The Role of Financial Advisors in The Negotiated Sale of Tax-Exempt Securities

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Abstract

This paper analyzes the role of independent financial advisors in the negotiated sale of tax-exempt securities. The empirical results indicate that the costs of contracting with financial advisors are not significantly offset by corresponding benefits in the form of lower borrowing costs. There is no evidence that advisor certification reduces reoffer yields; advisor monitoring activities are shown to reduce modestly the costs of under-

Introduction

This paper analyzes the role of independent financial advisors in the negotiated sale of tax-exempt bonds. In a negotiated debt offering advisory services are supplied as part of the bundle of services provided by investment bankers. In contrast, in a competitive sale, distribution and underwriting (risk bearing) services are purchased separately from origination and advisory services. It is especially interesting to note, therefore, that many tax-exempt issuers also contract with firms outside of the underwriting syndicate to provide independent advice in a negotiated sale. This study provides a rationale for this seemingly redundant practice.

Financial advisors may be viewed as supplying both certification and monitoring services. The joint supply of these services is a consequence of the unique characteristics of the tax-exempt market and the informational asymmetries between issuers and investors on the one hand, and between issuers and their investment bankers on the other. The tax-exempt market is composed of a large number of relatively small issues; moreover, tax-exempt securities are not subject to the regulation and disclosure requirements of the Securities and Exchange Commission (SEC). In addition, issuers are not subject to mandatory Federal reporting requirements nor are they required to follow uniform standards for accounting or financial reporting.

Given these non-reporting characteristics, it is reasonable to presume that issuers have superior information regarding future cash flows and the "true" quality of their debt. This informational advantage stimulates the demand for external certification services and is reflected in part by the choice of a negotiated method of sale. However, as previous research (Baron, 1982) has indicated, negotiated sales can lead to incentive problems and agency costs for issuers. While the literature indicates that these incentive problems can be resolved by designing appropriate contracts, we suggest that contracting with financial advisors for monitoring services can also represent a solution.

In this paper we use regression analysis to estimate the effects of advisor supplied certification and monitoring services on issuer borrowing costs.

The paper is organized as follows. The second section provides some background information on the services provided by financial advisors in the tax-exempt market and the "industry" structure of advisory firms. The third section develops theoretical reasons that may explain the use of advisors in negotiated sales; the fourth section states the hypotheses, describes the methodology, and provides some empirical estimates of the effects, if any, of advisors on the terms of the bond sale. The final section summarizes the results and suggests other factors that may explain the use of advisors.

Financial Advisory Services and Firms

A recent publication of the Government Finance Officers Association (GFOA) defines a financial advisor as:

> *a consultant that advises governmental clients on matters relating to the issuance of securities including things such as the structure and timing of issues, documentation relating to sales, marketing and pricing, procuring bond ratings...(Petersen and Watt, 1986 ,p.3)*

According to the Spring 1990 edition of the *Directory of Municipal Bond Dealers*, published by the Bond Buyer, more than 200 firms were listed as financial consultants. These firms included commercial banks and investment banks - both of which also act as underwriters and dealers in tax-exempts- and independent firms that specialize only in advisory services. Exhibit 1 provides some perspective on the structure of the financial advisory "industry" by listing the ranking of leading advisory firms for 1989, based on the volume of bonds issued by their clients in that year. Of the top 20 firms, eight are specialist firms providing only advisory services. The remaining 12 firms also function as underwriters and/or dealers in tax-exempt securities.

EXHIBIT 1
Rankings of Financial Advisors for 1989

Rank	Advisor	Total Bond Sales By Clients ($Billion)	Number Of Sales
1	Public Financial Management	$3.884	134
2	First Boston Corporation	2.998	11
3	First Southwest	2.821	148
4	Lazard Freres	2.689	35
5	P.G. Corbin & Company	2.197	20
6	Public Resources Advisory Group	1.810	35
7	Lehman Brothers	1.633	41
8	Evensen-Dodge	1.488	164
9	Security Pacific Securities	1.397	11
10	Caine Gressel Midgley Slater	1.369	40
11	WR Lazard & Company	1.366	14
12	Raucher Pierce Refsnes	1.201	86
13	Lovett, Underwood, Neuhaus & Webb	1.201	49
14	Ponder & Company	1.147	41
15	O'Brien Partners Inc.	1.133	6
16	PaineWebber	1.117	31
17	Government Finance Associates	0.966	31
18	Grigsby Brandford Powell Inc.	0.919	15
19	Fray Municipal Securities	0.913	5
20	William R. Hough & Co.	0.780	17

Source: IDD Information Services/PSA Municipal Database July 30, 1990.

