Dinsmore

International Municipal Lawyers Association 2023 Annual Conference

Municipal Finance – It Drives the System

SEPTEMBER 29, 2023

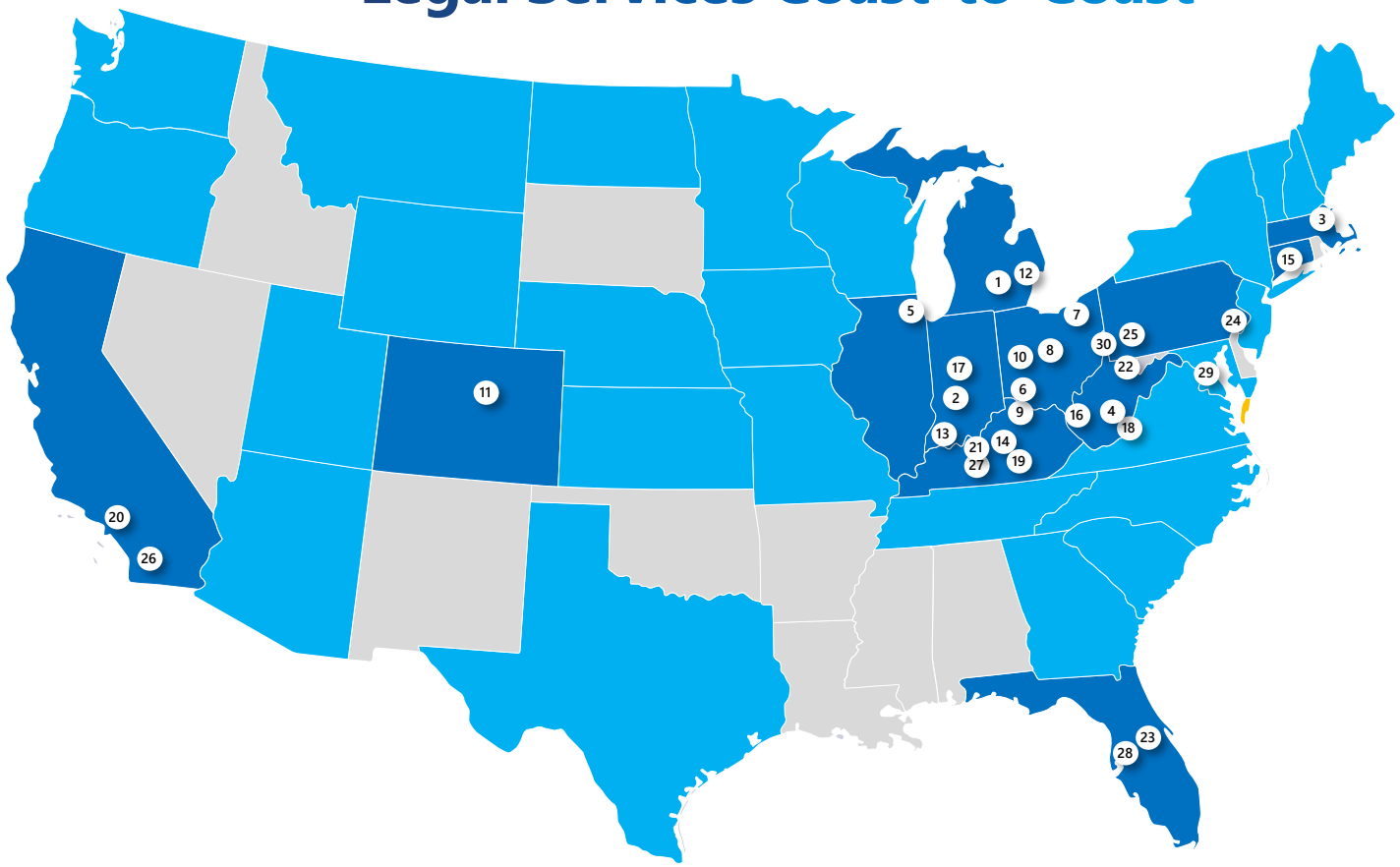


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BIOGRAPHY

Matt is a public finance attorney who advises clients on municipal bond transactions. A focus of his practice is the tax component of public finance, including the use of proceeds, private use, arbitrage, and rebate compliance.

