



TEXAS EDUCATION AGENCY

1701 North Congress Ave. ★ Austin, Texas 78701-1494 ★ 512/463-9734 ★ FAX: 512/463-9838 ★ <http://www.tea.state.tx.us>

Shirley J. Neeley, Ed.D.
Commissioner

June 12, 2006

RECEIVED

JUN 15 2006

OPINION COMMITTEE

RECEIVED

JUN 14 2006

OPEN RECORDS DIVISION

RQ-0500-GA

The Honorable Greg Abbott
Texas Attorney General
Post Office Box 12548
Austin, Texas 78711-2548

FILE # ML-44844-06
I.D. # 44844

Dear General Abbott:

I am writing to request your guidance concerning the effect of Sections 44.031 and 44.033, Texas Education Code ("Section 44.031" and "Section 44.033", respectively), if any, on the procedures for the purchase of property by lease-purchase agreement under Sections 271.004 and 271.005, Texas Local Government Code ("Section 271.004" and "Section 271.005", respectively)¹, as well as Chapter 2254, Texas Government Code ("Chapter 2254"). The Texas Education Agency recently performed an audit in which questions regarding the operation of those statutes were raised².

School districts are authorized to purchase real property under Section 271.004 through a lease-purchase arrangement, subject to publication of notice and voter approval if a petition signed by five percent of the registered voters in the district is presented. Section 271.005 authorizes a broad range of "governmental agencies", including school districts, to purchase personal property through a lease-purchase arrangement, though without the publication and election requirements in Section 271.004. Purchases under sections 271.004 and 271.005 may involve the services of a financial consultant and financing charges in addition to the underlying purchase of real or personal property.

Section 44.031 requires "all school district contracts³" valued above \$25,000 to be made by one of ten listed methods. Subsection 44.031(e) provides that "[t]o the extent of any conflict, this subchapter prevails over any other law relating to the purchasing of goods

¹ Sections 271.001 through 271.009 make up Subchapter A of the Texas Local Government Code, known as the "Public Property Finance Act".

² Attached to this request are a copy of the agency preliminary audit, as well as correspondence from the district, the district's financial consultant and legal counsel. The agency has left pending the issues raised in this request and finalized the remainder of audit. A copy of the final audit report is also attached.

³ Section 44.031(a) excludes contracts for "produce or vehicle fuel".

"Good, Better, Best—never let it rest—until your good is better—and your better is BEST!"

and services⁴. Subsection (f) excludes services of an architect, attorney or fiscal agent and provides an option to contract with a financial consultant in the manner provided by Section 2254.003, Government Code. Section 44.033 applies to purchases of personal property valued between \$10,000 and \$25,000 and requires creation of a "vendor list" for such purchases.

Your office has previously considered the relationship between a different subchapter of Chapter 271 of the Local Government code and Section 44.031. Attorney General's Opinion DM-387 (1996) held that a school district was required to comply with competitive bidding procedures in Subchapter B of Chapter 271 when the district chose to utilize competitive bidding under Section 44.031. That opinion includes the statement "to the extent any of the procedures mandated by Chapter 271, subchapter B conflict with section 44.031 of the Education Code, section 44.031 prevails." Opinion JC-0037 later held that a more specific provision in Chapter 44 of the Education Code (Section 44.040, enacted in 1997) superseded that conclusion and required compliance with Chapter 271 only as specifically set out in that section of the Education Code.

Attorney General's Opinion JC-0492 (2002) also appears relevant to the issues of this request. That opinion held that a school district could not utilize the provisions of Chapter 304, Local Government Code, to purchase electricity because the "political subdivision corporation" authorized by that chapter was not listed among the permissible purchasing options in Section 44.031⁵. The opinion concludes that "a school district may not use a purchasing method provided by a statute outside of the Education Code that is not expressly listed or included within those methods listed in Section 44.031."⁶

My questions are as follows:

1. Are school districts required to use a method authorized by Sections 44.031 or 44.033, as applicable, to enter all or part of lease-purchase agreements under Sections 271.004 and 271.005?
2. If your answer to Question 1 above is "yes", must the financing agreement entered into by the district be selected pursuant to a method authorized by Sections 44.031 or 44.033, as applicable, distinct from the underlying purchase of real or personal property?

⁴ Subsection 44.031(e) also makes explicit that it is subject to statutes relating to contracts with historically underutilized businesses.

⁵ Section 44.031 was subsequently amended to authorize the formation of a political subdivision corporation as a permissible method by the addition of Subsection 44.031(a)(10).

⁶ We wish to be clear that we do not suggest that school districts may not use the provisions of subsections 271.004 and 271.005. Our inquiry is limited to the question of whether the competitive procedures under sections 44.031 and 44.033 must be used to enter into agreements under Sections 271.004 and 271.005. We assume those sections remains valid methods for the lease-purchase of real and personal property. Note in that regard that Section 46.004, Education Code, was enacted subsequent to Section 44.031 and provides for state financial assistance for lease-purchase agreements.

