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GFOAT Regions 8 &13 Roundtable

January 11, 2013

Government Finance Officers Association of Texas



SUMMARY OF TOPICS

- Economic Update
- Refunding Overview
- What Do We Do Now and Who is Responsible for What?
- Plan of Finance
- Official Statement Preparation
- Credit Ratings and Bond Insurance
- Pricing
- Continuing Disclosure
- New Regulatory Environment

ECONOMIC UPDATE





ECONOMIC UPDATE

Significant Q4 2012 Events

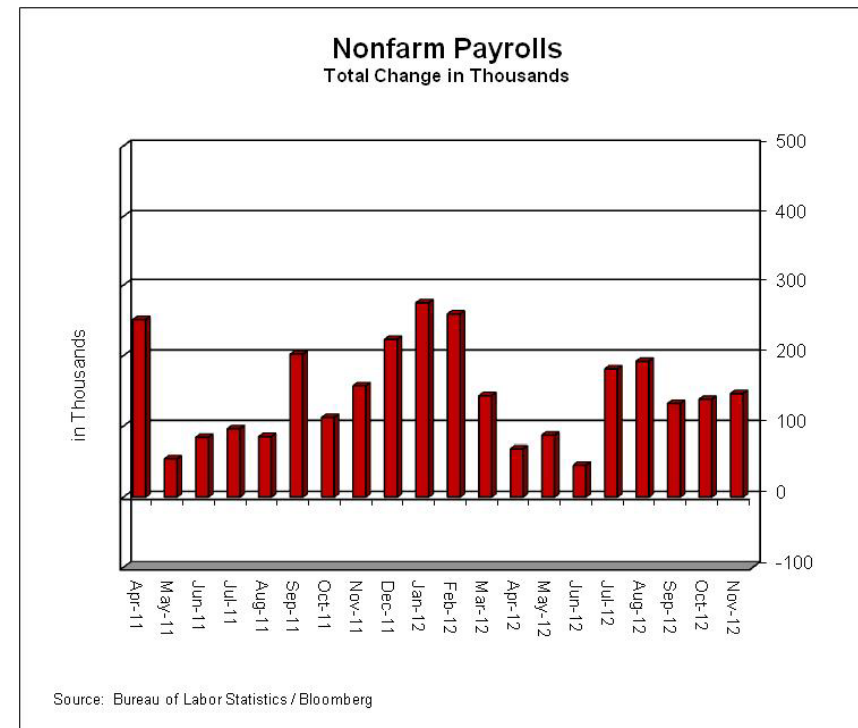
- **Global economies slow** – The **17-member European Union** and **Japan officially reenters recession**. This will have a negative effect on the U.S. economy as exports will likely slow.
- **Superstorm Sandy** hammers the eastern seaboard on Halloween and forces the first unscheduled, **market-wide shutdown since 9/11**, and the **first weather-related close in over 100 years**.
- **The Fed exchanges its expected tightening date for economic data targets**. Now, the Fed will wait for **unemployment to fall below 6.5%** and/or **consumer inflation (CPI)** to move above **2.5%** before starting to raise interest rates. This is probably still many years away.
- Gasoline prices **fall** more than **\$0.60 per gallon**. The effect of lower gasoline prices is **similar to a tax cut**.
- Just after quarter-end, “**Fiscal Cliff**” negotiations resulted in a **reluctant compromise that ensured fiscal frustrations** would spill over into the first quarter of 2013, **including tax exemption questions**.



ECONOMIC UPDATE Cont.

