CALIFORNIA DEBT & INVESTMENT ADVISORY COMMISSION

• GENERAL OBLIGATION BOND ISSUANCE •

An Overview of Local Government General Obligation Bond Issuance Trends

1985–2005

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AN OVERVIEW OF LOCAL GOVERNMENT GENERAL OBLIGATION BOND ISSUANCE TRENDS (1985-2005)[1]

General obligation (GO) bonds have historically provided local agencies with the lowest borrowing costs among the types of long-term bonds they may issue because of their broad security pledge, which yield the highest possible bond rating and widest investor acceptance. In California, GO bonds are backed either by a pledge of the full faith and credit of the issuer or by a promise to levy *ad valorem* property taxes in an unlimited amount as necessary to pay debt service. Local governments use the latter approach because they generally are not authorized to issue full faith and credit bonds. Because of this pledge of revenues, the State Constitution requires that local governments seek voter approval prior to issuing GO bonds (see sidebar "What are California's GO Bond Requirements?").

Even though the voter approval process may be time intensive and costly to mount, California local governments have continued to rely on GO bonds as a financing tool to construct, acquire, and make improvements to real property such as public buildings, roads, school facilities, and equipment. While the volume of issuance over the past two decades has varied significantly, several patterns emerge. This issue brief provides an overview of changes in the volume of long-term local government debt issuance from 1985 to 2005 (focusing on GO bonds), discusses the variation in issuance by issuer and purpose, and identifies where the greatest changes have occurred. While this issue brief does not seek to identify the many factors that influence the issuance of debt on a micro level, the significant change in the level of GO bond issuance after 1999 coinciding with the approval of Proposition 39 points to the influence this law change has had on the municipal finance market.

WHAT ARE CALIFORNIA'S GO BOND REQUIREMENTS?

GO bonds are secured either by a pledge of the full faith and credit of the issuer or by a promise to levy property taxes in an unlimited amount as necessary to pay debt service, or both. GO bonds issued by the State of California are full faith and credit bonds that are pledged by the state's general fund instead of tax revenue, whereas local agencies typically are authorized to issue GO bonds payable from *ad valorem* property taxes. In addition, State bonds require majority voter approval as opposed to GO bonds that are issued by local agencies, which require either two-thirds or 55 percent voter approval. Article XVI, Section 18 of the State Constitution, states that local agencies (i.e., county, city, town, or school district) may not incur indebtedness without two-thirds voter approval.

In 2000, Proposition 39 modified this article, which authorizes bonds for repair, construction, or replacement of kindergarten through 12th grade school facilities, community college districts, and county education offices for safety, class size, and information technology needs if the bonds receive 55 percent approval of the local vote.

1 The California Debt and Investment Advisory Commission (CDIAC) provides information, education and technical assistance on public debt and investments to state and local public agencies and other public finance professionals. CDIAC maintains a debt issuance database that includes information on all public debt issuance sold since 1985.

WHAT HAS BEEN THE TREND IN VOLUME OF LONG-TERM DEBT ISSUANCE?

Between 1985 and 2005, local governments issued 19,920 long-term bonds totaling $429.5 billion. FIGURE 01 shows the distribution of issuance by volume in five-year intervals over the 20 year period. Revenue bonds, certificates of participation/leases (COPs), and GO bonds accounted for $335.0 billion (78.0 percent) of the total volume of local government bond issuance. Revenue bonds, which are repaid through a specific source of revenues but not via a pledge to levy additional taxes as necessary, accounted for $202.9 billion (47.2 percent) of the total volume of debt issuance. COPs, which involve the leasing of public property in connection with the sale of municipal securities that represent undivided interests in the rental payments under the tax-exempt lease, were $73.7 billion (17.2 percent) of the total volume. GO bond issuance ranked third in terms of total issuance volume ($58.4 billion or 13.6 percent). [2]

FIGURE 02 shows the trend in issuance over the period for the three types of bonds with the greatest volume of issuance.

Revenue bond growth over the period remained fairly steady, with a slight upward trend (see FIGURE 02). [3] The annualized average growth rate of revenue bonds over the 20 years was 0.6 percent. The same general pattern holds for COPs, though their annualized average growth rate over the period actually declined somewhat (-2.1 percent). In contrast, the volume of GO bond issuance grew significantly from 1985 to 2005—the annualized average growth rate for GO bonds was 18.2 percent. The increase in GO bond volume is particularly significant after 1999—the annualized average growth rate from 1999 to 2005 is 30.6 percent. Of the $58.4 billion in GO bonds issued over the period, $41.0 billion (70.1 percent) was issued after 1999. Even when the data are adjusted for inflation and population growth, these trends hold. [4]

2 Revenue bonds include pooled revenue bonds, conduit revenue bonds, public enterprise revenue bonds, public lease revenue bonds, and sales tax revenue bonds. The approval processes for these bonds varies considerably, and may or may not require a vote of the electorate, depending on the issuer and source of repayment. For more information, see CDIAC's California Debt Issuance Primer at www.treasurer.ca.gov/cdiac.

