

The American Recovery and Reinvestment Act of 2009; What it Means for School District Financing Options



Presented to:

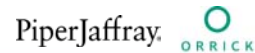
California's Coalition for Adequate School Housing
March 2009 Workshops
Tuesday, March 24, 2009, Sacramento, California
Friday, March 27, 2009, Ontario, California

Presented by:

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Piper Jaffray & Co.

Topics To Be Covered

1. Big Picture — State Law Perspective
2. Build America Bonds (BABs)
3. Tax Credit Bonds (QSCBs, QZABs, QECBs & New CREBs)
4. Changes Intended to Improve Market for State and Local Obligations



Big Picture — State Law Perspective

- The American Recovery and Reinvestment Act of 2009 (the “Recovery Act”) does not expand the debt financing techniques available to school districts under State law
- The Recovery Act and existing federal law make additional features (i.e., tax credits, etc.) applicable to debt instruments permitted under existing State law if an issuer elects and the debt issuance meets the federal requirements
- Federal provisions create subsidy and tax credit bond programs (not grant programs)
- Use of the term “bonds”

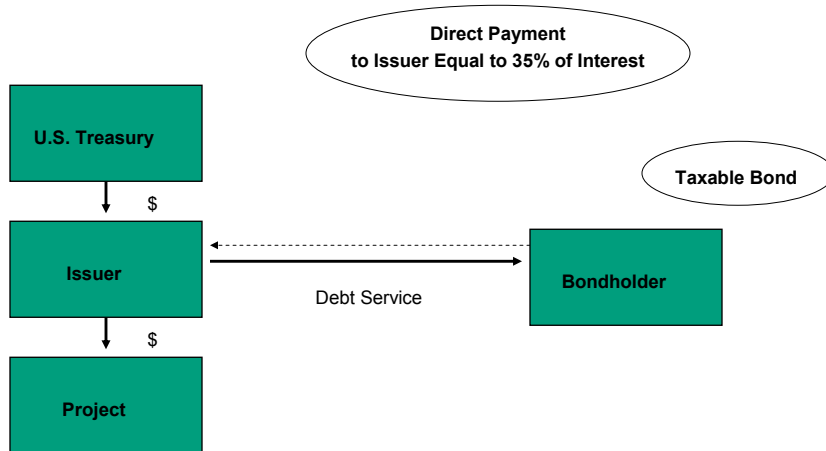
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Build America Bonds (BABs) — What are they?

- All State and local government issuers may issue BABs
- The interest on BABs is “taxable”
- The bonds must be a “governmental bond” (i.e., private use is limited) and have no more than a *de minimis* amount of original issue premium
- Issuers elect to receive either a direct federal cash subsidy with respect to certain BABs (“Subsidy BABs”) or to provide bondholders with a federal tax credit (“Credit BABs”)
- BABs may be issued in 2009 and 2010
- Tax-exempt bond rules apply to BABs (e.g., arbitrage rebate, too much private use will jeopardize the subsidy)

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Direct Subsidy – Build America Bonds



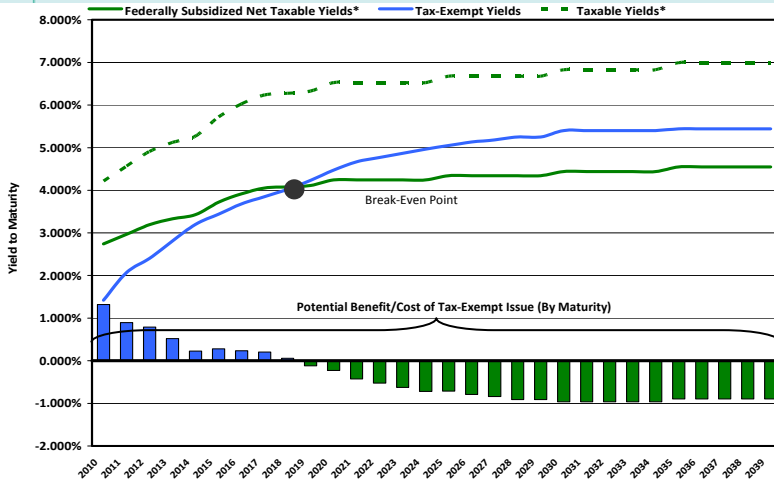
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How Do Direct Subsidy BABs Work?

