

Local Government Bond Debt: Understanding Alternatives & Consequences

NACDEP

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Sub-title:

How to avoid making bad decisions!

- Answer: Hire a good financial advisor!
- Once you do that, all is well. End of story!
- But, what if local leaders **want** and **need** to know a bit more than that?

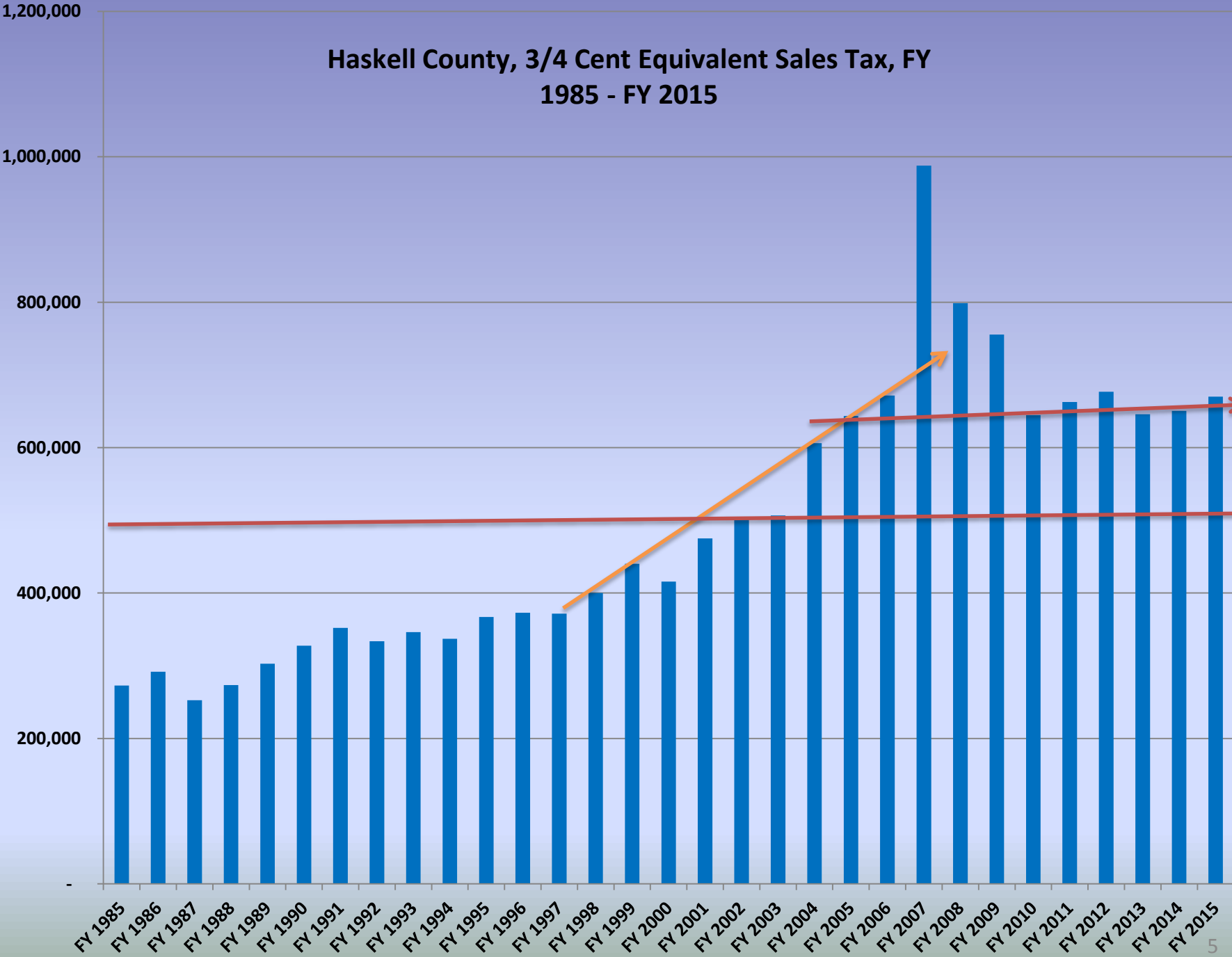
Common Questions

- How much debt is allowed?
- How can borrowed money be used?
- How long can debt term be?
- What are the options for paying off the debt?
- What are the costs and how can those costs be managed?
- Is a vote of the people required?

