ATTACHMENT B

STATE ALLOCATION BOARD
SUBCOMMITTEE ON PRIORITIES IN SCHOOL CONSTRUCTION, CASH MANAGEMENT
February 8, 2011

PURPOSE

To present options and viability of implementing a new cash management system.

AUTHORITY

Education Code Section 17070.35(a) states, "In addition to all other powers and duties as are granted to the board by this chapter, other statutes, or the California Constitution, the board shall do all of the following:

(1) Adopt rules and regulations, pursuant to the rulemaking provisions of the Administrative Procedure Act, Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3 of Title 2 of the Government Code, for the administration of this chapter…

(2) Establish and publish any procedures and policies in connection with the administration of this chapter as it deems necessary…"

Budget Letter 10-09 requires that if there are insufficient bond proceeds, departments and agencies are responsible for prioritizing the projects that will be funded consistent with the prioritization criteria outlined (including job creation). It also indicates that if bond proceeds are not managed efficiently, additional bonds may not be sold for the program.

Government Code Section 15503 states, "Whenever the board is required to make allocations or apportionments under this part, it shall prescribe rules and regulations for the administration of, and not inconsistent with, the act making the appropriation of funds to be allocated or apportioned. The board shall require the procedure, forms, and the submission of any information it may deem necessary or appropriate. Unless otherwise provided in the appropriation act, the board may require that applications for allocations or apportionments be submitted to it for approval."

SFP Regulation Section 1859.90.2 states that a priority funding rounds may be established pursuant to a public notice and announcement by the Board at one of its monthly meetings.

SFP Regulation Section 1859.129(b)(2) and 1859.197 (b)(2) state that If the district is requesting an Apportionment pursuant to Section 1859.90.1 or 1859.90.2, the Board will require that this time limit be reduced to no more than 90 days from the date of the apportionment.

BACKGROUND

The State is currently in a financial situation which requires a heightened awareness of cash management. The Board has taken steps to counteract the financial crisis and help expedite the flow of cash into the economy through priority funding rounds, establishing fiscal crisis regulations and the creation of the unfunded approvals list.

Due to the State's fiscal crisis in early 2009, the Board adopted emergency regulations that would allow the Board to make findings that certain apportionments are "inactive" to relieve school districts from meeting various statutory requirements. In December 2010 the Board took action to extend the Regulations for six months.

In March of 2009 the Board approved an item to create an Unfunded Approvals list up to the available bonding authority.

At the April 2010 Board meeting, the Board discussed the current system of making apportionments and providing fund releases to districts which is based on the date the complete application was received for processing and placed on the Unfunded List. The Board took action to establish the SAB Priorities in School Construction Funding Sub-Committee which met in May of 2010. At the May 2010 Board meeting, the Board established the first priority funding round based upon careful consideration of the subcommittee recommendations. Priority funding was created to provide a viable and valuable way to accelerate the flow of cash directly into the economy by creating a mechanism allowing projects that are ready to move forward and request a fund release within 90 days to receive an apportionment.

The first priority funding round is complete and successfully infused $408.1 million into the economy. Due to the success of the first round, the Board took action to adopt priority funding as a valid form of making apportionments. At the August 25, 2010 meeting, updated regulations were approved granting the Board the ability to create future priority funding rounds on an as needed basis. Through priority funding, the Board has established a system in which an Unfunded Approval moves to an apportionment to a district fund release in just over five months, approximately thirteen months faster than the eighteen month policy that had been in existence since the inception of the SFP.

On October 28, 2010, at the direction of the Board, the Subcommittee on Priorities in School Construction Funding Part II (Committee II) met to discuss options for expediting the flow of cash to districts ready to request funds for projects on the Unfunded Approvals list. The majority of options presented revolved around projects that currently have a standard apportionment which are on an 18 month fund release request timeline. The Committee II weighed options that would allow districts to “buy time” by switching from an active apportionment to and Unfunded Approval, allow districts to “swap projects” by placing a project with an apportionment back on the Unfunded Approvals and receive an apportionment for a project ready to move forward on the Unfunded Approvals list in exchange, and to allow districts to receive an apportionment for a project on the Unfunded Approvals list ready to request funds in exchange for the rescission of a project that had already received an apportionment. The final option discussed was a cash availability model based on providing apportionments in excess of available cash.