3. May a school district enter into a lease-purchase agreement under Section 271.004 or Section 271.005 as part of a single transaction that includes the retention of a financial consultant under Section 2254.003, Government Code without utilizing the procedures required by Section 44.031 or Section 44.033?
4. To the extent a financial consultant is contracted for under Chapter 2254, must a request for qualifications or similar competitive process be used to select the provider? Does the selection and negotiation procedure in Section 2254.004 apply to contracting with a financial consultant⁷?

Thank you for your consideration of this request.

Sincerely,



Dr. Shirley J. Neeley, Ed. D.
Commissioner of Education

⁷ Section 2254.004 applies by its terms to contracts for "architectural, engineering, or land surveying services", but appears to be incorporated by reference in Section 44.031(f).



TEXAS EDUCATION AGENCY

1701 North Congress Ave. ★ Austin, Texas 78701-1494 ★ 512/463-9734 ★ FAX: 512/463-9838 ★ <http://www.tea.state.tx.us>

Shirley J. Neeley, Ed.D.
Commissioner
April 26, 2006

Mr. Trey Lawrence, Superintendent
Shiner Independent School District
P. O. Drawer 804
216 W. 13th Street
Shiner, Texas 77984

Subject: Preliminary Report

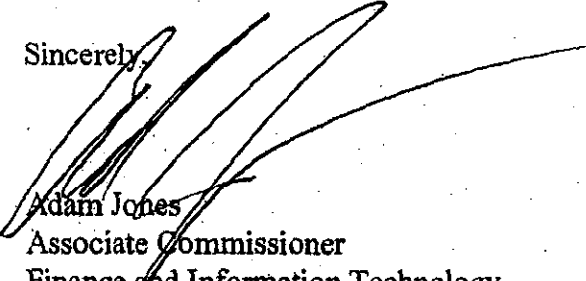
Dear Mr. Lawrence:

Attached is a preliminary report from Rita Chase, Acting Managing Director, Division of Financial Audits, detailing the findings and required actions resulting from an on-site investigation of the Shiner Independent School District. The auditors' findings are issued initially as a preliminary report for your review and comment.

Please review the report carefully and file a written response within 20 business days from the date of this letter that addresses both the auditors' findings and required actions. Your response will be incorporated as an attachment to the final report.

Should you have any questions, please feel free to contact me or Rita Chase at (512) 463-9095.

Sincerely,


Adam Jones
Associate Commissioner
Finance and Information Technology

AJ:RC:rs
Attachment

c: Board Members, Shiner ISD

"Good, Better, Best—never let it rest—until your good is better—and your better is BEST!"

MEMORANDUM

TO: Adam Jones, Associate Commissioner, Finance and Information Technology
FROM: Rita Chase, Acting Managing Director ^{RC}
DATE: April 17, 2006
SUBJECT: Investigation at Shiner Independent School District #143-903

From February 15 through February 17, 2006, Texas Education Agency (TEA) auditors Michael Richmond and Paul Delaney from the Division of Financial Audits conducted an on-site investigation at the Shiner Independent School District (SISD), in response to written complaints that were forwarded to this office. The exhibits in this report contain illustrations of investigative findings and are not all-inclusive. During the visit, the auditors contacted the following individuals:

Gloria Reindl, Trustee
Michael Huser, Trustee
Trey Lawrence, Superintendent
George Grimes, Attorney at Law
Ken Leach, Consultant

We disclosed, through verbal inquiries and examination of district records, the following:

1. Concern: The school district was not in compliance with Section 271.004 of the Local Government Code regarding the construction of the new instructional facility.

Finding:

After reviewing documentation provided by the district as described below, it appears that the district was in compliance with §271.004 of the Local Government Code in the construction of the new instructional facility (see Exhibit J page 1).

The district advertised in the Shiner Gazette on February 10, 2005, to enter into a lease-purchase contract for an amount not to exceed \$5,600,000 (see Exhibit A). On May 2, 2005, the board of trustees voted to enter into a lease-purchase contract between the SISD and the SISD Public Facility Corporation (see Exhibit B page 88).

In addition, the subsequent approved agreement was submitted to the Texas Attorney General's office in accordance with the requirements in §271.004 of the Local Government Code.

Note: Prior to the board of trustees vote to approve the contract, district patrons submitted a petition. However, the district's attorney determined that the petition submitted to the district did not meet Section 271.002 of the Texas Election Code.

2. **Concern:** The school district was not in compliance with Section 44.031 of the Texas Education Code (TEC) regarding the financial loan agreement for personal property.

