



An Audit Report on

Certification of the Permanent School Fund's Bond Guarantee Program for Fiscal Year 2016

February 14, 2017

Members of the Legislative Audit Committee:

The State Auditor's Office certifies that, for the fiscal year ended August 31, 2016, the amount of school district and charter district bonds guaranteed by the Permanent School Fund's (Fund) Bond Guarantee Program (Program) was within the limits applicable to the Program. In addition, the Fund had sufficient capacity of \$4.9 billion to meet the State Board of Education's (Board) requirement to hold no less than 5 percent of the total guarantee capacity in reserve for the same time period.

As of August 31, 2016, the total principal of the 3,279 outstanding bond issues guaranteed by the Program was \$68.3 billion. (See attachment for additional information on the Program's fiscal year 2016 activity.)

Table 1 shows the limits applicable to the Program as of August 31, 2016, imposed by the Board, state statute, and the U.S. Internal Revenue Service. As of August 31, 2016, the Program could guarantee an additional \$24.7 billion in bonds before reaching the limit imposed by Board rules and statute, net of its \$4.9 billion reserve. The final remaining capacity is equal to 25 percent of the Program's statutory capacity.

Table 1

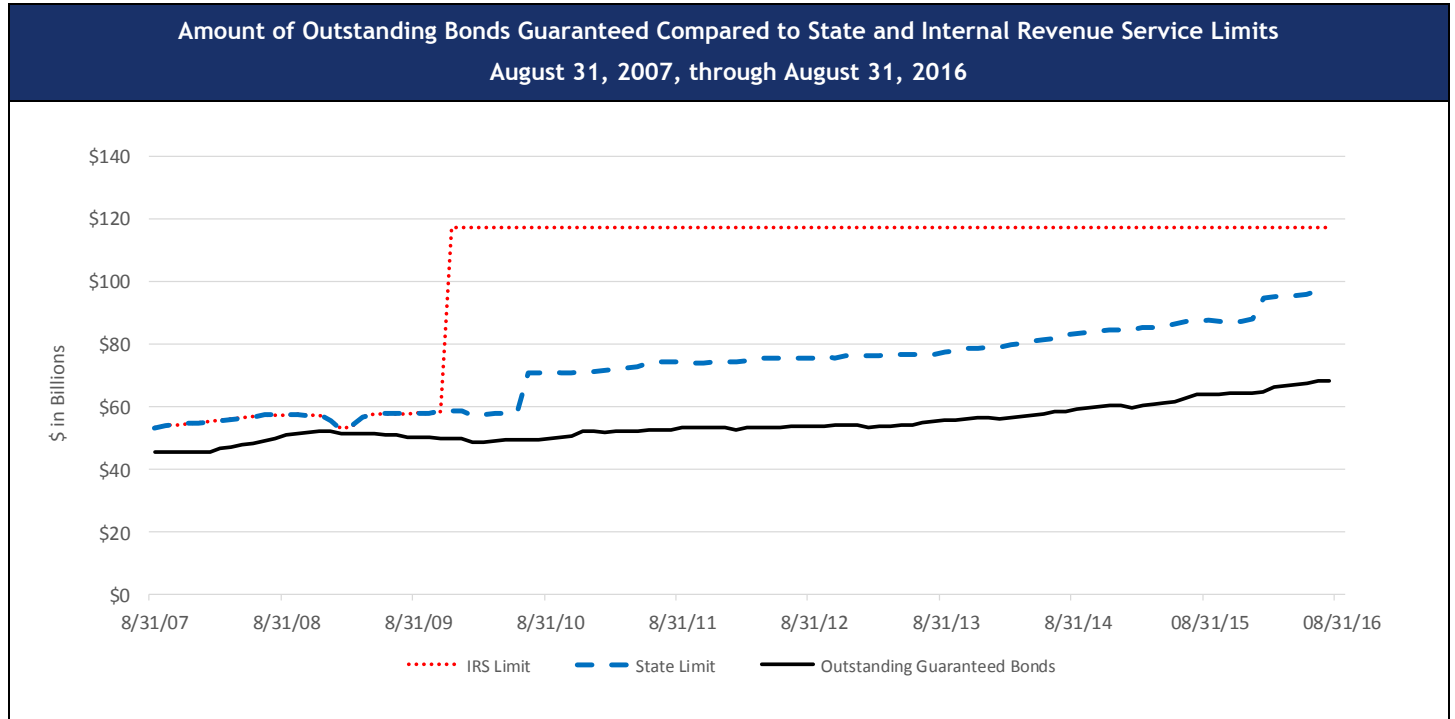
Limits Applicable to the Program		
Type of Limit	Limit Amount	Total Applicable Bonds Guaranteed as of August 31, 2016
Total guarantee capacity limit imposed by the Board and statute	\$97.9 billion ^a	\$68.3 billion
Total guarantee capacity limit imposed by the U.S. Internal Revenue Service	\$117.3 billion ^b	\$68.3 billion
Charter district allocation	\$1.1 billion ^c	\$961.0 million
Charter district refunding bonds	\$549.8 million ^d	\$382.7 million
<p>^a Title 19, Texas Administrative Code, Section 33.65(e), set a limit on the Program's bond guarantee capacity of 3.25 times the cost value of the Fund, as permitted by Texas Education Code, Section 45.053(d).</p> <p>^b Title 26, Code of Federal Regulations, Section 1.148-11(f), established a bond guarantee capacity limit of no more than 500 percent of the total cost of the assets held by the Fund as of December 16, 2009.</p> <p>^c Texas Education Code, Section 45.0532(a), limited the available bond capacity for charter districts based on the percentage of the number of students enrolled in open-enrollment charter districts compared to the total number of students enrolled in all Texas public schools. For fiscal year 2016, that percentage was 4.68 percent.</p> <p>^d Texas Education Code, Section 45.0532(a-1), limited the amount that the commissioner of education can approve for charter district refunding or refinanced bonds for guarantee to one-half of the total amount available for the guarantee of charter district bonds.</p>		

