PUBLIC TESTIMONY SUMMARY

I-900 STATE AUDITOR'S PERFORMANCE AUDIT:

Opportunities for the State to Help School Districts Minimize the Costs and Interest Paid on Bond Debt (August 24, 2009)

As Heard by the Joint Legislative Audit & Review Sub-Committee on I-900 Performance Audits on September 23, 2009

The performance audit being discussed at this hearing was conducted solely and independently by the office of the State Auditor, under the authority of legislation approved by the voters in Initiative 900. The State Auditor is elected directly by the people of the State of Washington and operates independently of the Legislature and the Joint Legislative Audit & Review Committee. Staff to the Joint Legislative Audit & Review Committee prepare a summary of public testimony on State Auditor reports. These summaries are for informational purposes only, and do not serve as an assessment by committee staff of the findings and recommendations issued by the State Auditor nor do they reflect a staff opinion on legislative intent.

<table>
<tr><td colspan="2">Title: Opportunities for the State to Help School Districts Minimize the Costs and Interest Paid on Bond Debt</td></tr>
<tr><td colspan="2">Audit Scope and Objectives:
The audit examined all district general obligation bonds that were reported to the state Department of Commerce (formerly the Department of Community, Trade and Economic Development) and sold from January 1, 2003, to December 31, 2007.
The primary objectives of the study were to answer the following questions:
• Is the State of Washington providing districts with adequate guidance on how to sell general obligation bonds in the most cost-effective manner?
• If guidance is not sufficient, what are the resulting costs and what can be done to reduce them?
In addition, the report indicates that the audit was conducted in accordance with the required elements of Initiative 900.</td></tr>
<tr><td>SAO Findings:</td><td>SAO Recommendation:</td></tr>
<tr><td>The audit found that, although some districts obtained competitive rates on their general obligation bonds, from 2003 to 2007, districts as a whole paid higher interest costs and fees than they should have. SAO estimates that the districts could have saved between $44.6 million and $79.4 million over that five-year period if they had followed the best practices identified in the report.
The audit also found that Washington school districts could save money if they received more guidance from state government on how to sell bonds.</td><td>The audit recommends that the Office of the Superintendent of Public Instruction work with school districts, educational service districts, and the Office of the State Treasurer to develop guidance and training that follow best practices to incur lower costs on bond sales.
This report does not contain recommendations to the Legislature.</td></tr>
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Agency Responses in Audit Report?	Yes; Appendix E contains separate responses from the Office of the State Treasurer and the Office of the Superintendent of Public Instruction.
Legislative Action Requested?	No

Agencies Testifying:

The Office of the State Treasurer (Jim McIntire, State Treasurer; Ellen Evans, Deputy Treasurer/Debt Management)

The Office of the Superintendent of Public Instruction (Randy Dorn, Superintendent of Public Instruction)

Summary of Testimony from Audited Agencies:

We agree with the report's recommendation. The Office of the Treasurer, working with OSPI, can provide some additional outreach to the school districts to help districts improve the way they issue their bonds. For example, we can work with the School Directors' Association to help it update its school bond manual. However, it is important that we preserve our role as advisor rather than telling OSPI and the local districts what to do. Remember that the savings estimate in the report does not include the costs to districts of hiring financial advisors. We also note that the school bond guarantee program in Washington offers significant savings to districts.

We worked in conjunction with the State Auditor's Office and the Treasurer's Office. There are a number of factors behind school districts' decisions on how to sell bonds. These factors include the services districts receive by taking a certain approach. We have a balancing act in this state between state directives and local decision-making. This audit will heighten the awareness of school districts to find the best opportunities available in the market. Guidance is available for districts such as the OSPI manual, but it does not take the form of requirements.

Other Parties Testifying:

Dan Steele, Washington State School Directors' Association

Barbara Mertens, Washington Association of School Administrators

Randall Pozdena, Regional Bond Dealers Association

Richard Schober, Seattle Northwest Securities

Summary of Testimony from Other Parties:

The Treasurer's Office and OSPI do provide assistance and outreach to school districts, and districts welcome that information and advice. Our association also prepares a bond manual for districts. Our three organizations have worked together and will continue to do that. Local school districts make decisions that make sense for their local communities. The flexibility currently in the system is appropriate. In terms of competitive versus negotiated bond sales, it is likely that school districts had reasons for choosing one over the other. It is not clear from the report whether school districts were given the opportunity to respond to this issue. It is in the best interest of the bond houses to give their school district clients the best advice. The SAO report talks about districts hiring financial advisors; however, the report does not identify the portion of the estimated savings that would be taken up by the costs to districts of hiring these advisors.

We are here in support of the comments offered by the Treasurer and OSPI. We are the connecting link between the school district administrators, the school boards, and the state offices. We also offer a link to the educational service districts. It is our responsibility to ensure that our members are well-informed about these matters. This is an on-going responsibility. A report like this offers a chance to review how well we informed our local districts. We offer our help to the Treasurer and the Superintendent as they move forward on this.

Competitive bond issuance may be a misnomer; it may give a sense that there is a lot of competition underlying this approach. However, because of factors such as a due-diligence requirement, this approach may not be cost-minimizing. A negotiated settlement may sound less competitive, but this may not be the case. The statistical analysis conducted for the audit used a very small sample size, and the statistical findings are ambiguous. A different study conducted using a much larger sample size found no meaningful difference in the cost of issuance using competitive or negotiated approaches. I would urge caution in requiring districts to use one approach over another.

Our firm devotes significant resources to the K-12 school district bond market. In terms of the negotiated approach, our firm represented about 28 percent of the market in 2008. There is tremendous competition in this marketplace. If you add in the work we do as independent financial advisors for individual districts, our firm holds about 40 percent of the market. When acting as a financial advisor, we help our clients determine whether to use the competitive or negotiated approach to their bond sales. A number of the larger, more well-known districts do choose the competitive approach; typically they have higher ratings than other school districts around the state. We are committed to finding ways to save money for our school district clients. We support the intent of the SAO report but not necessarily all of its conclusions.