3 Two noticeable "spikes" in revenue bond issuance occurred in 1985 and 1993. In 1985, there were 621 revenue bond issuances, more than any other year over the period. While some of these issuances were significant in size (e.g., Orange County issued a $787.1 million revenue bond), the spike in issuance appears to be attributable to the shear number of issuances. While the number of issuances in 1993 was second only to 1985, 14 issuers accounted for over half of the total volume issued ($8.2 billion of the $15.5 billion issued). These issuers included the Los Angeles Department of Water and Power ($1.8 billion), San Joaquin Hills Transportation Corridor Agency ($1.2 billion) and Los Angeles County ($1.0 billion).

4 Data presented are unadjusted unless noted. Adjusting for inflation and population growth, while tempering the magnitude of change over the period somewhat, did not change the overall findings.

FIGURE 01:

VOLUME OF LONG-TERM DEBT ISSUANCE [1]

(dollars in millions)

DEBT TYPE	1985–1989	1990–1994	1995–1999	2000–2005	TOTAL
Certificates of Participation/Leases	$ 15,505	$ 21,810	$ 16,535	$ 19,826	$ 73,677
General Obligation Bonds	2,003	5,057	10,373	40,969	58,402
Limited Tax Obligation Bonds	3,619	9,421	4,357	8,398	25,794
Other Bonds [2]	1,396	4,251	4,634	12,360	22,641
Revenue Bonds [3]	33,603	39,644	50,679	79,009	202,934
Special Assessment Bonds	4,145	3,067	3,166	2,520	12,899
Tax Allocation Bonds	5,523	8,456	5,360	13,822	33,161
Total	$ 65,795	$ 91,705	$ 95,104	$ 176,905	$ 429,508

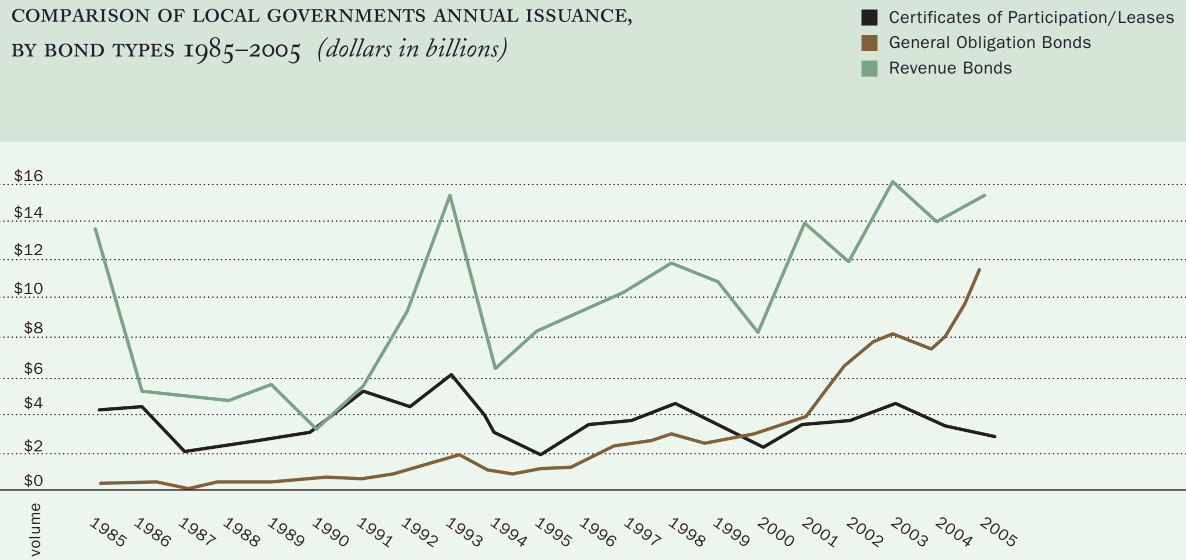
1 Totals may not add due to rounding.

2 The types of projects financed under “other bonds” were tobacco securitization, pension obligation, court judgments, and worker’s compensation.

3 This category encompasses the following revenue bonds: pooled revenue bonds, conduit revenue bonds, public enterprise revenue bonds, public lease revenue bonds, and sales tax revenue bonds.

FIGURE 02:

COMPARISON OF LOCAL GOVERNMENTS ANNUAL ISSUANCE, BY BOND TYPES 1985–2005 *(dollars in billions)*



WHAT TYPE OF LONG-TERM DEBT INSTRUMENTS DO LOCAL GOVERNMENTS USE?