- A Federal subsidy equal to 35% of the interest will be paid to the issuer
- Direct Subsidy BABs may be issued for new money capital expenditures (no working capital financings)
- 100% of the sale proceeds of a BAB must be used for:
 - capital expenditures
 - costs of issuance not exceeding 2% of the issue price
 - a reasonably required debt service reserve fund

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Potential Benefits of Federally Subsidized Taxable Issues



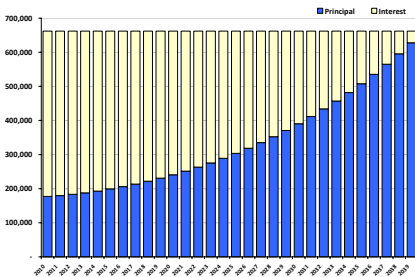
* Assumes non-callable structure

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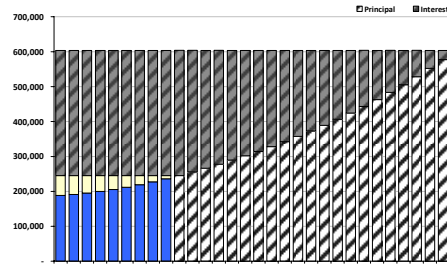
Hypothetical Comparison of Tax-Exempt vs. "Hybrid" Approach

Fully Tax-Exempt Bond Structure Scenario



Par Amount:	\$10,000,000.00
Total Debt Service:	\$19,857,596.13
TIC:	5.152%

"Hybrid Bond" Structure Scenario



Note: Hashed bars represent federal subsidized taxable debt service

Par Amount:	\$10,000,000.00
Total Debt Service:	\$18,112,698.28
Hybrid Effective TIC:	4.358%

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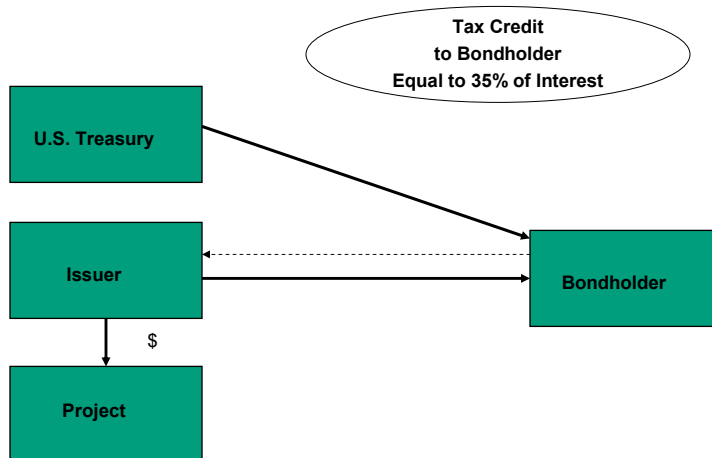
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Direct Subsidy BABs — Implementation

- Waiting for guidance from IRS re: implementation of program:
 - Register bonds with IRS?
 - How do you supply information re: interest amounts and payment dates?

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Tax Credit – Build America Bonds



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How Do Tax Credit BABs Work?

- In lieu of cash subsidy paid to the issuer, a federal tax credit equal to 35% of the interest is provided to the bondholder
- Unlike Direct Subsidy BABs, Credit BABs may be issued for both refunding purposes and working capital purposes
- If credits cannot be used in a tax year, they may be carried forward
- The tax credits may be stripped from the bond and separately sold

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Tax Credit Bonds

- A. Qualified School Construction Bonds (QSCBs)
- B. Qualified Zone Academy Bonds (QZABs)
- C. Qualified Energy Conservation Bonds (QECBs)
- D. New Clean Renewable Energy Bonds (CREBs)