The ultimate determination of the Committee II was to develop a new cash management system based within the parameters of the current SFP allowing forward progress while honoring the desire of the Board to keep the current program intact.

DESCRIPTION

Since December 2008 the Board has taken actions on an emergency and/or temporary basis to continue to provide approvals and apportionments for School Facility Program (SFP) projects. It has been stated that the previous way of using AB 55 loans to manage cash within the program most likely will not resume again. The purpose of this meeting is to discuss options for management of available cash on hand, future bond sales and residual cash made available via rescissions, closeouts or other possible avenues of cash returning to the program.

Options for Managing Cash and Making Future Apportionments

Option 1: Modified Priority Funding – create an additional Unfunded Approvals “Priority List” detailing projects that are willing to request funds as soon as cash is available.

This option would create two separate Unfunded Approvals lists. The current Unfunded Approvals list would go unchanged. The major modification to the priorities in funding system under this option would be the creation of a second Unfunded Approvals list (Priority List) for applications ready to submit a *Fund Release Authorization* (Form SAB 50-05) within 90 days of apportionment regardless

of when cash is available. All applications receiving an apportionment approval would be placed on the Unfunded Approvals list. Districts would then have the option to submit a certification letter requesting placement on the Priority List. This would allow the Board to make apportionments on a flow basis in addition to keeping the 90 day fund release timeline. The benefits of this option appear to be substantial. The ability to provide apportionments on a flow basis allows for seamless processing, better prediction of cash need by bond and with the proper safeguards could be easier for districts and Staff.

Pros:

- The Priority List can be used to specify the exact cash need to the State Treasurer for use in determining which bonds to sell.
- Would help distribute cash in a quick manner while helping to stimulate the economy.
- Would help to reduce/eliminate any residual cash issues.
- Would greatly reduce the number of Staff hours currently assigned to priority funding rounds.
- Would release some of the restrictive burden of set priority funding rounds, allowing districts a much simpler method for requesting placement on the Priority List that coincides with actual or realistic project timelines.
- Transparency – districts would have easy access to the Priority List and would easily be able to see their place in line.
- District control – districts could be placed on or removed from the list at the district's discretion.

Cons:

- Districts could remain on the Unfunded Approvals list for an indefinite period of time if no request is submitted to place an apportionment on the Priority List.
- Two separate lists could create confusion for districts.

Questions:

- How do we keep the Priority List current?
    - The Office of Public School Construction checking in with districts on timed intervals of 3, 6 or 12 months in the form of survey reminders.
    - Re-certification from districts on timed intervals of 3, 6 or 12 months.
- If districts are eligible to be added or removed from the list at any time, what process timeframe be established for district removal from the Priority List (i.e. a Board action as part of the consent calendar every month)?
- What long term effects would the change have on school districts?
- Are districts only complying with the 90 day requirement for priorities in funding because there is currently no other way to receive cash?
- Are there districts that can not meet the 90 day requirement and therefore will never be able to request an apportionment?
- What process should be used if more cash becomes available than apportionments on the Priority List?
    - Example: Start funding down the Unfunded Approvals list based on the original 18 month timelines.
    - Should the Board want to make this determination now or if/when the situation presents itself?

Program Changes:

1) Regulations would need to be modified to outline the new procedures (possible update of Regulation Section 1859.90.2 or the addition of a new regulation section).
2) SFP Regulation Sections 1859.90 and 1859.197 would need to be modified to clarify the change of time limit for fund release if priority funding becomes permanent.

Option 2: Priority Funding – continue to use the current model, with clarification on timing of new rounds

The current system for priority funding has been a successful and fairly seamless process. To date the state has apportioned approximately $1.85 billion through priority funding. The success and demand for this method of cash disbursement has shown that priority funding is a viable and valuable way to accelerate cash directly into the economy. Any new program is a learning experience, and as with any new program priority funding could continue with a few modifications to make the process more efficient while keeping the core of the program intact. Specific rules should be determined concerning the frequency of priority funding rounds, minimum cash thresholds and the timing of priority funding rounds in relation to bond sales. Existing regulations allow the Board to establish priority funding rounds at Board meetings. The Board could direct staff to place new rounds on the agenda when a certain dollar threshold is reached, or when bond sales are anticipated. The Board could also set the threshold or timelines in regulation.