Finding: On February 3, 2005, the SISD board of trustees voted to enter into a lease-purchase agreement with First Community Bank, N. A. for the purchase of personal property in the amount of \$2,232,720 (see Exhibit B pages 46 and 60). On July 13, 2005, at the recommendation of the district's administration, the district entered into a lease-purchase agreement with AIG Commercial Equipment Finance, Inc. in order to refinance the prior agreement with First Community Bank, N. A. (see Exhibit C pages 1-2). According to information provided to the auditors, the district incurred refinancing costs as follows: \$77,307 in transactional costs and an estimated \$221,282.33 in additional interest costs over the term of the loan. The superintendent stated the purpose for the refinancing was to extend the term of the lease-purchase from a 12-year term to a 15-year term to reduce the annual payments.

The TEC Section 44.031 requires that all contracts of \$25,000 or more are to be competitively procured utilizing one of the methods allowed under this section. The district did not provide the auditors with documentation showing that the district utilized a method under §44.031 of the TEC to competitively procure the financing contract. However, the Division of Financial Audits is seeking a legal opinion on this concern.

3. **Concern:** The school district was not in compliance with Section 45.207 of the Texas Education Code regarding the competitive procurement of its depository contract.

Finding: Documentation provided to the auditors disclosed that the district solicited bids for the 2005-2006 and 2006-2007 depository contracts on April 22, 2005 (see Exhibit D). Bid notices were sent to two financial institutions which both responded to the district's notice with sealed bids (see Exhibit E pages 1-29 and 30-48). Texas Education Code Section 45.207 (c) states in part that, "In determining the highest and best bid, or in case of tie bids the highest and best tie bids, the board of trustees shall consider the interest rate bid on time deposits, charges for keeping district accounts, records, and reports and furnishing checks, and the ability of the bidder to provide the necessary services and perform the duties as school depository, together with all other matters that in the judgment of the board of trustees would be to the best interest of the school district." The district's bid notices that were sent to the two financial institutions stated that the bidders would be evaluated on the following criteria: 1. Cost of services 2. Interest rates offered on time deposits, checking accounts and/or repurchase agreements 3. Experience in providing depository services to similar accounts 4. Financial strength of institution and 5. Location(s) and hours of operation of bank offices (see Exhibit F pages 1-4 and 5-8). In a school district memorandum, dated February 23, 2006, a district official states that the district did not have any documentation showing how the board of trustees actually evaluated the banks based on the above criteria (see Exhibit G). Documentation provided to the auditors did show; however, that one of the bidders, Lone Star Bank, appeared to offer higher interest yields on its time deposits and money market accounts than did the other bidder, First National Bank. In addition, First National Bank imposed transaction fees for certain banking services such as wire transfers and stop payments, whereas Lone Star Bank imposed no transaction fees for the same services. The district's board of trustees voted on June 8, 2005, to award the depository contract to First National Bank.

Subsequent to the June 8, 2005, board meeting, it was learned that a board member who voted for the contract had a conflict-of-interest. In a special meeting on June 27, 2005, the board of trustees voted to rescind its prior action and consulted with the district's attorney concerning the re-bid of the contract (see Exhibit B page 90). On July 13, 2005, the board voted to award the contract to First National Bank (see Exhibit B page 94). It was noted that the district allowed First National Bank to submit a revised bid that altered the terms of the original bid instead of rejecting all bids and going through the competitive procurement process for the depository contract.

It was also brought to the auditors' attention that the district may not have been receiving the correct amount of interest, as stated in the depository contract with First National Bank, on its time deposits. The auditors requested that the district conduct a comparison of the interest rate stated on its depository contract to the interest rate that was actually received on its time deposits from January 1, 2005, through June 30, 2005. In a letter addressed to the school district and dated February 22, 2006, the Executive Vice President of First National Bank states that an interest rate comparison was conducted and that some discrepancies were discovered (see Exhibit H). Also enclosed in the letter was a check for \$1,347.97, made out to the district for the additional interest due (see Exhibit H page 3).

4. **Concern:** The district did not comply with the Texas Education Code (TEC) 44.031 Subchapter B regarding purchasing contracts.

Finding: The following items are excerpts from SISD board minutes concerning the construction of a pre-kindergarten through 12th grade instructional facility:

- On May 26, 2004, Mr. Ken Leach of Leach and Associates presented the board of trustees the long-range planning process concerning this project.
- On June 16, 2004, the board of trustees decided to allow the former superintendent to discuss with Ken Leach the long-range planning process. In addition, the former superintendent was to obtain a price quote from Mr. Leach for his services.
- On July 5, 2004, the former superintendent presented a proposal from Ken Leach & Associates for the consulting services for the long-range planning process. The board of trustees decided to place this item on the agenda for the next board meeting.
- On July 14, 2004, the board of trustees voted to enter into an agreement with Leach and Associates for long-range planning process services.
- On September 15, 2004, the board decided to allow Mr. Leach to look at the agriculture building to determine whether it could be repaired or if a new building needed to be built.
- On October 13, 2004, the former superintendent presented the board of trustees with a progress report, which included surveys, from Ken Leach & Associates regarding the needs assessment for Shiner ISD.
- On November 10, 2004, Leach and Associates presented the board of trustees a report on the facility needs for the SISD.

