

Budget and Accounting Practice Tip

February 2010:

How does a Cash Flow Projection help a District in implementing a bond program?

A Cash Flow analysis minimizes the expense of bond issuances, maximizes the potential for interest earnings, while providing the available funds needed to implement the bond program in an efficient manner.

Many districts rely on borrowing cash from multiple funds to loan to other funds to meet obligations during cash shortages. With state deferrals continuing and revenue cuts depleting local agency reserves, borrowing is becoming limited.

Cash flow is simply a pattern of income and expenditures, or inflows and outflows. When the amount of expenses are higher than the amount of income, the District has a negative cash flow – and its fiscal health is at risk.

Cash flow projections need to be accurate and continuous because Districts need to know when to borrow, how much to borrow, and which borrowing options make the most sense. Sometimes, though, borrowing can be out of range as a possible solution. When cash dips into the negative, Districts need to prepare for borrowing or implement budget reductions to retain reserves and cash. Knowing ahead of time enables Districts to stay in the black and maintain solvency.

Poor cash flow analysis and reconciliation, along with failure to recognize year-to-year trends, such as declining enrollment or deficit spending, can affect cash flow tremendously and create fiscal distress.

Hillsborough City School District

A key component to planning and implementing any bond program is the cash flow analysis – the driver for many decisions in planning a capital outlay building program.

A District must consider the costs and priorities of various bond projects throughout its district. The estimated costs of those projects in conjunction with the availability and timing of funds determines the timing of the implementation. A strategy must be developed that takes this into consideration minimizing the expenses of bond issuances, maximizing the potential for interest earnings, while providing the available funds needed to implement the bond program in an efficient manner.

Cash flow analyses are especially critical for Proposition 39 bonds, which allow for a lower voter approval thresholds of 55 percent, but caps the maximum debt service to \$60 per \$100,000 of assessed value for unified school districts or \$30 per \$100,000 for elementary and high school districts. These caps often create a situation where the bond authorization exceeds the current assessed value so the program is cash-flow constrained.

In the case of Hillsborough City School District, the voters provided the District with authorization to sell \$66.8 million in General Obligation Bonds. However, the assessed value would not support the sale of

the entire authorized amount. In fact, the maximum first issuance that could be supported by the assessed value was only \$13.5 million. The future sales had to rely on increased assessed property values. Based on the market projections it was estimated that there would have to be four cycles of bond issuances with the last being estimated to occur in 2013. CPM then used the cash flow analysis tool to determine the best strategy by running different scenarios. One of these scenarios was to consider the issuance of Bond Anticipation Notes or "BAN's." BANs are a short-term financing option that provides funds in advance of being able to issue the General Obligation Bonds. CPM calculated the cost difference between the cost of issuance of the BAN's against the escalation cost of delaying projects for five to six years. It was determined that the BANs would not only save the District millions in escalation, but would deliver the new facilities many years sooner. We now are happy to report that the BANs were sold in 2008, the projects have been completed, and the students are now enjoying their new facilities years ahead of a conventional bond sell schedule. The savings have been applied to implanting additional projects.

Cash Flow analyses are also very critical when determining the timing for the next round of bond or BAN sells. During these critical periods, CPM increases the quarterly cash flow projections to detailed monthly cash flow projections to ensure that work does not exceed the District's capacity to pay and informs critical decisions with the District's bond underwriter to maximize proceeds. The timing of obtaining the most current tax information from the County and optimizing the bond market timing can mean significant proceed differences.