	Special Tax
Voter Approval	2/3	2/3	Simple Majority of Property Owners Based on Amount of Assessment	2/3*

* Requires 2/3 of votes if there are more than 12 registered voters or 2/3 of property owners if there are less than 12 registered owners.
Source: Capital Facilities Financing Strategy. 2000. San Jose, CA: Office of City Manager.

The Council Opted for the Issuance of G.O. Bonds

After reviewing the available financing options, the City Council decided to use G.O. bonds to fund its infrastructure and service needs. Several factors helped the Council in making this decision. In the year 2000, the economy of Silicon Valley was at its peak. The City had a budget surplus and the residents were upbeat about the future. Year 2000 was arguably the best time for the city to seek voter approval for the issuance of G.O. bonds. A public opinion poll conducted by the San Jose Library Foundation showed that 71% of the voters would support a $185 million library bond measure. The poll also showed support for parks and recreational facilities, public transport, and public safety (Desmond 2006). It was opined that a G.O. bond measure that could “bundle” some of the unfunded needs from various master and strategic plans could present the first phase of a longer-term capital financing strategy (City of San Jose 2000a). On November 7, 2000 the voters authorized the issuance of $228 million Neighborhood Parks and Recreation and the $212 million Neighborhood Libraries G.O. bonds. On March 5, 2002, the voters authorized $159 million Neighborhood Security Act G.O. bonds to fund the capital improvement needs of the police and fire departments. Since then G.O. bonds have been issued four times – in 2001, 2002, 2004 and 2005. The 2001 Series totaled $71 million - $40 million for parks and $30 million for libraries. The 2002 Series totaled $116.09 million - $46.715 million for parks, $30 million for libraries, and $39.375 million for public safety. The 2004 series totaled $118.7 million - $46.0 million for parks, $58.3 million for libraries, and $14.4 million for public safety. The 2005 series totaled $46.3 million - $21.3 million for libraries, and $25.0 million for public safety

(Persselin 2006). Thus till date, bonds worth $132.715 million of the total authorized $228 million have been issued for parks. The projected tax burden of the Neighborhood Parks and Recreation Bond was $19.60 per $100,000 of assessed value (Borgsdorf 2000). Table 2 summarizes all the bond issuances up till now.

TABLE 2: TOTAL BOND ISSUANCES

Series	Parks	Libraries	Public Safety	Total
2001	$40 million	$31 million	-	$71 million
2002	$46.715 million	$30 million	$39.375 million	$116.09 million
2004	$46 million	$58.3 million	14.4 million	$118.7 million
2005	-	$21.3 million	$25 million	$46.3 million
Total	$132.715 million	$140.6 million	$78.775 million	$352.09 million

The rest of the paper focuses on the Neighborhood Parks and Recreation G.O. bonds, in short called the Parks bonds.

Neighborhood Parks and Recreation Bond Measure (Parks Bond Measure)

The Parks bond measure, in part, was a result of a year-long planning process that began in January 1999 when the city initiated an interdepartmental strategic planning process "to identify future needs for parks, community facilities, and recreation programs and neighborhood services" (City of San Jose 2000). The result of the strategic planning process is the *Greenprint* – a 20-year strategic plan for the provision of parks and other recreational services.

According to the *Greenprint*, a community needs assessment conducted during the first phase of the strategic planning process found that:[7]

- The population of the city doubled between 1970 and 1998 without a commensurate increase in parks, community facilities and programs.
- By the year 2010 the city will no longer have a White majority. It will be ethnically diverse with 39% Hispanic, 33% White and 24% Asian population. The parks and allied services would need to cater to this diverse population.
- In the next five years, the number of residents above the age of 40, and between 10 and 19 years will significantly increase. This would mean increased emphasis on the youth and elderly population in the provision of parks and recreational services.
- San Jose will continue to be a city of homeowners with only 1/3 renter population. This means that parks would continue to be important to building community in residential neighborhoods (City of San Jose 2000b).

