

# Task Force on Bond Accountability



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# Legacy of the Great Recession



- **The Great Recession exposed weaknesses and abuses in municipal bond issuance and management practices.**
  - Internal Controls
  - CABs
  - BANs
  - AV Projections
  - Intra-fund Borrowing of Capital Building Funds
  - “Shall Issue”
  - COPs
  - Pay-to-Play

# Framework for Internal Controls



- **Control Environment**
  - Provide the foundation for the internal control system – fundamental discipline and structure.
- **Risk Assessment**
  - Identification and analysis of relevant risks
- **Control Activities**
  - Policies, procedures, and practices that ensure managements objectives are achieved and risk is mitigated. Segregation of duties, review and verification procedures, etc.
- **Information and Communication**
  - Supports all other control component by communicating control responsibilities to employees and by providing information in a timely manner so that employees can carry out the assigned tasks to mitigate risk.
- **Monitoring**
  - Internal and external oversight by management or others to ensure that controls are effective and that processes and procedures are being complied adhered to.

# Framework for Internal Controls

## Assessment of Key Control Activities – Information and Communication



- Is there a formal organizational chart which identifies the responsibilities for processing/approving/recording debt? Are the responsibilities clearly defined?
- Are interest and principal payments reconciled to debt service schedules and the general ledger?
- Are the following responsibilities performed by different people?
  - Reviewing and reconciling control accounts separate from the person who records the information?
  - Recording cash separate from the recording of the debt?
  - Maintaining detail records of debt separate from cash functions?
- Do evidences of debt and principal checks/warrants/wires require the signature of two responsible officials who are authorized and who are independent of each other?
- Does a responsible official review use of proceeds from bonds sales to ensure that proceeds are used in accordance with legal requirements and report results to a higher authority?

# Legacy of Long-dated CABs



- Long-dated CABs have saddled taxpayers with excessive future debt service.
- CABs have limited future debt issuance capacity of some school districts.
- The passage of AB 182 placed limits on CAB financings to bring them inline with CIB (current interest bond) cost metrics.

# Bond Anticipation Notes



- **Bond Anticipation Notes were issued post the Great Recession real estate market collapse based on an expectation of a V-shaped rebound in Assessed Valuations.**
- **The Assessed Valuation recovery did not materialize.**
- **School Districts who issued BANs across the State found themselves unable to refinance the debt with long maturity GO bonds due to Prop 39 restrictions.**
- **Most school districts lacked the general fund capacity to repay the BANs or could not issue COPs.**
- **Some school districts resorted to long-dated CABs as the only solution to refinance the debt.**

# Assessed Valuation Projections



- Assessed Valuation Projections calculated by advisors to determine reasonableness of GO debt issuance vs. bonding capacity are often too optimistic.
- Projections are often calculated to maximize debt issuance. Projected rates are “solved for X” to justify financing structure.
- Past AV performance is no guarantee of future performance.
- There is no clearly defined methodology in CA Code.

# Assessed Valuation Projections



- AV projections are not disclosed and made part of the record in resolutions or official statements.
- AV projections are not required to be approved for reasonableness by the Auditor-Controller, Tax Collector, or Assessor (or any other official).

# AV Projection Example



## Historical AV Rates

Duration	From	To	% Change
10 Years	2005/2006	2014/2015	3.82%
15 Years	2000/2001	2014/2015	3.45%
20 Years	1995/1996	2014/2015	5.19%
25 Years	1990/1991	2014/2015	4.35%
28 Years	1987/1988	2014/2015	5.24%

## Projected AV Rates

Compound Annual Assessed Valuation Growth Rate			
Duration	From	To	%
5 Years	2015	2019	4.50%
10 Years	2015	2024	5.62%
13 Years	2015	2027	5.85%
25 Years	2015	2039	6.19%
28 Years	2015	2042	6.23%

Fiscal Year Ending	Districtwide Assessed Valuation	
	Total	Growth % <sup>[1]</sup>
2014	\$5,910,941,492	4.62%
2015	\$6,395,820,692	8.20%
2016	\$6,683,632,623	4.50%
2017	\$6,984,396,091	4.50%
2018	\$7,298,693,915	4.50%
2019	\$7,627,135,141	4.50%
2020	\$8,125,187,066	6.53%
2021	\$8,655,761,782	6.53%
2022	\$9,220,983,026	6.53%
2023	\$9,823,113,218	6.53%
2024	\$10,464,562,511	6.53%
2025	\$11,147,898,443	6.53%
2026	\$11,875,856,211	6.53%
2027	\$12,651,349,622	6.53%
2028	\$13,477,482,752	6.53%
2029	\$14,357,562,375	6.53%
2030	\$15,295,111,199	6.53%
2031	\$16,293,881,960	6.53%
2032	\$17,357,872,452	6.53%
2033	\$18,491,341,523	6.53%
2034	\$19,698,826,124	6.53%
2035	\$20,985,159,470	6.53%
2036	\$22,355,490,384	6.53%
2037	\$23,815,303,906	6.53%
2038	\$25,370,443,251	6.53%
2039	\$27,027,133,195	6.53%
2040	\$28,792,004,993	6.53%
2041	\$30,672,122,919	6.53%
<b>Total</b>		<b>N/A</b>

# Inter-Fund Borrowing of Bond Proceeds



- ED Code Section 42603 allows “any” fund to be borrowed against if repaid within the same fiscal year (or repaid in the following fiscal year if the transfer takes place within the final 120 days of the fiscal year).
- However, most bond official statements specify that the building funds may *only* be expended on project construction costs (often citing specific named projects).

# “Shall Issue,” Authority and Responsibility



- Existing law allows for a school district to issue its own GO debt without the consent of the County, unless the district has received a qualified or negative certification in its most recent interim budget report wherein the County must issue on the districts behalf. Ed Code Section 15140(b) & Gov Code Section 53508.7(c).
- Existing Law allows for a school district to issue Tax and Revenue Anticipation Notes under Gov Code Section 53853 (b), if issued as part of a “pool.”
- If the district has received a Qualified or Negative certification on its most recent interim budget report, the district is prohibited from issuing a TRAN (or other non-voter approved debt) on its own pursuant to Ed Code Section 42133, and the County must issue on the district’s behalf.

# COPs Concerns



- **COPs non-voter approved debt**
- **Lack of central oversight/monitoring**
- **Pledging/earmarking volatile revenue repayment sources.**
- **State deferrals**
- **Negative impact to the general fund reserves and ongoing discretionary funding.**
- **Defaults on COPs lease payment obligations**

# COPs Problems



- Refrain from earmarking/pledging volatile revenue sources as repayment.
  - Developer fees
  - Fine and forfeiture revenues
  - Property/sale tax revenues
  - AB26x1 tax increment revenue
    - ✦ Pass through agreements
    - ✦ Residual tax increment

# Pay-to-Play



- **AB 621 (2013) attempted to amend Gov Code Section 53593.5 to prohibit firms that provide bond campaign services from providing bond financial advisory or underwriting services.**
- **The practice of prepaying bond campaign costs as a quid pro quo for securing advisory and negotiated underwriting services increases the cost of issuance for taxpayers.**
- **School districts are prohibited from using taxpayer funded resources to fund bond ballot measure campaigns and should be prohibited from entering into such agreements with firms.**

# Contact



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