



NOV 16 2009

Memorandum by City Manager's Office**TO:** HONORABLE MAYOR
AND CITY COUNCIL**FROM:** Debra Figone
City Manager**SUBJECT:** AGENCY PROPOSED BUDGET -
QUESTIONS ON 4TH & SAN
FERNANDO GARAGE DEBT**DATE:** 11-16-09

INFORMATION**Purpose of the Memorandum**

The purpose of this memorandum is to provide the background and context to fully respond to Mayor Reed's questions during the November 9th Study Session and Councilmember Liccardo and Pyle's November 12th memorandum regarding the Redevelopment Agency's current obligation to pay debt service on the "Bonds" issued to construct the 4th Street Parking Garage. The proposed Agency Budget impacts the Parking Fund in two ways. First, it recommends a second deferral of repayment of a \$6.8 million loan from the Parking Fund to the Redevelopment Agency originally approved in April 2005. Second, it recommends 2 ½ years of debt service (\$8.33 million) on the Bonds be paid from the Parking Fund.

The City Administration understands the difficult financial challenges facing the Agency and is prepared to work collaboratively to help resolve those challenges. However, the proposed request from the Agency should be structured along similar lines as previous requests for assistance from the Parking Fund – in the form of a loan. The primary rationale for this approach is to ensure that when parking development may be needed at a future date all City and Agency resources would not be depleted for that purpose.

Background of the Financing Structure for the 4th & San Fernando Garage

The City and Redevelopment Agency, with the Downtown Parking Board, have worked collaboratively over the years to provide safe, convenient, and accessible parking Downtown. The decision to use Redevelopment Agency funds to pay the debt for the 4th and San Fernando Garage had its origins back in 1998. At that time, the Executive Director proposed to the City Manager that the City establish a Free Parking Program during the evenings and weekends to encourage more activity in the Downtown. Recognizing the impact this would have on the Parking Fund's ability to finance parking facilities, the Redevelopment Agency planned to fund parking structures at 4th and San Fernando and Block 3 (San Fernando between 2nd and 3rd) to meet future parking needs. The City implemented a Free Parking Program in 1998; and the Redevelopment Agency commenced planning for both parking structures.

In 2000, under the direction of a new Executive Director, the Redevelopment Agency in collaboration with City staff, proposed a new financing structure to the Council/Agency

Board/City of San José Financing Authority Board for review and consideration. The Bonds were issued by the City of San José Financing Authority (the "Authority") in 2001. The Bonds' financing structure created a pledge of "Revenues" as the security for the Bonds. Revenues include the revenue of the parking system and Surplus Agency Revenues to cover the debt service on the Garage. Surplus Agency Revenues are the estimated amount of tax increment revenue remaining after the Agency makes payment on its senior obligations, and all other legally available revenues of the Agency. In practical terms, Surplus Agency Revenues are those revenues still available after senior tax increment debt obligations have been met, yet prior to meeting other junior debt obligations and the Agency Capital Program.

For the financing structure to be successful in achieving the desired rating and to attract a bond insurer, the Agency and the Authority entered into the Agency Pledge Agreement under which the Agency agreed to make payment of the Garage's debt service from Surplus Agency Revenues to the trustee for the Bonds. The City and the Authority entered into the City Pledge Agreement under which the City is obligated to pay debt service from parking system revenues to the extent that the Agency had not made payment of the debt service to the trustee. To the extent that the Agency has Surplus Agency Revenues, the Agency is obligated to make debt service payments on the Garage.

This financing structure allowed for the Bonds to be subordinate to the tax increment debt issued by the Agency allowing for greater flexibility in the use of tax increment revenue. As part of the financing structure, the Agency receives the benefit of the any net revenues from the Garage to partially offset the debt service payments. At the time the Bonds were sold, it was not expected that the Garage would generate sufficient revenue to cover the annual debt service until possibly 2015 to 2020, if ever. In fiscal year 2008-09, the Garage had revenues of \$706,000 and expenses of \$705,000, essentially operating on a break even basis.