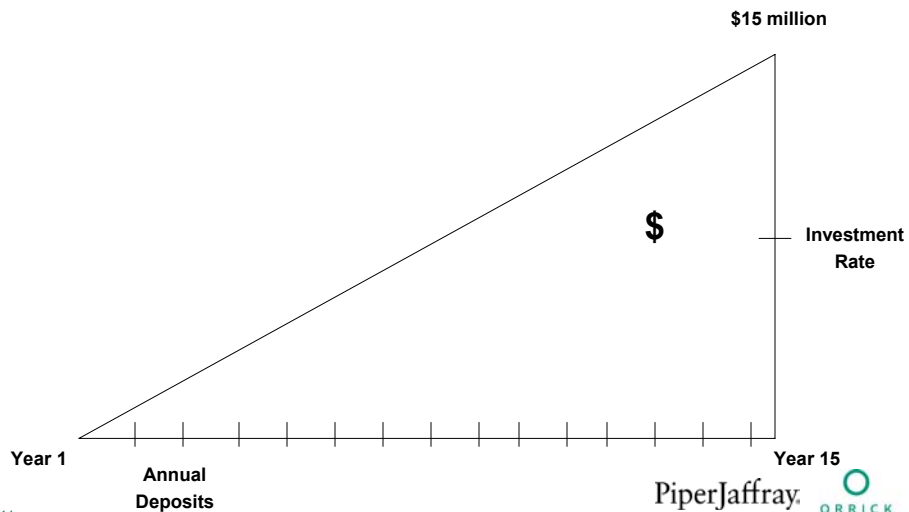
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How Do Tax Credit Bonds Work?

- Tax Credits to bondholders in lieu of issuer interest
- New money only
- Proceeds in project fund not subject to arbitrage rebate provided 100% spent within 3 years
- Funds can be set aside annually by the issuer to repay the bonds and investment earnings may be retained up to stated limits (i.e., possible to earn “arbitrage” in a sinking fund)
- The tax credits may be stripped
- Bullet maturity (14 – 15 years)

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Investment of Sinking Fund



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Qualified School Construction Bonds

- Permitted Issuers: States and certain school districts
- Eligible Projects: Construction, rehabilitating or repairing public school facilities and acquiring land for public school facilities
- Tax Credit Bonds: Bondholders are provided a federal tax credit in lieu of interest by the issuer

Policy is to provide issuers with a 0% cost of funds

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Qualified School Construction Bonds (continued)

- Volume Cap: \$11 billion – 2009
\$11 billion – 2010
- Allocation Process: 60% to States in proportion to the respective amounts of government funds each State is eligible to receive under the Federal Elementary and Secondary Education Act of 1965

40% to 100 largest school districts and 25 school districts chosen by Secretary of Education
- Prevailing Wages: Federal Davis-Bacon prevailing wage rules apply to projects financed with proceeds of such bonds

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Qualified Zone Academy Bonds

- Permitted Issuers: School districts
- Eligible Projects: Renovation, equipping or training teachers and personnel at qualified schools (no new construction)
- Tax Credit Bonds: A “tax-credit bond” that provides bondholders with a federal tax credit against income and seeks to provide issuers with a 0% cost of funds

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Qualified Zone Academy Bonds (continued)

- Volume Cap: \$1.4 billion – 2009
\$1.4 billion – 2010
- Allocation Process: Among States on the basis of population below poverty line
- Prevailing Wages: Federal Davis-Bacon prevailing wage rules apply to projects financed with proceeds of such bonds

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Qualified Zone Academy Bonds — Qualifications

- To be eligible to use a QZAB, 100% of the proceeds must be used for a “qualified purpose” with respect to a “qualified zone academy” established by an eligible local education agency
- The school or program must receive written commitments from private entities to make “qualified contributions” having a present value of not less than 10% of the proceeds of the QZAB

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Qualified Zone Academy Bonds — Qualified Purpose

- A “qualified purpose” with respect to any qualified zone academy means any of the following:
 - Rehabilitating or repairing the public school facility in which the academy is established
 - Providing equipment for use at such academy
 - Developing course materials for education to be provided at such academy
 - Training teachers and other such personnel in such academy
- Even though permitted under the QZAB law, if the QZAB is structured as part of a lease financing, expenditures on developing course materials and teacher training will not be permitted under the Education Code