Pros:

- The program has allowed for efficient and effective distribution of cash.
- Process is established and would require minimal additional resources to continue.
- To date, the program has had a 100% success rate and the OPSC has not had to rescind any priority funding apportionments.

Cons:

- Under the current regulations priority funding can be viewed as temporary fix.
- Does not allow the Board the ability to apportion projects on a flow basis.

Questions:

- Should there be a minimum amount of cash available to institute new filing rounds (i.e. is $30 million in project rescissions enough to hold a new filing round)?
- Timing – how can the Board set up an effecting system for timing the funding round in accordance to bond sales, rescissions and project closeouts?
- Should a system be instituted to line up priority funding rounds with anticipated fall/spring bond sales?
- Should new timelines be established in regulation?

Program Changes:

1) SFP Regulation Sections 1859.90 and 1859.197 would need to be modified to clarify the change of time limit for fund release if priority funding becomes a permanent institution.

Option 3: Cash leveraging model

This option revolves mainly around $233 million in projects with an 18 month time limit expiration in October 2011. Under this option, without additional cash becoming available, the Board would provide apportionments through a priority funding round for $233 million allowing districts that are ready to submit fund releases to access the cash currently available for the 28 projects that currently have seven months left on their current fund release timeline. This model balances the need to have cash available with the rate at which it is being drawn down by districts. Under this option the Board would use proceeds from a future bond sale to replenish the cash pool to cover all 28 projects currently on an 18 month timeline. A similar option was presented at the Subcommittee on Priorities in School Construction Funding, Part II on October 28, 2010.

Pros:

- Would help distribute cash in a quick manner while helping to stimulate the economy.
- This option could be implemented for all applications that have not yet received an Apportionment.
- School construction needs for future bond sale consideration may be more accurately demonstrated.
- Districts with an Apportionment that is ready to move forward may act more quickly to access the cash to avoid waiting later on if the cash available is all released.

Cons:

- The Board could be liable as cash could not be available if all projects requested funding before cash to cover the additional $200 million in apportionments becomes available.
- In an item presented at the November 2010 Board meeting, Staff in conjunction with the DOF determined the course of action to be very risky.
- Selecting this option would only speed up the distribution of cash by four months. It would take three out of the remaining seven months for the item to be presented to the Board and have regulations approved by the Office of Administrative law allowing this course of action, thus providing little impact for the amount of possible liability.
- Currently there is no spring bond sale scheduled and as of this point in Staff can not be sure of when the next bond sale will take place. Therefore, it is unknown when cash would be available to cover the original apportionments.
- Would most likely be a temporary fix and not a long term option due to liability issues.

Program Changes:

- Regulations would be required to make future apportionments conditional.

Selective Ordering Based on the Ability to Provide Full Apportionments

In the current system and each of the new options above a dilemma is created if, for example, the Board has $1 million in cash and the next project in line requires a $100 million apportionment. Here the Board has three options: which include

- Wait until the full $100 million is available before moving down the appropriate list,
- Offer partial funding for the project, or
- Moving past projects in line that can not be fully funded in favor of the next project that can be fully apportioned out of the remaining cash. This would be a departure from the FIFO methodology and is something that has not been standard practice in the SFP, however it may be a concept that the Board would like to investigate.

Pros:

- The board would be able to fully apportion as many projects as possible up to the available cash.
- Builds on the Priority in Funding model to expedite moving cash out into the economy as quickly as possible.
- Cash does not remain idle.

Cons:

- Would be a departure from the standard FIFO practice, thereby compromising list integrity.
- The large projects may want partial funding or want cash to continue to accumulate until their project can be fully apportioned as opposed to having their project skipped.
- May be a liability to the State as this goes against current regulations.

Program Changes:

- SFP Regulation Section 1859.93 and 1859.93.1 would need to be modified or removed as projects may no longer be following a FIFO methodology.