

Date of Hearing: May 7, 2013

ASSEMBLY COMMITTEE ON ELECTIONS AND REDISTRICTING

Paul Fong, Chair

AB 621 (Wagner) – As Amended: April 25, 2013

SUBJECT: Local government: bonds.

SUMMARY: Prohibits a local agency from entering into specified relationships with an individual or firm with respect to a new issue of bonds requiring voter approval if the individual or firm provides bond campaign services to the bond campaign. Specifically, this bill:

- 1) Prohibits a local agency from entering into a financial advisory, legal advisory, underwriting, or other similar relationship with an individual or firm, with respect to a new issue of bonds that requires voter approval on or after January 1, 2014, if that individual or firm, or an employee, agent, or person related to an employee or agent of the individual or firm, provided or will provide bond campaign services to the bond campaign.
- 2) Provides that "bond campaign services," for the purposes of this bill, includes fundraising, donation by the individual or firm to the bond campaign, public opinion polling, election strategy and management, organization of campaign volunteers, get-out-the-vote services, development of campaign literature, and advocacy materials.
- 3) Provides that "bond campaign services" does not include advice and support related to the preparation of tax rate statement and other documentation required for inclusion in the voter pamphlet published by the applicable county registrar of voters or public opinion polling that is conducted before a bond measure is placed on the ballot for the purposes of gathering information regarding, and evaluating the potential for, the adoption of the bond measure by the electorate.
- 4) Provides that the term "related," for the purposes of this bill, includes, but is not limited to, a family relationship, an affiliation between business associations, or business associations with directors or principals in common.

EXISTING LAW:

- 1) Makes it unlawful for any elected state or local officer, including any state or local appointee, employee, or consultant, to use or permit the use of public resources for a campaign activity, or personal or other purposes which are not authorized by law, and provides for civil penalties for a violation of this provision.
- 2) Makes it a felony for an officer of the state, or of any county, city, town, or district of the state, to use public moneys for any purpose not authorized by law. Provides, for the purposes of this provision, that "public moneys" includes the proceeds derived from the sale of bonds.
- 3) Makes it a crime to use school district or community college district funds, services, supplies, or equipment to urge the support or defeat of any ballot measure or candidate.
- 4) Requires counties, cities, and school districts to get voter approval for long-term debt.

- 5) Requires the governing board of a school district or community college district, before selling bonds, to disclose specified information about the method of sale, the identity of the bond counsel, underwriter, and financial adviser involved in the sale, and cost estimates. Requires the governing board, after the bond sale, to present actual cost information for the sale at its next scheduled public meeting, and to submit an itemized summary of costs of the sale to the California Debt and Investment Advisory Commission.
- 6) Allows local agencies to issue and sell general obligation (GO) bonds through the negotiated sale method, and imposes nearly identical requirements as apply to school districts and community college districts, as identified above, on any city, county, city and county, or special district that sells bonds at a negotiated sale.

FISCAL EFFECT: Keyed non-fiscal by the Legislative Counsel.

COMMENTS:

- 1) Purpose of the Bill: According to the author:

Currently, it is illegal for school officials to use public funds to hire political consultants to pass a bond measure. However, all over the state, school districts are having their banks or outside financial advisors hire political strategists to run the bond campaigns.

When the bonds are approved they end up costing the taxpayers millions of dollars. For example, one \$22 million borrowing will end up costing taxpayers nearly \$280 million. The reason that it grows to such a large amount of debt being that these are capital appreciation bonds, which no payments are required for up to 40 years while interest builds; interest which the taxpayers have to cover.

AB 621 seeks to close this loophole that is being exploited for the sake of a desire to build with taxpayer money. It will prevent any local agency from entering into these bond services with any individual or firm that provided any type of campaign service for the bond campaign. And in the end, this will hopefully save taxpayers millions of dollars.