The types of long-term debt issued by a local government are a function of many factors (such as legal authorization, debt policy guidelines, existing portfolio composition, project type, costs of issuance, and market demand). FIGURE 03 details debt type and volume (in aggregate) by five local government issuer categories with the largest total volume of bond issuance over the period; the remaining local issuers—mostly special districts—are grouped together into the sixth “Other Issuers” category. The largest issuers by volume of long-term debt over the period (excluding the “Other Issuers” category) have been authorities ($79.5 billion), followed by cities ($76.2 billion) and school districts ($50.8 billion). The type of debt issued, however, differed significantly by issuer category. While authorities and cities have mostly issued revenue bonds over the period (approximately $64.5 billion and $42.0 billion, respectively), school districts largely have issued GO bonds ($39.0 billion), followed by cities ($4.7 billion or 8.0 percent) and counties ($2.6 billion or 4.4 percent).

FIGURE 03:

LONG-TERM DEBT ISSUANCE, BY DEBT TYPE AND ISSUER CATEGORY [1]

1985–2005 *(dollars in millions)*

DEBT TYPE	CITIES	COUNTIES [2]	SCHOOL DISTRICTS	AUTHORITIES [3]	REDEVELOPMENT AGENCIES	OTHER ISSUERS	TOTAL
Certificates of Participation/Leases	$ 17,189	$ 15,595	$ 11,664	$ 6,615	$ 1,073	$ 21,541	$ 73,677
General Obligation Bonds	4,655	2,572	39,045	0	0	12,131	58,402
Revenue Bonds [4]	41,972	14,320	85	64,463	5,973	76,121	202,934
Other Bonds	12,413	12,769	24	8,426	27,495	33,368	94,495
Total	$ 76,229	$ 45,256	$ 50,818	$ 79,504	$ 34,541	$ 143,161	$ 429,508

1 Totals may not add due to rounding.

2 Includes county issuers and the City and County of San Francisco.

3 Includes public financing authorities, joint powers authorities, and conduit issuers, among others.

4 This category encompasses the following revenue bonds: pooled, conduit, public enterprise, public lease, and sales tax revenue bonds.

The increased use of GO bonds particularly by school districts becomes more apparent when viewed over time. FIGURE 04 shows a comparison of GO bond issuance by issuer category aggregated in five year increments over the 20-year period. Between 1985 and 1990, water districts issued the greatest volume of GO bonds ($1.1 billion), followed by school districts ($425 million) and counties, cities and city/county ($396 million). From 1990 to 1994, however, this rank-order changed—school districts exceeded all other public agency issuers in volume of GO bond issuance, though the amount (approximately $3.0 billion) was still less than half of the total volume of GO bond issuance. During 1995 to 1999, school districts became the dominant issuer of GO bonds, selling $8.0 billion (77.2 percent). The amount of school district GO bond issuance grew dramatically after 1999; from 2000 to 2005, school districts issued $36.2 billion (88.4 percent) of the total volume of GO bonds.

FIGURE 04:

COMPARISON OF GO BOND ISSUER CATEGORY BY VOLUME [1]

1985–2005 *(dollars in millions)*

	1985–1989		1990–1994		1995–1999		2000–2005	
ISSUER CATEGORY	VOLUME	% OF TOTAL VOLUME	VOLUME	% OF TOTAL VOLUME	VOLUME	% OF TOTAL VOLUME	VOLUME	% OF TOTAL VOLUME
School Districts	$ 425	21.2 %	$ 2,148	42.5 %	$ 8,012	77.2 %	$ 36,199	88.4 %
Counties, Cities, City/County	396	19.8	1,594	31.5	1,685	16.2	3,551	8.7
Special Districts	64	3.2	82	1.6	264	2.5	146	0.4
Water Districts	1,078	53.8	1,147	22.7	386	3.7	710	1.7
Miscellaneous	10	0.5	27	0.5	25	0.2	321	0.8
Utility Districts	31	1.6	59	1.2	0	0.0	42	0.1
Total	$ 2,003	100.0 %	$ 5,057	100.0 %	$ 10,373	100.0 %	$ 40,969	100.0 %

1 Totals may not add due to rounding.

WHAT TYPES OF PROJECTS HAVE BEEN FINANCED WITH GO BONDS?

The types of projects financed through debt issuance vary widely depending on the type of debt being issued. For example, counties, cities and school districts may use GO bonds to finance the acquisition, construction, or completion of projects involving "real property" such as hospitals, parks and school buildings. Revenue bonds (such as public enterprise revenue bonds and public lease revenue bonds) typically are used to finance projects for which a stream of revenues, rents, or fees are generated to support repayment of the bonds including power systems, stadiums, and airports. COPs may be issued to finance a project for which the local agency has statutory authority to lease the facility including school buildings, police stations and fire stations.