He also acts as bond counsel, disclosure counsel, underwriter's counsel, and issuer's counsel for various public and private clients. Matt also has experience in election law, government affairs, and tax increment financing (TIF).



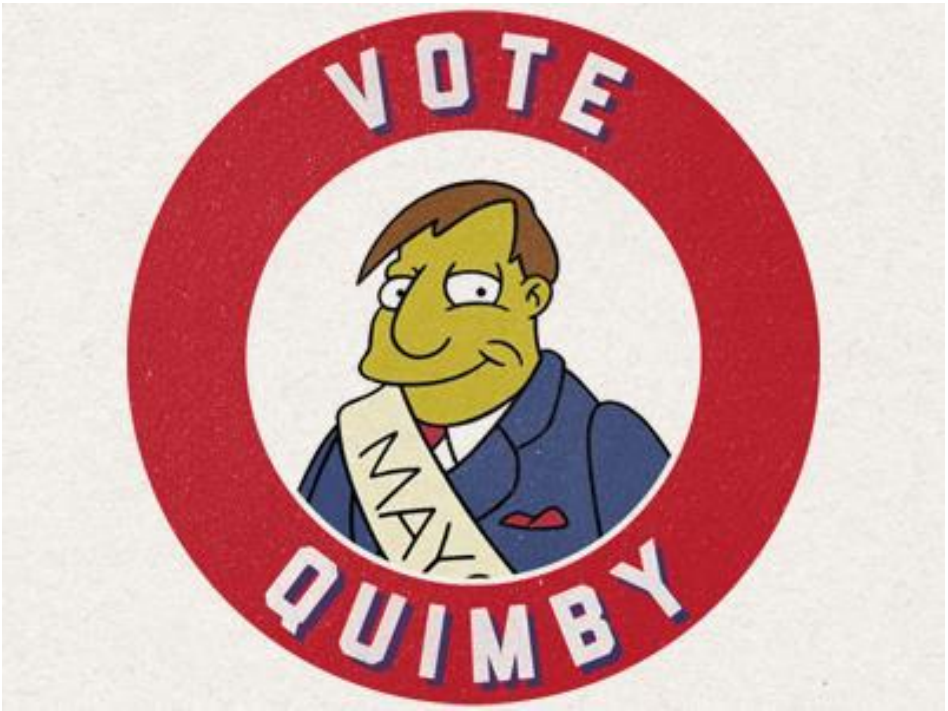
Springfield Atoms threaten to leave Springfield unless City builds team new stadium



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Quimby pledges to do all it takes to keep the team





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Municipal Finance

The Engine That Drives The System

- The municipal securities market is critical to building and maintaining the infrastructure of our nation.
  - Maintenance of the “heart and soul”, or essence of a municipality, is dependent upon capital
  - Apart from generating its own revenues, a municipality may tap the capital markets to borrow money by issuing municipal bonds



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Municipal Finance

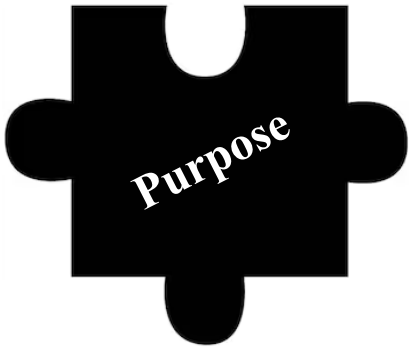
The Engine That Drives The System

- The ability of municipalities to issue debt and borrow money is governed by state law.
- State law may include both constitutional and statutory restrictions.
- Local governments, districts and special authorities (e.g., port authority) have the ability to issue bonds.