- 2) Competitive Sales vs. Negotiated Sales of Bonds: "Competitive sale" and "negotiated sale" are the two principal methods that public officials use to select an underwriter to purchase bonds and resell them to investors. In a competitive sale, underwriters deliver sealed bids and public officials award a contract to the lowest bidder. In a negotiated sale, public officials negotiate with an underwriter on terms and prices.

Until recently, schools districts and community college districts were the only local agencies authorized to sell GO bonds at a private sale using the negotiated bid method. However, AB 1388 (Hernandez), Chapter 529, Statutes of 2009, authorized cities, counties, and special districts to sell GO bonds at a negotiated sale. Proponents of AB 1388 argued that negotiated sales would give local agencies greater flexibility with regard to the timing of the bond sale, and would allow a bond underwriter to work with the local agency to pre-market bonds to investors to enhance the sale effort. Proponents further maintained that negotiated bond sales, by providing greater certainty to the bond underwriters, could reduce the interest rates on bonds due to a reduced need to build in allowances for risk.

When local agencies issue bonds at negotiated sales, they may reach agreements with underwriters or financial advisors to provide a package of bond-related services, including campaign services. Since existing law prohibits the use of public funds for campaign purposes, a local agency cannot use public money (including the proceeds of bond sales) to pay for the costs of those campaign services. In light of this restriction, according to full service financial advisors that provide services to local agencies in California, a full service firm that is providing campaign services typically will have a separate contract with the campaign committee to provide those campaign services. That contract is funded by campaign contributions received by the campaign committee.

Proponents of this bill, on the other hand, are concerned that the nature of negotiated bond sales could allow firms to recover campaign costs through fees that agencies pay for other bond-related services, resulting in campaign costs being indirectly paid for with public funds. To support these allegations, the author points to an investigative report from the Orange County Register from February that detailed extensive campaign activities by an underwriting firm that has issued dozens of bonds for local agencies in California. In addition to violating long standing prohibitions against the use of public funds for campaign purposes, the proponents of this bill argue that such arrangements can drive up the costs to the public of local bond sales. If firms are recovering campaign costs through inflated fees for other bond-related services, it would be expected that firms that provide campaign services as part of a negotiated sale would charge higher fees to local agencies for other bond-related services than the local agencies would pay for similar services without a campaign component. However, committee staff is not aware of any comprehensive analysis that demonstrates whether negotiated sales for bond-related services result in higher costs for the non-campaign related services provided.

- 3) Restrictions on Campaign Contributions: Unlike previous similar legislation, which is described below, this bill provides that donations to a bond campaign by an individual or a firm is a basis for prohibiting an agency from entering into an advisory or underwriting relationship with that individual or a firm with respect to an issue of bonds. This new provision appears to be in response to the Orange County Register investigation discussed above. In that investigation, it was reported that the underwriting firm had made a contribution of \$25,000 to a campaign committee in support of a bond measure for which the firm had been hired by the agency proposing the bond to provide bond-related services.

Notwithstanding the author's concerns about such campaign contributions, donations to a bond campaign are not "bond campaign services" that are comparable to other services identified in this bill. The committee may wish to consider whether such donations should remain in the sphere of permissible political activity.

- 4) Capital Appreciation Bonds: Notwithstanding the author's and the supporters' stated concerns about local governments issuing capital appreciation bonds (CABs) that have interest costs that are several times the amount of money that is borrowed, it should be noted that this bill does not prevent the issuance of such CABs, and the provisions of this bill are not applicable solely to CABs, but rather apply broadly to any issuance of bonds by a local agency. Furthermore, committee staff is unaware of any evidence that the relationships that would be prohibited by this bill have any effect on the likelihood of a local government

issuing a CAB.

- 5) Arguments in Support: The California Association of County Treasurers and Tax Collectors writes, in support:

AB 621 would reform some current practices in negotiated bond sale in order to eliminate the "pay-for-play" atmosphere. Treasurers and Tax Collectors throughout the state report that in many cases, the negotiated sale of bonds leads to higher underwriting costs, which are then passed on to the taxpayer....