FIGURE 05 shows the distribution by purpose of the total volume of long-term debt issuance. From 1985-2005, local governments issued a total of $227.4 billion (52.9 percent) for capital improvements, $75.2 billion (29.6 percent) for education purposes, and $38.6 billion (9.0 percent) for housing purposes using both GO bonds and non-GO bonds. [5]

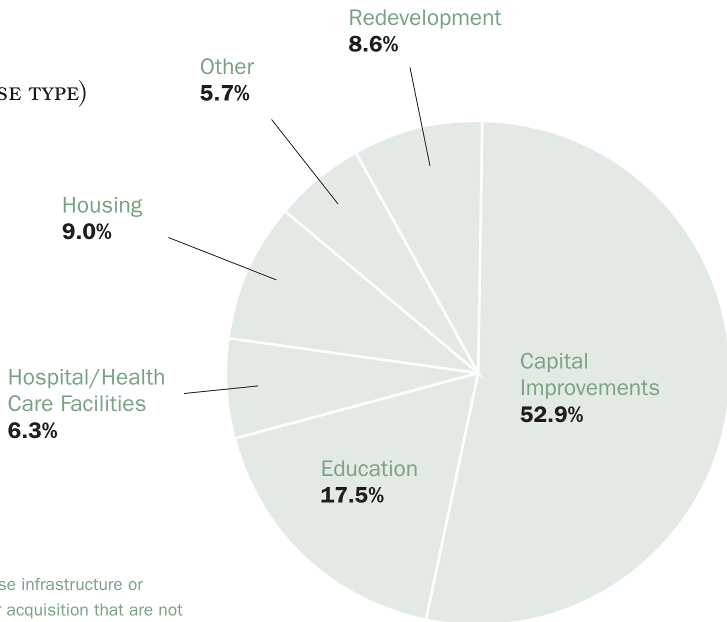
While the amount of issuance for capital improvements exceeds all other categories, issuance for this purpose is done primarily using non-GO bonds (see FIGURE 06). Capital improvements were the primary purpose for issuing $216.8 billion (58.4 percent) of non-GO bonds over the period, followed by $38.5 billion for housing (10.4 percent) and $37.1 billion for redevelopment (10.0 percent).

In contrast, FIGURE 07 shows that GO bonds were almost exclusively issued for education purposes (80.7 percent), followed by capital improvements (18.0 percent) and hospital/health care facilities (1.1 percent). The significant use of GO bonds for education purposes is a relatively new phenomenon.

FIGURE 05:
LONG-TERM ISSUANCE
(GO AND NON-GO DEBT BY PURPOSE TYPE)
1985–2005

TOTAL VOLUME

$429.5 *billion*



5 CDIAC defines "capital improvements" as those infrastructure or public property improvements, construction or acquisition that are not related to education, hospital/health care or housing. Projects that would be grouped under capital improvements include those involving correctional facilities, airports, water, waste water, public transit, etc.

FIGURE 06:
NON-GO BOND ISSUANCE
BY PURPOSE TYPE 1985–2005

TOTAL VOLUME

$371.1 *billion*

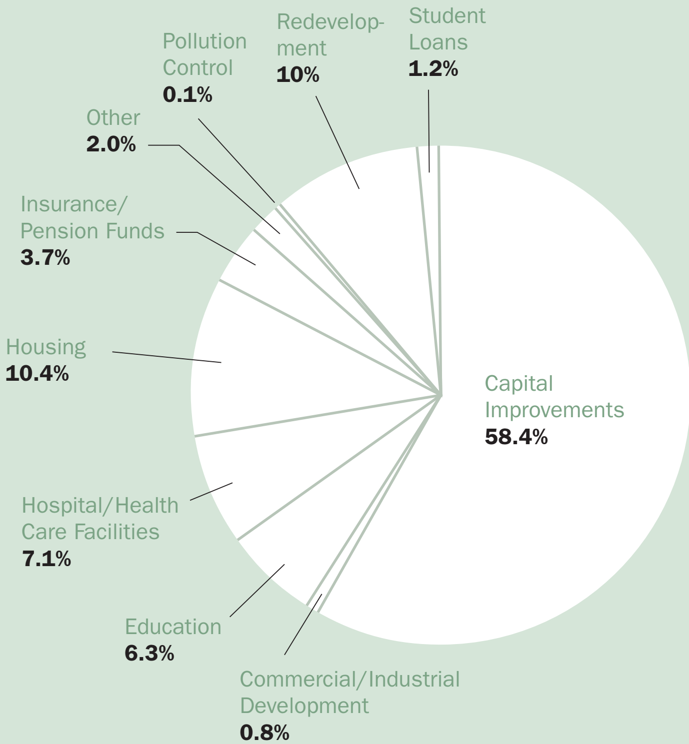
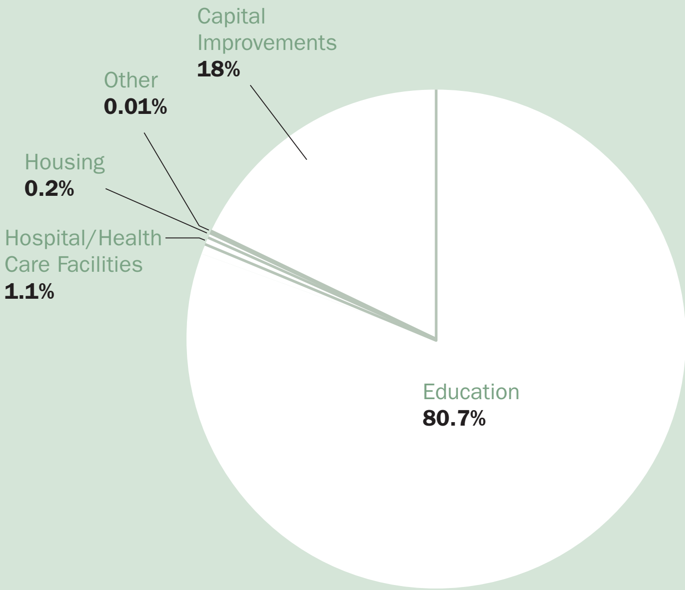


