

Current Topics in Debt Management

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HISTORIC
FRANKLIN
TENNESSEE



Greetings from Downtown Franklin



2020 in the Life of the Public Finance Officer



*"I can't worry about that now.
I'm worrying about something else."*

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2020 in the Life of the Public Finance Officer



Public Finance Issues in 2020

- **Public Health & Safety Emergencies (plural)**
- Fears of Falling Revenues
- Increasing Expenses
- Changes in Work Settings
- COVID Related Grants to Local Governments
- Etc., Etc., Etc.
- And Now.....Debt Management!!!!!!!

Hot Topics in Debt Management

1. Does the End of LIBOR (12/31/2021) Impact My Government, and if So, What Should the Finance Officer Do in 2021?
2. Continuing Disclosure- SEC Rule 15c2-12
3. GASB Statement 87- Leases
4. Topics of Interest for Rating Agencies
 - a) Cybersecurity
 - b) Environmental/Social/Corporate Governance (“ESG”)
 - c) Pensions & OPEB
 - d) 2020 Impact upon Business Travel/Tourism/Event Related Bonds

END OF LIBOR BENCHMARK INDICES AT END OF 2021



What is LIBOR and Why Do I Care About Its Demise?

- The London Interbank Offered Rate (“LIBOR”), established in 1986, is a globally accepted benchmark interest rate. It is intended to reflect the rate at which major banks lend money to one another. United States municipal market has generally accepted LIBOR as a benchmark rate for many years.
- In 2017, the British Government announced it would stop publishing the LIBOR rate as of December 31, 2021. All forms of debt that use this benchmark will need to transition to a different benchmark or refinance into fixed rate debt. There are many unknowns and undetermined questions for the next benchmark.
- Examples of governmental debt that may be benchmarked to LIBOR:
 - Interest Rate Swap Agreements with underlying Variable Rate Demand Notes
 - Variable Rate Bank Loans
 - May Apply to Tax Exempt and Taxable Debt

Next Steps for the Finance Officer

1. Inventory all debt for LIBOR exposure
 - ❖ Notes of the CAFR (Long-Term Debt)
 - ❖ Transcripts for prior Bond Sales
 - ❖ Clerk/Recorder files for resolutions related to Debt
 - ❖ MSRB's Emma website- www.emma.msrb.org
2. For loans, VRDNs/swaps, identify, at minimum, the following info:
 - ❖ Current principal outstanding, or notional amount
 - ❖ Date of final maturity
 - ❖ If a swap, what is its current fair market value?
 - ❖ What is the spread to LIBOR as stated in the contract or executed documents?
3. Advise Administration (City Administrator/County Mayor) of the Inventory of Affected Debt.
4. Consult with Public Finance Professionals- Bond Counsel & Municipal Adv.
5. Preliminary Discussion with Comptroller's Office- Division of Local Finance
6. Develop a Recommendation along with a Timeline
7. *Do Not Wait until 2nd Half of 2021 to Start*

Example: City of Franklin Series 2019 C & D Fixed Rate Refunding Bonds



- Refunding of Two Issues
 - \$20 million variable rate bond issued in 2007 (current refunding) with an interest rate swap (LIBOR benchmark).
 - \$15,725,000 taxable Series 2010 Recovery Zone Economic Development Bond (advance refunding).
- \$29,245,000 Tax-Exempt Series 2019C GO Refunding Bonds
 - Structure- 13 year final maturity.
 - True Interest Cost (TIC) of 1.738%.
- \$2,305,000 Taxable Series 2019D GO Refunding Bonds
 - Fund, in part, termination cost of an interest rate swap agreement for the 2007 variable rate bonds.
 - Structure- 8 year final maturity.
 - True Interest Cost (TIC) of 2.057%.
- Results
 - Total Savings, net of city contribution to swap termination, of \$3.1 million in future debt service expense.
 - Eliminate risk of future appropriation of interest subsidy for Recovery era municipal bond programs.
 - Eliminate exposure to end of LIBOR indices at end of 2021.
 - Eliminate long term swap counterparty risk.

Take-Aways from Terminating LIBOR Swap and Refinancing Underlying Variable Rate Debt

1. Approach the transaction as a project.
 1. It will require an investment of staff time. Professionals are important, however they are not a replacement for staff. Staff should own the process and overall debt management for the government.
 2. Develop a schedule with multiple steps. Even if timelines shift, the steps are identified.
 3. Regular check-ins with finance officer, bond counsel, municipal advisor & swap advisor (Financing Team)
 4. Update Administrator or Mayor on a regular basis along the way.
2. Schedule a preliminary conversation with Comptroller's Office Division of Local Finance.
 - ❖ All refundings require advance approval of the Comptroller's Office
 - ❖ Public Finance Officer should be on the call along with professional advisors
 - ❖ Identify if the underlying transaction is Balloon Indebtedness and whether a refinancing will keep the same structure or be modified as part of the new transaction.
 - ❖ Follow up with a Plan of Refunding and if applicable, a Request for Balloon Indebtedness
3. SEC rules may have changed since your swap was executed- A swap advisor will be required in addition to Bond Counsel and MA.
4. Objectively present quantitative and qualitative benefits & risks of each option for serious consideration to Administration and Elected Officials.
5. Consider costs of swap termination in the context of interest rate savings secured from refinancing into traditional fixed rate debt.
6. Consider restructuring underlying principal- paying principal earlier than planned in original bond issue. May soften Balloon Indebtedness of refunding bonds.