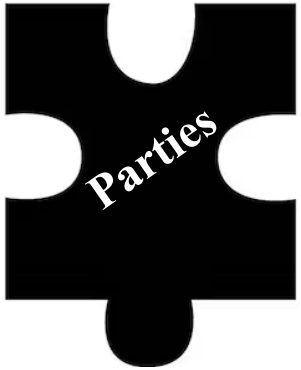


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Municipal Finance



1. For what purposes do Cities borrow money?



2. Who are the Parties involved when a city borrows money?

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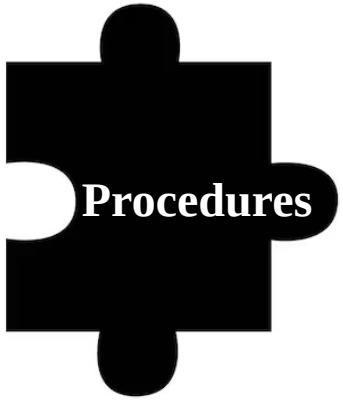
Municipal Finance



3

What are the various types of debt that may be issued by a city?

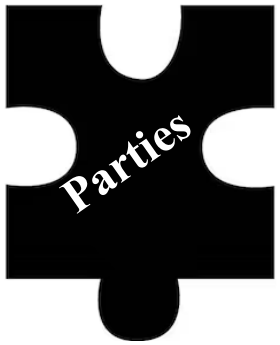
- What is the security for the repayment of the debt?



4

What procedures are followed in issuing the debt?

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Participants in the Municipal Financing Process

- Issuers: public entity authorized to issue municipal securities
- Underwriters : provider of funds for municipal projects (i.e., purchasers and resellers of bonds)
- Financial Advisors: independent firm that assist and advise issuer
- Credit Enhancer : bond insurer or financial institution issuing a supporting letter of credit, which improves credit rating
- Trustee: appointed under a bond resolution or trust indenture
- Bond Counsel: represents and advises the issuer in legal matters
- Underwriter's Counsel: separate legal counsel representing underwriters. Often the initial coordinators of the disclosure document
- Issuer's Counsel: government attorney for issuer

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Primary forms of municipal debt