Note: Credit is given to each financial advisor for the entire issue.

The financial advisory activities of underwriters (including commercial banks) are regulated by the Municipal Securities Rulemaking Board (MSRB). Under Rule G-23 of the Board, underwriters can have concurrent relationships as advisors and underwriters with a client in a competitively-bid bond sale. In negotiated sales, however, underwriters are required to first resign as advisors prior to entering into underwriting contracts. As stated by the Board,

> *The rule is designed to minimize the "prima facie" conflict of interest that exists when a municipal securities professional acts as both financial advisor and underwriter with respect to the same issue (MSRB, 1982, p.3574).*

Firms that specialize only in municipal financial advisory services are not regulated by the MSRB or the SEC.

Although specific advisory contracts may specify a wide range of services, including long-term capital planning and financing, a 1984 survey by the GFOA, summarized in Exhibit 2, indicates that "certification " and "underwriter monitoring" services are common to most advisory contracts. In this context, activities such as the preparation of the Official Statement(or prospectus), rating agency presentations, and investor relations meetings, can be viewed as "certification" services performed by an external agent - the advisor- to resolve potential informational asymmetries between issuers and investors or other outside parties. Other activities, such as verifying bids, negotiating with underwriters, and opining on debt maturities can be viewed as advisory services designed to monitor underwriter performance. The following section develops theoretical rationale for the provision of these services in conjunction with the issuance of securities through a sale by negotiation.

EXHIBIT 2
Services Provided by Financial Advisors

Services	Number of Governmental Units Using Service	Percent
Prepares Official Statement	746	93%
Recommends Maturity Schedule	708	88
Recommends Registration Procedures	536	67
Conducts Investor Relations Meeting	363	45
Aids in Rating Agency Presentation	676	84
Verifies Bids and Aids Negotiations	684	85
Analyzes Bond Sale Results	620	77
Analyzes Capital Budget	98	12
Analyzes Debt Position	320	40
Analyzes Financing Options	416	52
Reviews Debt Management	147	18
Reviews Investment Strategy	108	13
Prepares Annual Financial Report	110	14
Performs Other Services	19	2
Total	806	

Note: The survey was conducted by GFOA during 1984. The number of respondents was 999 out of approximately 4,600 member governments. Of the 999 respondents, 806, or 81%, had used a financial advisor.

Source: J.E. Petersen and P. Watt, eds., *The Price of Advice: Choosing and Using Financial Advisors* (GFOA, 1984).

Theoretical Rationale for Financial Advisors in Negotiated Sales

Certification Services

The underlying problem with selling risky debt is the potential wealth transfer from outsiders (potential investors) to insiders (resident taxpayers in a political jurisdiction, firm owners and/or managers). Insiders can be assumed to possess an information advantage regarding the estimated cash flows to be received by investors from purchasing a new debt security (Beatty and Ritter, 1986; Booth and Smith, 1986; Smith, 1977; Tinic, 1988). If outsiders are unable to purchase insider information or if insiders' assessments of value are not credible to outsiders, then an Akerlof-type (Akerlof, 1970) market failure may result. The potential for market failure stimulates the demand for an external agent to certify the prices of new securities issues.

In a recent paper, Booth and Smith (1986) develop a theory of the role of underwriters in the sale of new securities. Their work is an extension of the literature on reputational signaling (DeAngelo, 1981; Easterbrook, 1984; Klein and Leffler, 1981; Mayers and Smith, 1982; Wakeman, 1981). Booth and Smith show that an underwriter's reputation can serve as the bonding investment which serves as the guarantee necessary to satisfy investors that the security's price is accurate. An underwriter who does not certify the true equilibrium price will lose either potential investors (if the price is too high) or potential issuers (if the price is too low). In either case, an underwriter diminishes the value of its reputation capital and its ability to earn future returns on that capital.

