



CALIFORNIA STATE TREASURER JOHN CHIANG

TASK FORCE ON BOND ACCOUNTABILITY

Comments Received

Public Comment Period October 27, 2015 to November 30, 2015

Robert Campbell, Auditor-Controller, Contra Costa County

Julie Hagen, CPA, CPFO, Chief Deputy Controller, County of Santa Barbara

Alicia Minyen, CPA, CFE, Pleasant Hill, California

California Association of County Treasurers and Tax Collectors (CACTTC)

California State Association of County Auditors (CSACA)

TASK FORCE ON BOND ACCOUNTABILITY PUBLIC COMMENTS ON GUIDELINES

FROM: ROBERT CAMPBELL, AUDITOR-CONTROLLER, CONTRA COSTA COUNTY

DATE: NOVEMBER 28, 2015

TRANSMITTED BY: EMAIL

Below are some comments from a sub group of the State Association of County Auditors (SACA).

1. This document will be very useful and an important tool for Counties.
2. More emphasis should be placed on the importance of monitoring compliance regarding the use of proceeds, private use, required timing of expenditures, and disposition of bond-financed facilities.
3. I am a proponent of keeping a document as short as possible so people will be more likely to read it. This document is very large. Will the final product be shorter? (I couldn't tell if the whole document would be part of the final published product.)
4. Page 6, 2nd paragraph, last sentence "... bond proceeds and the manner in which public agencies ensure that they are used safely..." I'm not sure "safely" is the word that is intended?
5. Appendix A, page 1, 2nd paragraph, first sentence "... and objectives that set a positive attitude towards and wiliness to employ internal control ..." I think they meant willingness, not wiliness?

TASK FORCE ON BOND ACCOUNTABILITY PUBLIC COMMENTS ON GUIDELINES

FROM: JULIE HAGEN, CPA, CPFO, CHIEF DEPUTY CONTROLLER, COUNTY OF SANTA BARBARA

DATE: NOVEMBER 28, 2015

TRANSMITTED BY: EMAIL

1. This document will be very useful and an important tool for Counties.
2. More emphasis should be placed on the importance of monitoring compliance regarding the use of proceeds, private use, required timing of expenditures, and disposition of bond-financed facilities.
3. I am a proponent of keeping a document as short as possible so people will be more likely to read it. This document is very large. Will the final product be shorter? (I couldn't tell if the whole document would be part of the final published product.)
4. Page 6, 2nd paragraph, last sentence "... bond proceeds and the manner in which public agencies ensure that they are used safely..." I'm not sure "safely" is the word that is intended?
5. Appendix A, page 1, 2nd paragraph, first sentence "... and objectives that set a positive attitude towards and wiliness to employ internal control ..." I think they meant willingness, not wiliness?

TASK FORCE ON BOND ACCOUNTABILITY PUBLIC COMMENTS ON GUIDELINES

FROM: ALICIA MINYEN, CPA, CFE, PLEASANT HILL, CALIFORNIA

DATE: NOVEMBER 30, 2015

TRANSMITTED BY: EMAIL

Please consider the following when finalizing the bond accountability guidelines. My thoughts below are primarily derived from experience serving on the bond oversight committee for Mt. Diablo Unified located in Concord, CA, and through other related volunteer work. I greatly appreciate the work of the Task Force and believe the Guidelines will serve as an excellent tool to ensure the proper use of public funds in the form of bond proceeds.

1. Local Government Agencies - Swap Agreements

I obtained a list of government agencies within California from CDIAC that have entered into swap agreements. This list identified agencies, including ABAG, transportation authorities, and many others. For example, in reviewing Official Statements on EMMA for the Contra Costa Transportation Authority (CCTA), CCTA had entered into a swap agreement resulting in substantial liability exceeding \$39 million, including that CCTA had to post about \$10 million in collateral. It is concerning that debt proceeds may be wasted to pay for unintended uses such as termination payments associated with derivative hedging instruments.