Case: Haskell County Jail

1. New jail needed
2. Facilities Trust Authority Created, 2005
3. Sales Tax Election, $\frac{1}{2}$ cent ($\frac{3}{8}$ + $\frac{1}{8}$), 25 yr
4. Bonds, \$5.5 million, 25 yr ('06 – '31)
5. More bonds, \$2 million, 25 yr, 2006
6. Sales Tax Election, $\frac{1}{4}$ cent, permanent, 2014
7. \$7.235 million refinance bonds, '14 – '31
8. \$450,000 junior lien sales tax rev note, 2015

Haskell County, 3/4 Cent Equivalent Sales Tax, FY 1985 - FY 2015



Haskell Jail Situation Summary

- 4/8 cent initially, 6/8 cent finally, sales tax pledged to pay bonds
- Early years, sales tax was adequate and unused \$ returned to county and spent on other things
- Now, bond payments require all of it.
- But, voters approved only 5/8 for debt; 1/8 for operating the jail.
- Sold county property to make April 1, 2016 payment
- BOCC call for another ½ cent sales tax vote on June 28.
- Is this particular sales tax ballot legal?

Let's watch a clip

- Setting about 9:30 a.m. on a Monday, June 6
 - Board of County Commissioners Meeting
 - Citizen's Jail Advisory Committee present
 - Many alarmed citizens present
 - Question: Can we legally vote this June 28 sales tax to help make our jail payments?
 - Farley Ward, District Attorney & county legal counsel is not present but his findings are discussed. (He speaks at meeting on June 7)



Primary Players

- Board of County Commissioners (BOCC)
- Facilities Authority Trustees – Paul Storie, Marvin Nolen, & Kenny Short (BOCC)
- Authority Counsel – Emily Virgin, Esq, Virgin Law Firm
- Bond Counsel – Jeff Raley, Esq, Floyd Law Firm
- Underwriter’s Counsel – Steve Likes, Esq, Kutak Rock LLP
- Financial Advisor – S.H. McDonald & Associates
- Trustee - Bancfirst

What can Extension do?

1. Explain the players.
2. Explain the process.
3. Explain the costs.
4. Explain the payments.
5. Explain the funding vehicles.
6. Provide other resources and contacts.

1. Players/Terms

- Financial Advisor – fiduciary relationship with local government
- Bond Counsel – opinion of taxable status of bond issue & authority of issuer
- Method of Sale – competitive or negotiated
- Underwriter – buys the bonds then sells them
- Trustee/Paying Agent – often escrows funds and makes payments to bond holders

Potential Additional Players

- State Agency/Attorney General
 - e.g. Oklahoma Bond Advisor
- Underwriter's bond counsel
- Trust Authority Counsel
- Rating Agencies
- Auditor

2. Debt Issuance Process

- Determine legitimate uses of debt
 - Capital Improvements (OK)
- Determine legal debt limits
 - 5% of Assessed Valuation (OK County Govts)
 - Trust Authority (created by OK County), unlimited
- Vote?
 - 60% super majority for property tax funded
 - 50% majority if sales tax funded
- Term – max of 25 years
- Interest rate – max of 10%
- Sale Price – no less than par value

Debt Issuance continued

- Secure a good financial advisor
 - RFP process recommended by GFOA
 - Set fee structure up front
 - Confirm no relationship to bond counsel, underwriters, trustee/paying agent
 - This person/firm must be 100% working for only your benefit in a truly fiduciary relationship
 - This is the KEY player for smaller governments who have limited in-house expertise

