

**Poway Unified School District
Building for Success
Program Financing
Bond Transaction
Proposition C, Series B**

**Report of Investigation
ESI International, Inc.**

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Introduction

In August 2012, ESI International, Inc. (ESI) was asked to review the circumstances relating to the Poway Unified School District's financing of renovations to its school sites located within the School Facilities Improvement District (SFID), and in particular the August 2011 sale of \$105 million of general obligation bonds. This transaction is formally called, General Obligation School Facilities Improvement District No. 2007-1 of the Poway Unified School District, 2008 Election, Series B, but is referred to as the Prop C, Series B bonds. The school sites involved in the SFID are the sites that lie outside of the District's Mello Roos Community Facilities Districts (CFDs).

Of particular concern to the District and its Board of Trustees were assertions published in media accounts that Poway Unified Schools District had not followed a sound business plan in financing the construction projects, which led the taxpayers within SFID 2007-1 being obligated to repay bonds in an amount that would approach one billion dollars for the initial borrowing of just over \$105 million. Media accounts attributed the causes for the billion-dollar repayment as being the use of capital appreciation bonds maturing in many years, and the issuance of bonds with original premium.

Capital appreciation bonds became the target of critics because of the structure of the bond, that being where interest compounds and is reinvested within the instrument with maturity and payment often being put off for years, and sometimes decades.

With regard to the Prop C, Series B bond sale, ESI was asked to find information that could answer a number of questions being posed concerning the bond sale. Essentially, these questions included:

- 1) Had the District acted responsibly?
- 2) Did the District's advisors provide advice that met the District's needs?
- 3) Was the compensation paid to the advisors reasonable?
- 4) Did the people involved in the bond sale act properly in their transaction roles and in the interests of the District?
- 5) Were the processes followed during the transaction correct?

ESI International Inc. is a California licensed private investigations firm, which conducts a wide range of investigations, but has a particular expertise in fraud and accounting investigations. The principal investigator assigned to this matter was Robert Price, a founder and manager of the firm. Before starting ESI, Mr. Price was an employee of the Federal Bureau of Investigation, beginning his career as a support employee in the San Diego Office in 1976. After receiving a degree in accounting in 1977, Mr. Price was appointed as a Special Agent Accountant in 1978 and served in the FBI's Sacramento and New York City field offices. During that time, Mr. Price specialized in the investigation of financial and economic crimes including government fraud and the corruption of public officials. Mr. Price left the FBI in 1986 and began Economic and Specialty Investigations, the predecessor to ESI International, Inc.

Executive Summary

ESI International, Inc. (ESI) was tasked to conduct a review of the sale of bonds by the Poway Unified School District in August 2011. This transaction is called the Proposition C, Series B transaction.

ESI conducted its inquiry by reviewing a substantial amount of documentation, including written communications regarding this bond sale and other related bond sales. ESI also researched issues that had been raised by critics of the bond sale and the circumstances that led to the bond sale. ESI conducted interviews of people involved in the transaction to clarify and develop points suggested from the review of the documentation and communications.

Observations:

The provisions of Proposition 13 (People's Initiative to Limit Taxation), Proposition 39 (School Facilities Local Vote at of 2000), and to some degree the statewide school funding bond measures like Proposition 55 (Kindergarten-University Public Education Facilities Bond Act of 2004), have created a situation where school districts finding the need to raise money to build new schools or improve existing sites are to operate within a set of regulations and constraints that define when and how much money the school district will be able to raise once it has the approval of the electors.

Because they do not have in-house capabilities to handle large financial transactions without assistance, school districts like Poway Unified have turned to consultants to guide them through the construction fund raising process. These consultants have specialized skill sets, experience in similar campaigns, and access to public and proprietary data that allows the consultant to fashion a program to meet the school district's needs. Factors involved in the construction fund raising process include estimating how much money can be raised and under what terms the electors will likely authorize a bond measure. Having this information improves the school district's chances at having a successful bond measure. Consultants also determine how much debt the school district can issue and service, while estimating and negotiating the cost of the debt repayment. Consultants help the district to comply with IRS regulations concerning the issuance of tax-exempt municipal bonds, and navigate the regulatory steps in selling the bonds to the public.

In the case of Poway Unified's *Building for Success* program, consultants were brought in early to work with the District to identify needs. Thereafter the consultants put a

financing program together to generate the amount of money that the school district needed for its construction program.