Employment: Nonfarm Payrolls

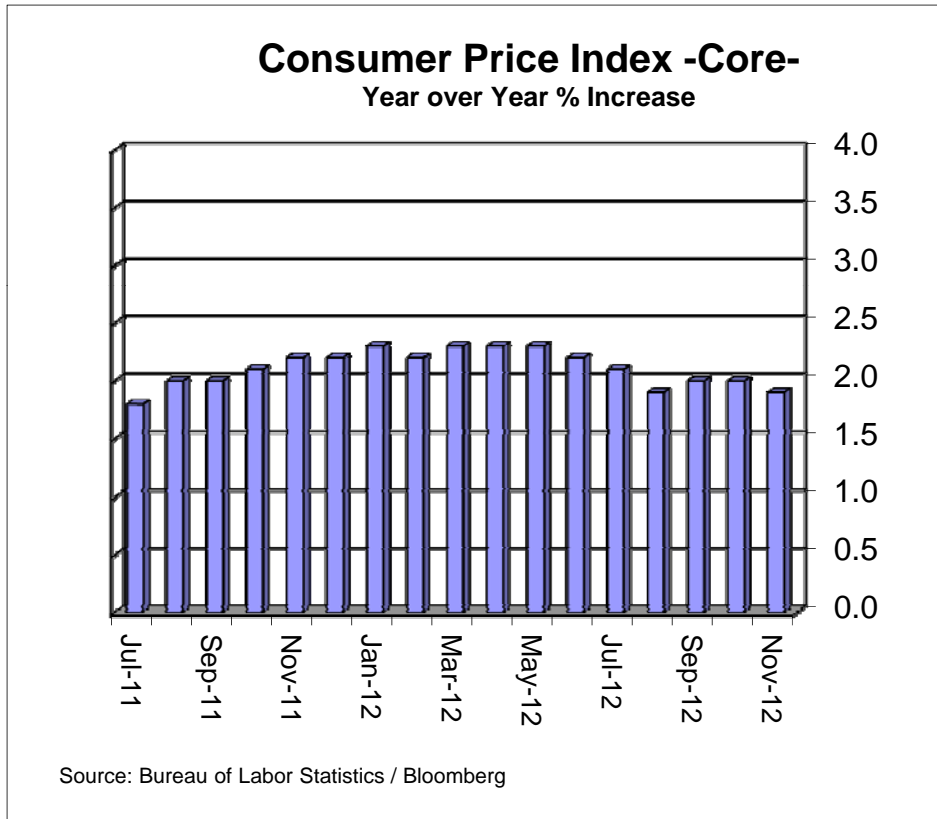
- Job creation is positive, *but not nearly strong enough* to provide full-time jobs to **12.2 million Americans still out of work.**
- In 2012, company payrolls increased by an average of 153k per month, the exact same as in 2011.
- The **unemployment** rate remained at **7.8%** in December. It averaged **8.1%** in **2012**, **8.9%** in **2011** and **9.6%** in **2010.**
- Unfortunately, **unemployment seems to be falling primarily because the labor market participation rate is falling.** Before the recession, this percentage of Americans who are either working or would like to work, **was above 66%.** Now, it's at a near record low of **63.6%.**





ECONOMIC UPDATE Cont.