The problems of asymmetric information and, therefore, the value of certification services, are likely to be more pronounced in the tax-exempt market than in the corporate bond market. The debt issues of governmental units are not subject to the registration requirements of the SEC, and there are no mandated disclosure requirements for tax-exempt securities. While disclosure documents and practices are subject to the general anti-fraud requirements of the Securities Acts, the SEC has been extremely cautious in bringing enforcement actions against governmental units.(1) Moreover, the tax-exempt market is comprised of an extremely large number of relatively small issues. In 1989, for example, more than 8900 new issues of debt were sold and more than 6900 were less than $10 million in par value. For many governmental units, new debt sales are very episodic events and, therefore,"current" prospectuses quickly become outdated information.

A financial advisor may provide additional certification regarding the true value of a new securities issue. Financial advisors, many of whom also provide underwriting services in the tax-exempt, corporate, and U.S. government securities markets, have built-up a stock of non-salvageable reputational capital over time. As a result, financial advisors, like underwriters, are able to provide credible pricing information to outsiders.

Underwriters in the corporate market are subject to Section 11 of the Securities Act of 1933, which holds that every underwriter is liable to purchasers for misleading or untrue statements or omissions of material facts in a prospectus. As a result, corporate underwriters typically carry out "due diligence" investigations and employ underwriter's counsel to verify disclosure documents.

Section 11 does not apply to the tax-exempt market, however, because municipal securities are exempt from the Act's registration requirements. Underwriters, instead, are subject to the more general antifraud provisions of the 1933 and 1934 Securities Acts. These differences in underwriter liability suggest that the certification activities of a financial advisor in tax-exempts may have significant additional value to investors and issuers.(2)

Underwriter-Monitoring

One of the leading traditional reasons advanced for employing financial advisors in negotiated sales is based on the assumption of monopsony powers by underwriters (Baron, 1982). According to this hypothesis, negotiated underwriters have private information on the demand for an issuer's securities and on the level of effort needed to distribute them. Because of this informational asymmetry, underwriters have an incentive to misstate the level of effort needed to distribute the securities and to overcharge for their services. This argument is well entrenched among many government finance officers and the GFOA publication *An Elected Official's Guide to Government Finance* warns that "in negotiated underwritings, procedures should be implemented to ensure that underwriter profits are reasonable... (Petersen and Watt, 1986, p.63)." According to this reasoning, contracting with advisors to monitor the terms of a bond sale (i.e., interest rate, underwriter spread) should result in more favorable terms to the issuer.

One could argue, however, that there is a significant degree of competition among underwriters to be appointed as senior managers in negotiated sales, and this competition insures that the superior knowledge of the banker is used to benefit the issuer. Accordingly, it is possible that while an advisor may provide "insurance" for the issuer, there will be no significant effect on the terms of the issue. Joehnk and Kidwell (1984) observed that underwriter spreads on nationally sold tax-exempts were not significantly different than spreads on competitive issues. As they indicate, their results suggest that "it may be more difficult for underwriters to extract monopolistic rents from nationally sold issues because these municipalities usually have the alternative of selling their bonds successfully in the competitive market or of selecting another negotiated underwriter (Joehnk and Kidwell, 1984, ,p.42)."

Analysis Certification Effect

In section III we identified two potential explanations of why issuers of tax-exempt securities sold through negotiation use a financial advisor. The certification hypothesis suggests that financial advisors provide incremental certification of the offering price beyond that provided by the managing underwriter. This hypothesis is tested by examining the reoffer yields on new issues of tax-exempt bonds sold by negotiation. Ceteris paribus, a greater level of certification reduces investor uncertainty, leading to greater demand for the securities and lower reoffer yields.

The empirical model, estimated by ordinary least squares regression, is

RY = f(RAT, AMT, MAT, BBI, USE, A

where

RY = Reoffer yield on the last term bond or last serial bond of the issue, measured in percent;

RAT = A set of zero-one dummy variables for Standard and Poor's credit rating classes AAA, AA, BBB and below, not rated; A-rated bonds are the omitted set. If the S&P rating was not available, the Moody's rating was used;

AMT = Issue size, in logarithms; measured in thousands of dollars;

BBI = Level of interest rates in the tax-exempt bond market at the time of sale as mea sured by the weekly Bond Buyer Index of 25 Revenue Bonds, measured in percent;

USE = Zero-one dummy variable for use of bond proceeds; a value of one is given to high risk bonds (hospital, housing, and utility) and a value of zero is given to low risk bonds (education, water and sewer, and all other public uses);

MAT = Number of years to maturity, in logarithms;

ADV = Zero-one dummy variable that indicates whether the issuer employs an advisor (ADV = 1) or not.