A facility analysis conducted as part of the needs assessment study found that:

[7] The second phase was Strategy Development and the third, Action Plan Development.

a) The City of San Jose has the lowest acreage per 1000 population of the neighborhood/community parks compared to five West Coast cities similar to San Jose in population.[8] The park acreage is also substantially lower than the National Parks and Recreation Association standards. The facility analysis documents need for an additional 931 acres of neighborhood/community parks by the year 2020.
b) The City of San Jose currently provides 330 square feet of community facility space per 1000 population. This figure again was the lowest among the comparison cities.
c) The city owns 26 community centers of which 22 require modernization, renovation or replacement.
d) Additionally there is demand for –
    - more recreational facilities in city-wide/regional parks;
    - additional sports fields in the existing neighborhood and community parks;
    - more city-wide sports complexes,
    - gymnasiums in future community centers and youth centers,
    - renovation of existing restrooms and provision of additional restrooms,
    - skate parks for youth,
    - community gardens,
    - dog parks, and
    - expanding the trail system (City of San Jose 2000b)

The *Greenprint* identified a total need of approximately $1.2 billion to fund the City's parks and recreational needs for the next 20 years. The funding was grouped in three phases. $192 million of capital improvements were recommended during Phase I (2000-2005), $257 million during phase II (2005-2010), and $704 million during Phase III (2010-2020). Detailed breakdown of the funding need is provided in Table 3.

[8] The selected cities were Portland, Seattle, San Diego, Sacramento and Phoenix.

TABLE 3: STRATEGIC PLAN CAPITAL INVESTMENT BY FACILITY TYPE

Facility Type	Investment Phase 2000-2005	2005-2010	2010-2020	Total	%
Park Acquisition and Development	$13,060,000	$51,100,000	$459,280,000	$523,440,000	45.4%
Neighborhood Parks Improvements	$49,060,000	$14,240,000	$34,940,000	$98,240,000	8.5%
School Recreational Facility Improvements	$3,020,000	$16,700,000	$35,060,000	$54,780,000	4.7%
Sports Facility Improvements	$12,816,662	$6,150,000	$31,704,338	$50,671,000	4.4%
Regional Parks Improvements	$41,177,000	$25,997,000	$17,180,000	$84,354,000	7.3%
Community Gardens	$310,000	$450,000	$560,000	$1,320,000	0.1%
Trails Improvements	$9,870,000	$30,530,000	$28,300,000	$68,700,000	6.0%
Other Recreational Facility Improvements	$27,140,000	$12,850,000	$20,925,000	$60,915,000	5.3%
Community Centers Improvements	$35,590,000	$99,060,000	$76,580,000	$211,230,000	18.3%
TOTAL INVESTMENT REQUIRED	**$192,000,000**	**$257,100,000**	**$704,500,000**	**$1,153,700,000**	**100.0%**
% OF TOTAL	**17%**	**22%**	**61%**	**100%**	

Note: All cost estimates are in 2000 dollars.
Source: Chapter 7, Greenprint for Parks and Community Facilities and Programs: A Twenty-Year Strategic Plan. 2000. City of San Jose, CA.

In total, the *Greenprint* identified need for $450 million for capital improvements in Phase I and II (2000- 2010). The plan also identified the specific capital improvements needed during this time period.

The list of capital projects identified in the *Greenprint* was "pruned" by the Office of City Manager to come up with a shorter list of projects for G.O. bond funding. It is not clear what criteria were selected for project selection. However one of the major objectives of the pruning was the reduction in the 10-year capital cost of $450 million to an amount that could be financed through the G.O. Bonds. "The projects to be funded from the issuance of Parks bonds include:

- Renovation of 90 play areas
- Construction of 28 restrooms

- Construction of nine community centers and senior centers
- Construction of a lighted soccer complex
- Enhancements to Almaden Lake Park
- Enhancements to Emma Prusch Memorial Park
- Enhancements to Happy Hollow Park and Zoo and Kelley Park
- Enhancements to the Municipal Rose Gardens
- Development of five trail segments" (City of San Jose 2006)