- On January 26, 2005, Ken Leach and Associates presented the board of trustees a report on another phase of the facility needs assessment for SISD. In addition, Mr. Leach addressed the board concerning a lease-purchase contract from Chancellor Financial which would provide the district with additional funds necessary to complete the building project. The board of trustees voted to accept the proposal by Chancellor Financial.
- On February 9, 2005, the former superintendent reported to the board of trustees that Mr. Ken Leach had fulfilled his contractual agreement with SISD. During this discussion, the board directed the former superintendent to negotiate another agreement with Mr. Ken Leach at a flat rate to see this project through completion.
- On March 9, 2005, a final invoice from Leach & Associates was given to the board for the hours worked on the needs assessment from September 1 through January 31, 2005. During this meeting, the board of trustees voted to hire Mr. Ken Leach as consultant and project manager for the new construction site.
- On April 13, 2005, Mr. Ken Leach addressed the board of trustees regarding the Phase I Environmental Study, Asbestos Survey/Inspection and the Geo Tech report. In addition, Mr. Leach briefly discussed the six methods for selecting a contractor for a construction project. After the presentation, the board of trustees voted to select the competitive sealed proposal as the method for selecting a contractor. The board of trustees voted to approve Jim Singleton as the SISD architect.
- On May 2, 2005, the board of trustees voted to sell certain land to the Shiner ISD Public Facility Corporation.
- On July 13, 2005, Jim Singleton of JSA Architects presented the board of trustees with a detailed presentation regarding the site plan. The board voted to approve the master plan and program.
- On August 10, 2005, Mr. Ken Leach updated the board of trustees on proposals submitted by five contractors. Mr. Leach advised the board that he would present his selection at the August 29, 2005, board meeting.
- On August 29, 2005, Mr. Ken Leach discussed with the board of trustees the proposals submitted by the five contractors. On the recommendation of Mr. Leach, the board of trustees voted to award the contract to Sterling Structures of Houston/Columbus, Texas. In addition, the board of trustees voted to approve the proposal of PSI Inc. of Victoria, Texas for performance of a subsurface exploration at the site of the building project.
- On January 11, 2006, the board of trustees was presented a list of subcontractors and their bid amounts. The board voted to direct Sterling Structures to proceed by January 25, 2006, with an initial contract sum of \$7,353,000 pending approval from the district's attorney.

Review of board minutes (see excerpts above) and other district documentation and interviews with district personnel disclosed the following deficiencies in the process and procedures utilized by the district in procuring construction services for the new campus facility:

- a. On July 14, 2004, the SISD board of trustees voted to enter into an agreement with Leach and Associates for long-range planning process services (Exhibit B page 15). On February 9, 2005, the former superintendent informed the board that Mr. Leach had fulfilled his contractual agreement with SISD. On March 9, 2005, the board of trustees voted to hire Mr. Ken Leach as consultant and project manager for the new construction site (see Exhibit B page 68).

The district did not provide the auditors with any written and signed agreements or contracts between SISD and Ken Leach and Associates. The only information provided by the district was a draft proposal for consulting services from Mr. Ken Leach to the former superintendent (see Exhibit I). Without a written agreement or contract, outlining the compensation method and the responsibilities of SISD and Mr. Leach regarding the services to be performed, the auditors could not determine if Mr. Leach had been properly compensated or if the services performed by Mr. Leach were in accordance with the intent of the parties involved.

The original draft proposal dated June 25, 2004, stated that Leach & Associates bills at an hourly rate of \$85 per hour (see Exhibit I page 2). In addition, the proposed draft included certain services which the board of trustees did not direct the former superintendent to negotiate nor were these services approved by the board during the July 14, 2004 (see Exhibit B pages 13-17).

As of April 2006, Mr. Leach and Associates have been paid a total of \$34,110. Of the total paid to Mr. Leach, \$14,930 was for services performed as part of the long-range planning process and the remaining amount paid was for services as project manager. The actual construction of the new campus has recently begun, and it is anticipated that Mr. Leach will receive additional future compensation as project manager. On February 9, 2005, the board of trustees directed the former superintendent to negotiate with Mr. Leach a flat-rate contract for services as a project manager. However, without a written contract which states the amount to be paid by the district, it could not be determined whether the contract amount would exceed the threshold requiring the district to competitively procure the services under TEC §44.031 (see Exhibit J pages 3-5).

