West Contra Costa USD

Presentation to the Facilities Subcommittee

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CABs in the News

- Capital appreciation bonds continue to be in the news.
    - News coverage of CABs started with articles in the Voice of San Diego last September.
    - Recent articles in California Watch (Thursday, January 31st) and the New York Times (Sunday, February 10th).
    - What's driving the continued media attention?

Case against CABs

- In general, the articles make the case that CABs are overly expensive and pass costs unfairly to future generations.
    - Articles focus on high repayment ratios and long terms.
    - They look to connect specific projects with individual financings.
    - They make the case that all the costs of the specific project are paid by future taxpayers.

Mitigating Factors

- In truth, few financings match the straw man description contained in the articles.
    - School districts typically finance projects on a program-wide (rather than project-by-project) basis, and assess debt structure on an authorization (rather than transaction by transaction) basis.
    - Even when CABs are involved, current taxpayers are almost always paying their share (on a tax rate basis) and tax rates are typically projected to decrease over time (or at least stay level).
    - CABs are most commonly used to smooth future repayment schedules (rather than to shift costs).
    - CAB transactions seem far less egregious when viewed in the context of an entire authorization.

Do the Critics Have a Point?

- Still, the recent attention on CABs has raised some issues worthy of consideration.
  - Did school districts become too comfortable in relying on future tax base growth in designing bond programs?
  - To what extent should future tax base growth be used to increase capacity for future debt versus paying for past issues?
  - Should bond programs funding long overdue facilities improvements be structured differently than bond programs funding necessary maintenance and modernization?
  - How and when should a school district consider de-leveraging a bond program?

Reform Legislation

- California lawmakers have introduced legislation that will curb the use of long-maturity and non-callable CABs.
  - AB 1482 was put together with input from State Treasurer Bill Lockyer and representatives from the County Treasurer organization and has been proposed by Joan Buchanan (D-Alamo) and Ben Hueso (D-San Diego).
  - The legislation will reduce maximum terms on school bonds (from 40 years to 25 years), limit the repayment ratio for individual transactions (to 4 to 1), reduce the maximum nominal interest rates (from 12% to 8%), and require call provisions on any bond maturing in more than ten years.

Impact on Existing Bond Programs

- If AB 1482 is approved, we expect that the most significant impact on the District will come from the reduction in maximum term.
  - We generally agree that the District should be issuing its bonds with call features whenever possible.
  - Although the reduction in maximum interest rate may impact the District's ability to efficiently create premium on its bond transactions, we have already begun discussing alternatives to this past practice.
  - Although the District has no plans to issue bonds with repayment ratios exceeding 4 to 1, the financing team should be careful to structure individual financings with an eye on future flexibility.
  - The twenty-five year term limitation may have significant impact and may reduce individual issue sizes by up to 15% on an apples-to-apples basis.

Back to the Education Code

- In many ways, the new legislation will leave the District in a similar position as to when you were issuing bonds under provisions of the Education Code.
  - Twenty-five year maximum term was widely followed by school district issuers prior to the reform of Government Code bond regulations in 2008.
  - The reform of the Government Code bond regulations was one factor in allowing some of the more aggressive financings during the past four years.
  - Whether it is appropriate for other public agencies (including the State and State-related entities) to be permitted to borrow under the more permissive statutes remains an outstanding question.