In 1998 Poway Unified began planning its *Building for Success* program to improve the older schools in the district by modernizing the older schools and thereby creating parity with the newer schools in the District. By the time the construction was completed in 2011, the District asserts that it had expended about \$543 million for construction and had completed the facilities and financing arrangements ahead of schedule without deviating from the estimates that the District gave to the electors regarding the tax rate and the length of the bond terms during the bond measure elections.

The District financed \$377 million through its bond authorizations with Proposition U contributing \$198 million and Proposition C contributing \$179 million. Other sources of funds included state grant matching funds, developmental revenues, and other district revenues such as annual Redevelopment Tax Increment revenue (RDA). Property taxpayers from the area of the District where the renovated schools are located will pay an estimated \$55 per \$100,000 of assessed valuation to service the debt. Over the length of the repayment period, these payments total just over \$1.6 billion. Of that amount, \$981 million will go to service the August 2011 issue of \$105 million in bonds.

The issuance of bonds with original premium provided funds for the District that were used to retire interim financing, pay the interest and other costs on the interim financing, and pay the costs of issuance on the sale of the general obligation bonds.

Findings:

ESI found that the District's consultants put together a strategy to finance the *Building for Success* program and to deliver the funds that the program needed on a timely basis.

ESI found that District administrators and board members received the information necessary to make informed decisions as to whether or not to proceed with the consultants' financing plans and bond sales.

ESI found that the District accepted the advice of the consultants and implemented the program. This implementation led to the accomplishment of the District's program goals ahead of schedule.

ESI found that although the bond transactions had some complex and potentially controversial components, the District's consultants and lawyers anticipated and understood the problems and took action to minimize the potential exposure to the District while preserving the

District's goal of successfully completing the *Building for Success* program within the financial guidelines approved by the electors.

ESI found that by issuing the bonds with premium, the District preserved the amount of the bond authorization it received from the electors to be used in the construction of the facilities. The use of premium in this manner did increase the total amount that taxpayers will repay, although the estimated tax rate was unaffected and remained the same as represented to the electors in the bond measures.

ESI found no fault in the District's use of original premium from the Proposition C, Series B bond issuance to pay the interest resulting from interim financing and retire the interim debt. ESI found that this action was consistent with the recent enactment of AB 794, which is the amendment of Education Code Section 15150, and the findings of the Superior Court in the validation actions undertaken by the District.

ESI found that there is a controversy concerning the District's use of original premium to pay the costs of issuance of the Proposition C, Series B bond sale. In a March 2011 letter to Poway Unified's bond counsel, the office of the attorney general asserted that the use of premium in this fashion was not authorized by law.

However, in a validation action, as they had done with earlier bond issues, the District's bond lawyers sought and received a judgment of the Superior Court favorable to the use of premium in the manner described above. Additionally, ESI's research supported assertions by the District and its consultants that school districts at the time of the August 2011 bond sale were regularly using original premium to pay for costs of issuance.

ESI found no evidence that anyone involved in the transaction acted improperly within his or her respective role in the transaction. ESI also found no evidence that anyone involved in the transaction acted in a manner that was harmful to, or in conflict with, the District's interests.

With regard to the consultant compensation, ESI found that the amounts paid to the financial consultants for the Proposition C, Series B transaction and some of the other Poway Unified bond issues exceeded median amounts reported in a published study that surveyed issuance costs for 2009-2011. However, ESI does not know if the study's findings are applicable to the Poway Unified bond issues because the author of the study acknowledged that, "there was no effort to account for differences in the type or level of services provided by members of the financing team."

It is for this reason, and because of the likelihood that any survey that ESI would

conduct or locate would have similar constraints, ESI feels that the reasonableness of the fees charged by the consultants could best be determined by the District by taking into consideration the results obtained and the District's ability to pay for those results. Similarly, ESI looked to the District and its financial consultants to review questions regarding financial consultant compensation calculations that were posed by ESI during this investigation. The District and its consultants reviewed the calculations and informed ESI that they agreed with the calculations as originally submitted by the financial consultants, and that the District was completely satisfied with the amount of compensation paid to the financial consultants and the work that the consultants did.