- b. On April 13, 2005, the board of trustees voted to select the competitive sealed proposals as the method for selecting a contractor. During this meeting, upon Mr. Leach's recommendation, the board voted to approve Jim Singleton as the district's architect (note: no documentation was provided that stated Mr. Leach had this authority). The district did not provide documentation evidencing compliance with TEC §44.039 (b) (competitive sealed proposals) which states in part, if the engineer or architect is not a full-time employee of the district, the district shall select the engineer or architect on the basis of demonstrated competence in accordance with §2254.004 of the Government Code (see Exhibit J page 9). In addition, the district did not provide documentation evidencing compliance with TEC §44.031 (g) which requires published notification of the request for qualifications (RFQ) (see Exhibit J page 4).

The district did not provide the auditors documentation evidencing that a formalized RFQ process was utilized in selecting the district's architect. Additionally, the district did not provide documents disclosing the qualifications of the architects considered nor their ranking based on their qualifications. According to information obtained from the district, Mr. Leach and the former superintendent contacted a few architects and through verbal interviews selected Jim Singleton as the district's architect.

In addition, the district did not provide documentation evidencing compliance with TEC §44.039 (c) which states, "the district shall provide or contract for, independently of the contractor, the inspection services, the testing of construction materials engineering, and the verification testing service necessary for the acceptance of the facility by the district. The district shall select those services for which it contracts in accordance with §2254.004, Government Code, and shall identify them in the request for proposals."

As of the date of the auditors' visit, the district had not provided documentation evidencing compliance with this section.

- c. On August 29, 2005, on the recommendation of Mr. Leach, the board of trustees voted to award the construction contract to Sterling Structures of Houston/Columbus, Texas. Information provided by the district disclosed that Mr. Leach had conducted the evaluation of the proposals submitted by the contractors. The district did not provide the auditors with any documentation that authorized Mr. Leach to conduct the evaluation of the proposals. In addition, there was no documentation provided evidencing compliance with TEC §44.0312, Delegation (see Exhibit J page 8). The newspaper advertisement and request for proposal (RFP) documentation did not disclose delegation authority to Mr. Leach to evaluate the RFPs (see Exhibit K).

The district did not provide the auditors documentation evidencing how the contractor proposals were evaluated, based on the criteria published in the RFP as required under TEC §44.039 (e), (f) and TEC §44.035 (see Exhibit J pages 6 and 10).

5. **Concern:** The entering into the lease-purchase contract to build a new pre-kindergarten through 12th grade facility has resulted in a major negative impact to the district's financial condition.

Finding: A review of school district records and interviews with district personnel disclosed that the district has been able to strengthen its financial position by increasing its general fund balance over the past two years. The fiscal year 2006 adopted budget indicated that the district has sufficient financial resources to meet current obligations without drawing down the district's general fund balance. However, the current variability of revenues over expenditures has substantially decreased as a result of the new financial obligations incurred by the district. The district's current tax rate is at the maximum for maintenance and operations which leaves limited options for the district to increase revenues if substantial increases in payroll and other costs (i.e. energy costs) occur in the future.

Required Actions:

1. The district ensure compliance with the competitive procurement laws found in TEC §44 and §2254 of the Government Code. In addition, district officials receive training regarding the competitive procurement laws.
2. The district provide the Division of Financial Audits a budget forecast for fiscal years 2007 and 2008. (We note that the current state financing system is subject to major change; however, any budget forecasts should be revised to reflect any changes resulting from legislative action. In addition, it is understood that this required action will not be completed in the time allotted for the district to respond to the report; however, the district should provide an approximate date that it anticipates completing the required action).



Chancellor Financial, L.L.C.
10005 Spicewood Mesa
Austin, Texas 78759
www.chancellorfinancial.net
1-800-213-4580



March 10, 2006

Mr. David Anderson, General Counsel
Texas Education Agency
1701 N. Congress Avenue
Austin, Texas 78701-1491

VIA FACSIMILE

Dear Mr. Anderson:

I have been requested by legal counsel for Shiner Independent School District to provide legislative intent information relative to the Public Property Finance Act 1979 64th Legislative Session.

BACKGROUND: The Public Property Finance Act was the idea of various Superintendents in my Legislative District in 1979. Several of the superintendents had attended national educational conferences and became familiar with lease purchase financing in other states. Indeed, some 47 states have lease purchase financing. In tandem with the superintendents request bond counsel also advised me of the need for this type of financing in order to provide school districts with an alternative financing tool. To that end, I agreed to sponsor the legislation, which passed overwhelmingly in the House and Senate. The 1979 Act 271.005 dealt specifically with lease purchase personal property transactions.

In 1993 the Legislature amended the act to authorize school districts to construct school buildings through lease purchase financing with very specific guidelines found in 271.004. Since 1993 the Attorney General's Office has through "all bond counsel letters" refined the requirements necessary for the issuance of lease purchase revenue bonds for real property development.