FIGURE 07:
GO BOND ISSUANCE BY PURPOSE TYPE
1985–2005

TOTAL VOLUME

$58.4 *billion*



FIGURES 08 and 09 show the variation in non-GO bond issuance and GO bond issuance for the types of projects with the highest total volume over the period: capital improvements, education, and housing. Non-GO bond issuance includes revenue bonds and COPs.

For most of the period, non-GO bond issuance remained fairly steady, regardless of project type. Except for 1993 and 2003, the volume of non-GO capital improvement issuance generally ranged between $6 billion and $12 billion annually. The variation in volume of non-GO bond issuance for education or housing purposes had a smaller range—between $0 and $4 billion annually over the 20 year period.

By contrast, the variation in volume of GO bond issuance for education purposes is significant.

FIGURE 10 contrasts the increased use of GO bonds in the latter half of the period with COPs issued for education purposes. From 1985 to 1995, issuance levels are fairly flat. Beginning in 1996, and particularly after 1999, the volume of GO bond issuance for education purposes increases rapidly. GO bond issuance grew from $2.0 billion in 1999 to $10.4 billion in 2005. The average annualized rate of growth over this six-year period was 31.2 percent. By comparison, the average annualized rate of growth for COPs during this period was 0.03 percent.

This rather sharp increase in the use of GO bonds for education purposes coincides with the passage of Proposition 39 in November 2000.

FIGURE 08:
NON-GO BOND ISSUANCE
1985–2005 *(dollars in billions)*

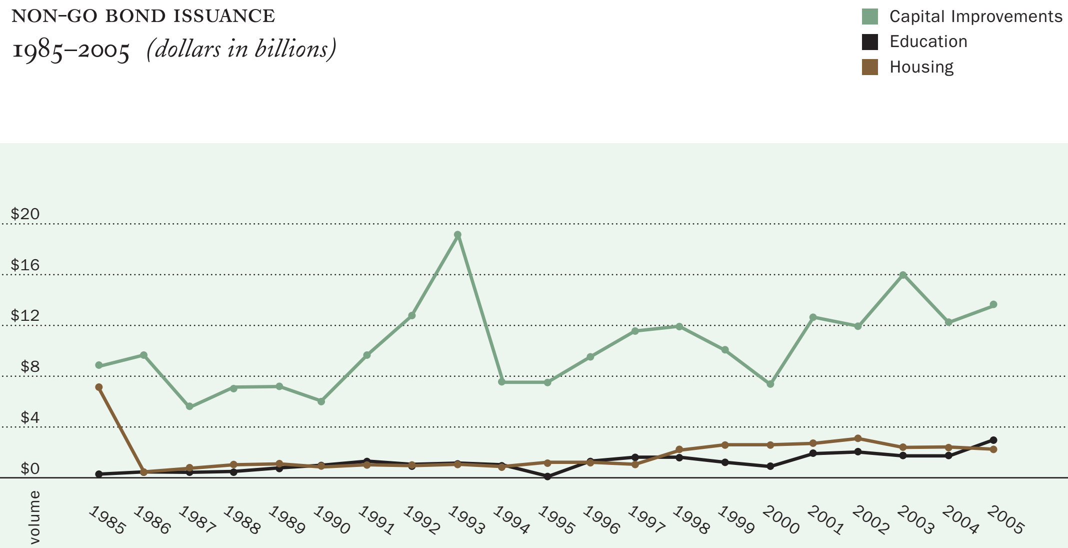


FIGURE 09:

