

# CDIAC Workshop

## The ABC's of School Debt Financing

### Session I

### Considerations for School Debt Financing

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A Division of Zions First National Bank

# Why Are We Here?

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- Purpose of today's workshop:
  - Understand basics of school district debt
    - Terminology
    - Options
  - Understand obligations and responsibilities
  - Know what questions to ask
  - Resources for future reference
- Current economic climate presents unique challenges and opportunities
- Like a home mortgage, taking on debt has long-term implications for a school district

# ABC's of Debt Financing

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- What do we mean by “debt”?
  - Borrow now, pay back later with interest
- What do we mean by “financing”?
  - The technical side of borrowing
    - the legal documentation
    - the interest rates & amortization
    - the on-going obligations
  - Must be in place for someone to give you the money

# Constitutional Debt Limit

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- California Constitution, Article 16, Section 18a:

*No county, city, town, township, board of education, or school district, shall incur any indebtedness or liability in any manner or for any purpose exceeding in any year the income and revenue provided for such year, without the assent of two-thirds [now 55% for schools] of the voters of the public entity voting at an election to be held for that purpose [...]*

- In other words, public agencies can't go into debt without voter approval
- TRANs are exempt because the repayment obligation does not extend beyond the fiscal year
- Leases are exempt because the repayment obligation is contingent on use of equipment or property

# Why Borrow?

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- Economics of debt & time value of money
- Future students and homeowners will benefit, they should pay for some of the costs
- Reduce one-time burden and match repayment to useful life of project
- Bridge financing or cash flow needs
- To qualify for State matching funds
- Reduce energy and maintenance costs – savings to the General Fund

# Questions to Start the Process

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1. What is the District's financing need?
  - Cash flow deficit
  - Capital project (real property or equipment)
2. How much will you need to borrow?
  - Offset by other sources of funds, interest earnings
  - Increase by costs of issuance, reserve fund, capitalized interest
3. Who will pay it back?
  - District (General Fund)
  - Designated revenue (e.g., developer fees)
  - Taxpayers
  - Specific neighborhood



# Other Considerations

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- Length of repayment
  - Must match useful life of project
  - For cash-flow borrowings, generally must be repaid within one year
- Board & community support
- Staff time/capabilities



# Match Repayment Term to Use

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| <b>Useful Life Table (Partial)</b><br>(from SACS & ASBO) |                   |
|--|-------------------|
| <b>Capital Asset</b>                                     | <b># of Years</b> |
| School Buildings   | 50                |
| Portable Buildings                                       | 25                |
| Site Improvements  | 20                |
| HVAC Systems   | 20                |
| Roofing  | 20                |
| Kitchen Equipment  | 15                |
| Vehicles (Buses)   | 8                 |
| Copiers  | 5                 |
| Computer Software (Instructional)                        | 10 - 20           |
| Computer Software (Administrative)                       | 5 - 10            |
| Computer Hardware  | 5                 |

# Sources/Types of Financing

| Type of Financing   | Voter-Approved | Not Voter-Approved | Who's responsible for repayment?                              |
|---|----------------|--------------------|---|
| General Obligation Bonds (GOB)  | X              |                    | All Taxpayers   |
| School Facility Improvement District (SFID)                                       | X              |                    | Taxpayers within specific SFID                                |
| Mello-Roos (Community Facility District (CFD))                                    | X              |                    | Property owners within CFD                                    |
| Direct Lease (under \$3 million)  |                | X                  | District  |
| Certificates of Participation (COPs) (over \$3 million)<br>Or Lease Revenue Bonds |                | X                  | District  |
| Tax and Revenue Anticipation Notes (TRAN)   |                | X                  | District  |
| Bond Anticipation Notes (BANs)  | X              |                    | Taxpayers   |
| Refundings – GOB or COP   |                | X                  | For GOB Refunding – Taxpayers<br>For COP Refunding - District |

# Features

| Type of Financing                                       | Uses                                    | Amount        | Term                   |
|---|---|---------------|------------------------|
| General Obligation Bonds (GOB)                          | Capital Projects on Voter List          | \$500,000+    | Up to 40 years         |
| School Facility Improvement District (SFID)             | Capital Projects on Voter List          | \$500,000+    | Up to 40 years         |
| Mello-Roos (Community Facility District (CFD))          | Capital Projects                        | \$500,000+    | Up to 40 years         |
| Direct Lease (under \$3 million)                        | Capital Projects, may include equipment | \$50,000-\$3M | 2-10 years             |
| Certificates of Participation (COPs) (over \$3 million) | Capital Projects, may include equipment | \$3M+         | Up to 30 years         |
| Tax and Revenue Anticipation Notes (TRAN)               | Cash flow deficit or working capital    | \$50,000+     | 1 year                 |
| Bond Anticipation Notes (BAN)                           | Capital Projects on Voter List          | \$500,000+    | Up to 5 years          |
| Refunding GOBs or Refunding COPs                        | Refinance existing bonds or COPs        | \$3,000,000+  | Same as original issue |

# Key Features to Evaluate

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- Key features used to determine best financing option:
  - Interest rates (short/long term + costs)
  - Type of interest (variable/fixed)
  - Cost of issuance (one time costs)
  - Prepayment penalty
  - Need for credit rating or bond insurance
  - Paperwork
  - Approximate processing time

# Debt Management Policy

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- Sets guidelines for debt issuance decisions
  - Caps on General Fund Debt
  - Parameters for technical terms and conditions of debt
- Provides opportunity to educate Board and staff on roles and responsibilities
- Look to CDIAC and other advisors for help developing policy

# Pre-Financing Process

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- Determine needs – even if you don't think you can afford them all
- Research alternatives – other funding sources, timelines, requirements
- Communicate with stakeholders – Superintendent, Board, Staff, Community

# Managing the Financing Process

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- Bring in the experts
- Check references
- Interest rates are big part of picture; but also look at other up-front costs
- Compare net funds to district to the net payment(s) by district
- Is disclosure complete, accurate, and not misleading?
- How complicated is the ongoing management? Who is going to do it?1



# The Financing Process

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## 1. Identify “team” to coordinate financing

- Retain Financial Advisor and/or Underwriter
- Retain Bond Counsel

## 2. Legal Framework

- Voter approval
- District Board approval
- County Board approval

## 3. Disclosure & Credit Review

Information provided to investors must be:

- Accurate
- Thorough
- Up-to-Date

# Process Overview, continued

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## 5. Pricing

- Can be done competitively or negotiated
- Interest rates are determined
- Repayment schedule is set

## 6. Closing

- Paperwork is signed
- Money changes hands

## 7. Ongoing responsibilities

- Repayments
- Investing proceeds
- Other obligations

# Parties to a Securities Transaction



**Bond Counsel**



**Financial  
Advisor**



(Wants lowest cost)



**County  
Treasurer/  
Auditor**

**Seller of Bonds (Borrower)**

**Buyer of Bonds (Lender)**



**Bond Trustee/  
Registrar/  
Paying Agent**



**Disclosure  
Counsel**



**Rating Agency**



**Underwriter**



**Investors  
(Wants highest return)**



**Underwriter's  
Counsel**