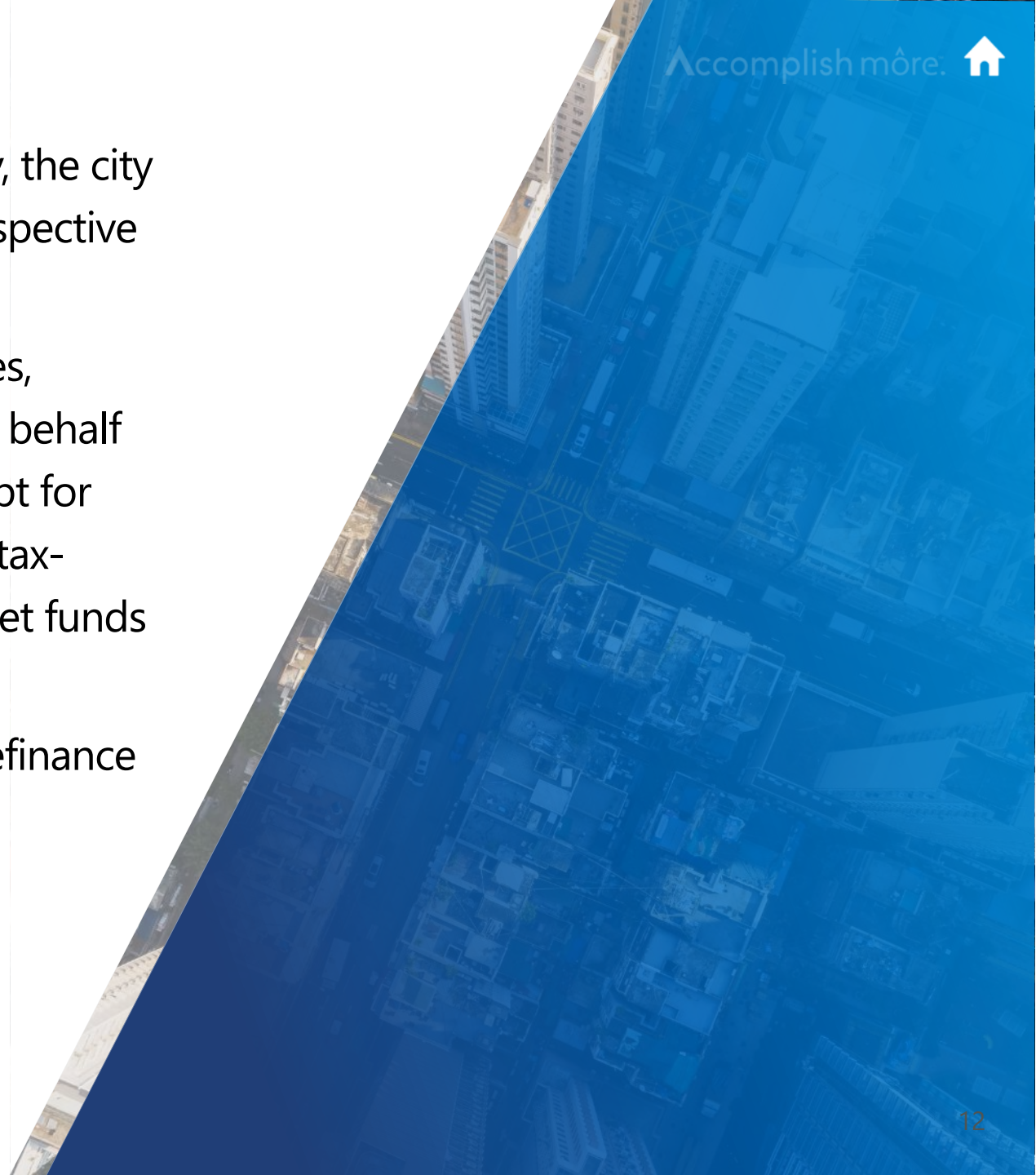
- General Obligation Bonds: most commonly used, these bonds typically involve a full faith and credit pledge.
- Revenue Bonds: bonds which are payable only from anticipated revenue; these bonds finance permanent improvements for a proprietary operation (i.e., sewer or water); these bonds are secured by revenues generated by the mortgage of the properties of the system and a franchise (dormant) to operate the system.
- Judgment Bonds: bonds issued to pay final judgments and court-approved settlements when the issuer is unable to pay the judgment from other funds.

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- Refunding Bonds: also available, but not as frequently used.
- Conduit Bonds: permitted by state and federal law, bonds issued by a local government or special authority for the benefit of a private entity and payable exclusively from revenues received from the private entity.
- Conduit bonds are generally obligations of the private borrower; in other words, no tax dollars or other public funds are pledged for payment (e.g., hospitals or colleges).
- Federal law places additional restrictions on tax-exempt conduit financings.

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- When a municipality chooses to borrow money, the city acts as the borrower, with the approval of its respective council or commission.
- The purchaser may consist of a variety of entities, including but not limited to, your local bank on behalf of itself; banks or underwriters who buy the debt for resale to others; trust customers; corporations; tax-exempt mutual funds; tax-exempt money market funds or private investors.
- Bonds may be refinanced much like you may refinance a house.



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- The market requires information about your city, its financial condition and the particular issue, before it will invest.
- This information is distributed through services such as Electronic Municipal Market Access ("EMMA"), and ratings provided by Moody's Investors Service and Standard & Poor's Corporation.
- These entities provide reports on debts to be sold as well as credit ratings for the particular issuers.

EMMA®
Electronic Municipal Market Access
A service of the MSRB

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Federal Tax Exemption



- Taxable or Tax-exempt?
- Bonds issued by state or local governments may qualify for federal tax exemption. Interest paid on the bonds is usually excludable from the gross income of bondholders for the purpose of federal income taxes.
- Tax-exempt bonds are more attractive because investors are willing to accept lower rates on bonds that are tax exempt, thus reducing the interest costs paid by the governmental borrower.

