Case Study—Sacramento Regional Transit District $32.44 Million California Transit Finance Corporation Certificates of Participation, 1992 Series A

In the spring of 1992, the Sacramento Regional Transit District of Sacramento, California, participated in the sale of $32.44 million COPs to finance the acquisition of approximately 75 buses, a fare collection system, and a radio system. The COPs represented proportionate interests in the lease payments to be made by the District to the California Transit Finance Corporation (CTFC), a nonprofit corporation, for lease of the project. One of the sources of revenue supporting the District's lease payments is a FTA Section 9 capital grant.

The Parties

The **Sacramento Regional Transit District** is a legislatively created transit district that encompasses an area of 340 square miles, including the City of Sacramento and most of the urbanized area within Sacramento County. The City of Sacramento is the state capital of California located approximately 75 miles northeast of San Francisco. The County of Sacramento has a population of over 1 million, approximately one-third of which live within the City of Sacramento. The District operates a fleet of 200 buses and an 18.3-mile light rail line.

CTFC is a nonprofit public benefit corporation created in 1990 by the California Transit Association to provide financing assistance to California transit entities. CTFC provides transit agencies with standardized lease financing documents for stand-alone and pooled COPs supported in part by FTA Section 9 capital grants. The CTFC structure has been market tested by the major rating agencies as well as the public finance capital markets. Typically, CTFC transactions involve a preestablished financing team of financial advisors, bond counsel, underwriter, and underwriter's counsel. To date, CTFC has participated in at least six successful COP financings involving FTA Section 9 funds.

The Project

The project included three components: (1) Purchasing 75 heavy-duty transit buses, (2) Installing a fare collection system, and (3) Installing a new radio system. The buses are approximately 40 feet long by 102 inches wide, equipped with natural gas engines, air conditioning, and front and rear doors with a wheelchair lift at the front door. Delivery of the buses was anticipated to take place over a period of 16 to 22 months. Cost of the buses was estimated at $21.5 million, which included acquisition and delivery costs.

The new fare collection system was for the District's bus fleet (now 200 buses). The fare collection system consisted of 200 registering fare boxes plus cash boxes, five receiver vaults, and a data collection system to record cash received onboard the buses. The onboard registration feature aids the drivers in determining whether proper fare has been received and also provides information that can be used to reconcile and audit cash receipts. The cost was estimated at $2.0 million.

The radio system replaced an aging 14-year-old, three-channel system that was experiencing frequent breakdowns and gaps in geographical coverage. The new system was to be a six-channel “trunk” radio system providing the necessary flexibility for bus, rail, and paratransit services over the next 12 years. The equipment procured consisted of three base stations, 300 mobile units, and a number of hand-held portable radios. The cost was estimated at $4.0 million.

The Financing

As indicated in the Official Statement dated April 8, 1992, proceeds of the Certificates were allocated as follows:

Acquisition Fund (1)	$25,194,696
Lease Payment Fund (2)	3,231,382
Reserve Fund (3)	3,213,601
Financing Fee (4)	496,332
Original Issue Discount	303,989
Total Principal Amount of Certificates	$32,440,000

(1) Includes Delivery Costs.

(2) All of the interest accrued with respect to the Certificates from the date of execution and delivery of the Certificates through December 1, 1993, and a portion of the interest due on the Certificates from January 1, 1994 through April 1, 1994, was capitalized.

(3) Equal to 10% of principal amount of the Certificates, less original issue discount.

(4) Includes Underwriter’s discount and certain costs of issuance associated with the execution and delivery of the Certificates.

The Lease Payment Fund was funded with COP proceeds sufficient to make all lease payments due prior to the expected completion date of the project.

Each Certificate represents a proportionate interest in the lease payments to be made by the District to the Corporation under the financing lease. The Corporation, pursuant to an assignment agreement, assigned its rights and remedies under the Lease Agreement (except certain rights to indemnity and reimbursement of expenses) to the trustee bank for the benefit of the owners of the Certificates, including its right to receive lease payments. Principal and interest due with respect to the Certificates is made from the lease payments payable by the District; insurance or condemnation proceeds pertaining to the project, to the extent that such proceeds are not used for repair or replacement; and interest or other income derived from the investment of the funds and accounts by the Trustee pursuant to the Trust Agreement. Lease payments are paid from revenues of the District.

The District applied for a Letter of No Prejudice from FTA, pursuant to ISTEA, for the reimbursement of a portion of the capital costs of acquiring the project. Prior to the closing of the financing, the District received a notification from FTA indicating FTA's preliminary approval (subject to final review of legal documents) for the annual reimbursement to the District of 80 percent of the lease payments net of capitalized interest and the earnings on the reserve fund (the "Net Lease Payments").

The District included the following disclosure in its official statement for the financing:

> Although ISTEA provides federal funding for transportation purposes through the federal government's fiscal year ending September 30, 1997, receipt of funding by the District for any fiscal year beyond the current federal fiscal year is subject to future Congressional appropriation for transit purposes and future submittal of grant applications by the District with the FTA. Receipt of funding by the District for any federal fiscal year beyond the federal fiscal year ending September 30, 1997 is subject to future Congressional authorization. Furthermore, although ISTEA establishes the federal matching ratios for transit projects at 80%, no assurances can be made that the funding level for the FTA Project Grants at 80% of Net Lease Payments expected to be preliminarily approved by FTA under Section 9 for the FT Act (as hereinafter defined) will be continued in any future Congressional authorization.
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> The District expects to fund the remaining portion of Lease Payments which are not funded with the FTA Project Grants from Revenues, which include State and local funds and other legally available sources.

Due to the contingent nature of the federal grants, rating agencies rely on the ability of the District to make lease payments from other revenue sources in assigning a credit rating to the transaction. The District receives portions of the local sales tax and gas tax moneys levied pursuant to state law and a local sales tax initiative. This revenue, which is independent of fare box revenue, is used for the local match for the FTA grants. For this issue the District was assigned a rating of A-1 by Moody's Investors Service.

The lease payments were structured with equal principal payments of approximately $2,705,000 each year, resulting in a declining annual payment in order to approximate the depreciating value of the buses and to protect investors from a possible change in FTA funding.

The issuance of the COPs enabled the District to receive a favorable bid on a large bus order, resulting in more capital assets for less expenditure of funds. Economy of scale was also realized in the low issuance costs allocable to the remaining portions of the project.

The key legal issue as to what authority existed under state law to enter into the lease was determined by the District's special counsel. The FTA's approval or letter of no prejudice was the key factor in allowing the District to determine to proceed with the financing. The role of Agency counsel, as is true for most innovative financing techniques, is to render opinions that the Agency has the authority to engage in the transaction and to ensure that the proper procedural steps for the adoption of the required Agency resolutions have been followed by the Agency. Special counsel is customarily engaged to provide opinions to the investors in the COPs or to the counterparties involved in other innovative financing transactions.