Debt Issuance Considerations and Strategies
Speaker: Brian Della, Public Finance Director, PMA Securities, LLC
Moderator: Dave Frohling, County Board Chair, Dodge County
PMA Services Overview

PMA COMPANIES

MUNICIPAL ADVISORY SERVICES

- Long-Term Financial Planning
- Debt Transaction Management
- Continuing Disclosure Services
- Economic Development (TID)
- Enterprise Cash Flow Modeling
- Referendum Assistance
- Policy Development

INVESTMENT PRODUCTS & SERVICES

- Pooled Investment Solutions (WISC)
- Competitively Bid CDs / Securities
- Bond Proceeds Management (BPM)
- Arbitrage Rebate
- Cash Flow Management
- Separately Managed Accounts
- OPEB Investment Management
Today’s Presentation

**Presenter**
- Brian Della joined PMA in 2018
- Over 18 years of municipal advisory experience to Wisconsin local governments
- Has advised on 159 Wisconsin county debt issues totaling over $2.7 billion
- Bachelor & Master degrees in Civil Engineering from UW-Madison (PE license)
- MBA from Indiana University (Chartered Financial Analyst “CFA” designation)

**Outline**
I. Financial Planning Examples
II. Best Practices for Selling Bonds
III. Who Do You Want to Receive the 0.20%?
IV. What are Anticipation Notes
V. Summary
I. Financial Planning Examples
A county’s property tax levy can be thought of as Operating Levy and Debt Service Levy.

\[
\text{Operating Levy} + \text{Debt Service Levy} = \text{Total Levy}
\]

<table>
<thead>
<tr>
<th>Operating Levy</th>
<th>Debt Service Levy</th>
<th>Total Levy</th>
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<tbody>
<tr>
<td>Subject to Levy Limits</td>
<td>Existing Debt Service</td>
<td>Levy ($)</td>
</tr>
<tr>
<td>Not Subject to Levy Limits</td>
<td>Plus: Future Debt Service</td>
<td></td>
</tr>
<tr>
<td>- General Fund</td>
<td>- Library</td>
<td></td>
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<tr>
<td>- Human Services</td>
<td>- Bridge Aid</td>
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<tr>
<td>- Highway</td>
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<tr>
<td>- Special Rev.</td>
<td></td>
<td></td>
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<tr>
<td>- Other</td>
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</tbody>
</table>

- State statutes (Levy Limits) generally limit the percent growth of the Operating Levy to the percentage of Net New Construction.

- No limits exist for general obligation debt service and certain Operating levies (e.g., Library).

- These Levy Limits have forced counties to finance an ever-increasing share of their capital with general obligation debt.
The capital planning process should be iterative.

- Prioritize projects
- Create a desired schedule (5-yr typical)
- Estimate funding sources (how much debt?)
- Work with your Municipal Advisor on customized debt service structuring options

Are the projected impacts acceptable?

- Debt Service Property Tax Levy
- Enterprise Fund Cash Flows (airport, landfill)
- Credit Rating Considerations
- Other Considerations?
Three Common County Debt Issuance Scenarios

10-year Annual Borrowings
- Existing levy supported general obligation debt service is *gently downwards sloping*
- Desire to keep aggregate levy supported debt service near current levels
- Plan calls for borrowing 10-year notes on an annual basis for projects

1-year Annual Borrowings
- Existing levy supported general obligation debt service has a *sharp drop*
- Desires to keep aggregate levy supported debt service near current levels
- Plan calls for borrowing 1-year notes on an annual basis for general projects

Multiple 20-year Borrowings
- Little existing debt
- Very large building project
- Phased borrowing approach will allow:
  - Gradual increases to debt service levy
  - Increases likelihood of being able to retain positive spread on investments
Existing levy supported general obligation debt service is gently downwards sloping.
Annual capital needs going forward are estimated to average approximately $5,000,000