3. Costs

	Issue Par	Bond	Financial	Authority	Underwriting	Total
<u>State Issuer</u>	<u>Value</u>	<u>Counsel Fee</u>	<u>Advisor Fee</u>	<u>Counsel Fee</u>	<u>Spread</u>	<u>Expenses as % of Par Value</u>
Oklahoma Turnpike Auth., Series 2011A	\$ 524,010,000	\$ 177,000 #	\$ 143,500	\$ 57,901	\$ 1,465,040	0.35%
Grand River Dam Auth., Series 2014A/B	\$ 310,480,000	\$ 114,000	\$ 133,448 ¹	\$ 33,448	\$ 746,047	0.33%
OU General Revenue Bonds, 2015A/B	\$ 34,625,000	\$ 26,000	\$ 23,363 ¹	\$ 7,425 ²	\$ 126,563	0.53%
OCIA (Capitol Repairs), 2015A	\$ 50,000,000	\$ 12,717	\$ 7,400 ¹	\$ 10,500 ²	\$ 128,500	0.32%
OCIA (Refunding), 2015B	\$ 39,535,000	\$ 9,500	\$ 6,354 ¹	\$ 8,407 ²	\$ 101,269	0.32%
OU General Revenue Bonds, 2015C/D	\$ 255,760,000 ³	\$ 56,000	\$ 53,626 ¹	\$ 31,076 ²	\$ 668,940	0.32%
ODFA Master Real Property Lease, 2015A	\$ 41,990,000	\$ 17,100 ³	\$ 6,599 ¹	\$ -	\$ 164,591	0.45%
ODFA Master Real Property Lease, 2015B	\$ 42,145,000	\$ 15,100 ⁴	\$ 5,076 ¹	\$ -	\$ 150,818	0.41%
<u>Local Issuer</u>						
Creek County Educ. Facilities Auth., 2015	\$ 26,800,000	\$ 204,000 #	\$ 201,000	\$ 46,900	\$ 201,000 #	2.44%
Grady Co. School Finance Authority, 2015	\$ 11,955,000	\$ 113,584	\$ 110,584	\$ 23,910	\$ 119,550	3.08%
Okmulgee Co. Educ. Fac. Authority, 2015	\$ 6,295,000	\$ 65,950	\$ 62,950	\$ 14,164	\$ 68,450	3.69%
Marshall Co. Educ. Fac. Authority, 2015	\$ 8,055,000	\$ 83,550	\$ 83,850	\$ 18,124	\$ 86,050	3.82%
Delaware Co. Educational Fac. Auth., 2015	\$ 11,690,000	\$ 119,900	\$ 120,200	\$ 26,302	\$ 122,400	4.99%
Tulsa Co. Ind. Auth. (Jenks Schools)	\$ 83,725,000	\$ 378,000	\$ 315,000	n.a.	\$ 586,075	1.53%
Beckham Co. Educ. Facilities Authority	\$ 7,590,000	\$ 78,900	\$ 75,900	\$ 17,078	\$ 81,400	3.11%

Costs continued

- **The four largest contributors to total issuance costs were underwriter discounts, legal expenses, financial advisor fees and rating agency charges – in that order. We argue that some combination of increased price transparency and intervention from higher levels of government could substantially reduce issuance costs faced by local governments, especially smaller ones.**

Joffe, Marc D., Public Sector Credit Solutions, “Municipal Bond Cost of Issuance,” UC Berkeley Haas Institute for a Fair and Inclusive Society working paper.

Costs continued

I **TABLE 1**
Issuance Cost Per Bond Amount

Bond amount	Number	Percent of bond amount
\$0 to \leq \$500,000	35	7.29
\$500,000 to \leq \$1 million	43	6.38
\$1 million to \leq \$5 million	457	5.92
\$5 million to \leq \$10 million	376	4.03
\$10 million \leq \$20 million	360	2.88
\$20 million to \leq \$50 million	461	2.19
\$50 million to \leq \$100 million	263	1.65
\$100 million to \leq \$500 million	210	1.29
Over \$500 million	32	0.92
Total	2,237	

Robbins, Mark D. and Bill Simonsen, "Municipal Bond New Issue Transaction Costs," Public Financial Publications, Inc., 2013.

4. Payments

- Semi-annual interest payments
 - Simple interest
 - Rates may be greater for more distant bonds
- Annual principal payment
- May or may not be callable