Inflation: Consumer Price Index

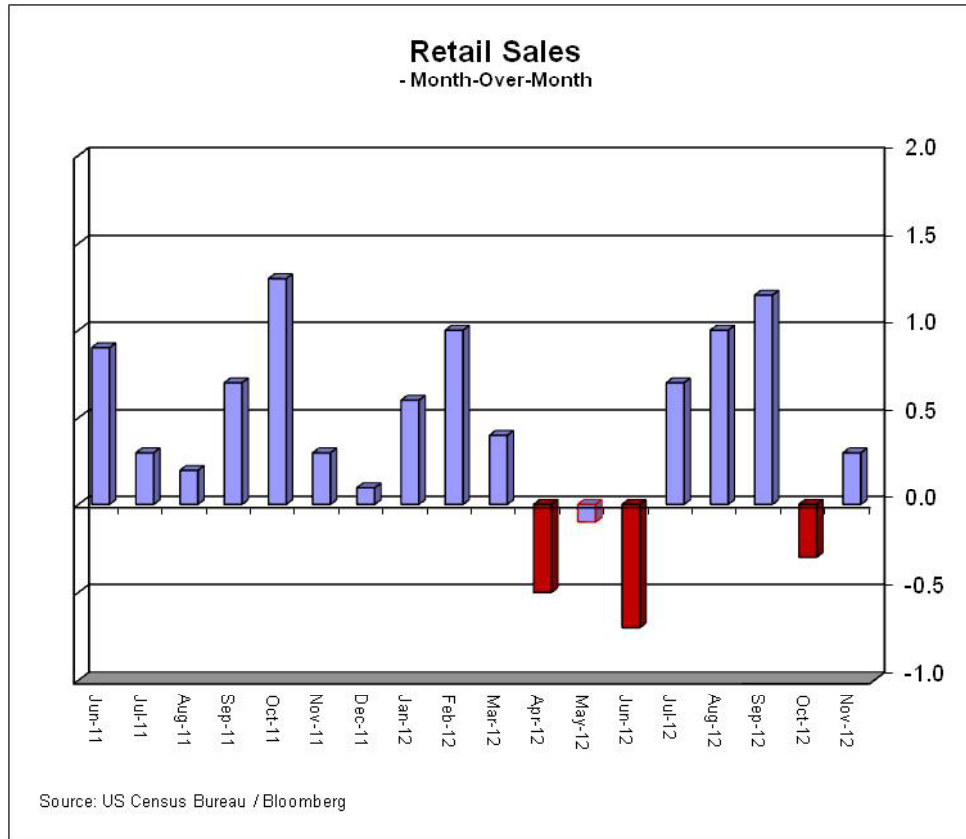


- For the Fed to keep interest rates low, core inflation (which excludes volatile food and energy prices) **must remain below 2.5%.**
- On a **year-over-year basis**, core **CPI is up 1.9%**, matching the lowest rate in 16 months.
- Core CPI History
 - rose 2.6% in 2006
 - rose 2.4% in 2007
 - rose 1.8% in 2008
 - rose 1.8% in 2009
 - rose 0.8% in 2010
 - rose 2.2% in 2011
 - rose 1.9% in 2012



ECONOMIC UPDATE, Cont.

Consumer Spending: Retail Sales



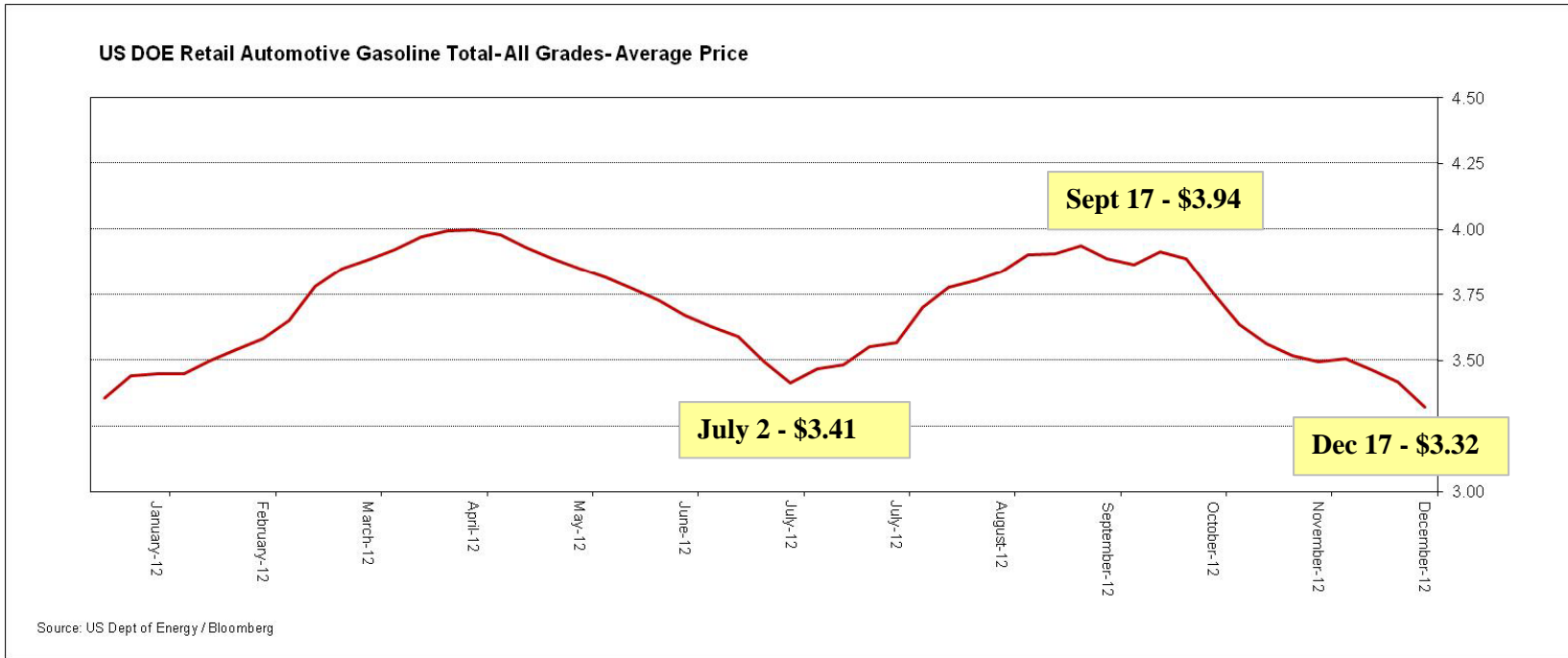
- **Key:** Historically, the consumer accounts for **2/3rds of economic growth**. For the U.S. economy to grow, **consumers have to spend**.
- After a very **solid third quarter**, retail sales have **slowed down**. This is due in large part to **fear and uncertainty over the “Fiscal Cliff,”** and to some degree, **Hurricane Sandy**.
- **Car and light truck sales rose** to a recovery high of **15.5 million** annualized units in November as **vehicles destroyed by Superstorm Sandy were replaced**.
- The **price of gasoline** can have a **major influence** on future spending by **putting more discretionary dollars** in consumer pockets.