The renovation of play areas and the construction/renovation of the restrooms would be part of the 73 neighborhood park projects. The nine community and senior centers would be provided by construction of multi-service centers. These community centers are – Almaden Joint Facility – Community Center/Library in Parma Park, Berryessa Community Center, Camden Multi-Service Center, Gardner Satellite Community Center, District 6 Community Center, Mayfair Community Center, Roosevelt Community Center, Solari Community Center, and Southside Community Center. The five trail projects include: Coyote Creek Trail – Los Lagos Golf Course to Kelley Park, Guadalupe River Trail – Highway 280 to Willow Park, Los Alamitos Creek Trail, Los Gatos Creek Trail – Lincoln Avenue to Auzerais Avenue, and San Tomas Aquino-Saratoga Creek Trail – Bollinger Avenue to Prospect Road. Appendix A provides a map of the City of San Jose's parks, recreational and neighborhood facilities.

The Issuance of Parks Bond

The entire process of issuance of Parks bond can be divided into three phases – the pre-origination, origination, and the post-origination phase.

Pre-Origination Phase

For the Parks bond measure the pre-origination phase included the above described strategic planning process, a city-wide election for voter approval of the bond measure, and the selection of projects to be funded through the bond proceeds. Apart from these activities, the pre-origination phase also included highly specific procedural steps required to get ready for issuance of the bonds. These steps, described in detail below, included ensuring that the all legal requirements were met, a financing team was put in place, and the method and process of bond sale were clearly laid out. This case study will focus on the 2004 Series of Parks G.O. bonds for describing the technical details of the bond issuance.[9] As mentioned earlier, the total bond issuance in the 2004 series was $118.7 million, including $40 million of Park bonds.

From the legal perspective there are a number of limitations on the issuance of G.O. bonds. These include the Internal Revenue Service (IRS) requirement that the bond issue

[9] The procedure adopted for the sale of other series (2001, 2002, 2003 and 2005) of G.O. Bonds was very similar. However, for simplicity the 2004 Series has been chosen for in-depth study.

have a reasonable expectation to expend the proceeds within three years. The IRS, through this limitation, seeks to minimize the tax revenue loss to the federal government and prevent issuance of bonds for arbitrage purposes. The three-year requirement also presents a cash flow and encumbrance requirement. The bond issuing jurisdiction should know how much money will be expended in the next three years and how much it wants to encumber. This is important as the City of San Jose will not enter into a contract with another party without making sure that it has the funds required to fulfill its contractual obligations. Hence the bond issue should be large enough to meet the encumbrance needs but not more than the three-year spending needs. The knowledge of expenditure and encumbrance needs helps size the bond (Persellin 2006).

Once the bond issuance received the City Council's approval, a financing team was put together. This team consisted of the bond counsel, financial advisor, and the disclosure counsel. Sidley Austin Brown & Wood LLP were the bond counsel as well as the disclosure counsel. RBC Dain Rauscher Inc of San Francisco, CA was the Financial Advisor. All these team members were paid on a contingent basis - that is, their payment was contingent upon the successful issuance of the bond. They were paid at the closing of the bond proceeds (Persselin 2006).

In order to make certain issuance-related decisions, the financing team discussed specifics of the bond issuance with the City. These decisions are discussed below.

<u>Form of Sale</u>

In general, bonds may be sold through competitive bidding or the negotiated sale (Elmer 2005). The factors influencing the form of sale include:

- The level of complexity of the bond financing
- Whether the issuer is well-known and its credit worthiness well-understood
- The size of the issuance

In the case of the 2004 series of G.O. bonds, the level of complexity was low, the issuer (City of San Jose) was well-known as it had issued several municipal bonds (primarily revenue bonds) in the recent past, and had a very high credit rating. The size of bond ($118.7 million) was typical of bonds of this nature. Hence a decision was made to use a competitive bidding method.

<u>Fiscal Agent (FA)</u>

The FA acts as a trustee and ensures that the bond holder receives debt service payments from the issuer in a timely manner. The FA also acts as the custodian of the bond funds. Thus separate sub-accounts – one for park projects and another for library projects – were created for the 2004 series of G.O. bonds.[10] The FA ensures that the bond issuer (in this case the City of San Jose) deposits funds into these accounts fifteen days before they are to be disbursed to the bond holders (Persselin 2006). Wells Fargo Bank, National Association was chosen as the FA.