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Qualified Zone Academy Bonds — Qualified Zone Academy

- A “qualified zone academy” includes any public school or academic program within a public school (below the post-secondary level) if:
 - such school or program is designed in cooperation with business to enhance the academic curriculum, increase graduation and employment rates, and better prepare students for the rigors of college and the increasingly complex work force;
 - the comprehensive education plan of such school or program is approved by the governing school district and the students in such school or program are subject to the same academic standards and assessments as other students; and
 - either the school is located in an empowerment zone or enterprise community or there is a reasonable expectation as of the date of issuance of the bonds that at least 35% of the students attending such school or participating in such program will be eligible for free or reduced cost lunches under the federal school lunch program (National School Lunch Act).

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Qualified Zone Academy Bonds — Qualified Contributions

- A “qualified contribution” includes any contribution (of a type and quality acceptable to the eligible local education agency) of:
 - equipment for use in the qualified zone academy (including state-of-the-art technology and vocational equipment);
 - technical assistance in developing curriculum or in training teachers in order to promote appropriate market driven technology in the classroom;
 - services of employees as volunteer mentors; or
 - internships, field trips, or other educational opportunities outside the academy for students.

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Qualified Energy Conservation Bonds

- Permitted Issuers: All types of State and local government issuers
- Governmental Bonds/
Private Activity: At least 70% of each state's volume cap allocation must be used for governmental purpose bonds

Up to 30% of each state's volume cap allocation may be used for private activity bonds, meaning proceeds may be loaned to private companies and/or for privately owned or operated projects
- Tax Credit Bonds: A "tax-credit bond" designed to provide the issuer with a 70% interest subsidy

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Qualified Energy Conservation Bonds (continued)

- Volume Cap: \$3.2 billion
- Allocation Process: Based on State population
- Prevailing Wages: Federal Davis-Bacon prevailing wage rules apply to projects financed with proceeds of such bonds

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Qualified Energy Conservation Bonds (continued)

Projects that may be financed with QECBs include the following categories:

Type I – Capital expenditures incurred for purposes of —

- Reducing energy consumption in publicly owned buildings by at least 20%,
- Implementing green community programs,
- Rural development involving the production of electricity from renewable energy resources, or
- Any facility eligible for the production tax credit under Section 45 of the Internal Revenue Code (*i.e.*, New CREBs projects).

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Qualified Energy Conservation Bonds (continued)

Type II – Expenditures with respect to research facilities and research grants to support research in —

- Development of cellulosic ethanol or non-fossil fuels,
- Technologies for the capture and sequestration of carbon dioxide produced through the use of fossil fuels,
- Increasing the efficiency of existing technologies for producing non-fossil fuels,
- Automotive battery technologies and other technologies to reduce fossil fuel consumption in transportation, or
- Technologies to reduce energy use in buildings.

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Qualified Energy Conservation Bonds (continued)

Type III – Mass commuting facilities and related facilities that reduce the consumption of energy, including expenditures to reduce pollution from vehicles used for mass commuting.

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Qualified Energy Conservation Bonds (continued)

Type IV – Demonstration projects designed to promote commercialization of —

- Green building technology,
- Conversion of agricultural waste for use in the production of fuel or otherwise,
- Advanced battery manufacturing technologies,
- Technologies to reduce peak use of electricity, or
- Technologies for the capture and sequestration of carbon dioxide emitted from combusting fossil fuels in order to produce electricity.

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Qualified Energy Conservation Bonds (continued)

Type V – Public education campaigns to promote energy efficiency (other than movies, concerts and other events held primarily for entertainment purposes).