2. Local Government Agencies Issuing Bond Anticipation Notes and Other Bridge Financing

Debt proceeds could also be wasted when governments entering into bridge loan types of financing such as bond anticipation notes anywhere the government plans on using a subsequent bond issue to pay for such debt. This results in paying cost of issuance twice, and raises other risks, such as going concern, to the extent the bonding capacity does not allow for the subsequent sale of a bonds and the government agency is forced to pay off the bridge financing using the general fund.

3. Local Government Agencies Issuing Taxable Bonds

I've seen many instances where school districts issue taxable bonds and the governing board was not provided materials to substantiate or provide reasons for issuing a taxable bond.

4. Advanced Refunding

The public should be provided with the reasons for justifying an advanced refunding.

5. Monitoring Interfund Transfers/Interfund Borrowing

Controls should be in place to monitor permanent interfund transfers and borrowings involving bond proceeds.

6. Approved Vendor Lists/Creation of New Vendors

Vendors should be vetted and pre-approved. At least two persons should be involved in creating a new vendor to add to the approved list of vendors. Those persons approving purchase orders or approve

claims for payment shall not be allowed to create a new vendor. Governing Boards should receive detailed warrant reports prior to approval. Name of vendor, amount, and description of purpose should be included in the warrant report. Checks should not be released until board approval.

7. Controls to Protect Electronic/Facsimile Signatures

Controls should be implemented to protect electronic/facsimile signatures from unauthorized use.

8. Controls over Wire Transfers:

Before wire transfers are approved, detailed documentation showing the amount, purpose and destination of the wire should be presented for review and approval. Pre-approval of wire transfers could reduce the risk of errors or fraud. The government agency can also instruct the custodian to call at least 2 employees, prior to the wire being executed, to confirm the amount, destination, and purpose of the wire. Also, the custodian should be instructed to provide a written confirmation of each wire transfer within 24 hours.

9. Controls to Avoid Unauthorized or Secret Bank Accounts

Custodians should be instructed to inform at least two persons to confirm the opening or closing of a bank account. A complete list of bank accounts held in the name of the government agency and all accounts held carrying the government's federal tax ID shall be maintained in a secure location.

10. Change Orders

At Mt. Diablo Unified, the governing board approved change orders AFTER the work had already been done. In order to ensure change orders are necessary and to verify the work associated with the change order was actually completed, the governing board should pre-approve change orders and be provided with documentation supporting the need for the work associated with the change order.

11. Identifying Conflicts of Interest

Conflicts of interest can occur when government agencies are provided services at no cost or below the governing board dollar threshold. For example, Mt. Diablo received services at no cost relating to a design consultation services contract with a vendor where the vendor. Yet that vendor was subsequently awarded a no-bid construction contract relating to the project that was designed by the same vendor.

12. Developer Fees

Districts do not report the amount of developer fees used to subsidize the amount of a specific project. It would be helpful to report the amount of developer fees used to pay for a project.

13. Guideline 13 - "Information and Communication"

You state that "information of interest to stakeholders includes current status of bond funds - e.g., "spent and unspent, authorized and unissued,"....

It would be also helpful to disclose those bond proceeds that have been "committed." Often school districts interpret "spent" bond proceeds to be those proceeds that have physically been disbursed from the Building Fund. Therefore, the bond oversight committee is not aware of those situations where the school district has committed the value of an executed contract that has yet to be paid.



November 25, 2015

Task Force on Bond Accountability

c/o California Debt and Investment Advisory Commission
915 Capitol Mall, Room 400
Sacramento, CA 95814
ATTN: Mark Campbell—mcampbell@treasurer.ca.gov

To Members of the Task Force on Bond Accountability:

On behalf of the California Association of County Treasurers and Tax Collectors, I would like to commend the Task Force for developing the Bond Accountability Best Practice Guidelines, and to thank you for extending the public comment period until Monday, November 30.