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Basic Federal Tax Rules

- **Four Areas of Compliance**
  - Use of tax-exempt bond proceeds
  - Change of use and disposition of tax-exempt bond-financed property/facilities
  - Arbitrage and investment of tax-exempt bond proceeds
  - IRS Form 990 Schedule K
- **IRS Enforcement of rules**
  - Examinations of issues of tax-exempt bonds
  - Voluntary Compliance

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Basic Federal Tax Rules (cont.)

- **However, no need to get into too much detail on that today.**
- **Federal tax law requirements for tax-exempt bonds summed up in simple everyday terms:**
  - Don't issue too much
  - Don't issue too soon
  - Borrow for capital expenditures (with some exceptions)
  - Borrow for municipality's exempt purpose
  - Avoid nongovernmental use (i.e., private use)
  - Follow investment restrictions for proceeds of tax-exempt bonds

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Offering Document

- The offering document is meant to provide information from issuers to current bondholders, potential purchasers, underwriters, securities analysts, and rating services.

- Municipalities must provide a disclosure document, which is usually known as an Official Statement when sold publicly.

- The offering document contains required information regarding the municipality, its finances, and the debt being issued.

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Offering Document (cont.)

❖ Securities Offered – OS must describe provisions of the securities.

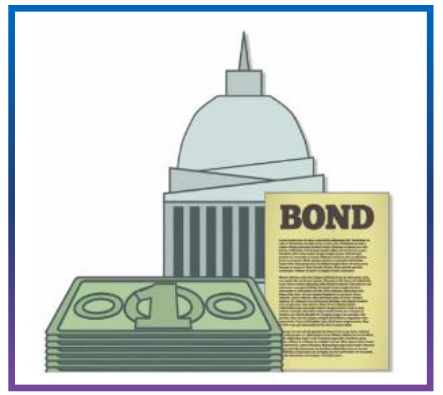
- Credit Enhancement – if the payment of any principal or interest on the securities is guaranteed or insured by any entity other than the issuer, information about the issuer of the credit enhancement must be provided.
- Description of Governmental Issuer – this section provides general background data and descriptive information about the issuer.
- Debt Structure – this information gives general guidelines for information pertaining to an issuer's debt, which should be included in an OS.
- Financial Information – statements and notes from the issuer's latest audited Comprehensive Annual Financial Report (CAFR) should be included in the OS.



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When a municipality sells bonds through a competitive sale, it is imperative that the market knows about the bond sale.

- In addition to sending bid packets to underwriters, advertisements may be sent to any daily newspaper devoted to news about municipal issues and debt. It is usually a publication very widely read in the municipal debt industry, virtually guaranteeing that municipal underwriters will see the bond sale advertisement by various jurisdictions (i.e. The Bond Buyer).





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Bond Counsel

- The municipal debt process is facilitated with the assistance of bond counsel.
- Bond counsel provides issuers with a legal opinion attesting to the validity of bond issues.
- Without the approving opinion of recognized bond counsel, the sale of a municipal bond becomes very difficult.
- Bond counsel's opinion gives investors assurance but does not guarantee that bonds are validly issued.



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Bond counsel's opinion provides comfort and information to investors in three areas…

- That the bonds are legal and binding obligations of the issuer;
  - The source of payment and/or security for the bonds; and
  - Whether and to what extent interest on the bonds is exempt from federal and state taxes.



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In addition to providing a legal opinion, bond counsel are often asked to provide some or all of the following services for issuers:



❖ Assisting in planning the financial structure of the bond issue;

- Preparing enabling bond legislation;
- Preparing or supervising bond proceedings, including documents necessary to the authorization, issuance sale, and delivery of the bonds;
- Obtaining appropriate and necessary rulings, approvals, permissions, and/or exemptions from governmental authorities with respect to the issue;
- Assisting in the preparation of official statements;
- Assisting in presenting information to bond rating organizations; and
- Assisting in other specified activities related to the bonds.

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Bond counsel will also render opinions on related matters such as:

- The applicability of particular provisions of federal and state securities laws;
  - The applicability of tax law provisions governing estate and gift taxation;
  - Eligibility of the bonds for investment by various fiduciaries and other regulated investors;
- The status of the bonds and related obligations under laws relating creditors' rights; and
- The validity and enforceability of security agreements, indentures, and other documents related to the bonds and their security
- Most municipalities hire a firm to act as bond counsel, and, providing the service is satisfactory, retain the same firm for an indefinite period.
- This arrangement affords the advantage of continuity in the provision of bond counsel services and allows the municipality to remain in the driver's seat.