DEBT SERVICE SCHEDULE
 BANCFIRST TRUST & INVESTMENT MANAGEMENT
 Effective: 11/18/2014

ISSUER: HASKELL CNTY PFA REV REFUNDING 2014 HASKELL14

Pay#	Date	Interest	Principal		Balance
1	10/01/2014	59,249.66	0.00		7,235,000.00
2	04/01/2015	112,262.51	405,000.00		6,830,000.00
3	10/01/2015	108,212.51	0.00	2.00%	6,830,000.00
4	04/01/2016	108,212.51	360,000.00		6,470,000.00
5	10/01/2016	104,612.51	0.00		6,470,000.00
6	04/01/2017	104,612.51	325,000.00		6,145,000.00
7	10/01/2017	101,362.51	0.00		6,145,000.00
8	04/01/2018	101,362.51	335,000.00		5,810,000.00
9	10/01/2018	98,012.51	0.00		5,810,000.00
10	04/01/2019	98,012.51	340,000.00		5,470,000.00
11	10/01/2019	94,612.51	0.00		5,470,000.00
12	04/01/2020	94,612.51	345,000.00	2.25%	5,125,000.00
13	10/01/2020	90,731.26	0.00		5,125,000.00
14	04/01/2021	90,731.26	355,000.00	2.50%	4,770,000.00
15	10/01/2021	86,293.76	0.00		4,770,000.00
16	04/01/2022	86,293.76	365,000.00	3.00%	4,405,000.00
17	10/01/2022	80,818.76	0.00		4,405,000.00
18	04/01/2023	80,818.76	375,000.00	3.125%	4,030,000.00
19	10/01/2023	74,959.38	0.00		4,030,000.00
20	04/01/2024	74,959.38	385,000.00	3.25%	3,645,000.00
21	10/01/2024	68,703.13	0.00		3,645,000.00
22	04/01/2025	68,703.13	400,000.00	3.375%	3,245,000.00
23	10/01/2025	61,953.13	0.00		3,245,000.00
24	04/01/2026	61,953.13	410,000.00	3.50%	2,835,000.00

“What if” spreadsheet

Place your local bond issue data in cells A3 through A7 then see payout below.

3,000,000	\$ Amount of Bond Issue				
20	Total Term (years)				
15	Term of Principal Payments				
3.50%	Initial Interest Rate				
0.05%	Rate of escalation of interest rate per year (if any).				



Contact Notie Lansford at OSU-CTP if you have questions or need assistance.

		Beginning				Ending
Pymt No.	Year No.	Debt Balance	Interest Rate	Int. Pymt.	Principal Pymt	Debt Balance
1	1	3,000,000	3.500%	52,500.00	-	3,000,000.00
2	1	3,000,000	3.500%	52,500.00	-	3,000,000.00
3	2	3,000,000	3.550%	53,250.00	-	3,000,000.00
4	2	3,000,000	3.550%	53,250.00	-	3,000,000.00
5	3	3,000,000	3.650%	54,750.00	-	3,000,000.00
6	3	3,000,000	3.650%	54,750.00	-	3,000,000.00
7	4	3,000,000	3.700%	55,500.00	-	3,000,000.00
8	4	3,000,000	3.700%	55,500.00	-	3,000,000.00
9	5	3,000,000	3.750%	56,250.00	-	3,000,000.00
10	5	3,000,000	3.750%	56,250.00	-	3,000,000.00
11	6	3,000,000	3.800%	57,000.00	-	3,000,000.00
12	6	3,000,000	3.800%	57,000.00	200,000.00	2,800,000.00

“What if” spreadsheet

What mill levy is needed to service the debt payments?						
\$	60,000,000.00	Net Assessed Valuation (total taxable value) of the local government				
Alternatively, what sales tax rate is needed to service the debt?						
\$	400,000.00	Average Annual Sales Tax Revenues the past Three Years				
	1.25%	The Average Annual Sales Tax Rate the past Three Years				
5.757	MAXIMUM	1.08%				
Additional Mill Levy by Year	or	Additional Sales Tax Rate Needed				
1.925		0.36%				
1.953		0.37%				
2.008		0.38%				
2.035		0.38%				
2.063		0.39%				
5.757		1.08%				

5. Funding Vehicles

- Property Tax
- Sales Tax
- Revenues Generated
 - Parking garage fees, Utility charges, Industrial park, Jail bed rental
- Other

6. Resources and Contacts

- A. GFOA Best Practices, www.gfoa.org
 - A. “Selecting & Managing Municipal Advisors”
- B. Electronic Muni Mrkt Access, Muni Securities Rulemaking Board,
<http://www.emma.msrb.org/>
- C. State Agency or Attorney General
 - A. OK State Bond Advisor,
<https://www.ok.gov/bondadvisor/>
- D. notie.lansford@okstate.edu (405) 744-8792



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Conclusions

- ❖ Critical for local government to first hire qualified financial advisor for reasonable fee interested only in the welfare of the local govt.
- ❖ Very important for local government leaders to truly understand the essential details and assumptions.
- ❖ Before signing, local leadership needs to question all aspects and ask “what if.”