We have reviewed the Guidelines and are very supportive of the State Treasurer's efforts to address this important topic. We believe the Guidelines are well-constructed and offer a solid framework with which to approach the administration of and reporting on the use of bond proceeds. The two Checklists provided by the Task Force are a particularly useful tool; although we would have preferred that the preceding 12 pages were perhaps a little more concise. Certain more detailed comments are provided as follows.

- **Guideline 1**

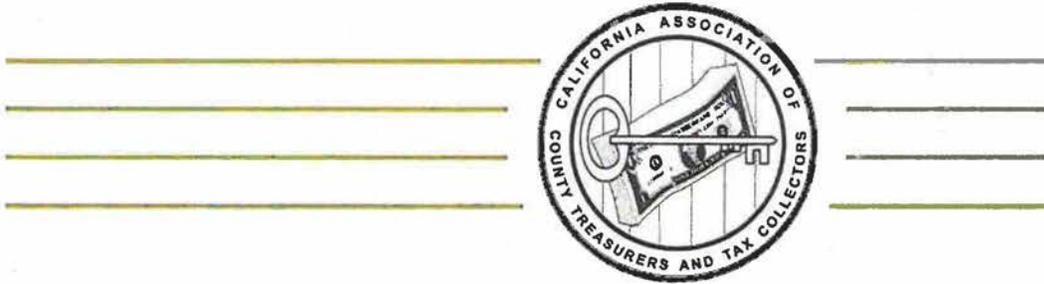
- Page 2, second bullet: **Documentation is reviewed by an authority independent of the transaction, typically accounting or treasury.** COMMENT: Delivery of goods or services and/or construction progress associated with an invoice needs to be verified against the invoice first before it is submitted to accounting or treasury. For instance, if the invoice is for architectural services, someone needs to visually inspect the set of plans before signing off on the invoice. If the invoice is construction related, an inspector needs to sign off on the invoice.
- Page 2, middle paragraph: **Bond compliance staff should assume primary responsibility for regularly monitoring and reviewing the use of bond proceeds to ensure that**

California Association of County Treasurers and Tax Collectors

1415 L Street, Suite 1000 • Sacramento, California 95814

(916) 441-1850 • Fax (916) 441-6178

Website: www.cacttc.org



proceeds are used in accordance with legal requirements. COMMENT: A bond compliance officer needs to be completely independent of the payment process.

- Page 2, middle paragraph: **Results of their review should be reported to and reviewed by management.** COMMENT: If management is one person, then the governing body needs to review the results.

- **Guideline 3**

- Page 3, end of paragraph: **The committee may also review the local agency's budgets, interim financial reports, and other financial documents as needed and make recommendations regarding the documents' adequacy or the need for improvements.** COMMENT: A special audit should be done that focuses solely on bond expenditures for a particular year and for a particular bond issuance.

- **Part 2**

- Page 5, middle paragraph: **A public agency's risk assessment must also focus on the potential risk of fraud or misuse as a consequence of weaknesses in its system of controls. These weaknesses may be the outcome of complex program structures, turnover and poor allocations of responsibilities, lack of training, or lack of clearly stated objectives.** COMMENT: For bond expenditures related to construction projects, a big risk factor is construction change orders during the project. A tight control process and policy related to change orders should be established up front before construction begins so change order expectations are known up front.

- **Guideline 9**

- Page 8, second bullet list: COMMENT: Add—Filing ongoing continuing disclosure reports pursuant to the bond continuing disclosure agreement.

- **Guideline 12**

- Page 9, last paragraph: **At the close of a bond sale, the public agency will deposit bond proceeds into funds and accounts with a trustee.** COMMENT: Or with the Treasurer of the District's respective County.

California Association of County Treasurers and Tax Collectors

1415 L Street, Suite 1000 • Sacramento, California 95814

(916) 441-1850 • Fax (916) 441-6178

Website: www.cacttc.org



- **Guideline 13**

- Page 10, second paragraph: **Regularly report to stakeholders on the outcomes of expenditures of bond funds.** COMMENT: During periods of heavy expenditures due to construction project progress, reporting should be more frequent such as weekly, biweekly or monthly so that if fraud is occurring, there is a better chance it is caught sooner. Reporting can become less frequent after project completion since most, if not all of the funds are expended.

