

## MEMORANDUM

To City or County Official

FROM Department of Finance

DATE April 9, 2010

RE Notice regarding restrictions on borrowing from Prop. 1B Funds

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This Notice describes certain restrictions related to the use of funds received pursuant to the Highway Safety, Traffic Reduction, Air Quality and Port Security Bond Act of 2006 (“Prop. 1B”). Pursuant to Prop. 1B, the State issues tax-exempt general obligation bonds and transfers proceeds from such bonds to local agencies (the “Prop. 1B Funds”) to fund various projects described under Prop. 1B (the “Prop. 1B Projects”).

ABX8 14, enacted on March 22, 2010, provides that the State will defer the apportionment of certain revenues from the Highway Users Tax Account in the Transportation Tax Fund, thus deferring the transfer of these revenues to local agencies. ABX8 14 also provides that during the period of that deferral, local agencies receiving Prop. 1B Funds may borrow from those Prop. 1B Funds to pay for local street and road maintenance and operations. However, any borrowing from funds disbursed by the State on or after March 1, 2010 must be repaid with interest. The relevant language of ABX8 14 describing the interest repayment is as follows:

Any such borrowing from funds disbursed by the State Controller's Office on or after March 1, 2010 shall be repaid with interest, computed at the current average rate of interest earned by the local agency with respect to amounts on deposit in the account from which the borrowing occurs, as determined by the local agency, within the fiscal year in which the borrowing initially occurs. Interest earned on amounts borrowed pursuant to this paragraph shall be applied by the local agency for the purposes set forth in the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006.

The effect of this restriction is that if a local agency borrows from its Prop. 1B Funds to pay for local street and road maintenance and operations, it must determine a rate of interest to be applied to such borrowing, must repay the borrowed Prop. 1B Funds with interest within the same fiscal year in which the funds were borrowed, and must use both the repaid Prop. 1B Funds and the resulting interest for Prop. 1B Projects.

Since Prop. 1B funds are tax-exempt bond proceeds and are subject to audit by both the IRS and the State Controller’s Office, a local agency will be required to retain records of any borrowing pursuant to ABX8 14, including the date of such borrowing and repayment, the total interest paid on the borrowing, and how the borrowed funds were spent. By receiving proceeds pursuant to Prop. 1B, a local agency is hereby agreeing to comply with the requirements set forth in ABX8 14 and to retain the appropriate records documenting compliance with the provisions.

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If you have any questions about this restriction on borrowing from Prop. 1B Funds, please contact Mark Tollefson or Jim Parks at (916) 322-2263.