Benefit of the Financing Structure to the Redevelopment Agency

Although the financing structure for the Garage used parking revenue bonds, it included two important features – an Agency payment and the system-wide parking revenue pledge – that made for a more secure structure than traditional parking revenue bonds that typically rely only on the revenues from the parking garage being financed. The benefit the Redevelopment Agency received from this financing structure is twofold. First, the Agency's financing capacity is less constrained than if the Garage had been funded with the proceeds of senior tax increment bonds, as is the traditional approach to funding public improvements in a redevelopment area. Second, the financing structure allowed for the Bonds to be a more highly rated and secure credit, resulting in lower total debt service costs; ultimately saving the Agency money compared to if the Garage had been financed with the proceeds from tax increment bonds.

The Agency is legally obligated through the Agency Parking Pledge Agreement to pay the \$3.4 million in annual debt service, less any net operating income from the Garage. The City has made a covenant to set rates and charges to cover both the debt service on the Garage, and necessary operating and maintenance costs of the Parking System. To the extent that Revenues, including Surplus Agency Revenues, are insufficient to make the debt service payments, the City Council will be obligated to raise parking rates. As it currently stands, due to its size, rate

structure, and the amount of revenue generated, the City's Parking System does not currently have the capacity to cover the debt service over the long term without the Agency payment.

Background on the Existing Loan from the Parking Fund

In 2005, when the Redevelopment Agency experienced reductions in its tax increment revenue, relief was requested from paying two years of debt service on the parking revenue bonds which would result in a savings to the Agency budget over two years of \$6.8 million. However, because this would result in a breach of the pledge of Agency Surplus Revenues as discussed above, the Agency instead made the required debt service payments and received a Loan from the Parking Fund to "ensure the continuity of Agency projects and essential redevelopment programs". The loan was originally scheduled for repayment in January of 2009. In 2007, the Redevelopment Agency requested deferral of the repayment of the loan until July 2012, including eliminating the accrual of interest if the loan was repaid by July 2012. The Agency requested the extended repayment schedule in part because of a settlement that required three annual payments of \$7.5 million to Santa Clara County, which concluded in July of 2009. The City agreed to the extended repayment schedule in June of 2007.

Conclusion

The proposed Agency Budget would completely eliminate any existing capacity to plan and prepare for future parking needs in the core of Downtown (e.g. 87 east to 4th Street), or in the emerging Diridon Station planning area in the short term. It would require the removal of all \$6.9 million from the Parking Capital Development Fund and \$1.43 million from fund balance, in order to have sufficient resources to cover the 2 ½ years of debt service the Agency is proposing be paid by the Parking Fund. By the end of the adopted CIP period (2013-14), the Parking Fund is projected to be near its minimum level of legally required and policy reserves.

The City Administration does however understand the difficult financial situation that the Agency finds itself in, and recognizes that parking development is neither needed, nor financially feasible in the core of Downtown for the foreseeable future. As a result, the Administration is willing to recommend the Agency's proposal in terms of the amount of relief requested under the conditions that the transaction is treated as a loan, with an agreed upon repayment schedule. This would return the Parking Fund to a financial position in which funding is available to assist in meeting future parking development and capital maintenance needs. Since 1998, building the capital reserves of the Parking Fund has been a priority, and as a result \$13.7 million has been accumulated over that time (\$6.9 million in the Parking Capital Development Fund and \$6.8 million loaned to the Agency). Furthermore, since the Agency is obligated to make the debt service payment as long as it has Surplus Agency Revenues, the loan structure such as that used in 2005, is necessary to avoid a breach of that debt covenant.

It is important to focus in on a particular short term implication of the Agency's proposed budget – that it provides no capacity or seed money in either the Agency or City Budget to respond to any parking planning needs in the Diridon/HP Pavilion area. As the Council is aware, the City has initiated the development of a Master Plan for the Diridon area, including a parking plan that will consider the parking needs of future land uses, and planned projects such as High Speed Rail

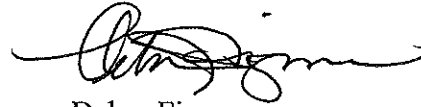
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and BART, as well as a potential future ballpark. From a timing standpoint, parking planning may need to be underway at some point in 2010. If the Agency Budget was approved as proposed, no funding would be available to support parking planning, environmental analysis or design work. Staff is in the process of determining cost estimates of these potential activities.



Debra Figone
City Manager

cc: Harry Mavrogenes
Downtown Parking Board

If you have questions please contact Julia Cooper, Assistant Finance Director at 535-7011 or Jim Ortbal, Assistant Transportation Director at 535-3845.