CONTINUING DISCLOSURE UPDATE



Continuing Disclosure for Municipal Debt- SEC Rule 15C2-12

Municipal Securities Rulemaking Board definition:

Continuing disclosure consists of important information about municipal bonds that arises after the initial issuance. This information generally reflects the financial health or operating condition of the state or local government as it changes over time, or the occurrence of specific events that can have an impact on key features of the bonds.

First Rule of Thumb- Consult Bond Counsel when a question arises, or even when in doubt, related to disclosure.

Types of Continuing Disclosures

- Audited financial statements (CAFRs)
- Annual financial information
- Notice of failure to provide financial information on a timely basis as agreed to at closing of bonds
- Specific events that may have effect on repayment of the debt, such as
 - ❖ Delinquent payments of interest and/or principal
 - ❖ Defaults
 - ❖ Substitution of credit or liquidity providers
 - ❖ Rating changes
 - ❖ Adverse tax opinions or rulings affecting the tax-exempt status of the security

Filing of Continuing Disclosure

1. Should be timely as agreed upon in closing documents.
2. Disclosure of events must also be timely but not later than 10 business days after the occurrence of the event.
3. The official repository of continuing disclosure is the MSRB's EMMA website- www.emma.msrb.org.
4. Issuer may hire a professional, a Dissemination Agent, to assist with filings on EMMA.

LATEST HAPPENINGS

- In recent years, SEC and Broker/Dealers have been calling for more timely posting of financial information for municipal borrowers. (MSRB created and maintains the EMMA site.)
- Common complaint is that some governments post audited financials significantly later than their continuing disclosure agreement allows. (The # is small.)
- Some market participants want to require more frequent financial disclosure using existing government documents such as monthly or quarterly reports provided to an elected body for informational purposes.
- See SEC announcement on May 4, 2020, “The Importance of Disclosure for our Municipal Markets”¹⁶

GASB Statement 87- Leases



Summary of GASB 87- Leases

- Issued June 2017 and now effective for Fiscal Year beginning July 1, 2021 (FY 2022)
- “Establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an asset.”
- Under GASB 87, there are no longer “capital leases” and “operating leases”. Going forward, there will be three types of leases:
 - ❖ Short term leases/rentals whose term is 12 months or less. (GASB 87 does not apply in this case)
 - ❖ Contracts that transfer ownership at the end of the term (GASB 87 does not apply)
 - ❖ All other leases are recognized and GASB 87 applies.

Debt Management and GASB 87

- Leases will be reported as financing transactions on the government's financial statements.
- Governments should review existing agreements to determine whether reporting liabilities for leases will affect compliance with debt covenants.
- Reporting financing agreements for intangible assets as leases may require revising of the government's capitalization of assets policy.
- An implicit interest rate must be determined for leases without a stated rate within the contract.

Implementation of GASB 87

- Delayed due to COVID 19 until July 1, 2021, for Tennessee entities who typically have 6/30 fiscal years.
- **START NOW.** Develop a game plan to gather all of the government's lease contracts. Review and update policies and procedures relating to capitalization of assets. Evaluate debt covenants for impact, if any.
- Educate departments on the new implications of entering into lease transactions, especially those longer than 12 months.
- Consult with external auditors on calculating liabilities and determining implicit interest rates when no rate is listed in the contract.

RATING AGENCIES

2020 TOPICS OF INTEREST



Hot Topics for Rating Agencies in 2020

- **Cybersecurity**
 - ❖ Growing area of Risk for governments, of all sizes.
 - ❖ Topic for auditors and continuing disclosure community as well.
 - ❖ Repercussions of an attack may be financial (ex: delayed revenue, additional expenses) as well as loss of trust and fear from citizens and customers.
 - ❖ Taking preventative steps and developing policies in advance of an attack are recommended.
- **Environmental, Social and Governance (“ESG”)**
 - ❖ Wide area of analysis of risk associated with financial, management and governance of ESG events, whether short or long term in nature.
 - ❖ Examples: Natural Disasters (Ex. Floods, Fires, Hurricanes, Tornadoes), Sociological Changes (Ex. Influx of new residents who depart other areas of the country) or Other Changes

Hot Topics for Rating Agencies in 2020

- Pensions/OPEB
 - ❖ Area of interest for a long time now. Interest in this topic continues.
 - ❖ Excessive liabilities in many states still receive national attention.
 - ❖ Tennessee Consolidated Retirement System (“TCRS”) remains one of the Top 5 well funded plans in the country.
 - ❖ Single Employer Plans require dedicated staff administration.
- 2020 Impact on Bonds Secured by Tourism/Conferences & Events/Business Travel
 - ❖ Downgrades in ratings & outlooks for Airport/Convention Center and Sports Authorities Revenue Bonds begun in April
 - ❖ What we know as of early October 2020- April and May were terrible for all of these entire sectors. Story since then has been varied. The next 12 months for these facilities are going to be different due to the size and nature of each one.

Parting Thoughts for Finance Officers in 2020

- *Last year we said, “Things can’t go on like this’, and they didn’t, they got worse.*
- *If you want to be successful, it’s just this simple. Know what you are doing. Love what you are doing. And believe in what you are doing.*

Humorist Will Rogers 1879-1935



THANK YOU FOR BEING PART OF OUR VIRTUAL CONFERENCE!

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