ESI explored the possibility that that District acted in error by not securing a redemption provision in the Proposition C, Series B issue. Because ESI cannot accurately recreate the market conditions at the time of the sale in order to gauge the market's response to a bond sale involving this quantity and quality of capital appreciation bonds with premium and a redemption provision, ESI can make no determination at what price the redemption provision could have been included, if at all. Other than the cost of the redemption provision, there are other factors that could turn an issuer away from a redemption provision, including whether the issuer's revenue stream would likely allow the issuer to redeem the bonds early.

Methodology of the Investigation

ESI's review of the bond program at Poway Unified School District focused on circumstances involving the August 2011 sale of the Proposition C, Series B bonds which were officially called the General Obligation School Facilities Improvement District No. 2007-1 of the Poway Unified School District, 2008 Election, Series B. The amount of the bonds sold was \$105,000,149.70. Because these bonds were just one transaction in a long series of transactions to fund the Poway District's *Building for Success* program, other bond transactions were reviewed but only to the extent necessary to understand the Prop C, Series B transaction.

During the investigation ESI reviewed thousands of pages of documentation, presentations, and communications. These included the official bond sales documents, legal filings, forecasts, projections, demographic material, proposals and communications between District administrators, members of the bond team, and outside entities.

ESI also conducted interviews of District administrators, employees, and outside consultants regarding the bond transactions.

ESI engaged in research to develop information relating to other bond issues occurring at the same time to develop a benchmark concerning these types of transactions and to verify information relating to the Prop C, Series B transactions provided by witnesses.

During this investigation, ESI relied upon the earlier work of the District's auditors and therefore did not retrace funds that had been disbursed for the bond sales or the construction projects.

Background Information

At the outset of this investigation ESI was provided with information from the District regarding the origin and operation of the District's *Building for Success* program. For the purposes of this report, the *Building for Success* program name is used to describe the planning, financing and construction program where schools located outside of the District's CFDs were modernized.

Materials provided by the District recount the situations that led to the *Building for Success* program and the subsequent funding of that program through taxpayer taxes and bond sales. According to the materials, and ESI interviews with District administrators, in 1992 the District began building new facilities using money raised through the formation of Mello-Roos CFDs attached to new housing developments being built within the District boundaries. By 1998 there was discussion within the District regarding equity in the facilities being provided to students living outside of the CFDs and who were attending the oldest schools in the District and those students attending the new, or relatively new schools in the District's CFDs.

The discussions within the District at the Superintendent's Cabinet level moved to community forums that were held to discuss the possibility of improving all 24 of the non-CFD schools. Following these discussions, the Board ordered the formation of the School Facilities Improvement District (SFID), which included 24 schools that served students living outside of the CFDs. In rough geographic terms, the SFID encompassed most of the District territory immediately adjacent to I-15 and areas east of the I-15 in the mature portions of Rancho Bernardo and Poway.

Following the establishment of the SFID, the Board voted to place a bond measure on the November 1999 ballot, the purpose of which was to fund improvements to the SFID schools. The improvements would include adding classrooms, upgrading or replacing heating, ventilation, and air conditioning systems, upgrading electrical systems, upgrading plumbing and sewer systems, upgrading technology infrastructure, meeting American with Disabilities Act requirements, and upgrading the schools to meet current safety codes.

The November 1999 bond measure, which was called Proposition A and requested \$149 million, failed to receive the required 66.7% of the vote when 64.37% of the voters approved of the measure. In November of 2000, the District again placed a bond measure on the ballot. This was called Proposition Y and requested \$156 million. Proposition Y failed when 62% of the voters approved, which was short of the 66.7% needed for the measure to pass.

Although Proposition Y failed to pass in November of 2000, statewide Proposition 39 was successful in the same election. Proposition 39 reduced the requirement for passage of school bond measures from two-thirds to a 55% “super majority.” When enacted, Proposition 39 was combined with Assembly Bill (AB) 1908 which limited the proposed increase in taxes to \$60 per \$100,000 of assessed valuation for unified school districts and \$30 per \$100,000 for high school and elementary school districts. The new legislation also required the formation of oversight committees and the institution of annual performance and financial audits.

Of all the Proposition 39 and AB 1908 provisions, the 55% super majority was the factor that would the increase passage of school bond issues to levels not generally enjoyed by school districts in California, while the \$60 per \$100,000 of assessed valuation would become the most vulnerable aspect of the bond transactions toward the middle of the decade, when housing prices stagnated, then decreased and new home construction slowed.

In November 2002, Poway Unified put Proposition U on the ballot, requesting \$198 million for the *Building for Success* program. This time the measure passed with 57% of the vote.

