



**CITY OF BALTIMORE
DEPARTMENT OF FINANCE
BUREAU OF TREASURY AND DEBT MANAGEMENT**

**PERFORMANCE AUDIT OF
COMPETITIVE BID PROCESS FOR HIRING
BOND UNDERWRITERS**

Fiscal Years 2014 through 2018

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CITY OF BALTIMORE

JOAN M. PRATT, CPA
Comptroller



DEPARTMENT OF AUDITS

100 N. Holliday Street
Room 321, City Hall
Baltimore, MD 21202
Telephone: 410-396-4783
Telefax: 410-545-3961

Honorable Joan M. Pratt, Comptroller
and Other Members of the
Board of Estimates
City of Baltimore, Maryland

Executive Summary

We have conducted a performance audit of the Department of Finance, Bureau of Treasury and Debt Management's competitive bid process for hiring Bond Underwriters for fiscal years 2014 through 2018 (stated period). The purpose of our audit was to determine whether the Bureau of Treasury and Debt Management's competitive bid process for hiring bond underwriters is open, fair and objective, and to determine whether its related controls, policies and procedures were effectively designed and placed in operation to ensure that the contracts awarded provided the City of Baltimore the lowest True Interest Cost for its bonds.

As a result of our audit, we determined that the Bureau of Treasury and Debt Management's competitive bid process for hiring bond Underwriters was open, fair and objective, and the related controls, policies and procedures were in place, and working effectively as designed during the stated period. However, we have noted the low percentage of bonds issued by competitive bid compared to the total bonds issued during the stated period. Our results are included in the Audit Note section of this report.

We appreciate the cooperation and assistance provided by the staff of the Bureau of Treasury and Debt Management while conducting our audit. Their knowledge and assistance were instrumental to the completion of this audit.

A handwritten signature in cursive script that reads "Sharon Lockley".

Sharon Lockley, CPA
Auditor Supervisor

April 10, 2019

Bureau of Treasury and Debt Management
Competitive Bid Process for Hiring Bond Underwriters
Background Information
Fiscal Years 2014 through 2018

The Bureau of Treasury and Debt Management (Treasury) manages the investment portfolio, issues new debt, manages existing debt, and evaluates loan requests of the City of Baltimore (the City). Treasury is also responsible for the day-to-day cash management of the City.

In its role of issuing new debt, Treasury is responsible for issuing City bonds to finance City projects. The types of bonds issued are general obligation (GO bonds) and revenue bonds. GO bonds are backed by the full faith and credit of the City and are repaid with tax revenue collected by the City. Revenue bonds are issued to finance capital projects or other special projects and are repaid with the revenue generated by those projects. Revenue Bonds are secured only by the specified revenue source, not the full faith and credit of the City.

When issuing City bonds, Treasury is responsible for assembling a team of professionals to assist in getting the bonds issued. This team consists primarily of bond counsel, who addresses legal aspects of the bond issue, a financial/municipal advisor, who assists in structuring and marketing the financing in the most economical way, and an underwriter, who agrees to sell the bonds to investors and to purchase any unsold securities at a set price.

All bonds are issued through either a negotiated sale or competitive bid sale process. The process of the sale depends on various factors, including the source, type and purpose of bonds to be issued. For the negotiated sales, the terms of the bonds and the terms of sale are negotiated by the City and the underwriter. The goal of Treasury is to obtain the lowest possible borrowing cost for the bonds by selecting an underwriter with the best potential for obtaining the lowest borrowing cost.

Both the negotiated and competitive bid sale processes require the services of an underwriter to sell the bonds. However, there is a difference in the process for hiring the underwriters. For a negotiated sale, an underwriter may be obtained in two ways. The underwriter can be selected through a solicitation process in which a request for proposal is distributed to obtain information on underwriting experience, fee proposal, size/sale network and rate structure. In other instances, an underwriter will approach the City with a financing proposal (refunding) resulting in debt service savings. The City then negotiates a price or “takedown” with the underwriter that will provide the City the lowest true interest cost for its bonds. In the competitive bid sale, underwriters submit bids to an electronic bidding platform that must meet the specific requirements of the City’s Notice of Sale, and the underwriter bidding the lowest true interest cost is awarded the bonds.

In both the negotiated and competitive sales processes, the Board of Finance’s authorization is obtained before bonds are issued. The Board of Finance’s authorization includes establishing the parameters for the maximum dollar amount and interest rate of bonds to be issued, the approved dollar amount of bonds to be issued, obtaining an underwriter to sell the bonds, the financing structure and the offering documents. If the requested bond amount exceeds the authorization limit, legislation is introduced to the City Council for approval to increase the maximum debt issuance level.

Bureau of Treasury and Debt Management
Competitive Bid Process for Hiring Bond Underwriters
Background Information
Fiscal Years 2014 through 2018

For bonds issued through the competitive bid process, after bond ratings are obtained from the rating Agencies, a bid Form is prepared. The Bond Counsel and Municipal Advisor arrange for the dissemination of the Preliminary Official Statement (POS) and Notice of Sale (NOS). The bond sale is advertised in the Bond Buyer (a national trade newspaper covering the Municipal bonds industry) and the local newspaper. Certification from contributors to the POS is obtained and Bond Counsel posts the POS on the Web.

