AASA Toolkit: Cost-Effective Financing for School Construction and Renovation



Helping school districts access tax-credit bonds to finance the construction and repair of public schools.

AMERICAN ASSOCIATION OF SCHOOL ADMINISTRATORS

EddieTech
Funding the Future of Schools

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Please note: As of March 2010, a pending jobs bill may affect the tax credit bonds. AASA will notify members and update this toolkit if changes occur.

March 2010

Dear AASA Member:

If you are like most school system leaders during these tough economic times, your district is facing severe budget shortfalls, with little or no funding to pay for school construction or repair.

The purpose of this toolkit is to connect your school district to cost-effective financing for school construction and renovation.

States and local governments typically finance public projects by selling tax-exempt bonds, which offer interest payments that are lower than conventional rates because the interest is tax-free. This toolkit will bring you up-to-speed on two tax-credit bonds created and expanded by the 2009 American Recovery and Reinvestment Act:

- **Qualified School Construction Bonds,** which can be used for constructing, rehabilitating or repairing a public school facility, or acquiring land for a public school.
- **Qualified Zone Academy Bonds, which can be** used for school modernization, equipment and developing curriculum/training.

While these bond programs offer billions of dollars for school facilities, some districts are facing increased costs and greater difficulty in successfully placing these bonds. The good news for school districts is that AASA has partnered with the nonprofit National Education Technology Funding Corporation ("Eddie Tech"), to help reduce the costs to school districts of investing in the nation's education infrastructure.

By working with Eddie Tech, you can take full advantage of these tax-credit bonds, which will allow you to build more for less and improve your facilities for students and teachers.

We encourage you to read the materials included in this toolkit and contact Brett Mandel, executive director of Eddie Tech, at bmandel@eddietech.org or 202.330.1438, with any questions.

Sincerely,

Daniel A. Domenech

Daniel A. Domenech
AASA Executive Director

Top 5 Questions and Answers
About School Investment Pooled Securities

1. **What is the School Investment Pooled-Securities ("SIPS") Program?**
The SIPS Program is an effort to help local school districts to take full advantage of federally subsidized financing through Qualified School Construction Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs). By packaging many, smaller bond issuances into a larger, geographically diverse pool of tax-credit bonds, Eddie Tech expects to offer public school districts *lower financing costs* and *simpler "pre-packaged" issuance mechanics*.

2. **Who created the program?**
The National Education Technology Funding Corporation ("Eddie Tech") is a non-profit organization, recognized legislatively by Congress in 1996 to improve education-technology infrastructure. In 2010, the American Association of School Administrators, the National School Boards Association and the National Education Association joined together to establish the SIPS Program to enable school districts access tax-credit bonding more efficiently and effectively.

3. **Why was the program created?**
As you may know, while QSCBs provide a significant financial subsidy for school districts, because there is not yet a mature and established market for these bonds, many districts have found it necessary to pay lenders an additional premium of as much as 3.0 percent or more per year to issue the bonds. Additionally, many districts have been frustrated by the complexity of marketing these bonds and have had to invest scarce district resources in outside professionals to facilitate transactions. Eddie Tech expects the SIPS Program to provide school districts with an efficient "pre-packaged" issuance process, reduced financing costs, and more-efficient pricing on the underlying debt.

4. **How does the program benefit schools?**
As a non-profit organization, Eddie Tech seeks to maximize the benefits offered by tax-credit bonds to school districts for financing the construction and repair of public schools, as well as the development and modernization of the technology infrastructure in the schools. By packaging QSCBs and QZABs into pooled securities in its SIPS Program, Eddie Tech makes them more attractive to investors, thereby broadening the array of potential buyers. Eddie Tech's SIPS Program is designed to reduce financing costs for school districts by achieving economies of scale through volume and simplify the process by which school districts can issue and investors can invest in these new financing tools.

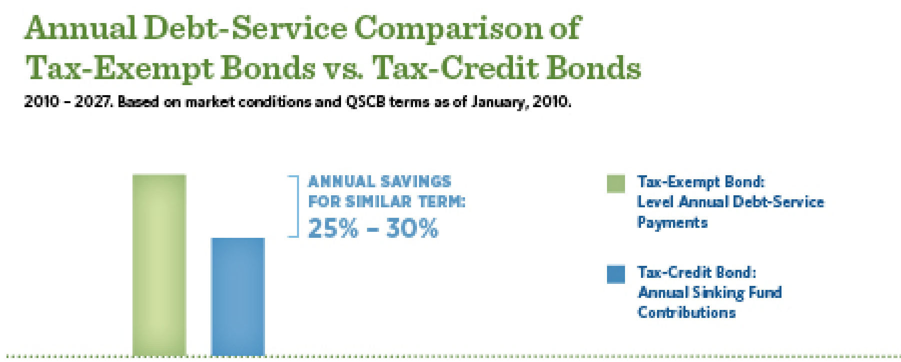
5. **How can my district take advantage of this program?**
If your school district is interested in exploring the potential cost savings and other benefits of the SIPS Program, please contact Eddie Tech Executive Director Brett Mandel at 202.330.1438 or bmandel@eddietech.org. Eddie Tech looks forward to working with you to fund the future of your schools.