In August 2003, the District sold \$75 million in general obligation bonds, which would be repaid over 24 years. This was the first of an anticipated series of four bond transactions where the District would sell the bonds authorized by Proposition U as assessed values in the SFID increased in order to support the debt service on the bonds with less than the \$60 tax per \$100,000 of assessed valuation required by Proposition 39 and the District’s bond measure. The next bond sale was scheduled for August 2006, when \$45 million would be sold, followed by a sale in August 2009 when \$44 million would be sold and finally a sale in August 2013 when \$34 million would be sold.

In March 2004, the voters in California approved Proposition 55, the Kindergarten-University Public Education Facilities Bond Act of 2004, which provided for the sale of more than \$12 billion in bonds to be used to relieve overcrowding and to repair older schools. Districts accessing the state funding would be required to have matching funds on hand. The District and its consultants realized that to access the full amount of state funding for which the District qualified, it would need the locally generated money for its construction projects earlier than the general obligation bond issue schedule would allow.

In August 2004, the District borrowed \$100 million, advancing funding against the future issuance of general obligation bonds under Proposition U. This was termed the 2004 School Facility Bridge Funding Program. At the time of the 2004 bridge funding, the District had estimated that the cost of construction on the SFID improvement projects would cost nearly \$298

million, \$198 million of which would come from the Proposition U general obligation bonds. State funding from the then recently passed Proposition 55 would contribute over \$71 million and CFD and RDA revenue would provide \$18.5 million. Because of the state requirement that the District have its portion of the construction costs in hand to receive the then immediately available \$62.92 million in state matching funds, the District proceeded with the bridge-funding program. A component of the bridge-financing program proposed by the District's financial consultants was to have the cost associated with the bridge financing paid with funds raised through the issuance of general obligation bonds with original premium.

In November 2006 the District sold just over \$119 million in current interest and capital appreciation bonds, with a \$9.7 million of original premium, from the remaining Proposition U authorization. About \$72.5 million of the proceeds went to pre-pay the bridge financing. The premium was used to pay the costs of the bridge financing, including interest expense, and the cost of issuance for the instant bond issue. About \$46.8 million that was raised from this issue went to the construction program.

Following the issuance of most of the bond authorization from Proposition U, the District recognized it did not have the funds necessary in Proposition U to accomplish its goal of bringing the SFID schools into parity with the CFD schools. In September 2007, the District hired a consultant to gauge support for a bond measure, which would be placed on the February 2008 ballot to continue to fund the *Building for Success* program. The consultant learned that there was adequate support by the electors for a new ballot measure when they were asked if they would support the bond measure if the measure would raise money without raising the tax rate, but would extend the tax rate to complete the second phase of facility renovations.

In February 2008, with 63.9% of the vote, the electors passed Proposition C, a \$179 million bond measure, requesting new bond authorization without an increase in the existing tax rate. The measure asked:

To provide safe and modern school facilities, improve student learning, and qualify for approximately \$20 million in State matching money, shall School Facilities Improvement District No. 2007-1 of the Poway Unified School District issue \$179 million in bonds at legal interest rates to upgrade aging classrooms, libraries, science & computer labs; replace roofs, plumbing, heating, ventilation and electrical systems; improve fire alarms and school security; remove hazardous materials; fund needed facilities, subject to mandatory audits, independent citizens' oversight and without an estimated increase in tax rates?

The measure also included language relating to the tax rate as follows:

Stabilization of Existing Tax Rates: It is the intention of the Poway Unified School District, on behalf of the Improvement District, that the existing maximum tax rates which may be levied to pay for the bonds of existing School Facilities Improvement District No. 2002-1 of the Poway Unified School District (which overlies the majority of the Improvement District) fifty-five dollars (\$55) per year per one hundred thousand dollars (\$100,000) of taxable property within Improvement District No. 2007-1 when assessed valuation is projected by the District to increase by the amount allowed by law in accordance with Article XIII A of the California Constitution shall not be increased as a result of the authorization and issuance of bonds by the Improvement District as described in this bond measure.

In June 2008, the District sold \$92.6 million in Lease Revenue Bonds, as part of a new interim-financing plan. To reuse the asset pledged in the earlier Proposition U Bridge Financing Program, \$14.6 million of the proceeds from the instant sale pre-paid the Proposition U Bridge Financing Program.