Since 1993 Chancellor Financial has been the authority and leader in alternative financing in Texas. I have held workshops at the Texas Association of School Boards and Texas Association School Administrators Conventions, Texas Rural Educators Association, and over 300 school boards. Our bond counsel has been in practice for 36 years and is one of the founders of the National Association of Governmental Leasing and Finance. The law firm has served as counsel on more than 1,800 tax-exempt finance transactions.

LEGISLATIVE INTENT: During the 64th Legislative Session the Public Property Finance Act had full committee hearings and floor votes in both the Texas House of Representatives and the Texas Senate. The intent was to provide school districts with an

RECEIVED



Anderson page 2.

unambiguous tool to secure financing for the purchase of personal property items ranging from computers to scoreboards. The intent was to give local school boards full authority to identify items needed by the district and then enter into a financing agreement with a financing source primarily banks and financing groups who would fund the entirety of the items needed. The legislation envisioned that financing was a specialized area and would most probably require some expertise from financial advisors/consultants familiar with the process. The lease purchase agreement is a tax-exempt instrument and must meet all of the statutory requirements for such tax-exempt status.

It was never the intent of the Legislature or my intent as author of the legislation to require a school district under Public Property Finance Act to be subject to the competitive bid laws as relates to the financing agreement. In all instances it was assumed that a district would competitively bid vendors offering to provide the personal property item. Therefore prior to the actual purchase of personal property items companies wishing to sell desks, chairs, cabinets, security equipment, lab equipment etc. would participate in a bid proposal under the competitive bid laws. However, it was never intended that the financing itself was subject to the bids laws due to the professional services of a bond attorney and financial advisor/consultant necessary for implementation of the lease purchase-financing contract. In addition, had the intent been to require compliance with the bids laws reference would have been included in the legislation.

I was also involved in the 1993 amendment to the Public Property Finance Act authorizing school districts to enter into lease purchase agreements for the financing of construction projects. The Legislature never intended to require the financing phase to be subject to competitive bid laws. Chancellor Financial was responsible for securing financing for the first lease purchase revenue bond in Texas. Therefore, we have been involved with this type of financing since 1993 and have probably financed more projects under this financing authorization than any company in Texas. Never has the financing been subject to competitive bid. Construction contracts for the construction of the project certainly fall within the competitive bid laws but not financing. Indeed, the Attorney General's bond counsel desk must approve the legal documentation for each transaction before the lease purchase revenue bond can be issued. Since 1993 the AG has never required the financing be competitive bid as a requirement before AG approval. The reason is simple there is no legal authorization to do so.

Since 1979 and 1993 respectively as relates to the Public Property Finance Law I know of no school districts that have competitively bid financing. All boards we have dealt with over the years have required competitive bids from vendor/suppliers of personal property equipment or items.



Anderson page 3

STEPS NECESSARY FOR FUNDING: I think it would be helpful to fully understand the process necessary to implement lease purchase financing:

1. **Engagement Agreement.** The school district approves and executes an engagement agreement with a financial advisor/consultant who outlines the responsibility of both the district and the financial consultant. For example, the engagement agreement authorizes the consultant to secure lease purchase tax-exempt financing for both personal and real property. The agreement indicates that the district must provide financial information to the consultant including but not limited to audited financial reports. The agreement sets out the fees for the consultant and bond counsel and underwriter.
2. **Credit Analysis.** The financial consultant secures audited financial reports, information as to existing debt, the district rating under the FIRST program and other financial information. The consultant reviews this information before seeking out a financing source for the project. Should the consultant determine that the district finances are poor the financing effort stops at that point. If the district meets the financial criteria then the next phase is implemented.
3. The financial consultant calls on the expertise and knowledge of underwriters, public securities officers at financial houses to determine the existing rates for tax-exempt school instruments and a recommendation as to banks or financial groups who have the best terms and rates. In addition, it is also important to have a financing source familiar with lease purchase financing in Texas and understands the legal documentation, school district finance and in particular the "non-appropriation" requirement in all lease purchase agreements in Texas.
4. The financial consultant makes contact with financing sources and request a payment schedule that will be consistent with the school district's budget. A payment/debt service schedule is provided and transmitted to the district for review usually by the Superintendent and/or the business manager. Upon a positive response from the district the financing phase begins. The financing sources request financial documents and their credit analyst review and submit questions relative to the district financial capabilities.
5. **Competent/qualified/experience bond counsel** is secured to draft legal documents for the transaction. Documents are drafted consistent with state law and then submitted to the district for approval. Further, bond counsel provides an "opinion letter" as to the legality of the transaction pursuant to state laws and as to the tax- exempt nature of the transaction.
6. Board of Trustees approve and execute legal documents usually reviewed by the district's school attorney prior to execution.
7. Project is funded upon the examination of the executed documents and execution by the funding source. The funding source or investor will have the documents reviewed by their own attorney before approval.



Anderson page 4.