- **Debt Issuance and Management Review Checklist**

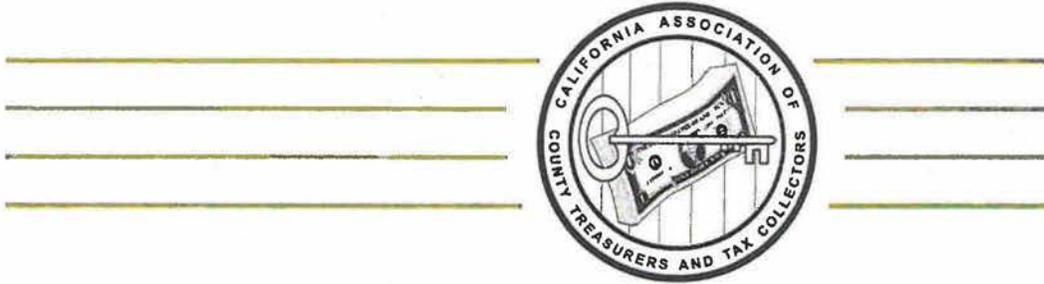
- Page 14, fourth box: **Establish a system to track expenditures that includes a review and approval process that conforms to the controlling bond document(s).** COMMENT: A key component to this system is to physically verify the delivery of goods or services and/or construction progress prior to invoice sign off.
- Page 14, second bullet: **Indicate where bond funds will be used to reimburse the agency for prior expenditures (e.g., planning and design) and identify the type and timing of the reimbursement.** COMMENT: Make sure the appropriate reimbursement resolution is established prior to bond issuance.
- Page 14, last bullet: **Investment of bond proceeds.** COMMENT: Make sure investment of bond proceeds is in accordance with government code requirements, bond covenants, and with liquidity requirements that match the draw down schedules of the bond projects.
- Page 15, third-to-last box: **Regularly monitor the investment of bond proceeds in conformity with the bond documents and state law.** COMMENT: And liquidity requirements.
- Page 15, last box, first bullet: **Prepare reports (such as a Bond Accountability Report) for the governing board and/or oversight committee as required that include: Expenditures to date and remaining balance.** COMMENT: This should be done as frequently as weekly, biweekly or monthly during heavy project expenditure time periods.

California Association of County Treasurers and Tax Collectors

1415 L Street, Suite 1000 • Sacramento, California 95814

(916) 441-1850 • Fax (916) 441-6178

Website: www.cacttc.org



- **Internal Control Checklist**

- Page 17, item 1: **Do you have a compliance officer? (Identify a compliance officer or establish a compliance team to verify internal controls and bond requirements.)** COMMENT: Must be completely independent of the progress verification and invoice payment processes.
- Page 18, item 6: **Establish an audit committee to review internal and external audits that include compliance tests of bond requirements.** COMMENT: And compliance tests of the invoice payment process.
- Page 18, item 5: **Identify and analyze risks (including potential fraud and misuse) related to the objectives and conditional elements of the bond administration program.** COMMENT: The construction change order process is a high risk activity that should be focused on.
- Page 19, item 1: **The agency applies the same system of internal control activities to bond funds as it does to all other governmental funds.** COMMENT: If not a higher system of internal control activities!

The following are a few additional points to consider:

- The report often makes the assumption that all bonds are issued on a tax-exempt basis, whereas there is considerable taxable municipal debt issued in California.
- The report should reference that the IRS form 8038 has a specific line item inquiring about tax compliance procedures and that the failure to have such written procedures could be an audit flag for the IRS.
- There is an assumption that bond proceeds will be held by a trustee (see Guideline 12 and Internal Control System Checklist), but the most common debt issuance in California is school district general obligation bonds. These monies are invariably held by the County Treasurer and are often audited by the County Office of Education.