This model is based on the substantial body of prior research (Braswell, Nosari, and Browning, 1982; Forbes and Leonard, 1984; Joehnk and Kidwell, 1978,1984; Kessel, 1971; Kidwell and Koch, 1982; Kidwell, Sorensen, and Wachowicz, 1987; Leonard, 1983,1984; Sorensen, 1979,1980) that has shown that tax-exempt bond yields (RY) are a function of capital market conditions at the time of sale and issue and issuer characteristics. Standard and Poor's ratings (RAT) are used as the measure of default risk. Bonds rated AAA that have a credit enhancement are a separate category.(3) Previous research (Braswell, Nosari, and Browning, 1982; Joehnk and Kidwell, 1978; Kidwell, Sorensen, and Wachowicz, 1987) has shown that yields on bonds with a credit enhancement are generally higher than on bonds with a AAA rating on their own merits. The number of years to maturity (MAT) and issue size (AMT) are specified in logarithms to reflect the diminishing effects on yield. Based on prior research (Leonard, 1983, 1984), hospital, housing, and utility bonds are classified as "high" risk (USE) while education, water and sewer, and all other public purpose uses are classified as "low" risk; that is, "private purpose" issues are considered to be more risky.(4)

EXHIBIT 3
Data Sample Description

	N=495		N=129	
	Means	Std. Dev.	Means	Std. Dev.
Issue Size (AMT) ($million)	11.942	3.241	21.581	2.658
Maturity (MAT) (years)	19.475	1543	19.537	1.500
RAT (percent of total)				
AAA Credit	0.400		0.488	
AAA	0.028		0.023	
AA	0.117		0.147	
A	0.214		0.227	
BBB and Below	0.048		0.015	
Not Rated	0.193		0.100	
BBI (percent)	7.770	0.393	7.671	0.320

The data for this study consist of tax-exempt bonds sold through negotiation during the last half of 1989 and the first half of 1990. Data were collected from the worksheet service provided by the Bond Buyer. The sample includes fixed rate bond issues sold through negotiation for which complete information was available. The sample contains 495 issues. Summary statistics for the sample are presented in Exhibit 3.

Table 1 presents the estimated regression coefficients for the reoffer yield equation. The estimated coefficients are consistent with our expectations and the results of previous studies. The rating (RAT) and use of proceeds (USE) variables indicate that "riskier" bonds carry higher reoffer yields, ceteris paribus. The issue size variable (AMT) coefficient suggests that larger issues increase market congestion and require higher yields to attract additional investor demand. The maturity variable (MAT) coefficient is not significantly different from zero, while the BBI coefficient has a high level of statistical significance. These results are expected due to the uniform long average life of bonds in the sample and the use of a long-

term market index. The advisor (ADV) coefficient is not significantly different from zero, indicating that for this sample of negotiated bonds, there is, on average, no advisor certification effect on reoffer yields in equilibrium.

The incremental value of advisor-supplied certification services may be a function of the prestige of the managing underwriter. Regardless of the Securities Act distinction between corporate and tax-exempt securities under Section 11, prestigious underwriters do have substantial reputational capital at stake in any underwriting. Since all of the major underwriters in municipals also participate in the corporate market, incomplete certification in the municipal market will reduce the underwriter's stock of reputational capital and its ability to provide credible certification in the corporate market. Indeed, the SEC noted in its report on the WPSS debacle that the prevailing practice of major firms in negotiated tax-exempt sales is to request a "10b-5" letter from underwriter counsel which states that the Official Statement does not contain "any untrue statement of a material fact or omit to state any material fact...(SEC, 1988, p.191)."(5) Therefore, the incremental value of advisor-supplied certification may be greater for issues sold with a non-prestigious underwriter, ceteris paribus.

We define a "prestigious" underwriter as one of the top ten investment banking firms or one of the top ten commercial banks in terms of the volume of issues underwritten during 1989. Four advisor-prestigious underwriter interaction variables are created: prestigious - no advisor (PNA), prestigious - advisor (PA), non-prestigious - advisor (NPA), and non-prestigious - no advisor (NPNA); these variables are specified as zero-one dummy variables. The regression results using these variables are shown in the top panel of Table 2. The estimated coefficients for MAT, RAT, USE, and BBI were not significantly different so they are not shown. The omitted variable is non-prestigious-no advisor (NPNA). If the value of advisor certification is related to underwriter prestige, we would expect that bonds sold through a non-prestigious underwriter would benefit the most (i.e., would have the greatest reduction in reoffer yields) from the use of an advisor, while bond sales involving a prestigious underwriter would benefit the least. As shown in Table 2, the NPA coefficient is not statistically different from zero, offering no support for the advisor certification hypothesis. Furthermore, the difference between the PNA and PA coefficients is not statistically significant. Thus, for both prestigious and non-prestigious issues, the use of an advisor had no impact, on average, on reoffer yields.