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ECONOMIC UPDATE Cont.

Gasoline Prices



Gas prices have plunged in the fourth quarter, continuing the quarter-to-quarter yo-yo pattern that asserted itself in 2012. The average nationwide price for unleaded gasoline is now at the lowest point of the year. ***Recall that a general rule of thumb among economists is that every \$0.01 decline in gasoline price adds a billion dollars to consumer wallets on an annual basis.***

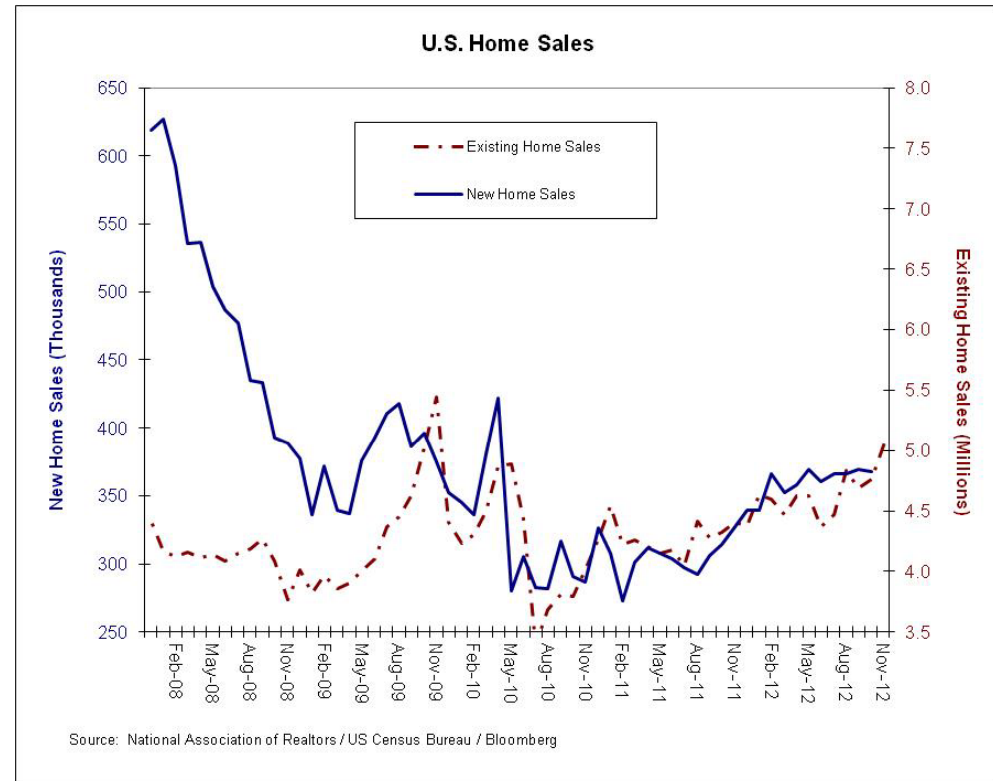
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ECONOMIC UPDATE, Cont.

