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MEMORANDUM

TO: Honorable Board of Supervisors
Jeffrey V. Smith, County Executive

FROM: James R. Williams, County Counsel JRW
Alan Minato, Director, Finance Agency AM

RE: Tax-Exempt Private Activity Bonds
Off-Agenda Response to Board Referral (August 13, 2019, Item 9)

DATE: October 3, 2019

INTRODUCTION

This off agenda report responds to requests made at the Board of Supervisors meeting of August 13, 2019 during consideration of Item 9 brought pursuant to the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA). TEFRA requires that the public approve the issuance of tax-exempt private activity bonds. The approval is typically provided in part by the approval of the governing body with jurisdiction over the area in which the bond-financed project will occur.

The specific requests made by the Board at the August 13, 2019 meeting pertained to (i) the range of projects eligible for financing in the form of tax-exempt private activity bonds that must be approved by the Board pursuant to TEFRA and (ii) the role of the County in the authorization process for the issuance of tax-exempt private activity bonds statewide.

DISCUSSION

Bonds are private activity bonds when a certain amount of the proceeds from the bonds are used for private business use or to make loans to nongovernmental persons. The interest income from these private activity bonds is typically taxable, meaning a higher yield may be required for buyers to invest in such bonds in lieu of tax-exempt bonds. However, the Internal Revenue Code provides that the interest income from certain types of private activity bonds may be tax-exempt if certain requirements are satisfied.[1] Private activity bonds that may qualify to be tax-exempt ("qualified private activity bonds") generally include:

- Bonds to finance the capital costs of exempt facilities, such as certain airport and transportation facilities; water, wastewater, and solid waste facilities; local energy facilities; qualified residential rental projects; and qualified public educational facilities;
- Bonds to finance residential mortgages for qualified borrowers;
- Small issue bonds used to finance manufacturing facilities and farm property;
- Bonds to finance student loans;
- Bonds to finance the redevelopment of blighted areas;
- Bonds to finance facilities owned by 501(c)(3) organizations; and
- Qualified current refunding bonds.[2]

The requirements that must be followed to ensure that interest on the income from qualified private activity bonds remains tax-exempt include, among others, statewide volume caps on the issuance of certain types of private activity bonds; bond form requirements; caps on the payment of issuance costs from proceeds; limitations on use of proceeds to qualified purposes and expenditures; restrictions on the investment of proceeds; and, maturity limitations. In addition, the private activity bonds, unless exempted, must comply with the requirements of TEFRA.

TEFRA provides that, prior to issuance, the sale of qualified private activity bonds must receive public approval, which can be provided by means of approval from the governmental unit issuing the bonds and from the governmental unit having jurisdiction over the area in which the bond-financed project is located.[3] In each case, approval occurs after a public hearing.[4] Under revised regulations adopted in 2018, if the project is located within an area under multiple overlapping jurisdictions, only one governmental unit needs to approve the issuance; however, if the project is an integrated operation involving non-proximate sites and spans across multiple non-overlapping jurisdictions, each separate portion of the project must be approved by the respective governmental unit with jurisdiction over such portion.[5] The new regulations also require notice of both the total maximum principal amount of bonds to be issued and, if there are multiple projects, the maximum principal amounts of bonds issued to finance each project.[6]

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[1] *See, e.g.*, 26 U.S.C. §§ 141-147.

[2] 26 U.S.C. §§ 142-45.

[3] 26 C.F.R. § 1.147(f)-1(b)(3).

[4] 26 U.S.C. § 147(f)(2)(B).

[5] 26 C.F.R. § 1.147(f)-1(b)(3).

[6] *Id.* § 1.147(f)-1(f)(2).

While TEFRA requires the County to conduct a public hearing and provide approval in order to provide the public an opportunity to approve or disapprove the bond issuance, the County incurs no financial liability from the approved financing, and neither the full faith and credit nor the taxing power of the County is pledged in any way in connection with the financing.[7]

The TEFRA hearing held on August 13, 2019, referenced a plan of finance involving the issuance of $300 million of qualified private activity bonds to be issued by a public entity and loaned to Waste Management, Inc. for purposes of solid waste projects throughout the state, including $26,000,000 in upgrades at two sites within Santa Clara County. Despite the reference to the $300 million plan of finance, the Board only approved the $26,000,000 in bonds to upgrade the two Santa Clara County sites; the other bonds were to be approved by the governing bodies with jurisdiction over the other projects. For future resolutions involving statewide plans of finance, County staff will work with bond counsel to better clarify the approval amount.

The issuer of the bonds approved on August 13, 2019 is the California Municipal Finance Authority (CMFA), a joint powers authority that issues qualified private activity bonds for the benefit of CMFA-qualified borrowers to support infrastructure; nonprofit health care, education, and cultural facilities; affordable housing; pollution control; and other projects throughout the state. CMFA also shares its issuance fees with the host community for each project and, for at least some transactions, donates a portion of its issuance fees to charitable organizations within the host community.

c: Miguel Márquez, Chief Operating Officer
Megan Doyle, Clerk of the Board

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[7] TEFRA is not intended to impose a pledge on the government entity providing approval of the bonds. The issuer or borrower is solely responsible for repayment of the bonds. The County typically makes this clear in public notices related to TEFRA hearings.