Fact Sheet: Federal Tax-Credit Bonds Available to Schools

Fact: School districts are able to use Qualified School Constructions Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs) to realize a significant financial subsidy for capital projects.

Fact: QSCBs and QZABs are federal tax-credit bonds, which allow bondholders to claim an annual tax credit equal to a specified credit rate as determined by the secretary of the treasury, for as long as the bond remains outstanding.

Fact: School districts are able to use these bonds to realize a significant financial subsidy for capital projects. This is illustrated in the chart below.



Fact: Tax-Credit Rate

The federal legislation relating to QSCBs and QZABs directs that the secretary of the treasury establish a tax-credit rate such that issuers need not pay interest cost or sell the bonds at a price less than the face value. In recent months, however, investors generally have required supplemental interest payments of 1-3 percent.

The Treasury on a monthly basis also establishes the maximum permitted maturity for the QSCBs and QZABs (recently in the 15- to 17-year range) and the "permitted sinking-fund yield" (the maximum rate at which borrowers can reinvest annual deposits to provide for principal repayment).

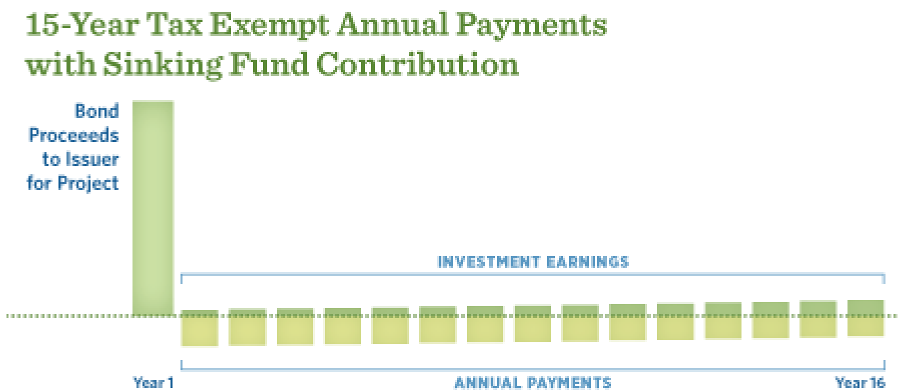
For the current tax-credit rate, maximum maturity, and sinking-fund yield from TreasuryDirect, go to https://www.treasurydirect.gov/GA-SL/SLGS/selectQTCDate.htm.

Fact: Tax Credits

Issuing government entities must only repay the bond principal, using local revenue sources such as property taxes. The federal government provides a return to the bondholder in the form of the tax credits. They are taxable for the bondholder, like interest income, and only have value to the extent a bondholder has current income tax liability.

Fact: Bond Payment

The value to school districts of QSCBs and QZABs is maximized if the bonds are structured as "balloon maturities," with all the principal remaining outstanding until the year of final maturity. Many states have legal requirements that school districts make annual level debt service payments to provide for the orderly retirement of debt. Eddie Tech envisions that most participants will make equal annual contributions to a central escrow account (the Sinking Fund). Districts would be credited with net earnings on sinking fund balances to reduce their contribution the following year.



Eddie Tech plans to market pooled QSCBs and QZABs through its SIPS Program on a quarterly basis, as demand warrants.

Fact Sheet: Qualified School Constructions Bonds

Qualified School Construction Bonds (QSCBs) were introduced in the American Recovery and Reinvestment Act of 2009 (P.L. 111-5) and have a national limit of $11 billion in each of 2009 and 2010. As tax-credit bonds, they offer investors an annual federal tax credit covering most, if not all, of the annual return required by investors. This much deeper federal subsidy conserves local tax dollars for other purposes. The bonds are allocated:

- 40 percent to the 100 largest local education agencies (LEAs) based on the number of children living below the poverty level; and
- 60 percent to states and territories based on the state's share of Title 1 Basic Grants, which the States then sub-allocate to school districts or issue themselves. Each state's share of the 60 percent is reduced by the LEA allocations.

Bond proceeds must be used for constructing, rehabilitating or repairing a public school facility, or acquiring land for a public school. Proceeds must be spent within three years, un-issued allocations may be carried forward by the State for one year, and Davis-Bacon rules requiring the payment of prevailing wages apply.