8. Normally funds are held by a Trust Bank with proceeds available to the district through requisition forms.
9. The district must secure bids from contractors, sub-contractors, vendors providing materials, and retain the services of an architect, engineer, construction supervision etc.
10. In addition, if the financing is a lease purchase revenue bond then Attorney General approval is necessary before the bond can be issued requiring several other steps, including but not limited to, the establishment of a Public Facility Corporation.
11. Every aspect of the transaction including the lease agreement, the financing terms, all executed documents and appropriate exhibits are assembled by bond counsel in a bound transcript and provided to the school district, counsel, and financing source.

In conclusion there have been literally thousands of lease purchase agreements implemented since 1979 and 1993 respectively. At no time have any purposed rules or guidelines been published by the TEA or the Attorney General's Office or the Texas Register outlining specific bid rules relating to the financing of a particular project either under the 271.004 or 271.005 of the Tex. Loc. Govt. Code. Indeed, Chapter 44 enumerates various bid methodologies directed toward construction and equipment but no definitive direction as to financing. At this juncture school districts do not have a specific workable guideline as to bidding financing and that in my opinion is because there is no legislative authority to do so.

The information herein is to help better understand the Legislative intent relative to the Public Property Finance Act and related matters.

Should you have any questions or need further information do not hesitate to call.

Best Regards,


Bill Caraway
President-Chancellor Financial

WALSH, ANDERSON,
BROWN, SCHULZE
& ALDRIDGE, P.C.

ATTORNEYS AT LAW

AUSTIN • SAN ANTONIO • IRVING • ALBUQUERQUE

March 10, 2006

Mr. David Anderson, General Counsel
Texas Education Agency
1701 N. Congress Avenue
Austin, Texas 78701-1491

VIA FACSIMILE

RECEIVED
2006 MAR 16 AM 7:50
HEARINGS AND APPEALS

Re: Shiner ISD/ TEA Audit

Dear Mr. Anderson:

This firm represents the Shiner Independent School District ("District"). I am writing this letter at the request of the District and its financial consultant, Bill Caraway, of Chancellor Financial LLC. Certain aspects of the District's operations are currently the subject of an audit by the Texas Education Agency. I understand the auditors have raised a question regarding the procurement of a lease purchase agreement for personal property. Specifically, the question appears to be whether the lease purchase agreement, as distinguished from the procurement of the underlying personal property, should be procured pursuant to Texas Education Code Chapter 44 Subchapter B ("Chapter 44"). The District agrees that the procurement of the underlying personal property is subject to Chapter 44. For the reasons set out below, in my opinion there is no authority requiring a school district to procure a lease purchase agreement pursuant to the requirements of Chapter 44.

School districts are authorized to finance the purchase of real and personal property by Texas Local Code, Chapter 271, Subchapter A, the Public Property Finance Act. Local Government Code Section 271.005 sets out the requirements for financing personal property with a lease, a lease with an option or options to purchase, an installment purchase, or any other form considered appropriate by the governing body of the school district. Tex. Loc. Gov't Code §271.005(a)(2). This section also provides that the lease purchase or other form of financing may be for a term approved by the governing body, and may be payable from a pledge of all or any part of any revenues, funds, or taxes available to the school district. *Id.* §271.005(a)(3) and (4). The lease purchase agreement may provide for the payment of interest on the unpaid amounts of the contract and may contain prepayment provisions, termination penalties, and other provisions determined within the discretion of the governing body. *Id.* §271.005(c). However, the net effective interest rate on the lease purchase agreement may not exceed the net effective interest rate at which public securities may be issued in accordance with Government Code Chapter 1204. Finally, Section 271.005 (d) provides: "Subject only to applicable constitutional restrictions, the governing body may obligate taxes or

Mr. David Anderson

March 10, 2006

Page 2

revenues for the full term of a contract for the payment of the contract." Lease purchase agreements for personal property are not required to be submitted to the Attorney General for review.

No provision of Section 271.005 requires a school district to procure a lease purchase agreement for financing of personal property under Chapter 44 of the Education Code or any other competitive procurement requirement. Clearly, if the Legislature's intent were to require competitive procurement of lease purchase agreements, it would have included that requirement in Section 271.005. I have found no authority suggesting that competitive procurement is required for lease purchase agreements for personal property.

Pursuant to Local Government Code Section 271.004, lease purchase agreements for real property and improvements are required to be submitted to the Attorney General for review. Tex. Loc. Gov't Code §271.004(g). Although I do not provide bond counsel services to school districts, I am advised by Mr. Caraway of Chancellor Financial that the Attorney General, in reviewing lease purchase agreements for real property and improvements, does not require competitive procurement of those lease purchase agreements. This lends further support to the belief that competitive procurement is not required for lease purchase agreements of personal property.