A final set of regression coefficients is presented in the lower panel of Table 2. It may be possible that "prestigious" advisors have a greater stock of reputational capital that enables them to provide superior certification services. Accordingly, we define a set of zero-one dummy variables for issues having an advisor ranked in the top 10 during 1989 (TOPADV), issues with a non-top 10 advisor (NONTOP), and issues with no advisor. As shown in Table 2, there is no significant difference in reoffer yields between the various advisor categories.

TABLE 1
Estimated Regression Coefficients Reoffer Yield Dependent Variable (N=495)

Independent Variable	Estimated Coefficient	t-Value
Constant	0.338	
BBI	0.795	16.776***
MAT(ln)	0.017	0.398
AMT(ln)	0.099	5.632***
RAT		
AAA Credit Enhancement	-0.193	3.898***
AAA	-0.208	-1.785*
AA	-0.203	-3.006***
BBB and Below	0.455	4.869***
Not Rated	0.404	6.876***
USE	0.296	7.129***
ADV	-0.038	-0.828
R Square	0.513	
SEE	0.408	

*** Coefficient significant at 1% level.
** Coefficient significant at 5% level.
* Coefficient significant at 10% level.

TABLE 2
Advisor Effect Reoffer Yield Dependent Variable (N=495)

Underwriter Prestige-Advisor Interaction Variables

Independent Variable	Coefficient	t-Value
PNA	-0.007	-0.132
PA	-0.106	-1.549
NPA	0.009	0.162
(NPNA omitted category)		
R Square	0.513	
SEE	0.408	

Advisor Prestige Variables

Independent Variable	Coefficient	t-Value
TOPADV	-0.029	0.311
NONTOP	-0.041	0.813
(No Advisor ommitted category)		
R Square	0.513	
SEE	0.408	

Monitoring Effect

The underwriter monitoring hypothesis explains the use of a financial advisor in a negotiated sale as a method to counteract the monopsony power of the managing underwriter. This hypothesis is tested by examining the gross underwriter spread on new issues of tax-exempt bonds sold by negotiation. We hypothesize that, ceteris paribus, the use of a financial advisor to monitor underwriter behavior will result in lower underwriter compensation (gross spread).

TABLE 3
Estimated Regression CoefficientsGross Underwriter Spread Dependent Variable (N=129)

Independent Variable	Estimated Coefficient	t-Value
Constant	25.495	
BBI	0.364	0.333
MAT(ln)	-0.719	-0.864
AMT(ln)	-1.381	-3.761***
RAT		
AAA Credit Enhancement	1.457	1.675*
AAA	1.077	0.462
AA	0.697	0.603
BBB and Below	7.457	2.672**
Not Rated	5.612	4.331***
USE	0.641	0.881
ADV	-1.040	-1.334
R Square	0.301	
SEE	3.779	

*** Coefficient significant at 1% level.
** Coefficient significant at 5% level.
* Coefficient significant at 10% level.

The empirical model, to be estimated by ordinary least squares regression, is

GUS = f(RAT, AMT, MAT, BBI, USE, ADV)

where GUS is gross underwriter spread measured in dollars per $1000 bond and all other variables are as defined above.

Previous research (Leonard, 1984) has shown that lower rated and non-rated bonds (RAT) and bonds with riskier uses of proceeds (USE) have higher spreads because there is more limited demand for these bonds, thereby increasing distribution costs. Larger issues (AMT) should have lower per bond spreads if there are fixed underwriting costs. Longer-term bonds (MAT) are thought to be more difficult to sell, thereby increasing distribution costs. Current market conditions (BBI) affect the expected distribution effort of the underwriter and the risk of purchasing bonds at a fixed price from the issuer. The data for this analysis are drawn from the same sample described in the previous section; the sample contains 129 issues. The sample was reduced because there were more issues with missing information on gross spread.