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Bond Counsel

- Today, all bonds must be issued in registered form with the name of the owner of each bond being recorded.

  - After the bonds are sold, interest and principal payments must be made to these owners as promised by the issuer.
  - One way to have this service performed is for the issuer to hire a bank to keep track of the original holders and all subsequent ownership changes, automatically mailing them interest checks from the issuer's funds on interest payment dates. That arrangement will last until the bonds mature.
  - This method causes the incurrence of the initial expense of printing bonds and the recurring bank fees charged to make the payments until the bonds mature.

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Book-Entry Only(BEO) System

- The BEO method is the most convenient and cost effective way to pay debt service to bondholders. Issuer does not hire a bank to facilitate payments or other bondholder services.
- All such services are performed by the Depository Trust Company (DTC) at no additional cost to the issuer. DTC operational costs are borne by its members, the investment and commercial banking industry.
- Issuer has fulfilled its legal responsibility after it wires the funds to pay bondholders to the DTC. The DTC then pays the bondholders.
- Bond counsel should be advised of the intent to utilize BEO so that the correct language will be presented in the official statement.

Founded in 1973, the Depository Trust Company is one of the world's largest securities depositories.

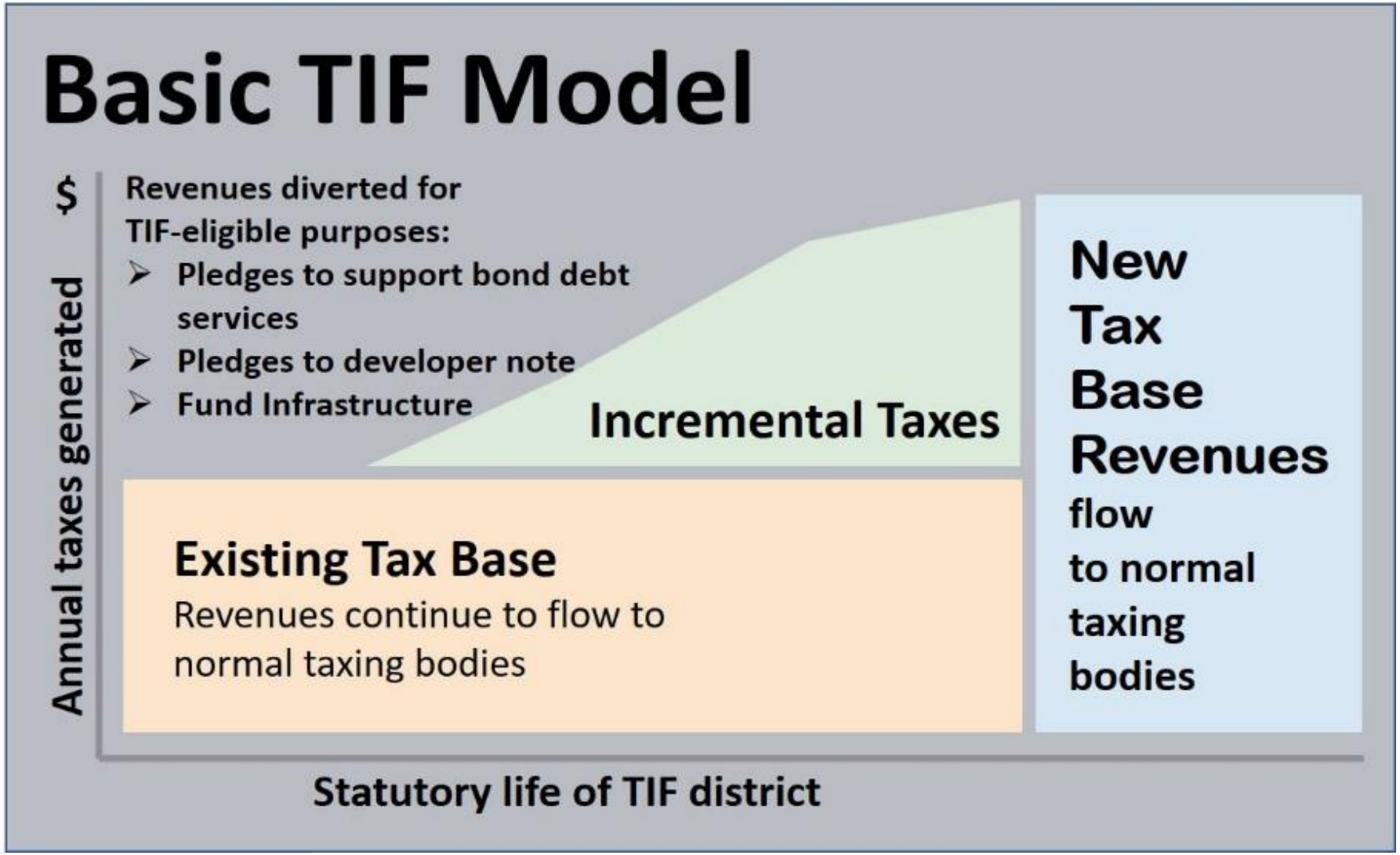
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Tax Increment Financing (TIF)