The purpose of competitive procurement is to "stimulate competition, prevent favoritism and secure the best work and materials at the lowest practicable price, for the best interest and benefit of the taxpayers and property owners." *Texas Highway Comm'n v. Texas Ass'n of Steel Importers, Inc.*, 372 S.W.2d 525, 527 (Tex. 1963). It is difficult to see how application of the competitive procurement requirements of Chapter 44 would further these purposes.

In order to comply with the requirements of Chapter 44, the school district would be required to: (1) publish notice in a newspaper in the county in which the District's central administrative offices are located once a week at least two weeks before the deadline for receiving proposals; (2) issue a request for proposals pursuant to Section 44.031(a); (3) receive proposals; and (4) select the proposal that provides the best value to the District.

Regarding the publication of the notice, I understand that few local financial institutions invest in governmental entity lease purchase agreements. Rather, the financial institutions which provide financing for these agreements are generally state-wide or national in scope. Accordingly, publishing notice in a Lavaca County newspaper is unlikely to assure notice to potential proposers.

In addition, financing of lease purchase contracts for personal property does not lend itself to a request for proposals. I understand that potential lenders analyze a variety of factors affecting the school district's ability to make lease payments under the lease purchase agreement including review of audited financial reports, information on existing debt, the school district's rating under the FIRST program, and other financial information. The lender's proposal, based on its analysis, will include not only an interest rate and term but other provisions such as pre-payment options and

Mr. David Anderson

March 10, 2006

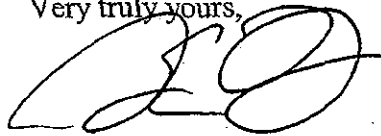
Page 3

termination rights. The school district's determination of best value for the District may be based not only on the "price", that is, interest rate, but other terms and conditions of the contract.

The school district's financial advisor's role is to identify potential lenders, provide information regarding the District's financial condition to those lenders, and advise the District regarding the terms and conditions of the lease purchase agreement. The financial advisor's efforts in procurement of the lease purchase agreement will generally exceed the requirements of procurement under Chapter 44 in terms of notice and obtaining the best value for the District.

In summary, in my opinion, there is no clear statutory requirement for a school district to procure a lease purchase agreement for personal property in accordance with the requirements of Texas Education Code Chapter 44, Subchapter B. The Attorney General does not appear to require competitive procurement of lease purchase agreements for real property. As a practical matter, the use of a financial adviser generally exceeds the requirement of Chapter 44. Accordingly, there is no basis for a determination that a school district has violated state law by failing to procure a lease purchase agreement for personal property pursuant to Texas Education Code Chapter 44 Subchapter B.

Very truly yours,



GEORGE E. GRIMES, JR.

GEG/smp

cc: Mr. Trey Lawrence - *Via Facsimile*
Mr. Bill Caraway - *Via Facsimile*



TEXAS EDUCATION AGENCY

1701 North Congress Ave. ★ Austin, Texas 78701-1494 ★ 512/463-9734 ★ FAX: 512/463-9838 ★ <http://www.tea.state.tx.us>

Shirley J. Neeley, Ed.D.
Commissioner

June 5, 2006

Mr. Trey Lawrence, Superintendent
Shiner Independent School District
P. O. Drawer 804
216 W. 13th Street
Shiner, Texas 77984

Subject: Final Report

Dear Mr. Lawrence:

This is to acknowledge your response to the preliminary report from Rita Chase, Director of the Division of Financial Audits. We note the district's response to the preliminary report and modifications were made to finding number four as the result of additional information provided with the district's response. This information was requested but was not provided by the district during the on-site visit by the Texas Education Agency (TEA) auditors. In addition, the district did not address any corrective actions that the district is undertaking to resolve the issues disclosed by the investigation.

Please note that the TEA will seek Texas Attorney General Opinions regarding certain competitive procurement issues dealing with financing contracts, financial consultants (advisors) and request for qualifications that were disclosed in this report.

This report is being issued as a final report which the district response is incorporated into the report as an attachment. However, this file will remain open until such time as the Attorney General Opinions are received and the district has provided an adequate corrective action plan which addresses the findings contained in the final report.

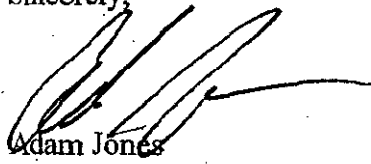
RECEIVED
2006 JUN -5 PM 2:17
LEGAL SERVICES

Mr. Trey Lawrence

Page 2

Should you have any questions, please feel free to contact Michael Richmond or Robert Sanchez at (512) 463-9095.

Sincerely,



Adam Jones

Associate Commissioner
Finance and Information Technology

AJ:RC:rs
Attachment

c: The Honorable Greg Abbott, Texas Attorney General
Vianne Huser, Lavaca County Attorney
Cynthia Thorton, State Board Member
David Anderson, General Counsel
Board Members, Shiner ISD