Home Sales

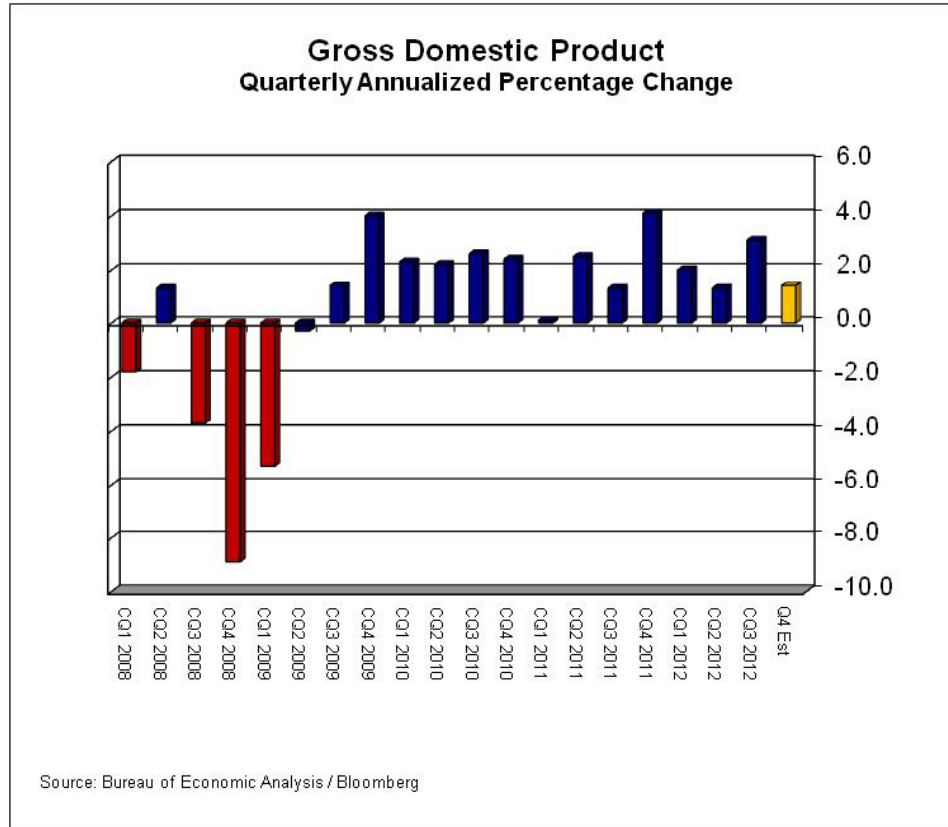
- The **Fed's efforts** to lower mortgage rates and stimulate housing have **paid off**.
- The **average rate on a 30-year, fixed rate mortgage** was **3.35%** in October and November.
- For the **first time in seven years**, the housing sector will make a **positive contribution** to U.S. economic growth.
- According to the National Association of Realtors, 2012 home sales reached a 5-year high.
- The **inventory of existing homes** nationally on the market is now **4.8 months**, the **lowest since 2005**, for **North Texas it is about 3.25 months**.
- The **median price** for a existing home **rose to \$180,600**, **10%** above a year ago.
- In **North Texas**, vacant developed lots continue to be drawn down.





ECONOMIC UPDATE Cont.

Economic Growth: Gross Domestic Product



- **GDP**, the most common measure of economic growth, **averaged 3.0%** for the **20-year period** prior to the beginning of the **recession**.
- *During “the Great Recession,”* which **started in December 2007**. U.S. economic growth **contracted** by **5.1%**, the worst showing in over **70 years**.
- In 2012, **first quarter GDP** growth was up just **2.0%** and **second quarter** growth was even **worse at 1.3%**.
- The economy grew at a surprising **3.1%** rate in the third quarter, but most experts believe it grew at a slower **1.5%** rate in the fourth quarter.

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ECONOMIC UPDATE Cont.