Sources: Texas Administrative Code; Texas Education Code; the *Texas Permanent School Fund Comprehensive Annual Financial Report for the Fiscal Year Ending August 31, 2016*; and Program data from the Texas Education Agency.

SAO Report No. 17-024

Figure 1 shows the amounts of outstanding bonds guaranteed and the statutory and U.S. Internal Revenue Service guarantee limits from August 31, 2007, through August 31, 2016. The Board’s additional reserve is not presented in the graph.

Figure 1



Sources: *Texas Permanent School Fund Comprehensive Annual Financial Report for the Fiscal Year Ending August 31, 2016*, and Program data from the Texas Education Agency.

The guarantee saves school districts and charter districts money by enhancing their bond ratings to the highest possible rating. Without the Program’s guarantee, school districts and charter districts would need to (1) purchase private bond insurance or (2) pay higher interest rates on the bonds they sell.

We appreciate the Texas Education Agency’s cooperation during this audit, particularly the cooperation of staff of the Permanent School Fund. If you have any questions, please contact Michael Owen Clayton, CPA, CISA, CFE, CIDA Audit Manager, or me at (512) 936-9500.

Sincerely,

Lisa R. Collier, CPA, CFE, CIDA
First Assistant State Auditor

Attachment

cc: The Honorable Greg Abbott, Governor
Members of the State Board of Education
Ms. Donna Bahorich, Chair
Mr. Lawrence A. Allen, Jr.
Ms. Erika Beltran
Mr. David Bradley
Ms. Barbara Cargill
Mr. Ruben Cortez, Jr.
Mr. Keven Ellis
Ms. Patricia Hardy
Mr. Tom Maynard
Ms. Sue Melton-Malone
Mr. Ken Mercer
Ms. Geraldine Miller
Ms. Georgina C. Pérez
Ms. Marisa B. Perez
Mr. Marty Rowley
Texas Education Agency
Mr. Mike Morath, Commissioner of Education
Mr. Holland Timmins, Executive Administrator
and Chief Investment Officer,
Permanent School Fund

Objective, Scope, and Methodology

The objective of this audit was to determine whether the total amount of school district and charter school **bonds the Permanent School Fund's (Fund) Bond Guarantee Program (Program)** guarantees is within the limits established by state statute.

The scope of this audit covered the Fund's valuation and all bonds guaranteed by the Fund at the end of fiscal year 2016.

Audit work included reviewing the State Board of **Education's bond guarantee limit and reserve calculations for accuracy and determining the Fund's total cost value as of the end of fiscal year 2016.**

Auditors also assessed the design and operation of applicable internal controls. That assessment included observing key controls relevant to the Program.

Audit fieldwork was conducted from November 2016 through December 2016. We conducted this audit in conjunction with the financial opinion audit of the Permanent School Fund and in accordance with generally accepted governmental auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit **objective. The following staff of the State Auditor's Office performed the audit:**

- Gregory Scott Adams, CPA, CGFM, MPA (Project Manager)
- Michael Karnes, MBA (Assistant Project Manager)
- Ann E. Karnes, CPA
- Brianna C. Pierce, CPA (Quality Control Manager)
- Michael Owen Clayton, CPA, CISA, CFE, CIDA (Audit Manager)



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Attachment

Section 1

Summary of Bond Guarantee Information

Tables 2 and 3 provide a summary of fiscal year 2016 activity for the Permanent School Fund's Bond Guarantee Program (Program) and show the changes in the number and dollar amount of outstanding bonds guaranteed by the Program.