GO BOND DEBT

1985–2005 *(dollars in billions)*

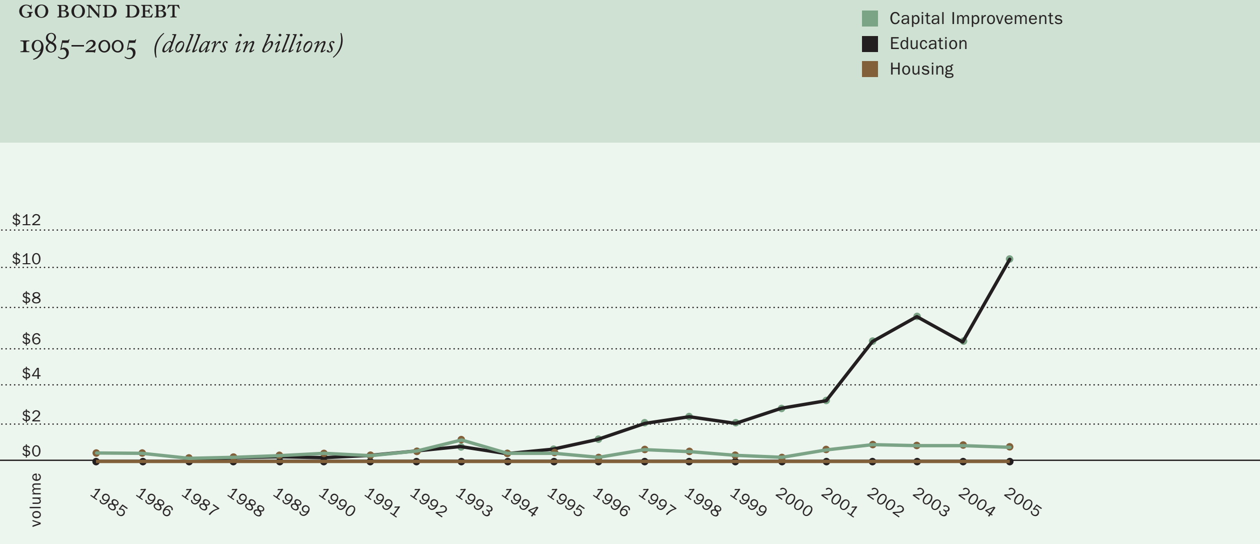


FIGURE 10:

COMPARISON OF CERTIFICATES OF PARTICIPATION TO GO BONDS FOR EDUCATION 1985–2005 *(dollars in billions)*

Proposition 39

Proposition 39 permits K-12 school districts, community college districts, and county education offices to issue bonds for school facilities if the bonds are approved by 55 percent of the vote, as opposed to the previous two-thirds approval requirement. However, in order to qualify a GO bond under Proposition 39, certain requirements must be met, such as class size, technology needs, independent performance and financial audits (see sidebar "What Does Proposition 39 Require?").

FIGURE 11 displays the major propositions affecting a local government's ability to issue bonds or raise fees overlaid on a graph of GO bond issuance volume. [6] The change in volume of GO bond issuance pre- and post-Proposition 39 is significant. The variation can be attributed in large part to a significant increase in the number of issuances since 2000. Since the passage of Proposition 39, both the number of education measures on the ballot and percent approved have increased substantially. Figure 12 provides a list of the passage and failure rate for Kindergarten through 12th grade (K-12) GO bond measures found on local general election ballots since 1986. During this period, the number of such measures increased from two in 1986 to a high of 88 in 2002. Also, the passage rate has increased since 2000. In 2000, 53 percent of the measures passed. Since then, in each election over three-fourths of all measures passed.

6 The enactment of Proposition 13 in 1978 restricted the ability of a local government to make an unlimited pledge of repayment on GO bonds by limiting (with certain exceptions) the *ad valorem* tax rate to not greater than one percent. With the passage of Proposition 46 in June 1986, voters were able to consider local GO bonds for the first time since 1978. Proposition 46 allowed the sale of GO bonds only for the acquisition or improvements of real property (e.g., fire and police stations, schools, streets and various public works projects), if such sale is approved by two-thirds of the voters. The approval of Proposition 218, the Right to Vote on Taxes Act, in the November 1996 General Election increased existing voter approval requirements for general taxes, property-related fees, and assessments. It also imposed restrictions and new procedural requirements for the passage of local fees and assessments. Additionally, Proposition 218 allowed voters to repeal by initiative previously approved taxes.

WHAT DOES PROPOSITION 39 REQUIRE?

California voters approved Proposition 39 in the 2000 General Election. This proposition lowered the voting requirement for passage of local school bond measures from two-thirds to 55 percent. In addition, it allows property taxes to exceed the one percent cap in order to repay the bonds. To issue a bond under the lower voter threshold, certain requirements must be fulfilled:

- Bond proceeds can be used only for construction, rehabilitation, equipping school facilities, or acquisition/lease of real property for school facilities.
- A list of school projects to be funded must be included in the issuance and certification that the school board has evaluated safety, class size reduction, and information technology needs in developing the list.
- School boards are required to conduct annual, independent financial and performance audits until all bond funds have been spent to ensure that the bond funds have been used only for the projects listed in the measure.

Proposition 39 also requires that each local K-12 school district provide charter school facilities sufficient to accommodate the charter school's students. The district, however, would not be required to spend its general discretionary revenues to provide these facilities for charter schools. Instead, the district could choose to use these or other revenues – including state and local bonds.