[10] A Public Safety G.O. bond was not issued in 2004, hence a Public Safety sub-account was not created.

Bond Structure

Specific decisions regarding the amortization schedule, maturity structure, redemption provisions, and bond insurance were made. In general, three types of amortization schedules are commonly used – level debt service, increasing debt service, and decreasing debt service. Under the first type, the debt service, which is the sum of principal plus interest, remains constant throughout the term of the bond. Under the second type, the debt service increases over time, and in the third type the debt service decreases over time. The use of the second type of amortization schedule is used to stretch the repayment of bonds, however this entails payment of higher interest cost. The City of San Jose decided to go with the third type – the decreasing debt service. This meant that the city was willing to pay more interest early on and thus minimize the interest cost to the taxpayer. It was decided to issue the bonds as "serial bonds" in denominations of $5,000 with maturity dates from September 1, 2005 till September 1, 2025 and to retain the option to redeem bonds maturing on or after September 1, 2014. It was also decided that the City would not buy bond insurance and would leave it this up to the Underwriter (City of San Jose 2004).[11]

Origination Phase

This phase includes preparing bond documents like the Preliminary Official Statement (POS), obtaining credit ratings for the bond, inviting the bids, preparing the Notice of Sale (NOS), and conducting the actual sale of bonds.

The POS for the 2004 Series of G.O. bonds, among others, includes the following:

- Overview of the city along with detailed economic and financial information
- Sources of payment for bonds
- Method of offer and delivery of bonds
- Description of bonds
- Sources and uses of funds
- Constitutional and statutory provisions affecting city revenues and appropriations
- Bond credit rating (City of San Jose 2004)

Three credit rating agencies - Moody's Investors Services, Fitch IBCA, and Standard and Poor's - were invited to rate the bond issue. Moody's Investor Services gave the Bonds an "Aa1" rating, while both Standard & Poor's and Fitch IBCA gave it an "AA+" rating.

[11] The underwriter buys the debt from the issuer and resells it to investors. They act as a broker except that they actually buy the issue. If they are successful they hold the loan only for a very short time and sell it for more than they paid for it. The "underwriter's spread" consists of their management fee for helping to plan and structure the debt; the take-down, which is the sales commission to the individual sales staff; expenses and a fee for the underwriting risk. If the issue is strong and not unusual, sometimes the local government can pressure the underwriter to waive the risk fee. The underwriter can be an investment banker, a securities dealer, or a bank (Elmer 2005, p.15).

These ratings are just one below the highest rating given by all these credit rating agencies.[12] The analysis supporting each bond rating is described below.

<u>Moody's</u>

Moody's Investor Services, in its report, *High Profile New Issue,* published on June 25, 2004, examine several key financial indicators like direct debt burden as a percent of assessed value, overall debt burden as a percent of assessed value; and General Fund balance as a percent of revenue that affect its rating of the San Jose bond issue (see Table 4).

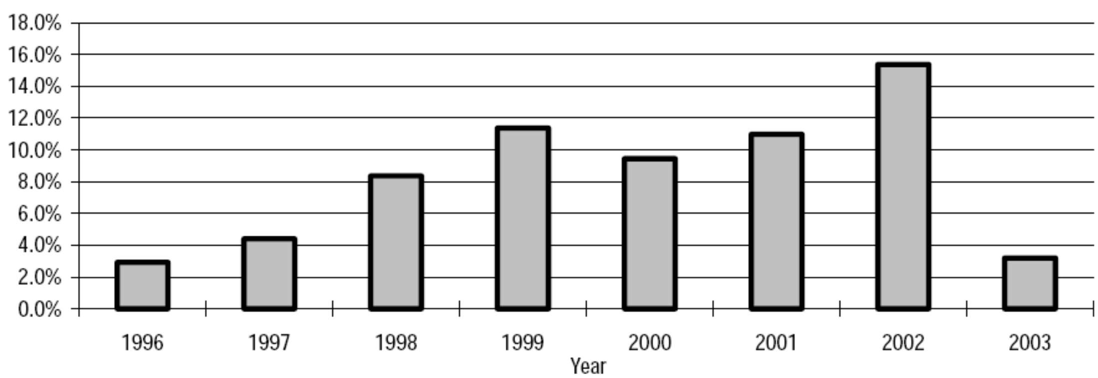
TABLE 4: KEY INDICATORS: CITY OF SAN JOSE, CA