TABLE 4
Advisor Effect Gross Underwriter Spread Dependent Variable (N=129)

Advisor Prestige Variables

Independent Variable	Coefficient	t-Value
TOPADV	0.439	0.314
NONTOP	-1.458	-1.729*
R Square	0.311	
SEE	3.769	

* Coefficient significant at 10% level.

The monitoring hypothesis test results are presented in Tables 3 and 4. Table 3 shows the estimated regression coefficients for the basic gross underwriter spread model. As expected, gross spread is inversely related to issue size (AMT); gross spreads are significantly higher on bonds rated BBB and below and on bonds with no rating. The maturity variable (MAT) coefficient is not significant; this finding is likely due to the lack of variability in the maturity of the bonds in the sample. The ADV coefficient is negative, but it is not statistically different from zero. This result offers no support for the monitoring hypothesis.

Finally, the set of advisor prestige variables are used; these results are shown in Table 4.The TOPADV coefficient is not statistically significant, but the NONTOP coefficient is negative and significant at the 10% level. These results indicate that issues sold with an advisor not ranked in the top 10 had gross spreads that were $1.46 per $1,000 bond lower, on average, than similar issues sold with no advisor.

Conclusions

Our results imply that the costs of contracting with financial advisors on negotiated sales are only moderately offset by corresponding benefits in the form of lower borrowing costs. There was no evidence that advisor certification reduced reoffer yields; advisor monitoring activities reduced the cost of underwriter services, but the savings were less than $32,000 for the average size issue in the sample ($21.5 million).

This modest level of savings suggests that there are other reasons, in addition to cost savings, for the use of a financial advisor. We suggest three additional motives. First, the use of a financial advisor is a form of "insurance" that protects elected officials from charges of

improper activity in connection with a bond sale. Second, a financial advisor provides "interpretative" and "reasonableness" services to an issuer; these services are particularly important to first time and infrequent issuers. The third reason has to do with the nontransferability of property rights to governmental units. In governmental units, ownership resides with the citizens. The property rights of the citizens can not be exchanged for rights to other resources, however. As a result, an important monitoring mechanism is unavailable, increasing the opportunity for public officials to engage in more opportunistic behavior.

In the private sector, the stock market acts as an effective mechanism for corporate control. The external market for corporate control reduces the cost of monitoring managers within widely-held corporations. In the public sector, however, citizens can not sell their property rights if they are dissatisfied with public officials. As a result, more resources must be spent for information gathering, monitoring, and contract enforcement. As noted by Zimmerman (1977), the costs of monitoring in the public sector are relatively high because the real estate market, which capitalizes the present value of officials' actions, is less liquid than the stock market.

Advisor contracting is an example of an agency cost analagous to that noted by Smith (1977) in his analysis of the corporate manager's choice of rights offering versus underwritten offering. We suggest that governmental officials may receive benefits from advisor contracting that do not accrue to taxpayers. A number of recent press reports have pointed out, for example, that investment bankers and other firms, including financial advisors, that are party to debt sales, are often large political contributors to political campaign funds.

Footnotes

1. In its recently released report on the $2.25 billion default by the Washington Public Power Supply System, the SEC staff concluded: "The experiences on the sale of Projects Nos. 4 and 5 bonds indicate that close attention to disclosure obligations and the use of appropriate disclosure practices are necessary in the sale of municipal bonds (SEC, 1988,p.376)." Yet, after a long litany of inadequate disclosures, the SEC decided not to pursue enforcement actions because of "the difficulty of assigning responsibility for disclosure deficiencies in a highly complicated factual situation under the federal securities law antifraud provisions applicable to exempt offerings (SEC, 1988, p.2)."

2. See (Booth and Smith, 1986) for a similar argument in corporate debt sales. It is interesting to note that the SEC report on the WPPSS observed that "underwriters contended that they had no legal obligation to conduct an investigation and that it was not industry practice to do so in competitive underwritings (SEC, 1988, p.15)."

3. Most of the bonds in the sample have a credit enhancement in the form of bond insurance from MBIA or AMBAC.

4. In part, the higher risk to investors may be related to the residual uncertainty over the legitimacy of these purposes in the tax-exempt market..

5. The reference to "10b-5" refers to the section of the Securities Act of 1934 relating to antifraud provisions. It is also interesting to note that in one negotiated sale of WPPSS bonds, the underwriters acquiesced in the issuer's choice of firm of counsel.

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