<table>
<thead>
<tr>
<th>Year</th>
<th>Budget / Calendar Year</th>
<th>Principal</th>
<th>Interest</th>
<th>Par</th>
<th>Dated</th>
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<td>5,705,000</td>
<td>380,945</td>
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<td>930,000</td>
<td>09/01/24</td>
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<td>4,475,000</td>
<td>1,465,000</td>
<td>3.50%</td>
<td>1,420,000</td>
<td>09/01/24</td>
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<td>2026</td>
<td>5,140,000</td>
<td>3,265,000</td>
<td>3.50%</td>
<td>3,760,000</td>
<td>09/01/24</td>
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<td>5,575,000</td>
<td>4,500,000</td>
<td>3.50%</td>
<td>4,685,000</td>
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<td>5,840,000</td>
<td>5,000,000</td>
<td>3.50%</td>
<td>6,090,000</td>
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<td>2029</td>
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<td>3.50%</td>
<td>5,575,000</td>
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<td>2030</td>
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<td>3.50%</td>
<td>4,300,000</td>
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<td>3.50%</td>
<td>3,850,000</td>
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10-year Annual Borrowings (table - projection)
Borrowing $5.0 million annually allows aggregate annual debt service to stay at $6.55 million.
1-year Annual Borrowings (chart - existing)

- Sharp drop in existing debt service exists between years 2024 – 2025
Annual capital needs going forward are estimated to average approximately $1,325,000

<table>
<thead>
<tr>
<th>Budget / Calendar Year</th>
<th>Existing Levy Supported Debt Service</th>
<th>2024 Notes</th>
<th>2025 Notes</th>
<th>2026 Notes</th>
<th>2027 Notes</th>
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<td>2020</td>
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<td>1,327,295</td>
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<td>521,740</td>
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</table>
Borrowing $1.325 million annually allows aggregate debt service to stay at $2.325 million.
County has little existing debt but has a very large upcoming building project.
A $60,000,000 building project has a projected three $20,000,000 borrowings

<table>
<thead>
<tr>
<th>Debt Service Levy</th>
<th>Gross Debt Service</th>
<th>Less: Debt Service Transfer In</th>
<th>Debt Service Levy</th>
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<td>2024</td>
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<tr>
<td>2046</td>
<td>794,828</td>
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<td>794,828</td>
</tr>
</tbody>
</table>

Multiple 20-year Borrowings (table)
Phased borrowing approach will allow for a 3-year step-up in debt service levy and then level
Wisconsin State Statute limits a County’s G.O. debt to 5.0% of equalized value.
Issuing $60,000,000 will still allow this County be at approximately half of its legal debt capacity.
A reasonable estimate for a County’s 20-year tax-exempt borrowing rate is 4.00%.

Current short-term investment rates are substantially higher than 4.00%.

If the County meets certain IRS spend down tests, it can keep any “excess” earnings.
Benefits of debt financing

Wisconsin counties have a variety of capital needs and financial resources, so it should come as no surprise that use of debt can vary greatly. Some counties issue tens of millions of dollars of debt annually as a matter of course while others only issue debt when there is a major building project to finance. If used prudently, debt is an invaluable tool for maintaining a county’s wide range of physical assets. Benefits of utilizing debt include:

Wisconsin’s levy limits – A county can increase its levy by the increase in its general obligation debt service requirement.

Construction cost inflation – The long-term, tax-exempt borrowing rate has traditionally been, and continues to be, lower than the rate of construction cost inflation.

Generational equity – Many capital assets have useful lives measured in decades. Levying for debt service creates a closer alignment between those who benefit from the asset and those who are paying for the asset.

Optimal life-cycle decisions – Debt financing can be used to better maintain assets, which provides for overall lower life-cycle costs.

Managing the levy – A comprehensive capital and financial plan will smooth out impacts to the overall levy associated with financing capital projects.
II. Best Practices for Selling Bonds
The **Government Finance Officers Association** (GFOA), has over 20,000 members and its mission is to advance excellence in public finance.

**Sale of Bonds – Best Practices**

There are five BPs related to the sale of bonds and they should be read and considered in conjunction with each other because of the interaction of the processes to which they apply.

1. Selecting and Managing the Method of Sale of Municipal Bonds
2. Selecting and Managing Municipal Advisors
3. Selecting Bond Counsel
4. Selecting Underwriters for Negotiated Bond Sales
5. Pricing Bonds in a Negotiated Sale

State and local governments engage municipal advisors to assist in the structuring and issuance of bonds whether through a competitive or a negotiated sale process.

**GFOA recommends that issuers hire a municipal advisor prior to the undertaking of a debt financing unless the issuer has sufficient in-house expertise and access to current bond market information.**
When a governmental entity accesses the capital markets for a debt issuance there will be:
- Financial Planning and Debt Transaction Management Services
- Municipal Underwriting Services

Some issuers will use a Municipal Broker-Dealer to provide the above services.

GFOA Best Practices state that these services should be performed by separate companies.
- Municipal Advisor
- Municipal Underwriter
Financial Planning / Debt Transaction Management

Duties and responsibilities associated with Financial Planning and Debt Transaction Management.