	2000	2001	2002	2003
Population	894,943	903,800	916,500	919,600
Assessed value (000)	63,889,556	70,902,962	81,809,506	84,427,410
Net direct debt (000)	149,116	325,380	270,057	754,622
Overall net debt (000)	808,219	1,311,265	1,436,605	2,157,539
Direct debt burden (% of AV)	0.2%	0.5%	0.3%	0.9%
Overall debt burden (% of AV)	1.3%	1.8%	1.8%	2.6%
Gen. Fund bal. as % of revenue	30.1%	38.6%	43.4%	36.0%

Source: Moody's Investor Services Report titled "High Profile New Issue" published on June 25, 2004, p. 1.

The report notes the historically strong financial performance of the City, and manageable debt levels despite recent aggressive borrowing. However, the report raises several concerns. These include: a) decline in the City's General Fund reserves; b) budget shortfalls in fiscal years 2002 and 2003 that are also projected to continue in the near future; c) a lease burden higher than similar size California cities;[13] an uncertain short-term economic outlook; high unemployment rates (8.0% in March 2004); high office vacancy rates (approximately 20%); and slowing growth in assessed valuation (see Figure 1 below).

FIGURE 1: ANNUAL CHANGE IN ASSESSED VALUE



Source: Moody's Investor Services Report titled "High Profile New Issue" published June 25, 2004, p. 3.

[12] Moody's Investor Services' highest rating is "Aaa". Standard and Poor's and Fitch IBCA's highest rating is "AAA".

[13] Lease burden means the level of debt directly supported by operations. City of San Jose's net peak lease burden was 5.6% compared to 3.5% for large California cities (population greater than 250,000).

Fitch

Fitch IBCA, in their report, *Tax Support New Issue: City of San Jose, California*, published on June 22, 2004, also examine several key financial indicators like direct debt per capita, direct debt as a percent of assessed value, overall debt per capita, overall debt as a percent of assessed value; the General Fund balance as well as the unreserved General Fund balance as a percent of total expenditures, transfers and other uses (see Table 5 below).

TABLE 5: DEBT STATISTICS AND RATIOS: CITY OF SAN JOSE, CA

Debt Statistics ($000)	
This Issue	116,500
General Obligation Bonds	178,480
Lease Revenue Bonds	801,100
Total Direct Debt	1,096,080
Overlapping Debt*	3,537,660
Total Overall Debt	4,633,740
Debt Ratios	
Direct Debt Per Capita ($)**	1,183
As % of Assessed Value†	1.22
Overall Debt Per Capita ($)**	5,003
As % of Assessed Value†	5.16

*Includes approximately $1.9 billion of San Jose Redevelopment Agency debt. **Population: 926,200 (fiscal 2004 estimate). †Assessed value: $89,794,115,000 (2004).

Source: Fitch IBCA's Report titled "Tax Support New Issue: City of San Jose, California" published on June 22, 2004, p. 2.

The report commends the city on its sound financial management, and affordable, though higher than average, debt burden. The report however notes the operating general fund deficit, and expresses concern over the possibility of a similar deficit in the year 2005. It also notes the decline in the unreserved general fund balance (from $197.31 million in 2002 to $163.735 million in 2003).

Standard and Poor's

Like Fitch IBCA, Standard and Poor's, in its report, *Summary: San Jose, CA; Appropriation; Tax Secured General Obligation*, published on June 10, 2004, acknowledge the sound financial practices of the City - especially its ability to manage operating budget deficits. The report also recognizes that the City's central position in the Silicon Valley will help its economic recovery. It also notes the stability of the city's tax base. However the report raises several concerns. These include: a) a low economy that has not shown enough evidence of recovery; b) a high unemployment rate; and c) continuing budget deficits that threaten to erode financial reserves.