In January 2009, the District sold \$74 million of general obligation capital appreciation bonds with \$9.5 million of original premium. The \$74 million went to the construction fund and the premium went to pay the costs of issuance of the instant bond measure and more than \$8 million paid costs relating to the interim financing, including interest expense.

Also in January 2009, the District sold \$3.7 million in general obligation capital appreciation bonds, which exhausted the authorization from Proposition U. These proceeds went to the construction program.

In March 2010, the District sold \$25 million of bond anticipation notes. The proceeds from this sale went into the building fund.

In August 2011, the District sold \$105 million of general obligation capital appreciation bonds exhausting the authorization from Proposition C. These bonds were sold with an original premium of \$21.4 million. The proceeds from this sale were used to make a deposit to partially pre-pay the outstanding lease revenue bonds (\$98.7 million); retire the bond anticipation notes (\$26.3 million); pay the costs of issuance of \$569,114; and to pay the underwriter's discount of \$813,751.

How Poway Funded the Building for Success Program

With the passage of Proposition U, where electors approved the bond measure that would allow Poway Unified to sell \$198 million of general obligation bonds, Poway Unified had to determine how it would raise the money, and at what pace it would proceed with the construction phase of the *Building for Success* program.

There were a number of factors that played a part in this strategy, including the necessity for Poway Unified to capture as much state money as possible to supplement the funds available to accomplish its building goals and to progress as quickly as possible to allow students to begin enjoying the benefits of the renovations. Additionally, Poway Unified desired to move ahead quickly to try to avoid increases in what it maintained were increased costs due to construction cost inflation occurring prior to 2008.

At the simplest level, Poway Unified then had just a few goals to attain, those being to renovate or rebuild the facilities; to accomplish the construction projects quickly; to stay within the estimated \$55 per \$100,000 of assessed value tax rate; and to raise enough money under those guidelines that when these funds were added to funds available from other sources, the total would be enough to pay for the program.

Poway Unified also wanted to raise money in a manner that would keep it from having to stop construction while waiting for additional funding. Poway Unified maintained that this strategy would avoid the financial costs and disruptions to students and their educational programs that would be caused by re-staging during the longer or renewed construction periods.

Frequently the amount of money that the electors authorized, when compared to what the school district's tax revenue stream will actually support, creates a situation where the revenue stream falls short of supporting the amount of money that the school district needs to complete its desired construction projects. Poway Unified's financial consultant told ESI that because of financing problems, many school districts fall far short of their goals and ultimately complete less than what they wanted to accomplish. As noted in the Citizen's Oversight Committee community report of March 12, 2012, and inferred by its submission of the final audit report of the Proposition C Bond Building Fund, dated January 31, 2012, Poway Unified has successfully funded its *Building for Success* program and has completed the construction work.

Poway Unified's strategy for maintaining construction cash flows during its extensive building projects at times when its consultants determined that it was not possible or advantageous to issue general obligation bonds immediately, was to engage in a series of interim financing transactions. Poway Unified used interim financing strategies, starting with the Proposition U authorization and continuing with the Proposition C authorization. The investment vehicles were different at different times. These included Certificates of Participation (COPs), Lease Revenue Bonds (LRBs), and later Bond Anticipation Notes (BANs).

Using the interim funding transactions, Poway Unified began and continued its construction projects and applied for and successfully accessed state money that would not have been released if Poway did not have matching funds in hand at the time of the funding transaction. Additionally, because the release of state money was not tied to the progress of the construction project or the costs incurred therein, the District had to have funds available to meet construction bills that came due before the state funds were released.

In all, Poway Unified told ESI that it obtained \$92,553,994 of state money for its SFID construction project by using its consultant's plans to issue interim debt to supplement the amount of money it could raise from an immediate general obligation bond sale and then use the sale of the remaining general obligation bonds in conjunction with other funds available to retire the interim financing securities.

Capital Appreciation Bonds

The primary type of bond that Poway Unified sold to raise the amount of money it spent to retire the interim debt and finance the *Building for Success* program was the capital appreciation bond. The Municipal Securities Rulemaking Board defines a capital appreciation bond as:

A municipal security on which the investment return on an initial principal amount is reinvested at a stated compounded rate until maturity, at which time the investor receives a single payment (the "maturity value") representing both the initial principal amount and the total investment return.