### Financial Planning

**Understand Existing Position**
- Review Financial and Debt Management policies
- Historical credit analysis utilizing rating agency models
- Model existing debt service by expected source of repayment

**Identify Capital Needs**
- Current year capital needs
- Projections of future capital needs

**Evaluate Financing Mechanisms**
- Sources of funding (Capital Markets, PP, State Loans)
- Credit pledges (G.O., Revenue, CDA Lease Revenue)

**Model Financing Alternatives**
- Model different debt structures
- Model different future years borrowing amounts
- Project debt service by expected source of repayment
- Project impact to required revenues (Levy, Enterprise Funds)
- Project impact to fund and cash balances

**Presentation to Policymakers**
- Present existing position, alternatives considered, recommended plan, impact of current borrowing, and projected impact of future borrowings
- A comprehensive, long-term financial plan that is regularly updated

### Debt Transaction Management

**Determine how the Underwriter will be selected**
- Pre-select the Underwriter, vs.
- Determine Underwriter on the day of sale

**Manage the Process from Start to Finish**
- Create a calendar of events
- Coordinate with other financing team members
- Attend Board meetings
- Develop a rating agency strategy
- Draft the POS for financing team review
- Determine structure, call provision, etc.
- Determine allow able coupon ranges
- Monitor market conditions and other sales
- Marketing of the debt
- Advocate for Issuer’s interest with Underwriter
- Sign off on final pricing
- Draft the Final OS for financing team review
- Coordinate settlement
- Prepare post-sale analysis

Financial strategies for stronger communities.
Duties and responsibilities associated with Municipal Underwriting.

- An Underwriter’s primary role is to purchase securities from the Issuer and resell the securities to investors.
- An Underwriter has a duty to purchase securities from the Issuer at a fair and reasonable price but must balance that duty with its duty to sell municipal securities to investors at prices that are fair and reasonable.

**Issuer**
Wants **Lower** Rates
Sells Bonds Once a Year

**Investor**
Wants **Higher** Rates
Buys Bonds Weekly

- Without representation, the Issuer is a disadvantage in these negotiations.
The County can tip the scales in its favor by hiring a qualified, independent Municipal Advisor to perform Financial Planning and Debt Transaction Management services. This separates advice from underwriting services.

**Municipal Advisor**
- A Municipal Advisor is an advocate for its County clients’ interests.
- A Municipal Advisor owes its clients a fiduciary duty when performing municipal advisory activities. (duty of loyalty and a duty of care)
- Municipal Advisor can insert competition and transparency into the Underwriter selection process, which drives down the interest rate that investors receive (Competitive Sale).
Issuing Bonds Ex. No. 1: **Without Municipal Advisor**

Below exhibit represents a Negotiated Sale.
Underwriter is Pre-Selected by County.
No competition between Underwriters. No transparency on rates.

(1) County sells its Bonds to the Underwriter, and the Underwriter resells the Bonds to the Investors.
(2) The County signs one contract with the Underwriter for both (i) Investment Banking, and (ii) Underwriting services.
(3) The Investment Banker provides financial planning and debt management services to the County.
(4) The Investment Banker directs the sale of the County's Bonds to its own Underwriting Desk.
Issuing Bonds Ex. No. 2: With Municipal Advisor

Below exhibit represents a Competitive Public Sale. Underwriter determined by Competitive Bidding Process. Creates a larger investor pool. WI Statutes Require this method of sale for General Obligation Bonds (see slide 39).

1. County sells its Bonds to the Underwriter, and the Underwriter resells the Bonds to the Investors.
2. The County signs two contracts, one with the Municipal Advisor and one with the winning Underwriter.
3. The Municipal Advisor provides financial planning and debt management services to the County.
4. The Municipal Advisor conducts a Competitive Sale on the County’s behalf to find the Underwriting Desk that offers the lowest rate.
Can’t Predict What Underwriter Will Make Best Bid

During 2022, Wisconsin counties contracted with Municipal Advisors to conduct a competitive public bidding of their debt issues 29 times.

There were 12 different winning Municipal Underwriters, located throughout the country.
Since 2017, 73% of Wisconsin counties used a Municipal Advisor on their debt issues.

255 Wisconsin county debt issues (2017-2022)
III. Who Do You Want to Receive the 0.20%?
On an annual basis, PMA creates a Wisconsin Counties Capital Market Debt Year in Review, which is emailed to at least one county staff member at all 72 counties.