The final action of the origination phase was the actual sale of bonds through the competitive bidding process. An Official Notice of Sale (NOS) was prepared. The NOS gave the bidders until 9 a.m. on June 29, 2004 to submit bids. Upon evaluation of the received bids, the bonds were sold to Goldman, Sachs & Co., who served as underwriters for the bond issue (City of San Jose 2004).

Post-origination Phase

From legal and fiscal perspectives, the post-origination phase involved: a) transfer of bonds, through the FA, to Cede & Co. – a nominee of the Depository Trust Company, New York; and b) preparation of the Official Statement (OS). The OS is similar to the POS, except for the inclusion of sales results such as the interest rate, and the maturity schedule. The maturity schedule for the 2004 Series of G.O. bonds is shown in Table 6.

TABLE 6: MATURITY SCHEDULE OF 2004 SERIES G.O. BONDS

MATURITY SCHEDULE

Maturity (September 1)	Principal Amount	Coupon	Yield	CUSIP	Maturity (September 1)	Principal Amount	Coupon	Yield	CUSIP
2005	$3,955,000	4.000%	1.600%	798135UX5	2016	$3,960,000	4.250%	4.350%	798135VJ5
2006	3,955,000	4.000	2.060	798135UY3	2017	3,960,000	4.250	4.420	798135VK2
2007	3,955,000	4.000	2.400	798135UZ0	2018	3,960,000	5.000	4.550(1)	798135VL0
2008	3,955,000	4.000	2.800	798135VA4	2019	3,960,000	5.000	4.630(1)	798135VM8
2009	3,955,000	5.000	3.100	798135VB2	2020	3,960,000	5.000	4.710(1)	798135VN6
2010	3,955,000	5.000	3.300	798135VC0	2021	3,960,000	5.000	4.790(1)	798135VP1
2011	3,955,000	5.000	3.500	798135VD8	2022	3,960,000	5.000	4.870(1)	798135VQ9
2012	3,955,000	5.000	3.700	798135VE6	2023	3,960,000	5.000	4.940(1)	798135VR7
2013	3,955,000	5.000	3.875	798135VF3	2024	3,960,000	5.000	5.000	798135VS5
2014	3,955,000	4.000	4.050	798135VG1	2025	3,955,000	5.000	5.090	798135VT3
2015	3,960,000	4.125	4.250	798135VH9					

Source: Official Statement, General Obligation Bond Series 2004

Usage of Bond Proceeds

As indicated in the Table 2, $132.715 million worth of Parks bonds have been issued to date. They were issued as part of the Series 2001, 2002, and 2004 G.O. bonds. The city is using the bond proceeds to actively undertake several improvement projects. The city intends to complete all the projects in a 10-year period (2001-2010). “On April 10, 2001, the City Council designated the Parks and Recreation Commission as a Committee of the Whole (Committee) to conduct the citizen’s oversight review responsibilities associated with Measure P [Neighborhood Parks and Recreation Bond Measure]. … The Citizen Oversight Committee provides the public with opportunities to understand, review, and address any significant and relevant issues related to the implementation of the parks and recreation bond projects” (City of San Jose 2002). The Citizen Oversight Committee annually prepares a report to track the implementation of the Parks bonds measure and “informs the [City] Council and the public of the appropriateness of bond expenditures, the progress of the various projects, and the results of the annual audit” (City of San Jose 2003).

Status of Bond Projects

All the neighborhood parks projects are complete. These projects involved renovation of play areas, and/or construction/renovation of restrooms. Although minor, these are high-impact projects and have helped garner public and political support for the parks projects. Additionally, three of the nine community center projects are complete. These include Almaden Joint Facility – Community Center/Library in Parma Park, Berryessa Community Center, and Gardner Satellite Community Center. Enhancements to the Municipal Rose Garden have been made. However, several major projects like enhancements to four regional parks, development of five trail segments, and construction of two sports complex have either been delayed or rescheduled. The primary reasons for moving the larger projects towards the back-end of the 10-year period are identified below.