Table 2

Number of Guaranteed Bonds Outstanding			
Category	School Districts	Charter Districts	Total Number of Issues
Balance on August 31, 2015	3,089	28	3,117
Issued during fiscal year 2016	447	8	455
Issues that matured during fiscal year 2016	(236)	(1)	(237)
Issues that refunded during fiscal year 2016	(56)	0	(56)
Number of Issues on August 31, 2016	3,244	35	3,279

Source: Supplementary information in the Permanent School Fund's *Comprehensive Annual Financial Report for the Fiscal Year Ending August 31, 2016*.

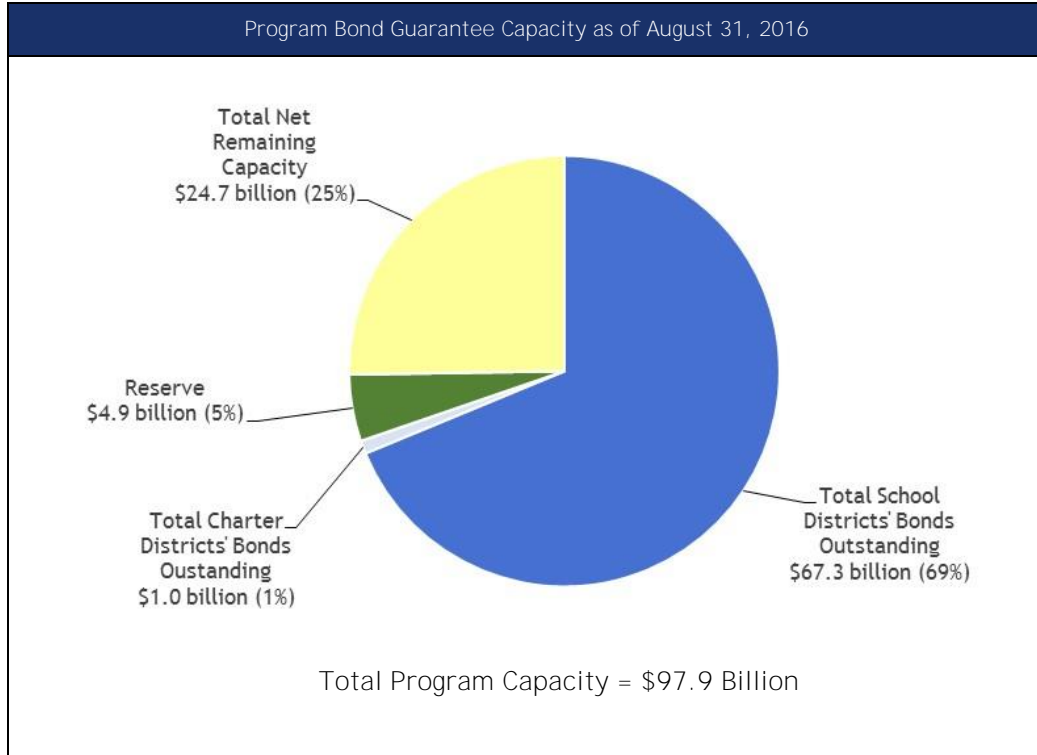
Table 3

Balance of Guaranteed Bonds Outstanding			
Category	School Districts	Charter Districts	Total Amount of Issues
Balance on August 31, 2015	\$ 63,197,514,047	\$ 757,935,000	\$ 63,955,449,047
Issued during fiscal year 2016	13,963,662,044	214,232,000	14,177,894,044
Issues that matured during fiscal year 2016	(2,572,253,005)	(11,142,000)	(2,583,395,005)
Issues that refunded during fiscal year 2016	(7,246,619,642)	0	(7,246,619,642)
Balance on August 31, 2016	\$67,342,303,444	\$961,025,000	\$68,303,328,444

Source: Supplementary information in the Permanent School Fund's *Comprehensive Annual Financial Report for the Fiscal Year Ending August 31, 2016*.

Figure 2 provides a summary of the Program's capacity as of August 31, 2016. The total net remaining capacity of \$24.7 billion includes \$23.6 billion for school districts and \$1.1 billion for charter districts.

Figure 2



Source: Based on Program data from the Texas Education Agency.