FIGURE 11:

ANNUAL GO BOND ISSUANCE AND PASSAGE OF SIGNIFICANT PROPOSITIONS

1985–2005 *(dollars in billions)*

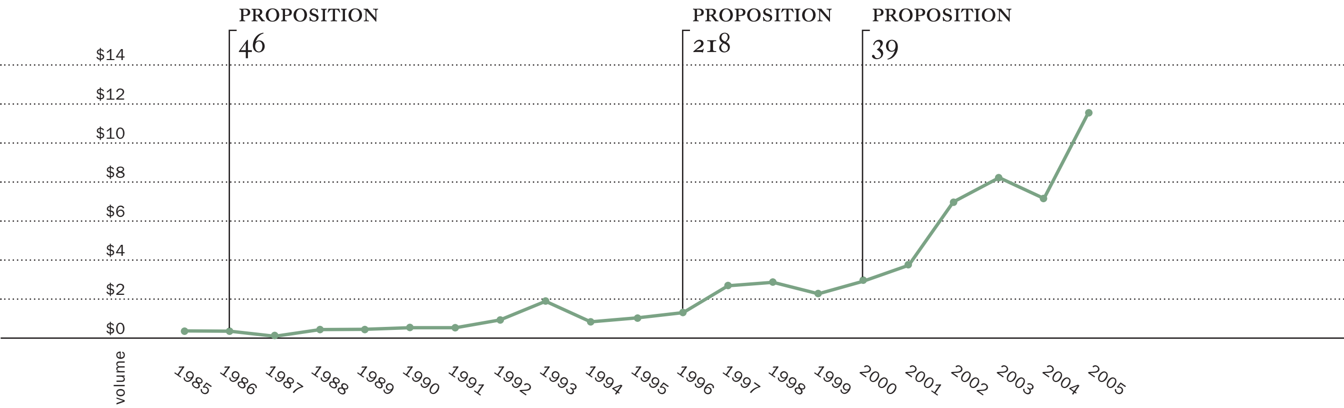


FIGURE 12:

NUMBER OF LOCAL GOVERNMENT K–12 GO BOND MEASURES [1]

PASSAGE, FAILURE, AND PASSAGE RATES

GENERAL ELLECTIONS, 1986–2006

YEAR	PASSED MEASURES	FAILED MEASURES	TOTAL MEASURES	PASSAGE RATE
1986	2	0	2	100.0%
1988	8	5	13	61.5%
1990	3	9	12	25.0%
1992	8	9	17	47.1%
1994	5	15	20	25.0%
1996	11	7	18	61.1%
1998	20	18	38	52.6%
2000	23	7	30	76.7%
2002	70	18	88	79.5%
2004	47	6	53	88.7%
2006	50	12	62	80.6%

1 Source: CDIAC State and Local Bond and Tax Ballot Measures reports for appropriate year.

Where have the greatest changes in GO issuance occurred?

The volume of GO bond issuance varies widely by region. This analysis divides the state into nine different regions as follows:

1. **Los Angeles**: Los Angeles, Orange, and Ventura Counties
2. **San Diego**: Imperial and San Diego Counties
3. **Inland Empire**: Riverside and San Bernardino Counties
4. **San Francisco (SF Bay Area)**: Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Santa Clara, Solano, and Sonoma Counties
5. **San Joaquin Valley**: Fresno, Kern, Kings, Madera, Merced, San Joaquin, Stanislaus, and Tulare Counties
6. **Sacramento Valley**: Butte, Colusa, El Dorado, Glenn, Placer, Sacramento, Shasta, Sutter, Tehama, Yolo, and Yuba Counties
7. **Central Coast**: Monterey, San Benito, San Luis Obispo, Santa Barbara, and Santa Cruz Counties
8. **North Coast**: Del Norte, Humboldt, Lake, and Mendocino Counties
9. **Mountain**: Alpine, Amador, Calaveras, Inyo, Lassen, Mariposa, Modoc, Mono, Nevada, Plumas, Sierra, Siskiyou, Trinity, and Tuolumne Counties

FIGURE 13 shows the total GO bond issuance volume for each region. Not surprisingly, the Los Angeles region issued the greatest total volume of GO bonds over the time frame, approximately $22 billion (37.6 percent) followed by the SF Bay Area ($16.8 billion, 28.7 percent) and San Diego ($4.8 billion, 8.3 percent). The region with the least amount in GO bond issuance was the North Coast region ($139.0 million, 0.2 percent). FIGURE 14 shows similar trends for the total GO bond issuance for education purposes for each region. The rising volume of issuance after 1999 is significant for many regions of the state, resulting in two- and three-fold increases from the previous period.