Lack of detailed project planning – The *Greenprint* does a good job of identifying the community needs. However, it does not include detailed project plans. Hence in many instances the City had to reduce the size of its proposed projects to keep them within budget. In other instances site selection, and/or acquisition has proven more difficult than anticipated.

City's Budgetary Situation – The Parks bond measure got voter approval in the year 2000 – a time of economic prosperity for the City. However, the ensuing five years have seen the dot com bust and economic recession affect the City's fiscal health. Since last four years, the City has been struggling to bridge its operating budget deficit. Hence the City has decided to "accelerate projects with minimal operations and maintenance costs and to defer those with additional significant operational and maintenance impacts" (City of San Jose 2003). The development of community centers and sports complex, and enhancements to regional parks have thus been delayed. As mentioned earlier, project details were not worked out prior to the issuance of bonds. Hence for several major projects, the magnitude of the operations and maintenance costs were not known.

Lessons Learned

During the interviews conducted as part of the research for this paper, the City officials identified several lessons, which they feel will: a) help them plan better in the future; and b) help other jurisdictions who may issue similar bonds in the future. The lessons include:

Prepare detailed plans – Development of detailed project plans would have helped the City to better estimate the projects' capital as well as the operations and maintenance needs. Furthermore, in the absence of detailed project designs, the City, in many instances, promised more than it could later deliver. For example, in a few cases the community centers had to be resized from 60,000 square feet to 40,000-20,000 square feet. The need for detailed plans is highlighted by the fact that the City, in the preceding several years, had not developed community centers or sports complexes of the size proposed in the bond measure and thus had no working model to assess the exact design, fiscal, staff, and other programmatic requirements to develop and maintain such facilities. The bond measure was driven primarily by the public officials. In the pre-origination phase it would have benefited from more extensive input from the City Departments, especially the PRNS, Public Works and the Planning Departments.

Be Conservative in what you promise – As mentioned above, in a few cases the City had to resize its projects, or postpone them. Hence to avoid disappointing the city residents it is advisable to be conservative in what you promise them.

Anticipate changes in economic environment – Between the approval of the Parks bond measure and present, the City's economic environment has dramatically changed. The City is experiencing operating budget deficits. The cost of construction has seen double digit increases. The escalation of construction costs has also led the City to revisit the scope and size of several projects. It is feared that as major capital projects (with their higher operations and maintenance costs) are deferred, it will get more difficult to develop them in the scope and size promised to the City residents.

Identify supplementary funding sources – It is advisable to identify other funding sources that can supplement existing funding sources in case of project cost escalation.

Make sure that the jurisdiction is organizationally capable of handling the extra work – The Parks bond measure significantly increased the workload of various City Departments. The work included development of detailed project plans, management of construction, and coordination among City departments like the PRNS, Public Works and Finance Departments. Hence it is important to ensure that the City is organizationally ready to absorb the increased workloads that such a bond measure can bring.

Conclusions

The City of San Jose's Parks bonds have been instrumental in addressing decades-long park infrastructure needs of the City (Mark 2006). They have provided the opportunity to undertake improvements that had been deferred for 30-50 years, to bring several existing facilities up to code, and to develop several new ones.

This case study first describes the circumstances that led the City of San Jose to investigate the different financing options to fund its $1.9 billion capital facilities needs. It then discusses the advantages and limitations of the four financing options – G.O. bonds, special tax bonds, special assessment bonds, and community facilities districts – considered by the City before deciding to use the G.O. bonds. Next, using the 2004 series of the Parks Bond Measure as an example, the case study describes the bond issuance process. Last, the case study identifies several lessons learned by the City as it developed the bond projects. While some of these lessons can help San Jose make mid-course corrections, all of them will be useful to San Jose or other jurisdictions planning a similar bond measure in the future.