Capital appreciation bonds are widely used in California by school districts to provide funds in the present day when existing debt, or a lower than needed assessed valuation, precludes servicing new debt immediately. In November 2012, the Los Angeles Times published a listing of more than 500 capital appreciation bond issues by school and community college districts in California over the past few years.

In the case of Poway Unified, the amount of money that it could put into the *Building for Success* program was limited by state law, primarily having its origin in Propositions 13 and 39; and by Poway Unified's statement to the electors in the Proposition C ballot measure that the \$179 million of new money would be raised "without an estimated increase in tax rates."

Because Poway Unified had existing debt from Proposition U that was being paid from the SFID's tax revenue stream, and that existing debt was estimated as requiring between \$46.41 and \$53.15 of the tax per \$100,000 of assessed valuation; there was very little of the tax revenue stream remaining to begin repaying additional Proposition C debt.

To live up to its pledge that the new Proposition C money would be obtained without an estimated increase in the tax rate, Poway Unified's consultants proposed a new plan of interim financing that would provide funds immediately and would later be taken out by the sale of general obligation bonds issued with original premium.

Findings of the Investigation

At the beginning of the engagement, ESI was asked to find the answers to a number of questions posed by the Superintendent of the Poway Unified School District, John Collins. The following is a discussion of ESI findings in response to these questions:

Did the District act responsibly?

During its investigation, ESI learned that the overall strategy for the bond sales was the product of years of planning and discussion by the finance team, combined with knowledge of changing government regulations and market conditions. Each member of the team, had specific responsibilities, but the overall product was a combination of efforts, some of which overlapped. The efforts led to the formation a proposed structure or structures for the bond sales. These scenarios were then presented to the District administrators, some of whom had worked actively on the development of the strategy, and then to the board of education.

Through investigation ESI located a number of documents that explained the proposed bond sales. ESI established that consultants, attorneys, and the underwriter met with the board of education at board meetings and discussed the proposed strategies. A proposed strategy was then adopted by the board of education, and through a vote steps were taken to implement the strategy and accomplish the sales.

At various stages during the run up to the bond sale, events occurred which required the finance team to update the board. In the case of the August 2011 sale, these instances included the receipt by bond counsel of a letter from the California Attorney General critical of the District's plan to pay cost of issuance out of premium from the sale, and to a lesser degree critical of the amount of premium being raised during the sale. Additionally, for the August 2011 bond sale, finance team members met with the board to examine the overall repayment costs of the bond sale under two strategies, the first of which used capital appreciation bonds over a longer term, using only an extension of the tax rate. The second strategy was a scenario where the tax extension strategy would be abandoned in favor of raising the tax rate, which could have effectively doubled the amount of taxes that the property owners would be paying, but would repay the bonds earlier, and save about one half of the cost.

ESI's investigation examined the circumstances surrounding the sale of general obligation bonds in August 2011. The process leading up to the sale was long, spanning nearly a year. ESI learned that during the period between the time that Poway began looking at ways to refund the interim financing from the Proposition C authorization and the time that the bonds were actually sold, a number of things took place in the municipal bond market that at first caused delays and later presented an opportunity to sell bonds and receive the amount of money necessary to clear the interim financing.

Findings:

With the closing of the August 2011 bond sale the District completed its original bond measure financing, obtaining a rate that allowed the District to make a contribution to retire the interim debt and observe its intention not to raise the tax rate to do so.

At the time of the sale, the municipal bond market had improved for issuers and favorable changes in the government code opened an opportunity where the bonds could be sold at a price, term, and with a premium that would clear all but a small portion of the interim debt used to construct the schools. This would remove the District's general fund from the financing mix, because the general obligation bonds are payable only from property tax revenue, unlike the interim financing, which could require repayment from the general fund.

Prior to selling the bonds the District took the bond transaction through a validation action in Superior Court where it was unopposed and a judgment was entered in the District's favor.

The Board had received presentations regarding the bond transaction and had approved the sale. Updates were made to the Board as the date of the sale approached. These were received without opposition or calls for changes in the sale transaction by the board.

The District and its consultants made calculations, which determined that with the forecast growth in the assessed valuation, the District had enough of a tax revenue stream to service the debt generated by the sale of the bonds. This would however require the use of capital appreciation bonds and a forty-year term.

The District, the board of education, the District's consultants, and the District's lawyers were all aware that the longer term and the use of a capital appreciation bond would carry a heavy overall interest cost and that the amount that would ultimately be repaid would be about \$1 billion.

