

**Rating Update: MOODY'S AFFIRMS Aa1 RATING ON WASHINGTON STATE SCHOOL BOND GUARANTEE PROGRAM; OUTLOOK IS STABLE**

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**APPROXIMATELY \$8.3 BILLION OF GUARANTEED DEBT AFFECTED**

Primary & Secondary Education  
WA

**Opinion**

NEW YORK, Dec 2, 2010 -- Moody's Investors Service has affirmed the Aa1 rating on the Washington School Bond Guarantee Program, affecting approximately \$8.3 billion of guaranteed debt outstanding. The rating outlook is stable.

**RATING RATIONALE**

Under the guarantee program, the state pledges its full faith, credit, and taxing power to guarantee debt service when due on qualified school districts' voter-approved general obligation bonds. Moody's assigns an Aa1 rating to school district bonds that are guaranteed under the state program, and assigns underlying ratings to individual bond issues at the request of the issuing district. The Aa1 program rating reflects the pledge of the State of Washington (rated Aa1 with a stable outlook); strong state oversight of local school districts and satisfactory program mechanics.

**SUCCESSFUL STATE PROGRAM PROVIDES FULL FAITH GUARANTEE OF SCHOOL BONDS**

In 1999 Washington's voters approved a constitutional amendment authorizing the state to pledge its full faith, credit, and taxing power to guarantee the voter-approved general obligation bonds of school districts. In April of the following year the first Certificate of Eligibility was issued by the Office of the State Treasurer for participation in the program. A Certificate of Eligibility evidences that the district's bonds will be guaranteed under the program so long as they are issued within one year. Once the bonds are sold, the guarantee is effective for the life of the issue. As of October 18 2010, more than \$8.3 billion of debt was outstanding under this program.

**STRONG STATE MONITORING AND CONTROL OUTSIDE OF GUARANTEE PROGRAM CONTRIBUTES TO HIGH CREDIT QUALITY OF PORTFOLIO**

School districts are not subject to credit review for purposes of participation in the guarantee program, beyond certifying that they are fiscally solvent. However, fiscal oversight of school districts in Washington is very thorough, contributing to the credit soundness of the guarantee program. School districts in Washington demonstrate a strong credit profile; Moody's median rating among 117 rated districts is Aa3, with a minimum rating of A2 for the sector statewide.

In Moody's view, the state's oversight helps support the credit strength of Washington school districts. Fiscal oversight of school districts in Washington is extensive. Oversight is accomplished by three entities: the state Board of Education, the Office of the Superintendent of Public Instruction (OSPI), and Educational Service Districts (ESDs). The OSPI is a constitutionally established elected office with primary responsibility for fiscal oversight. The OSPI is assisted in this effort by regional ESDs, agencies established by statute that provide technical assistance to local school districts as well as support to OSPI and the Board of Education.

School districts' budgets are developed and must receive approval of the OSPI and the ESDs. By law, budgets of larger districts are reviewed by the OSPI, while those of smaller districts are subject to approval by a budget review committee consisting of an ESD representative, a representative of the school district, and a representative of the OSPI. Over the course of the year OSPI provides the ESDs with financial and enrollment data for each school district, based upon which the ESDs identify and report to OSPI any districts which may have possible financial concerns. For districts needing immediate attention, OSPI will contact the ESD to establish a course of action. OSPI will also evaluate carefully any district that has requested an emergency advance, budgeted receivables, or had questioned audit costs in the prior year. Flagged districts whose situations are less urgent are reviewed more thoroughly during the annual budget and financial reporting processes. ESDs are required to notify OSPI during the year should a district's financial position change and require OSPI attention.

**TIGHT TIMELINE FOR NOTIFICATION AND IMPLEMENTATION OF STATE DEBT SERVICE PAYMENT UNDER PROGRAM**

In Washington the county treasurer serves as banker for all school districts within the county: all school district revenue and expenditure moneys are deposited with and released by the county treasurer. The county collects local taxes on behalf of the school districts, and directly transmits payment on any voter-approved debt to the bond paying agent. Under the guarantee program the County Treasurer retains this responsibility, and is further required to notify the paying agent and the State Treasurer immediately in the event he or she becomes aware of an inability to transfer sufficient funds. If the transfer has not been made on the payment date, the paying agent is required to notify the State Treasurer. Once the State Treasurer verifies that the district will not make the payment when due, the State Treasurer's office is required to immediately forward the funds for debt service.

Although timing associated with identification and notification of shortfalls may be very tight, Washington's school districts routinely use the same fiscal agent as the state, allowing for quick rectification once a shortfall is identified. In addition, the State treasury maintains sufficient staff to ensure that all payments will be expedited, a liquid portfolio of assets that averages over \$2 billion in treasury and agency securities, and wire transfer capability for movement of funds between financial institutions if needed.

Any district for which the State has made a debt service payment will be required to reimburse the State and pay both interest and a penalty. If the Treasurer determines the amounts forthcoming from the district will not reimburse the State in full within one year, the Treasurer has the right to pursue legal action. The State Treasurer also may direct the district and the county to amend collection of property taxes pertaining to the bonds and, to the extent that all other outstanding obligations of the district payable from those taxes are fully paid, direct that proceeds be

applied towards reimbursement of the State.

**PROGRAM RATING AND OUTLOOK ARE BASED ON STATE CREDIT QUALITY**

As the guarantee provided by the program is the State's full faith, credit and taxing power, the rating on the program is directly related to the rating of the State (Aa1 with a stable outlook). State credit strengths are:

- \*Institutionalized conservative budgetary controls
- \*Improved financial flexibility with increased rainy day fund (RDF) levels going into the 2007-2009 recession
- \*Strong demographic trends
- \*Satisfactory overall liquidity levels despite recessionary stresses

State credit challenges are:

- \*Economic weakness and steeper-than-forecast housing downturn drive large consecutive downward revenue revisions.
- \*Significant use of one-time actions to balance current biennial budget, including depletion of reserves, reduces flexibility to address unexpected revenue shortfalls
- \*Exposure to cyclical commercial aerospace industry
- \*Debt ratios above average and likely to increase
- \*Voter initiative activity adds element of fiscal uncertainty

For additional information about the State of Washington's rating, please see Moody's New Issue Report published October 22, 2010 in conjunction with the state's issuance of \$51.3 million Certificates of Participation, Series 2010D.

**LAST RATING ACTION AND PRINCIPAL METHODOLOGY USED**

The last rating action on the Washington State School Bond Guarantee Program was on January 4, 2010, when the municipal finance scale rating was affirmed and a negative outlook was assigned. The rating was subsequently recalibrated to a global scale Aa1 with a stable outlook on April 23, 2010.

The principal methodology used in this rating was Moody's State Rating Methodology, published in October 2004 and available on [www.moody.com](http://www.moody.com) in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

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