Economic Forecast (December 31, 2012)

- The looming “**Fiscal Cliff**” was more postponed than resolved, meaning that heated negotiations will continue into the new year providing still more uncertainty. Marginal tax rates will increase for the affluent 1%, while the **payroll taxes will revert back from 4.2% to 6.2% for everyone**. The **\$1.2 trillion** (over 10-years) across-the-board spending cuts were shelved ...at least for **another 60 days**.
- Nonfarm payrolls are expected to rise at a gradually increasing pace in 2013, as those businesses that have postponed hiring decisions finally increase payrolls.
- The leaner **housing market should continue to improve in 2013**.
- The **factory sector** is likely to **struggle** as a result of **low global export demand**.
- **Inflationary pressure should remain in check until Europe and Japan** emerge from recession, currently almost **12% unemployment**.
- The median forecast in the Bloomberg economist survey shows **1.4% GDP** growth for the **final quarter of 2012**, and **1.6%** for the **first quarter of 2013**. Some experts have suggested the **payroll tax increase could knock another half point off GDP growth** in the first half.



ECONOMIC UPDATE Cont.

Interest Rate Forecast (January 2013)

- The Fed *abandoned* its “extended period” timeframe, which held that they would leave the overnight funds rate near zero until at least mid-2015 in favor of the economic data points. Specifically, the Fed expects to hold interest rates low until **unemployment falls below 6.5%, or inflation rises above 2.5%**. Most experts believe this new trigger point is at least as far away as the mid-2015 date had been.
- The **overnight fed funds target**, which has now been at a range of **0.00% to 0.25% for more than four years**, is expected to remain **unchanged for at least another two years**.
- **Short-term rates** should remain **near record lows**, and could even fall further in **2013** as demand for short securities exceeds forecasted supply.
- **Long-term rates** are also expected to remain low as a result of the Fed’s ongoing commitment to purchase **\$85 billion in Treasury and mortgage-backed securities each month** for an unspecified period of time.



ECONOMIC UPDATE Cont.

FISCAL CLIFF COMPROMISE

■ What They Did

- Federal long-term unemployment benefits were extended for another year.
- The **Bush tax cuts were extended** permanently for individuals earning less than **\$400,000** and families earning less than **\$450,000**. Those earning above these thresholds will see incremental tax rates revert back **from 35% to 39.6%**.
- The **payroll tax**, which **funds social security**, will **revert back** from the “tax holiday” rate of **4.2% to 6.2%**. This means that **everyone will resume paying at least 2% more in 2013**.
- The **dividend and capital gains** tax rates will increase from **15% to 20%** for **individuals earning above \$400,000** and families above **\$450,000**.
- The **estate tax** will permanently increase from **35% to 40%**. **Individual estates** will be tax-exempt on the **first \$5 million**, while **family estates** will not be taxed on the **first \$10 million**.



ECONOMIC UPDATE Cont.

FISCAL CLIFF COMPROMISE, CONT.

■ What They Didn't Do

- Under the cliff compromise, **across-the-board spending cuts are delayed**, but only by **two months** and only by agreeing to \$24bn in new austerity. Unless there is new legislation, about \$110bn per year in spending cuts will kick in automatically at the beginning of March.
- **The Federal government has already hit its debt ceiling** and the Treasury estimates that it can **only sustain** spending **until late February or early March**. Once these extraordinary measures play out, the government must either stop making debt payments or cut spending enough to balance the budget immediately.

■ Effect on Municipal Market

- **The action this week by Congress brings value to municipal bonds:** there is increased value for the tax exemption given the higher taxes on the wealthy and the new investment income tax, at least for now.
- **The American Taxpayer Relief Act of 2012 (Act) leaves tax-exempt interest on municipal bonds alone, for now.**
- **Build America Bonds (BABs) subsidy could be impacted by sequestration.**



BOND BUYER INDEX

Bond Buyer 20 Year GO Index
September 1981 - December 27, 2012



Bond Buyer 20 Year GO Index is a weekly index estimating the composite yield on 20 general obligation bonds rated "A" or better.