The District, the board of education, the District's consultants, and the District's lawyers were all aware that if they abandoned their promise to the electors that the tax that related to Proposition C would not be assessed on top of the earlier tax from Proposition U, and instead assessed an additional \$60 rate, the resulting tax revenue stream would be large enough to retire the bond debt earlier at just over one half the cost of the longer term bonds. With this in mind, the District did not stray from the tax estimate that was described to the electors, and selected the bond transaction that would not require a larger tax rate but would take more time to repay.

By completing the original financing transactions for the *Building for Success* program with the bond sale in August 2011, the District removed uncertainty and potential future risk that would be involved if the transaction was postponed. The types of risks that could be avoided by closing the transaction in August 2011 would be the risk from the potential worsening of the municipal bond market for issuers, or changes in government regulations that could limit the District's ability to sell the types and amounts of bonds needed to retire the interim financing.

**Did the District's advisors provide advice to identify and meet
the District's needs?**

Findings:

The financing plan proposed by the consultants and adopted by the District provided the funding necessary for the *Building for Success* program on a timely basis. Advice provided by the consultants contributed to the following:

Market conditions and the use of interim financing with a streamlined construction timetable accomplished the District's building goals early, which allowed students to begin using improved facilities early.

The District avoided undue disruption to the educational process by providing the cash flow to complete work on each school in a fashion that discouraged stopping, starting and re-staging.

By completing the financing plan and general obligation bond sales early, the District avoided possible downturns in market conditions for bond issuers and possible adverse regulatory changes, both of which could have decreased the amount of money that could be raised.

The decision to issue the capital appreciation bonds without a redemption provision was an informed decision based upon the added cost of such a provision and the chance that the District would ultimately not be financially able to take advantage of the provision. Including a redemption provision could have changed the marketability of the bonds and decreased the amount that the District would realize from the bond sale.

Was the Compensation Paid to the Advisers Reasonable?

Findings:

ESI found that the amounts paid to the financial consultants for the Proposition C, Series B transaction, and some of the other Poway Unified bond issues, exceeded median amounts reported in a published study that surveyed issuance costs for 2009-2011. However, ESI does not know if the study's findings are applicable to the Poway Unified bond issues because the author of the study acknowledged that, "there was no effort to account for differences in the type or level of services provided by members of the financing team."

It is for this reason, and because of the likelihood that any survey that ESI would conduct or locate would have similar constraints; ESI feels that the reasonableness of the fees charged by the consultants could best be determined by the District by taking into consideration the results obtained and the District's ability to pay for those results. Similarly, ESI looked to the District and its financial consultants to review questions regarding financial consultant compensation calculations that were posed by ESI during this investigation. The District and its consultants reviewed the calculations and informed ESI that they agreed with the calculations as originally submitted by the financial consultants and that the District was completely satisfied with amount of compensation paid to the financial consultants and the work that the consultants did.

Did the people involved in the bond sale act properly in their transaction roles and in the interests of the District?

Findings:

ESI found no evidence that anyone involved in the transaction acted improperly within his or her respective role in the transaction. ESI also found no evidence that anyone involved in the transaction acted in a manner that was harmful to or in conflict with the District's interests.

Were the processes followed during the transaction correct?

Findings:

Procedurally there are a number of steps that the District, its lawyers, consultants, and underwriters have to accomplish to successfully and legally issue bonds. The District's responsibilities extend to obtaining the approvals for the bond sale from the Board of Education through resolution, and obtaining the certifications and documentation required for the public sale of the debt. In all cases that ESI reviewed, ESI found that the documentation was complete and the District had followed its procedures for obtaining Board approval.

Other requirements imposed on the District, such as providing audits and using a Citizens' Oversight Committee were observed by the District.

ESI found that the law firms representing the District in the bond sales provided the needed opinions for the sales, gave legal opinions to the District concerning the contemplated bond sales where needed, interfaced with governmental agencies where required, and successfully brought validation actions before the Superior Court when clarification was needed for aspects of their legal opinions. The law firms involved in the transactions were found to have fee agreements in place with the District.

ESI found that the bond underwriter provided disclosures to the District with regard to its services when required by the regulatory agency, had a fee agreement in place with the District, and provided the District with details regarding the transaction and the planned disbursement of funds on a timely basis.