On the date and time specified in the NOS, the City will receive bids for the Bonds. For competitive issues, the City uses an electronic platform to accept bids. Two nationally recognized platforms are Ipreo/Parity and MuniAuction/Grant Street Group. The City submits the NOS to the electronic bidding service and the details of the sale are posted on the website. Bidders register and submit bids using a standardized bid form prepared by the City that only allows the submittal of bids that meet the specific requirements of the NOS.

The City views the sale results, confirms the bid calculations and awards the bid electronically after the sale has closed. The Financial Advisor will verify the computation provided by the electronic bidding platform for the winning and cover bids. Bond Counsel will verify the bid meets all the parameters identified in the NOS.

The winning bid is awarded based on the lowest True Interest Cost (TIC). After the award of the bonds, the City requires a good faith deposit from the winning bidder, which is 1% of the par amount of the bonds. The good faith deposit is provided by wire transfer by a certain time on the day of the award. The good faith amount is deducted from the purchase price wired at closing.

According to Treasury, during fiscal years 2014 through 2018, the City issued General Obligation bonds of \$351.2 million, Water bonds of \$492.3 million, Waste Water bonds of \$615.4 million, Tax Incremental Financing, (TIF) bonds of \$56 million, Revenue Bonds of \$1.1 billion and Special Obligation Bonds of \$149.7 million, which totaled \$2.8 billion. Of the total \$2.8 billion in bonds issued, \$63.7 million or 2.3% were sold through the competitive bid process. (See Audit Note on page 5 of this report.)

Bureau of Treasury and Debt Management
Competitive Bid Process for Hiring Bond Underwriters
Audit Scope, Objective and Methodology
Fiscal Years 2014 through 2018

We have conducted a performance audit of the Department of Finance, Bureau of Treasury and Debt Management's competitive bid process for hiring Bond Underwriters for fiscal years 2014 through 2018. The purpose of our performance audit was to determine whether the Bureau of Treasury Management's competitive bid process for hiring bond underwriters is open, fair and objective, and to determine whether related controls, policies and procedures were effectively designed and placed in operation to ensure that the contracts awarded provided the City of Baltimore the lowest True Interest Cost for its bonds. Our audit was conducted in accordance with *Generally Accepted Government Auditing Standards* related to performance audits, issued by the Comptroller General of the United States. 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.

To accomplish our objectives, we interviewed key Treasury Management personnel to obtain an understanding of the policies and procedures used to ensure that the competitive bid process for hiring Bond Underwriters was open, fair and objective, and the City of Baltimore obtained the lowest true interest cost. We performed tests as necessary to verify our understanding of the applicable policies and procedures and reviewed applicable records. We also reviewed the internal controls to determine if they were placed in operation and working effectively as designed during the stated period and performed tests of the records and such other auditing procedures as we considered necessary in the circumstances. Our audit result is included in the Audit Note section of this report.

Bureau of Treasury and Debt Management
Competitive Bid Process for Hiring Bond Underwriters
Audit Note
Fiscal Years 2014 through 2018

Although the Bureau of Treasury Management's competitive bid process for hiring Bond Underwriters appears to be open, fair and objective, and the controls designed to ensure compliance with the policies and procedures appear to be operating effectively, we noted the low percentage of bonds issued by competitive bid to the total bonds issued during fiscal years 2014 through 2018. According to Treasury Management, of the \$2.8 billion in bonds issued during this period, only \$63.7 million or 2.3% were sold through the competitive bid process. As the competitive bid sale is generally considered to provide the lowest true interest costs to the City, Treasury should consider increasing the use of the competitive bid process for issuing bonds.

Appendix I

F R O	NAME & TITLE	Herny Raymond, Director of Finance <i>J/</i>	CITY of BALTIMORE <i>MEMO</i>	
	AGENCY NAME & ADDRESS	Finance 100 Holliday Street, Suite 454 Baltimore, MD 21202		
	SUBJECT	Competitive Bid Process for Hiring Bond Underwriters Audit Note		

TO

City Auditor
100 Holliday Street, Rm 321

DATE:

March 28, 2019

The Department of Finance acknowledges receipt of the Performance Audit of Competitive Bid Process for Hiring Bond Underwriters. The Department has the following response to the Audit Note contained in the report:

The Department of Finance disagrees with this note. As per the City Charter Article VII Section 21 it is the Baltimore City Board of Finance that determines the type and method of sale of City debt. This Board, after careful consideration, approved each bond sale through a duly enacted and authorized resolution. The Department believes the negotiated method was appropriate and within the purview of their authority and was done only after careful consideration of many issues such as complexity of the transaction, refunding opportunities, financial market conditions and federal program requirements.

Further the Department does not believe these financings resulted in higher interest costs. The City independently confirms market conditions and market rates of interest before the transaction is priced and settled. This analysis is then factored into the rate negotiation with the underwriter. In our view, these checks and balances ensure our rates are competitive and in the best interests of the City.

For example, during this audit period the Board of Finance elected to forgo a competitive bond sale for approximately \$421 million of water and wastewater debt and instead utilize the State Revolving Loan Fund. The rate of interest on this debt was approximately 1.5% well below the market rate of approximately 3.8%. In addition, during the audit period the Board authorized \$55 million of transportation bonds to be issued by the state of Maryland (foregoing a competitive sale) to take advantage of a higher bond rating and lower rate of interest.

The Board of Finance does in fact consider the competitive sale method - however, during this audit period the Board mostly determined other methods were the best option.