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New Clean Renewable Energy Bonds

- Permitted Issuers: All types of local government issuers, municipal utilities, electric cooperatives and certain cooperative lenders
- Eligible Projects: A broad range of renewable generation facilities

The project must be owned by a municipal utility, a state or local government, or a cooperative electric company, but may be leased to or operated by or its output sold to a private company

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New Clean Renewable Energy Bonds

- Tax Credit Bonds: A “tax-credit bond” designed to provide the issuer with a 70% interest subsidy
- Volume Cap: \$2.4 billion
- Allocation Process: Applications to be filed by issuers with IRS when “CREB window” is open
- Prevailing Wages: Federal Davis-Bacon prevailing wage rules apply to projects financed with proceeds of such bonds

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New Clean Renewable Energy Bonds

The types of projects that can be financed with New CREBs include:

- Wind energy facilities
- Closed-loop biomass facilities
- Open-loop biomass facilities
- Geothermal energy facilities
- Solar energy facilities
- Small irrigation power facilities
- Landfill gas facilities
- Trash combustion facilities
- Marine and hydrokinetic energy facilities
- Qualified hydropower facilities

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Changes Intended to Improve Market for State and Local Obligations

- Temporary suspension of AMT as applied to tax-exempt bonds
- Expansion of “Bank Qualified Bond” category
- Expansion of the IRS 2% *de minimis* rule to banks

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Summary of Pending Guidance

- Implementation of Direct Subsidy BABs (IRS)
- Allocation of Volume Caps for Tax Credit Bonds (IRS)
- Tax Credit Striping (IRS)
- State of California Application/Allocation Process for Tax Credit Bonds (State of California)

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Mr. Field is a Partner in the Public Finance Department of Orrick, Herrington & Sutcliffe LLP and the Co-Chair of Orrick's School Finance/General Obligation Bonds Practice Group. He has extensive experience, as both bond counsel and disclosure counsel, in the financing techniques used by school districts in California. His practice focuses on local governmental infrastructure financing, including general obligation bond financing, land-secured financing and municipal lease financing. He has appeared as panelist and lecturer for numerous organizations, including the Coalition for Adequate School Housing, the California Community College League, the Associated Press News Editor's Council, the League of California Cities and the California Society of Municipal Finance Officers. Mr. Field is the principal author and editor of the third edition of *The XYZ's of California School District Debt Financing*, published by Orrick in 2005.

Orrick, Herrington & Sutcliffe LLP has maintained a substantial practice in the area of public finance for over a century. It has been the premier bond counsel firm in California throughout that period, and has been ranked first in the country for most of the last ten years in total volume of financings for which it served as bond counsel. Orrick's public finance attorneys are located in Los Angeles, San Francisco, Sacramento, New York, Seattle, Portland and Washington, D.C. From these offices, Orrick serves as bond counsel for issuers in more than 40 states, several territories and other countries. For more information, please visit www.orrick.com.

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The Presenters – Mark Farrell

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Mark Farrell has over a decade of experience in the financial services industry advising both public agency and private industry clients. Mr. Farrell joined Piper Jaffray's public finance team in 2002 and has experience with a variety of financing vehicles for educational issuers including general obligation bonds, certificates of participation, Mello-Roos bonds, tax and revenue anticipation notes, bond refinancings and GASB 45 liability funding. His responsibilities in the California Education Group include overall transaction management, bond program structuring, credit enhancement strategies, cash flow and debt capacity analysis, legal document review, and other support of education financing transactions.

Since 2006, Mr. Farrell has led the issuance of over \$2.0 billion in tax-exempt financings for California school and community college district issuers. Mr. Farrell is the lead banker on the CSBA California Cash Reserve Program, the largest pooled tax and revenue anticipation note financing in the nation. During his career, Mr. Farrell has participated in financings for over 400 school districts with an aggregate par amount exceeding \$7.5 billion.

Mr. Farrell holds a Bachelor of Arts in International Relations from the University of Pennsylvania and a Masters of Business Administration from the Anderson School at the University of California, Los Angeles.

Piper Jaffray & Co. is a leader in structuring and underwriting bonds for California school districts and community college districts. Piper Jaffray provides financing options to Districts for General Obligation Bonds, Certificates of Participation, Lease Revenue Bonds, Mello – Roos Bonds, Community Facility District Bonds, Interim/Bridge Financing, Short-Term Notes (TRANS & BANs) and Qualified Zone Academy Bonds. Piper Jaffray has the largest and most experienced team of education finance dedicated K-14 bankers in California. Our 12 bankers represent more than 150 years of experience and service to the education industry. For more information, please visit www.piperjaffray.com.

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