Debt Management for Small Governments

Presenters

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- Member GFOA Debt Committee

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Assembling the Finance Team

- Issuer
- Municipal Advisor (fiduciary duty)
- Bond Counsel
  - Disclosure Counsel
  - Special Tax Counsel

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Assembling the Finance Team

- Underwriter
- Underwriter's Counsel
- Placement Agent (if direct placement)
- Paying Agent/Trustee

Other Service Providers
- Verification Agent (if refunding)
- Printer
- DTC
- Rating Agencies

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Assembling the Finance Team

- GFOA Best Practice
  "Unless the issuer has sufficient in-house expertise and access to market information, the issuer should hire a municipal advisor prior to undertaking a debt financing."
- Issuers should hire a Municipal Advisor (MA) and Bond Counsel before hiring other outside professionals.
- MA should assist with:
  - Assessing the objectives of the financing
  - Identifying strategies and priorities (including the bond rating process)
  - Selecting the method of sale that best fits the financing
  - Evaluating other members of the external financing team
  - Selecting the underwriting syndicate
  - Providing expert advice regarding the bond sale

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Debt Overview

- Types of Debt and Underlying Security
  - General Obligation
  - Revenue-backed
  - Debt limitation considerations
- Bonds or Notes
  - For a construction project an Issuer might want to issue notes until the project is completed, then issue bonds for the final project amounts.

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GFOA Resources

- Best Practice – Selecting and Managing Municipal Advisors
  http://gfoa.org/selecting-and-managing-municipal-advisors
- Best Practice – Selecting Bond Counsel
  http://gfoa.org/selecting-bond-counsel
- Debt 101 – Volume I
  http://gfoa.org/debt-101-volume-1-issuing-bond

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Debt Issuance Process

- State and local governments should sell their debt using the method of sale that is most likely to achieve the lowest cost of borrowing.
- Method of sale decision should be made based on a thorough analysis of the relevant rating, security, structure, market conditions, and other factors pertaining to the proposed bond sale.

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Methods of Sale

- Competitive Sale: Bond issue is prepared by the Issuer, MA and Bond Counsel and then offered (via a Notice of Sale or Invitation for Bids) for sale to underwriters on a specified date and time. Bonds are awarded to the firm that offers the lowest True Interest Cost (TIC). Bids are usually submitted electronically.
- Negotiated Sale: The Underwriter of the bonds is selected in advance of the sale and the pricing of the bonds (coupons, yields, spread) is negotiated by the Underwriter and Issuer (with their MA).
- Private Placement: The Issuer places the bonds directly with an investor and does not engage in a public issuance (key issue – placement of a security versus a direct bank purchase).

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Method of Sale Trends – Competitive Sale

- GFOA recommended when:
  - High rating (A or better)
  - Issuer is known in the marketplace
  - Nothing unusual about the structure
  - Market conditions are relatively stable
- Allows selection of the best offer based on the bids received

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Method of Sale Trends – Negotiated Sale

- GFOA recommended when:
  - Low credit rating (Baa/BBB or lower)
  - Issuer is not known in marketplace
  - Unusual structure
  - Unstable market conditions
- Results in the best pricing the selected underwriter can provide based on its marketing efforts and relationships with the investor community

Method of Sale Trends – Direct Purchase

- Popular for bond issues that have a short final maturity (15 years or less)
- Generally less issuance costs
- Potentially higher interest rate due to single investor
- Underwriter often acts as placement agent
- MA provides oversight

Debt Issuance Checklist

- Has the Issuer hired a MA to help with the sale, including determination of method of sale, and hired Bond Counsel to provide an opinion for the sale?
- Has the Issuer utilized the financing team's expertise in determining the debt structure best suited to fulfill the capital needs and complement the debt portfolio of the Issuer?
- Is the type of debt being issued appropriate for the project?
- Does the maturity structure and debt service match anticipated flow of revenue dedicated to pay the bonds?

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Debt Issuance Checklist

- If a competitive sale, are there flexible terms and conditions to provide for the most favorable bids?
- If a negotiated sale, has the Issuer used an RFP process to select the underwriter(s), outside of political influence? Does the RFP include a request for necessary information – cost of borrowing, pricing comparisons, experience, references, etc.?
- Does the deal have a credit rating? How many? Has the Issuer discussed with MA and/or Bond Counsel? Is there a need for bond insurance or other credit enhancement?

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Debt Issuance Checklist

- Has the Issuer developed a POS, OS and other disclosure documents with the assistance of Bond Counsel and/or Underwriter's Counsel (reviewed by the MA) and have they been distributed?
- Do the POS and other disclosure documents meet or exceed industry standards?
- Has the Issuer/team done an appropriate level of investor outreach?

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Debt Issuance Checklist

- Does the Issuer have post compliance policies and procedures in place?
- Does the Issuer understand the various fees associated with the transaction?

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Post-issuance

- GFOA recommends Issuers of bonds or other debt obligations develop and adopt formal, written post-issuance compliance policies and procedures to assist in meeting compliance requirements and in preventing, identifying and correcting possible violations that might occur during the term that bonds are outstanding.
- Such policies and procedures will help an Issuer mitigate the risk of violation and preempt enforcement action from federal parties. Issuers should revisit these policies and procedures at least every three years.

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Post-issuance

Policies and procedures should at least consist of the following elements:

- A list of all of the compliance actions at the time the bonds are sold for each series of bonds
- Documentation of the source and frequency of such compliance requirements
- Identification and assignment of compliance responsibilities to staff members by title

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On-going Procedures, Policies & Practices

The Debt Policy should provide guidance for management procedures, issuance practices and administrative activities including:

- On-going credit rating agency interactions
- Investment of bond proceeds
- Primary and secondary market disclosure, including annual certifications as required
- Arbitrage rebate monitoring and filing
- Federal and state law compliance
- Ongoing market and investor relations efforts

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GFOA Resources

- Best Practice – Selecting and Managing the Method of Sale of Municipal Bonds
  http://gfoa.org/selecting-and-managing-method-sale-bonds
- Best Practice – Debt Issuance Transaction Costs
  http://gfoa.org/debt-issuance-transaction-costs
- Best Practice – Primary Market Disclosure
  http://gfoa.org/primary-market-disclosure
- Best Practice – Post Issuance Compliance Policies and Procedures
  http://gfoa.org/post-issuance-policies-and-procedures

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Continuing Disclosure Responsibilities

- Continuing Disclosure Agreement (CDA) (SEC Rule 15c2-12)
  - Timeframe
  - Type of information to be provided
  - Material events
- For many governments, a Comprehensive Annual Financial Report (CAFR) may fulfill annual financial disclosure requirements
- If a government's CDA states that information will be provided that is outside the scope of the CAFR, that information may be included as a supplement to the CAFR when filing with EMMA https://emma.msrb.org/

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Continuing Disclosure Responsibilities

- Governments should make annual filings as soon as annual audited financial information is complete
  - GFOA recommends within 180 days after end of FY (Note:180 days does not equal 6 months!)
  - Prompt filing reduces risk that information may be found inadequate or misleading because of subsequent events
- GFOA recommends that governments do NOT indicate on EMMA that they will provide information 120 or 150 days following the fiscal year end. 270 days following the fiscal year end is the outside limit, so policies could provide that much flexibility

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GFOA Resources

- Best Practice – Understanding Your Continuing Disclosure Responsibilities
  http://gfoa.org/understanding-your-continuing-disclosure-responsibilities-0

- Debt 101 – Volume II
  http://gfoa.org/debt-101-volume-2-responsibilities-after-bond-issuance

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