FIGURE 13:

GO BOND ISSUANCE BY REGION [1]

1985-2005 *(dollars in millions)*

REGION	1985–1989	1990–1994	1995–1999	2000–2005	TOTAL
1 - Los Angeles	$ 874	$ 1,767	$ 3,333	$ 15,980	$ 21,954
4 - SF Bay Area	292	1,470	3,821	11,169	16,752
Multiple [2]	485	514	516	3,544	5,059
2 - San Diego	88	215	479	4,052	4,834
5 - San Joaquin Valley	196	496	930	1,834	3,456
3 - Inland Empire	41	348	514	1,779	2,682
6 - Sacramento Valley	15	204	433	1,598	2,250
7 - Central Coast	2	42	268	768	1,080
9 - Mountain	7	1	45	141	194
8 - North Coast	2	0	32	105	139
Total	$ 2,003	$ 5,057	$ 10,373	$ 40,970	$ 58,402

1 Totals may not add due to rounding.
2 Includes bond issues that span more than one county.

FIGURE 14:

GO BOND ISSUANCE BY REGION FOR EDUCATION [1]

1985-2005 *(dollars in millions)*

REGION	1985–1989	1990–1994	1995–1999	2000–2005	TOTAL
1 - Los Angeles	$ 81	$ 319	$ 2,614	$ 13,925	$ 16,939
4 - SF Bay Area	165	802	2,909	9,606	13,482
2 - San Diego	15	79	440	3,944	4,478
5 - San Joaquin Valley	177	495	904	1,701	3,277
3 - Inland Empire	9	251	443	1,698	2,401
6 - Sacramento Valley	5	200	391	1,581	2,177
7 - Central Coast	0	39	235	698	972
9 - Mountain	7	1	43	103	154
8 - North Coast	1	0	32	99	132
Total	$ 459	$ 2,186	$ 8,011	$ 33,355	$ 44,012

1 Totals may not add due to rounding.

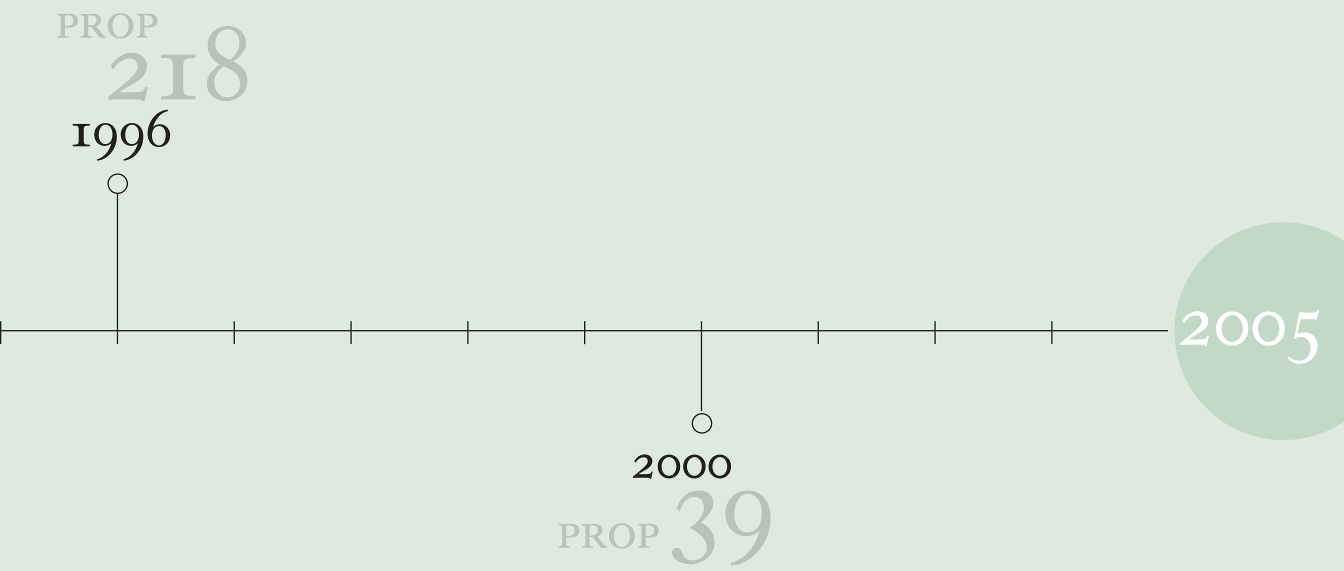
1985

1986

PROP 46

CONCLUSION

GO bonds have long been a useful financing method that local governments have relied on to assist in financing infrastructure projects because of their low borrowing costs and widespread investor appeal. Their use over the past 20 years has changed significantly, most notably after the passage of Proposition 39. Once primarily used by public utilities for capital improvements, GO bonds now are primarily issued by school districts for K-12 improvements. Most of the GO bond issuance for education purposes occurs in three regions of the state—Los Angeles, SF Bay Area and San Diego. However, even in other areas of the state, the use of GO bonds for education has increased substantially. Whether this trend will continue over the next 20 years will depend on many factors including the level of interest rates, population growth, infrastructure capacity/maintenance needs, and the use of alternative financing methods. While this issue brief does not address these causal factors, it does provide a baseline for understanding historical local government GO bond issuance patterns that may promote discussion on the choice of financing methods for providing for current and future infrastructure needs of local agencies throughout the state.



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