California Association of County Treasurers and Tax Collectors

1415 L Street, Suite 1000 • Sacramento, California 95814

(916) 441-1850 • Fax (916) 441-6178

Website: www.cacttc.org



- The Debt Issuance and Management Review Checklist assumes that bond proceeds relate to a tax-exempt capital project financing (see references to "Project" on pages 13-15). There are, however, many other uses of municipal bond proceeds, each of which carries the risk of fraud if not managed properly.
- The Debt Issuance and Management Review Checklist implies that disclosure filings and arbitrage reporting must be out-sourced to a consultant (see footnote 51). Similar references also exist in the Internal Control System Checklist. These statements overlook the possibility that an issuer may have the resources and expertise to manage these tasks internally.

Again, we commend the Task Force for developing the Bond Accountability Best Practices Guidelines and look forward to their implementation for a more responsible and transparent use of bond proceeds. We hope you find our comments and points helpful.

Very truly yours,

Russell V. Watts

President and Chief Executive Officer

California Association of County Treasurers and Tax Collectors

1415 L Street, Suite 1000 • Sacramento, California 95814

(916) 441-1850 • Fax (916) 441-6178

Website: www.cacttc.org

California State Association of County Auditors



November 30, 2015

Task Force on Bond Accountability
c/o California Debt and Investment Advisory Commission
915 Capitol Mall, Room 400
Sacramento, CA 95814
Att.: Mark Campbell via mcampbell@treasurer.ca.gov

Task Force members:

We have reviewed the draft report dated 10/27/15 and offer the following comments and suggestions:

1. This document, specifically Appendix A that sets out best practices, will be a useful tool to California counties and their special districts, and we welcome its statewide issuance.
2. The usefulness of the document, including the main report and the appendixes, can be enhanced by making it more succinct. The contents include generic information on internal control derived from the *COSO Internal Control Integrated Framework (2013)* that can be condensed or simply referred to in order to keep the focus on the actual best practices. We suspect that these bond accountability guidelines will be most beneficial to small issuers who would not have the resources to embrace the entirety of the document.
3. While acknowledging this effort initiated by the State Treasurer, we also recognize that the contents reflect largely the *Internal Control Guidelines for California Local Agencies* that were issued by the State Controller in December 2014. In this regard, given that the Controller has already set base guidelines for internal control, it would be more helpful for counties to receive further guidance on bond accountability from the Treasurer in the form of supplemental guidelines, focusing on pertinent best practices in this area.
4. Given the abundance of best practices, it is beneficial to point out certain key risk points in bonded debt issuance and management that have been the cause of most failures and provide specific examples to illustrate how internal control work in those situations. For examples, improper uses of bond proceeds; noncompliance with tax certificate covenants and other bond covenants; inadequate continuing disclosure.
5. We noted that the Task Force was focused on accountability for bond proceeds. An area that public agencies need guidance would be the decision making that precedes bond issuance, such as evaluation of debt burden, etc.
6. We noted a typographical error in Appendix A, page 1, 2nd paragraph, first sentence: "wiliness".

HOWARD NEWENS, PRESIDENT
PEGGY SCROGGINS, 1ST VICE PRESIDENT • JOHN NAIMO, 2ND VICE PRESIDENT
LAUREN KLEIN, SECRETARY • TRACY SCHULZE, TREASURER

Task Force on Bond Accountability
November 30, 2015

Overall, we appreciate the effort that the Task Force has put into preparing these draft guidelines and believe that its statewide issuance as well as subsequent training conducted by the CDIAC will improve bond accountability by public agencies in California.


Howard Newens
President

Cc:

Executive Committee, California State Association of County Auditors
Bob Campbell, Chair, Legislative Committee
Jim Erb, Chair, Accounting Standards and Procedures Committee

HOWARD NEWENS, PRESIDENT
PEGGY SCROGGINS, 1ST VICE PRESIDENT • JOHN NAIMO, 2ND VICE PRESIDENT
LAUREN KLEIN, SECRETARY • TRACY SCHULZE, TREASURER