The agreement between a public agency and bond underwriters can be non-competitive. These relationships are unique. Design and construction of facilities funded by the proceeds of bonds are awarded through a competitive process. Yet, the financial advisor, legal counsel and underwriting contracts can and most often are awarded without a competitive process.

In many cases, underwriters also provide campaign-related services "pro bono" to public agencies as part of the negotiated agreement. Tax Collectors report that the higher costs of underwriting that they see in negotiated bond sales are attributable to the "free" campaign services that are being recovered in the bond sale. Stated another way: taxpayers are paying for political campaigns.

- 6) Arguments in Opposition: In opposition to this bill, the Small School Districts' Association (SSDA) writes:

Many small school districts rely upon professional assistance in enacting local General Obligation bonds. These districts rely upon the expertise of entities which include financial services providers. SSDA believes AB 621 would restrict school district's flexibility to make a judgment on the most cost-effective means of conducting a campaign and providing information to their citizens.

The state is no longer helping fund new school facility projects for small, poor school districts. These districts do not have wealthy businesses or citizens that will fund local school bond campaigns. They do, however, have the need to ensure safe, clean school facilities for their students, just as wealthy districts and students receive. By restricting campaign contributions, AB 621 would result in small district community organizations not being able to raise campaign funds needed to pass local school bonds. That situation will effectively force the school districts to continue using inadequate school facilities.

- 7) Previous Legislation: Several attempts have been made to enact the provisions of this bill. AB 1045 (Norby) of the 2011-12 Legislative Session, was substantially similar to this bill, except that it did not include campaign donations in the types of activities that are considered "bond campaign services." AB 1045 was approved by the Assembly on a 48-14 vote, but subsequently failed passage in the Senate Governance and Finance Committee.

SB 1461 (Ashburn) of the 2009-10 Legislative Session, was similar to AB 1045. SB 1461 failed passage in the Senate Local Government Committee on a 2-3 vote.

SB 623 (Ashburn) of the 2009-10 Legislative Session, was gutted and amended in the Assembly with virtually the same language as SB 1461. SB 623 was approved by the Assembly on a 61-7 vote, but died in the Senate Local Government Committee.

SB 799 (Wiggins) of the 2009-10 Legislative Session, was another similar bill that was never heard in committee. Another similar bill, AB 2011 (Cook) of the 2007-08 Legislative Session, failed passage in the Assembly Local Government Committee on a 1-3 vote.

- 8) Double Referral: On April 17, 2013, this bill was approved by the Assembly Local Government Committee on a 7-2 vote.

REGISTERED SUPPORT / OPPOSITION:

Support

California Association of County Treasurers and Tax Collectors
California Taxpayers' Association
Howard Jarvis Taxpayers Association
Kern County Superintendent of Schools
State Treasurer Bill Lockyer

Opposition

Anderson Union High School District
Baker Valley Unified School District
Bennett Valley Union School District
Black Oak Mine Unified School District
Cabrillo Unified School District
California Association of School Business Officials
California School Boards Association
Chico Unified School District
Cloverdale Unified School District
Coalinga-Huron Joint Unified School District
Corning Union Elementary School District
Delhi Unified School District
Encinitas Union School District
Enterprise Elementary School District
Guerneville School District
Hueneme Elementary School District
Junction Elementary School District
Lincoln Unified School District
Morgan Hill Unified School District
Mt. Diablo Unified School District
Reef-Sunset Unified School District
Roseland School District
Shasta Union High School District
Small School Districts' Association
Somis Union School District
Southern Humboldt Unified School District

Southern Trinity Joint Unified School District
Summerville Union High School District
Taft City School District
Wasco Union High School District
West Hills Community College District
West Sonoma County Union High School District
Wheatland Union High School District
Whittier City School District
Wilmar Union School District
One individual

Analysis Prepared by: Ethan Jones / E. & R. / (916) 319-2094