The presentation includes a detailed review of all the county capital market debt issues for the year and summarizes several years of data for perspective.

The 2022 Year in Review included a detailed apples-to-apples case study comparing one issuer that followed GFOA Best Practices (hired Municipal Advisor and held Competitive Sale), vs a County that didn’t (No Municipal Advisor, Direct Sale, No Underwriter Competition).

The results of the analysis indicate that investors in the County’s debt received 0.20% higher yields than that of the Wisconsin issuer that followed GFOA best practices.

* A PDF copy or a link to a video presentation of the 2022 year in review presentation are available by emailing bdella@pmanetwork.com.
When a County issues 20-year general obligation bonds, it is very reasonable to assume that there is 0.20% (20 basis points) of rate that is “in play”.

For example:

- 3.80% (well executed bond sale)
- 4.00% (poorly executed bond sale)

This 0.20% can be quantified into dollars and these dollars will be allocated!

Because of the unique nature of municipal bond pricing, there are two ways these dollars are calculated.

County elected officials and staff, must decide if it wants its taxpayers to retain the 0.20%, or would the County rather give this money to investors.
Below shows difference in interest expense for bond issues that generate the same amount of proceeds on the day of sale, but have interest calculated at 3.80% and 4.00%.

### Hypothetical Well Executed Bonds Sale (3.80%)

<table>
<thead>
<tr>
<th>Borrow</th>
<th>Coupon</th>
<th>Rate</th>
<th>Future Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 10,000,000</td>
<td>3.80%</td>
<td>3.80%</td>
<td>$ 4,453,220</td>
</tr>
<tr>
<td>20,000,000</td>
<td>3.80%</td>
<td>3.80%</td>
<td>$ 8,906,440</td>
</tr>
<tr>
<td>30,000,000</td>
<td>3.80%</td>
<td>3.80%</td>
<td>$13,359,660</td>
</tr>
<tr>
<td>40,000,000</td>
<td>3.80%</td>
<td>3.80%</td>
<td>$17,812,880</td>
</tr>
<tr>
<td>50,000,000</td>
<td>3.80%</td>
<td>3.80%</td>
<td>$22,266,100</td>
</tr>
</tbody>
</table>

### Hypothetical Poorly Executed Bonds Sale (4.00%)

<table>
<thead>
<tr>
<th>Borrow</th>
<th>Coupon</th>
<th>Rate</th>
<th>Future Interest</th>
<th>Increase in Future Interest</th>
<th>Present Value Interest @ 3.80%</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 10,000,000</td>
<td>4.00%</td>
<td>4.00%</td>
<td>$ 4,713,600</td>
<td>$ 260,380</td>
<td>$ 180,635</td>
</tr>
<tr>
<td>20,000,000</td>
<td>4.00%</td>
<td>4.00%</td>
<td>$ 9,427,200</td>
<td>$ 520,760</td>
<td>361,270</td>
</tr>
<tr>
<td>30,000,000</td>
<td>4.00%</td>
<td>4.00%</td>
<td>$14,140,800</td>
<td>$ 781,140</td>
<td>541,905</td>
</tr>
<tr>
<td>40,000,000</td>
<td>4.00%</td>
<td>4.00%</td>
<td>$18,854,400</td>
<td>$1,041,520</td>
<td>722,540</td>
</tr>
<tr>
<td>50,000,000</td>
<td>4.00%</td>
<td>4.00%</td>
<td>$23,568,000</td>
<td>$1,301,900</td>
<td>903,175</td>
</tr>
</tbody>
</table>

(1) Level annual payments over 20 years with a 10-year prepayment provision.
Ex No. 2: County Gets Less Proceeds at Issuance

Below shows difference in gross proceeds on the day of sale for bond issues that pay the same amount of interest over the life of the bond issue.