Fact Sheet: Qualified Zone Academy Bonds

Qualified Zone Academy Bonds (QZABs) were introduced in the Taxpayer Relief Act of 1997 (P.L. 105-34) and had a limit of $400 million from 1998 through 2008. This limit was expanded by Congress to $1.4 billion for 2009 and 2010. The bonds are allocated to states and territories based on their portion of the U.S. population living below the poverty line. Each state then sub-allocates issuance volume to school districts. QZABs generally have the same features as QSCBs, with the following exceptions:

- Qualified Zone" schools must be located in an Empowerment Zone, Enterprise Community, or at a school where at least 35 percent of the students are eligible for free or reduced-lunch costs;
- Bond proceeds are limited to school modernization, equipment, or developing curriculum/training; and
- School districts must partner with private entities that contribute property or services with a value of 10 percent of the bond proceeds.

Press Release Template
Announcing Participation in SIPS Program

You may tailor this press release to fit your district and distribute it to your local media contact list to increase awareness of your participation in the School Investment Pooled-Securities Program.

FOR IMMEDIATE RELEASE
[Date]

Contact: [Name, phone number, e-mail]

[NAME OF DISTRICT] SAVES [$____] BY PARTICIPATING IN SCHOOL INVESTMENT POOLED-SECURITIES PROGRAM

[City, State] -- [Name of District] today announced that the district was able to issue bonds to fund the construction of [____________] at a cost of [$_________], saving the district and taxpayers [$_________] over the life of the bonds, by participating in the School Investment Pooled-Securities (SIPS) Program.

The SIPS Program is administered by the National Education Technology Funding Corporation — "Eddie Tech" — to help local school districts utilize federal mechanisms for interest-free financing of school construction and renovation.

Eddie Tech is a non-profit organization recognized legislatively by Congress in 1996 principally to improve education-technology infrastructure. Eddie Tech is working to be the preferred vehicle by which local school districts access capital to issue two forms of tax-credit bonds created and expanded by the 2009 American Recovery and Reinvestment Act: Qualified School Construction Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs).

The federal tax-credit bonds created and expanded by the 2009 American Recovery and Reinvestment Act provide a significant financial subsidy for school districts by authorizing the U.S. Treasury to pay "interest" to investors in the form of annual tax credits. However, because there is not yet a mature and established market for these bonds, many school districts across America have found it necessary to pay lenders an additional premium of as much as 3.0% or more per year. This raises the cost of much-needed investment in school safety, acquisition of modern technology, and enhancement of the learning environment.

"Eddie Tech's SIPS Program can offer efficient 'pre-packaged' issuance mechanisms, reduced transaction costs and more-efficient pricing for school districts," said Eddie Tech Executive Director Brett Mandel. "Through the work of Eddie Tech, public school districts can access low-cost financing to invest in America's schools and create an environment that supports excellence in our classrooms."

[Name, Title] commented, "By working with Eddie Tech, we were able to take full advantage of the tax-credit bonds, which allowed us to build more for less, improving our facilities for students and teachers without unnecessarily burdening our taxpayers."

The nation's leading education-advocacy organizations — the American Association of School Administrators, the National Education Association, and the National School Boards Association — have joined together to endorse and help market Eddie Tech's SIPS Program to reduce the costs to school districts of investing in the nation's education infrastructure.

EddieTech

Funding the Future of Schools

JOINTLY ENDORSED BY:

AMERICAN ASSOCIATION OF SCHOOL ADMINISTRATORS

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Eddie Tech maximizes the benefits offered by tax-credit bonds to public school districts for the construction and repair of schools as well as the development and modernization of the technology infrastructure in the schools.

Eddie Tech seeks to be the preferred vehicle by which local school districts access capital to issue two forms of tax-credit bonds: Qualified School Construction Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs).

In view of the dramatic expansion of tax-credit bonds by Congress in 2009 and limited demand from institutional investors, public school districts may face increased costs and greater difficulty in successfully placing these new types of bonds.

As a Congressionally recognized private non-profit corporation, Eddie Tech is able to use its special organizational status and support from the American Association of School Administrators, the National School Boards Association, and the National Education Association to connect local school districts to cost-effective financing for school construction and renovation.

Through its School Investment Pooled-Securities (SIPS) Program, Eddie Tech assists in assembling portfolios of QSCBs and QZABs that can be packaged and sold into the national capital markets.

Pooling individual tax-credit bonds is intended to confer the following benefits:

- Lower financing costs and simpler "pre-packaged" issuance mechanics for local school districts;
- Better market access for smaller or lesser-rated school districts, which will benefit from inclusion in a diversified pool;
- More efficient pricing on tax-credit bonds, due to better diversification, broader distribution, and enhanced liquidity;
- Easier de-coupling of principal from tax credits, potentially opening up demand for the bonds by new categories of investors such as pension funds;
- Strategic alliances with school-finance authorities and municipal-bond industry professionals to ensure efficient origination, structuring, and placement of bonds; and
- Effective marketing to both issuers and investors, using the education community's support of Eddie Tech.