- Tax Increment Financing (TIF) was originally used to assist in providing infrastructure and other public improvements for redevelopment of blighted areas and are secured by incremental increases in tax revenues received from the improvement of property in the tax increment area.
- TIF is also used for economic development.

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Tax Increment Financing (TIF)



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CONSIDER BEFORE USING A TIF

- Review your state's TIF statute
- Remember that other State law can impact the analysis
  - Are there bidding requirements in State law?
  - Are there restrictions on the ability to "loan" proceeds or TIF cash directly to private party (i.e. can cash be given directly to developer)?
- Negotiating terms
  - Developer skin in the game
- Cooperation of other/impacted governmental entities?



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CONSIDER BEFORE USING A TIF

- Prior Applicable Deal Standard
  - Often, have to deal with position municipality has taken in past
- Home Rule Powers
- Politics/Policy
- Federal Income Tax Law – Tax Exempt Bond Status
  - Private Activity Bond Rules
  - Exempt facility bonds



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DINSMORE'S PUBLIC FINANCE TEAM

TRANSACTION TYPES

- General obligation notes and bonds (including special assessment bonds)
- Sewer and water revenue bonds
- Sales tax bonds
- Certificates of Participation
- Lease-Purchase obligations and Lease Revenue Bonds
- Industrial/Economic development revenue bonds
- Refunding bonds/cross-over refunding bonds
- Preparation of pre-election proceedings for all types of voted bond issues and tax levies
- Assisted with the merger of two regional water and sewer districts, including related litigation matters
- Tax increment financings (TIF)
- Community reinvestment areas (CRA)
- Joint Economic Development Districts (JEDD)
- Urban redevelopment bonds/loans
- Property assessed clean energy bonds (PACE)
- Defeasance transactions
- Financings through the ODOD Energy Load Fund
- Experience with review of Energy Performance Contracts (including performance guarantees)
- Filings for property tax exemptions on public property (DTE-24)
- Creation of special improvement districts (SIDs)
- Routinely handle IRS Audits for clients
- Routinely handle arbitrage rebate calculations for clients
- Routinely handle annual and continuing disclosure matters (including material event postings)
- Preparation and review of management contracts for public facilities such as parking garages
- Application for volume cap for "exempt facility bonds" in conjunction with IDBs

- 35+ public finance attorneys practicing throughout the U.S.
- Handled 110 issues totaling more than *$3.1 billion in 2022*
- More than *950 issues totaling more than $22 billion* since 2018

Federal Tax Compliance Team

Attorneys



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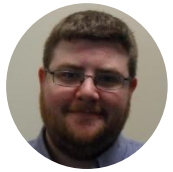


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Thank you.

Questions?



Special thanks to Rita Danish

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