### Hypothetical Well Executed Bonds Sale (3.80%)

<table>
<thead>
<tr>
<th>Borrow</th>
<th>Coupon</th>
<th>Rate</th>
<th>Gross Proceeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>$10,000,000</td>
<td>4.00%</td>
<td>&gt; 3.80%</td>
<td>$10,139,233</td>
</tr>
<tr>
<td>20,000,000</td>
<td>4.00%</td>
<td>&gt; 3.80%</td>
<td>20,278,465</td>
</tr>
<tr>
<td>30,000,000</td>
<td>4.00%</td>
<td>&gt; 3.80%</td>
<td>30,417,698</td>
</tr>
<tr>
<td>40,000,000</td>
<td>4.00%</td>
<td>&gt; 3.80%</td>
<td>40,556,930</td>
</tr>
<tr>
<td>50,000,000</td>
<td>4.00%</td>
<td>&gt; 3.80%</td>
<td>50,696,163</td>
</tr>
</tbody>
</table>

### Hypothetical Poorly Executed Bonds Sale (4.00%)

<table>
<thead>
<tr>
<th>Borrow</th>
<th>Coupon</th>
<th>Rate</th>
<th>Gross Proceeds</th>
<th>Reduction in Gross Proceeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>$10,000,000</td>
<td>4.00%</td>
<td>= 4.00%</td>
<td>$10,000,000</td>
<td>$139,233</td>
</tr>
<tr>
<td>20,000,000</td>
<td>4.00%</td>
<td>= 4.00%</td>
<td>20,000,000</td>
<td>278,465</td>
</tr>
<tr>
<td>30,000,000</td>
<td>4.00%</td>
<td>= 4.00%</td>
<td>30,000,000</td>
<td>417,698</td>
</tr>
<tr>
<td>40,000,000</td>
<td>4.00%</td>
<td>= 4.00%</td>
<td>40,000,000</td>
<td>556,930</td>
</tr>
<tr>
<td>50,000,000</td>
<td>4.00%</td>
<td>= 4.00%</td>
<td>50,000,000</td>
<td>696,163</td>
</tr>
</tbody>
</table>

(1) Level annual payments over 20 years with a 10-year prepayment provision.
(2) A reduction in gross proceeds is already in present value terms.
Comparison of 0.20% in Interest vs. Proceeds

Below are the present value dollars “in play” from the previous two slides based on the size of the debt issue and assuming a 0.20% rate difference between well executed and poorly executed.

*The reason 0.20% has less impact on price/proceeds is that there are callable premium bonds after year 10, and issuer does not receive full benefit in the purchase price.
I think we should let the taxpayers keep more of their money
IV. What are Anticipation Notes?
The majority of Wisconsin counties finance their projects directly with either:
- General Obligation Notes
- General Obligation Bonds

**General Obligation Notes**
- Must mature within 10 years
- State of Wisconsin does not prescribe the method of sale (either competitive or negotiated OK)

**General Obligation Bonds**
- Final maturity limited to 20 years (although there are exceptions)
- A permissive referendum is possible, but only for certain projects (highways, bridges, railroad, memorials)
- State of Wisconsin prescribes the method of sale (competitive sale is required per Chapter 67.08(2))

In other words, State Statutes prohibit Issuers of General Obligation Bonds from preselecting the municipal underwriter.
Some Wisconsin counties will finance a large building project with Anticipation Notes.

- Note Anticipation Notes (NANs)
- Bond Anticipation Notes (BANs)

Which are often refinanced within a few months with long-term (20-year) G.O. Refunding Bonds.

**Common Question:**

Why issue debt twice within the span of a few months when you could have just issued once?

**Common Answers:**

- In the absence of a Municipal Advisor, the County has been advised to use Anticipation Notes.
- There are no statutory requirements on the method of sale for G.O. refunding bonds.
- This allows the County to preselect its Municipal Underwriting firm on long-term G.O. debt.

State statute was designed to limit this behavior, and GFOA Best Practices related to the sale of bonds advises against it, yet it does still occur.
The case study included in the 2022 Wisconsin Counties Capital Market Debt Year in Review showed how a poorly executed debt issue could enrich investors (i.e., cost taxpayers) 0.20%.

In addition to the County not hiring a Municipal Advisor nor conducting a competitive sale, the County issued Anticipation Notes for 62 days before refinancing with 20-year G.O. refunding bonds.
V. Summary
Each county’s capital and debt structure are unique, thus requiring customized solutions.

Bond Proceeds Management is very important in the current interest rate environment.

GFOA Best Practices indicate Wisconsin counties should hire a Municipal Advisor (73% do).

GFOA Best Practices encourage Competitive Sales for Wisconsin county general obligation debt.

Wisconsin Statute’s require general obligation Bonds to be sold via a Competitive Sale process.

Anticipation Notes have been used to avoid the Statutory Competitive Sale requirement.

PMA has demonstrated that there is a range of 0.20% on 20-year bond issues.

County officials and staff will determine who gets the 0.20%.

- Buyers of the Bonds?
- County Taxpayers?
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