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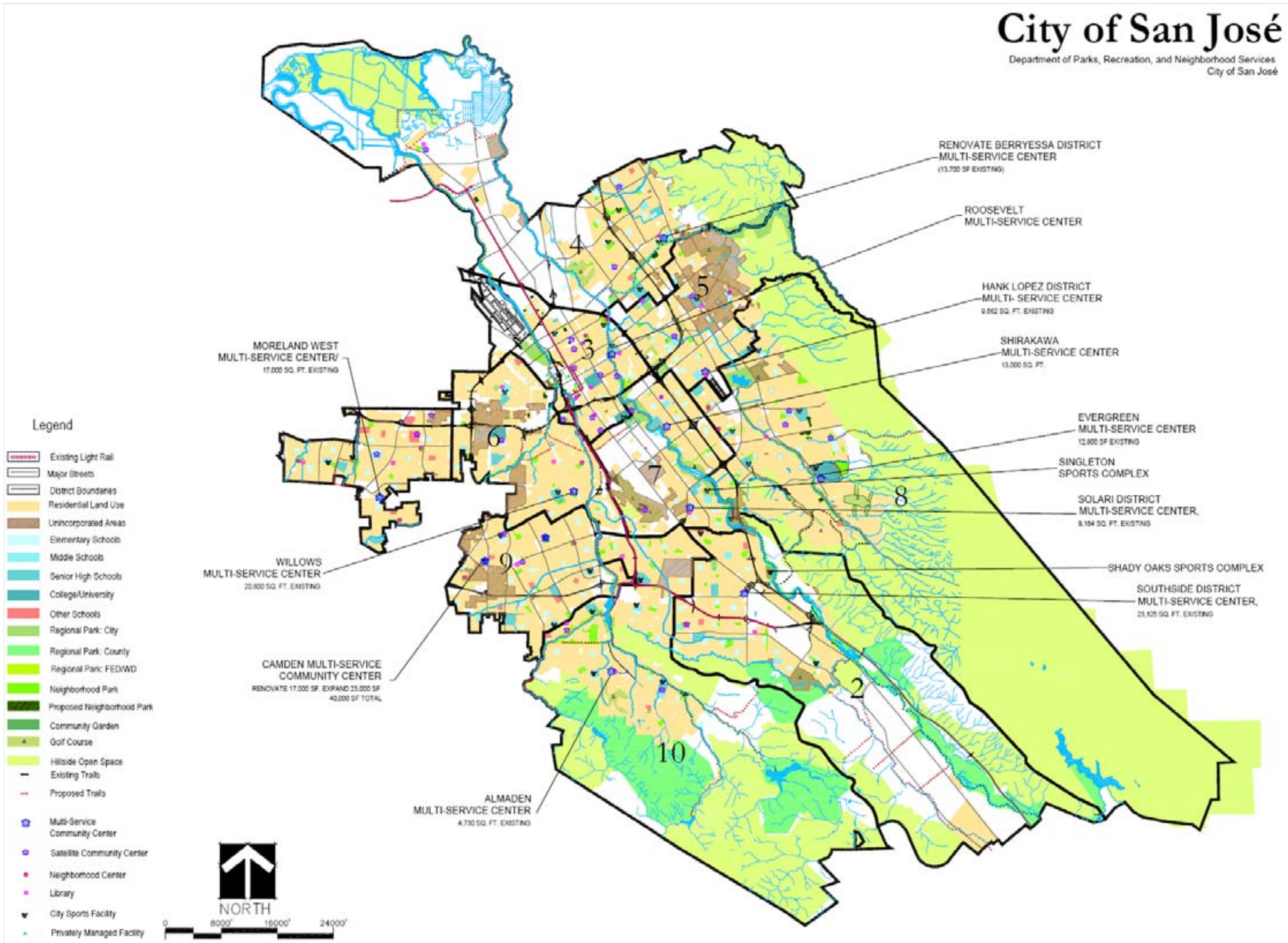
APPENDIX A: CITY OF SAN JOSE PROJECT MAP



Source: http://www.sanjoseca.gov/prns/Greenprint/Greenprint%20maps/dists17x22_7-00.PDF