



August 9, 2011

To: California County Treasurer-Tax Collectors  
From: CACTTC Executive Committee  
Re: CACTTC support of L.A. County white paper on school district general obligation bonds

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May of 2011, the Treasurer-Tax Collector of Los Angeles County issued a white paper regarding school district general obligation bonds. The white paper identified various bond financing practices and structural issues that were concerning from a financial best practices standpoint.

The purpose of this letter is to state CACTTC's support of the L.A. County white paper and the issues addressed therein. CACTTC feels these issues are of sufficient importance as to further highlight the need for school districts and the financial industry to understand that Treasurer-Tax Collectors up and down the State of California have similar issues and concerns and feel strongly about what they will and will not support.

CACTTC and its members understand the importance of General Obligation (GO) bond financings to school districts. However, County Treasurer-Tax Collectors are fiduciaries of GO bond funds and are involved in the tax collection process for those bonds and therefore have a vested interest in making sure that taxpayers are receiving the most for their dollars. CACTTC understands that many of the issues addressed in the white paper are not necessarily legal issues, but industry best practices and from a taxpayer advocacy standpoint make sure that important taxpayer safeguards are maintained with respect to the issuance of GO bonds.

During the many discussions that CACTTC members have had surrounding the white paper, it is clear that Treasurer-Tax Collectors do not want to have an adversarial relationship with their school districts. On the contrary, Treasurer-Tax Collectors want to be considered a resource that can assist their school districts during the debt issuance process, especially for those districts that do not access the capital market on a regular basis.

In summary, CACTTC believes that the issues highlighted in the white paper are meant to assist school districts in making sure that problems are avoided down the road with respect to tax exempt status and taxpayer lawsuits while insuring that taxpayer dollars are utilized in the most efficient manner.

Thank you for your continued support of CACTTC, if you have any questions or would like additional information please contact our office at (916) 441-1850 or [Sulema@slgs.org](mailto:Sulema@slgs.org).

CC: Honorable Bill Lockyer, California State Treasurer  
Mark Saladino, Los Angeles County TTC  
Jackie Denny, Kern County TTC  
CACTTC  
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Attachment

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# COUNTY OF LOS ANGELES TREASURER AND TAX COLLECTOR



**MARK J. SALADINO**  
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May 16, 2011

To School Finance Professionals:

## COUNTY OF LOS ANGELES SCHOOL DISTRICT GENERAL OBLIGATION BONDS - WHITE PAPER

The recent economic downturn in California has placed a significant financial burden on school and community college districts. This burden has been augmented by budget deficits at the State of California and the continuation of funding cuts and apportionment deferrals aimed at schools. To help manage the current fiscal challenges, many districts have sought to issue debt as one means of meeting their financial needs. While debt issuance can be part of a larger fiscal plan, the use of general obligation (GO) bonds to solve budget problems can pose a serious risk to school and community college districts. We recommend that districts take a conservative approach when issuing GO bonds in order to avoid any violations of State or Federal Law, and to ensure compliance with all tax and regulatory guidelines.

Through our participation in numerous GO bond financings, my office has observed several new financing practices that may place the issuing district at risk of both State and Federal scrutiny. Regardless of whether the GO bonds are issued under the California Education Code or Government Code, my office will not support any of the following practices:

1. **JPA Structure and QSCBs.** The use of a Joint Powers Authority (JPA) to augment a Qualified School Construction Bond (QSCB) issuance provides bond proceeds beyond the amount approved by voters in a GO bond measure. This results in taxpayers being charged a significantly higher rate of interest than the actual market rate for the QSCBs (net of the direct-pay subsidy). The JPA structure with QSCBs resembles the "cash-out" refunding method that in January 2009 was declared by the California Attorney General to be in violation of State Law. The use of this structure exposes the district to potential litigation on the part of local residents and could cause the Internal Revenue Service (IRS) to revoke the district's direct-pay subsidy from the U.S. Treasury.
2. **JPA Structure (Marks-Roos).** Issuing GO bonds through a Marks-Roos structure is generally used to augment construction fund proceeds beyond the amount approved by voters. This increases the cost to local taxpayers and is another example of a "cash-out" financing structure that was declared illegal by the Attorney General in 2009.

3. **Use of Federal Subsidy for District Operations.** In a taxable GO bond financing, the Build America Bond (BAB) or QSCB subsidy must be used as an offset to debt service. Any application of this subsidy to fund district operations will significantly increase the cost to local taxpayers and may result in enforcement actions by the IRS.
4. **Proposition 39 Tax Limits.** If a school district has already exceeded its Proposition 39 tax rate limit of \$30/\$100,000 or \$60/\$100,000, it cannot issue additional debt under that ballot measure. A district cannot avoid the Proposition 39 tax rate limits by issuing GO bonds in only those maturities that do not currently exceed the \$30 or \$60 limitations. Such structures are contrary to the original intent of Proposition 39 and pose a legal risk to the issuing district.
5. **Bond Premium to Pay Costs of Issuance.** A March 1, 2011 letter from the California Attorney General stated that "the law is clear that any premium, even if legitimate, must be deposited into a special fund, applied to pay debt service, and therefore cannot be diverted to pay costs of issuance." The views expressed in this letter from the Attorney General provide clear guidance that Government Code Section 23903 and Education Code Section 15146(f) do not allow for costs of issuance, including underwriter's discount and bond insurance, to be paid from bond premium.
6. **Borrowing from Bond Project Funds.** GO bond proceeds are statutorily limited to qualified capital expenditures and cannot be used to fund operating expenses or payroll disbursements. Borrowing from a GO bond project fund to finance working capital needs is in direct violation of both State Law and Federal Tax Law.

In addition to the above practices, we also wish to highlight a common type of GO bond financing that is exceedingly costly for both school districts and local taxpayers. My office will not support transactions that rely on the following bond structure:

**Long-Dated CABs.** The issuance of capital appreciation bonds (CABs) with maturities greater than 25 years will result in a significantly higher debt burden for GO bond issuers. A 40-year CAB will generate debt service more than ten times (10x) greater than the principal amount of bonds being issued. Unless a district is certain to exceed its Proposition 39 tax rate limits, it should not consider the issuance of CABs. Furthermore, reasonable assumptions for growth in assessed value must always be utilized when sizing a GO bond financing with CABs. If a district elects to issue bond anticipation notes (BANs) as an alternative to a CAB structure, a similarly conservative approach to assessed value must be used. BANs should never serve as a vehicle to extend the total years of debt service beyond the limits set forth in the Education Code and Government Code.

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In order to mitigate the use of those practices referenced in this letter, my department will work directly with local school districts on the structuring and sale of all GO bonds issued in the County of Los Angeles. If you have any questions regarding this letter, please contact Glenn Byers, Assistant Treasurer and Tax Collector, at (213) 974-7175.

Very truly yours,



MARK J. SALADINO  
Treasurer and Tax Collector

MJS:GB:DB:pab  
Pb/db/schldstgobondswitepaper

c: Los Angeles County Office of Education  
California Department of Education  
California State Treasurer  
California Attorney General  
California Association of County Treasurers and Tax Collectors