> "Eddie Tech's School Investment Pooled-Securities (SIPS) Program will reduce financing costs for public school districts and simplify the process by which school districts can issue tax-credit bonds."
>
> **DAN DOMENECH, EXECUTIVE DIRECTOR, AMERICAN ASSOCIATION OF SCHOOL ADMINISTRATORS**

The National Education Technology Funding Corporation, "Eddie Tech," is a non-profit organization, recognized legislatively by Congress in 1996 principally to improve education-technology infrastructure. Today, Eddie Tech is working to help local public school districts utilize federal mechanisms to access more cost-effective financing of school construction and renovation.

Eddie Tech's efforts to help fund the future of schools have been endorsed by the nation's leading education-advocacy organizations — the American Association of School Administrators, the National School Boards Association, and the National Education Association.

for SCHOOL DISTRICTS

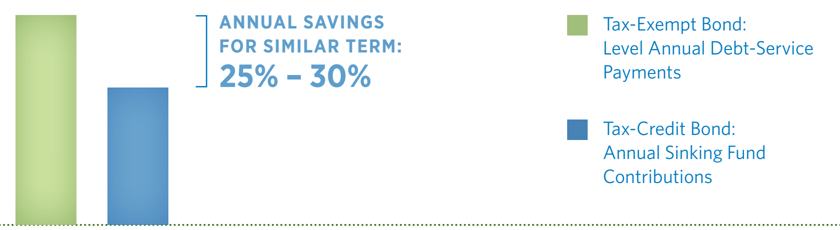
Qualified School Construction Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs) are federal tax-credit bonds, which allow bondholders to claim an annual tax credit equal to a specified credit rate as determined by the Secretary of the Treasury, as long as the bond remains outstanding.

That rate of credit is set at the time the bonds are sold, and is intended to enable issuers to sell their bonds at face value (par) and without interest cost. In recent months, investors generally have required supplemental interest payments of 1-3%. The Treasury also sets the maximum maturity date for the bonds (recently in the 15- to 17-year range). Issuing government entities must repay the bond principal from local revenue sources, while the federal government provides an annual return to the bondholder in the form of the tax credits. The credits are treated as taxable income for the bondholder like interest income, and are applied to the bondholder's current tax liability.

As illustrated in the chart below, school districts are able to use QSCBs and QZABs to realize a substantial financial subsidy for capital-project borrowings.

Annual Debt-Service Comparison of Tax-Exempt Bonds vs. Tax-Credit Bonds

2010 – 2027. Based on market conditions and QSCB terms as of January, 2010.



FOR MORE INFORMATION or to partcipate in Eddie Tech's SIPS Program, please call 202.330.1438 or email sipsprogram@eddietech.org.

"Many school districts have not been able to realize the full benefit of the QSCB and QZAB programs, but Eddie Tech's School Investment Pooled-Securities (SIPS) Program will help districts generate the maximum benefits from these financing tools."

ANNE BRYANT, EXECUTIVE DIRECTOR, NATIONAL SCHOOL BOARDS ASSOCIATION

for INVESTORS

The credit rate for tax-credit bonds is based on market yields of low- to mid-investment grade taxable corporate bonds of similar term. To the extent a public school district is rated single-A or higher, tax-credit bonds should provide a favorable return to purchasers with tax liability.

Qualified School Construction Bonds (QSCBs) and Qualified Zone Academy Bonds (QZABs) give the investor an annual tax credit, which is treated like interest. Thus, if the annual tax-credit rate for QSCBs and QZABs is 6.00%, a $1,000,000 bond would yield an annual tax credit of $60,000 for bondholders.

Bondholders without current-year tax liability who hold a tax-credit bond can either roll over the tax credit to a subsequent year when they expect to have tax liability, or sell the bond to other investors. In addition, forthcoming program regulations are expected to allow an investor to "strip" the tax credits from the bond and sell them to an entity with tax liability.

By allowing the separation of the tax credit from the underlying bond, tax-credit bonds are made more marketable to investors and financial intermediaries. Financial intermediaries can buy the tax-credit bonds, sell the principal to an investor looking for a stable, long-term investment, and then sell the stream of credits to another investor seeking to offset short-term taxable income.

Eddie Tech plans to achieve more-efficient pricing on tax-credit bonds, due to better diversification, broader distribution, enhanced liquidity, and easier de-coupling of principal from tax credits, opening up demand for the bonds by new categories of investors.

15-Year Tax-Credit Investment Return

> "QSCBs and QZABs represent important ways to invest in America's schools and to help take pressure off of strained school budgets so more resources can be devoted to our classrooms."
>
> **JOHN WILSON, EXECUTIVE DIRECTOR, NATIONAL EDUCATION ASSOCIATION**

Fund the Future of Your Schools Today!

www.eddietech.org

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