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Standing Up for QZABs

Missouri Firm Champions Small School Deals

By Mary Wisniewski

CHICAGO ---- Most underwriting firms approach the notoriously complex qualified zone academy bonds the way one would approach a porcupine - very carefully, if at all.

But the family-owned firm of **McLiney And Company** in Kansas City, Mo., has embraced the prickly securities, **making the firm's bankers among the few experts in a program** that gives buyers a tax credit in exchange for providing interest-free loans to schools.

"We've stumbled onto an expertise," said Joey McLiney, a member of the 34 year-old firm that includes his brother Eddie and father, George J. McLiney Jr.

By making a niche business out of a program that may not even be renewed by Congress this year, "we feel like we are specializing in coach whips," said Joey McLiney.

But even if the federal government doesn't extend the QZAB loan program, McLiney And Company's bankers believe the program is a useful tool to help rebuild rural schools. And though the QZABs are "enormously time-consuming" and not very profitable, they are helping McLiney And Company make connections, which may allow the firm to gain a role in bigger

bond deals in the future McLiney said.

McLiney & Co. is known regionally for placing non-rated issues. Besides education financings, they handle public utility issues for water, sewer, and electric systems, as well as public facilities, and lease transactions.

The company got into the QZAB busi-

ness last year, when Eddie McLiney was working with a Kansas school district that had been having trouble getting a \$300,000 loan to buy computers. McLiney told the district the firm would try for the interest-free QZABs, but would only charge the district for the services if the attempt was successful. McLiney And Company was successful in obtaining the

loan, and continued to work with Kansas districts until they had used up the state's entire \$8 million allocation. And the firm continued pursuing deals, branching out into North Dakota, until it had used up most of that state's cap by November 1999. The firm then received a call from the Organization Concerned About Rural Education in Washington, D.C., which was worried that Congress would kill the QZAB program because not enough schools were using it. Having heard about McLiney And Company's multiple QZAB deals, the organization flew Eddie McLiney out to Washington to explain to government officials how the program worked.

"It was sort of like telling a doctor how to take your heart out," Joey McLiney explained.

Eddie McLiney also discussed with officials the importance of getting the word out to school districts about the QZAB program, warning that Department of Education mailings about the bonds were not enough.

So McLiney And Company began sending what Joey McLiney calls "Ed McMahon" letters to

state boards of education and school districts, explaining how they can get the interest-free loans. The company currently has working agreements on QZAB deals with more than 60 school districts in 20 different states, including Oregon, West Virginia, Louisiana, Arizona, and Connecticut.

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interest-free, at par, with no additional coupons, according to the McLineys.

By contrast, some of the largest QZAB deals have sold below par. For example, the **Tennessee State School Bond Authority** sold a \$13.3 million QZAB deal at 97.25% of par. **The Houston independent School District sold \$8 million of QZAB bonds at par, but agreed to pay the buyer 1.54% interest for eleven-and-a-half years.**

THINK SMALL

According to McLiney And Company the trick behind successful QZAB deals is to think small.

"It's something perfect for a small school district," Joey McLiney said. If a big district like Chicago or Kansas City sent a request for proposals, we wouldn't respond. "We don't have time to go through the political hoops."

"The smaller schools have the capacity to move faster because they aren't encumbered by all the layers of bureaucracy," agreed McLiney And Company banker Tom McGuire.

Even with low-bureaucracy rural schools, QZAB deals are "incredibly time consuming" and require a lot of hand-holding, said Joey McLiney. To even qualify for a QZABs, at least 35% of the students in the schools that will benefit from the deal proceeds must qualify for the federal free school lunch program - that is, they must come from low-income families.

Another obstacle is that schools have to obtain a pledge of matching funds from a private entity totaling 10% of the value of the deal. The contribution can be difficult to obtain, since poor areas don't always have rich local businesses with cash at the ready for schools.

Finding these matching funds is one of the most time-consuming aspects of a deal, according to Joey McLiney. Often, it requires soliciting more than one business contribution "I was in Louisiana literally driving all around the school districts, looking for companies," McLiney said.

But the most difficult part of the deal is finding qualified lenders, who may be unimpressed with the tax credit the bonds provide, McLiney said.

The lenders, which are generally local banks, have to be convinced that participating in QZAB deals are in the public interest, even if the rate isn't terrific.

"You have to educate the lender," McLiney said. "You have to explain to them that you're helping a client."

CREATIVE MATCHING SOURCES

Drake School District was the first in North Dakota to try a QZAB deal. Drake is a town of 375 people, mostly wheat and sunflower farmers, and houses all 164 of its students in a single K-12 building. The district needed money because one of its 83-year-old coal-fired boilers had been condemned as unsafe, according to **George Wieland**, district superintendent.

"We had an extraordinary situation," Wieland said. "It would have been im

possible to have a bond issue passed in time for the heating season.

The superintendent responded to one of McLiney's "Ed McMahon" letters and was able to receive a \$190,000 interest-free loan for the boiler for 1999, plus another \$81,000 for the year 2000 for student transportation.

Wieland calls the QZAB program "fantastic." "Our total interest savings will be over \$100,000 over 12 years," he said. "That's really a big break. This is sort of a depressed area and that's really a big thing for us."

The 10% matching fund portion was contributed by teachers and coaches at the school, who agreed to donate extra time. "They probably had donated that already, but how they're getting credit for it," Wieland said.

North Dakota has now used all of its outstanding allocation and has a waiting list for future funds. "The school districts love it," said Tom Decker. Director of School Finance And Organization for the North Dakota Department of Public Instruction.

"It works best focused on small projects that are meaningful and necessary": Decker said.

Decker said that matching funds have mostly been provided as in-kind volunteer work - such as that provided by teachers.

These kinds of in-kind contributions are permissible under the QZAB law, which is intended to foster partnerships between business and the local community, according to George Mardikes of the law firm Davis, Wright, & Tremaine, who acted as bond counsel for two recent Oregon deals handled by McLiney And Company.

The Pepsi Cola-7-Up Bottling Co. is providing students at the Wallowa School District in Oregon with intern-ships for their 10% matching grant on a \$250,000 QZAB loan, according to Mardikes.

In a \$1.295 million QZAB deal for Enterprise Public Schools, Blue Mountain Computers has offered technical assistance, teacher training, volunteer mentors, and internships to fund its \$300,000 matching grant. Mardikes said.

Mardikes agreed with McLiney that constructing these partnerships takes much more work and creativity than the average plain-vanilla GO issue.

Joey McLiney admitted that with all the work that goes into QZAB deal's the whole state of North Dakota may have

been done on a break even basis for McLiney And Company. "If you're doing only \$200,000 or less you're lucky if you break even."

But McLiney feels the goodwill generated by the program is worth the effort. "When I do, a \$50,000 bond issue and I see it helps a student body of 300 kids, you've made friends." he said. !