This graph depicts historical interest rates. Future interest rates are dependent upon many factors such as, but not limited to, interest rate trends, tax rates, the supply and demand of short term securities, changes in laws, rules and regulations, as well as changes in credit quality and rating agency considerations. The effect of changes in such factors individually or in any combination could materially affect the relationships and effective interest rates. These results should be viewed with these potential changes in mind as well as the understanding that there may be interruptions in the short term market or no market may exist at all.

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REFUNDING OVERVIEW





BASIC MECHANICS OF A REFUNDING

- A “refunding” is when new bonds are sold to pay off the old bonds
 - Proceeds from the sale of new refunding bonds are used to make the scheduled principal and interest payments on the old bonds until the call date when the remaining principal is prepayed.
 - When the old bonds are not immediately callable, there is an escrow account that is funded with the proceeds for the new bonds and held at a bank until the call date on the old bonds.
 - Issuers have the option to call in the principal and interest on bonds after a date certain (the “call date”). The call date tends to be approximately 10 years after the original the original sale date.



WHY ARE BONDS REFUNDED

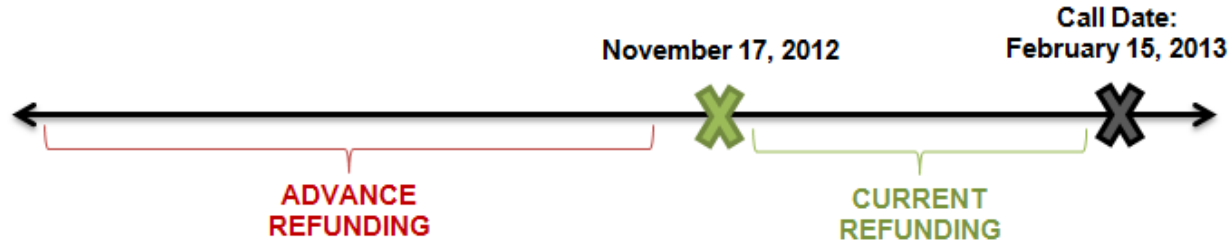
- To refinance existing debt into lower interest rates for cash flow savings
- To restructure existing debt payments due to revenue constraints
- To amend bond covenants



TYPES OF REFUNDINGS

“Advance” Refunding versus “Current” Refunding

- An **advance** refunding occurs when the refunding issue is delivered more than 91 days in advance of the date on which the outstanding bonds can be called (Series 2003 Certificates – February 15, 2013). If a refunding issue is delivered 90 days or less prior to the call date, the refunding bond issue is considered a **current** refunding.



- Tax law allows a tax-exempt bond issue to be **advance** refunded on a tax-exempt basis only once:
 - Example: if the proposed Series 2012 Refunding Bonds were to advance refund a Series 2003 issue, a subsequent advance refunding of the Series 2012 Refunding Bonds could not be accomplished on a tax-exempt basis. However, there is no limit on the amount of time an issue may be refunded on a current basis.
- By waiting until there are less than 90 days until the February 15, 2013 call date, the Issuer preserves the option to advance refund the proposed Series 2012 Refunding Bonds in the future.



ECONOMICS OF A REFUNDING

- Economics of a refunding depend on
 - Interest rates on new refunding bonds
 - Interest rates on old bonds
 - Call date of the old bonds
 - Available investment rates in the escrow
 - Transaction costs



REFUNDINGS FOR SAVINGS

- Because of the IRS limitation on advance refundings, issuers should measure the economic efficiency of the refunding
- Industry uses “present value savings”
 - Present value savings (dollars) is determined comparing the old debt service cash flow to the new, then discounting those semi-annual savings back to the closing date for the new bonds. The All Inclusive Cost (AIC) should be used as the discount rate.
 - Present value savings (dollars) divided by the principal amount of bonds refunded measures the relative efficiency of the refunding. Minimum present value savings percentage thresholds vary by issuer, but often 3% or 3.5% are minimum levels for advance refundings to be considered economical.



NEGATIVE ARBITRAGE

- **Arbitrage yield:** allowable investment return on bond proceeds for a tax-exempt bond issuance (approximates the average borrowing cost on bonds).
- **Negative arbitrage:** the difference between the actual escrow investment return and the allowable investment return (arbitrage yield); the dollar amount of the lost investment opportunity is the "negative arbitrage"
 - Consider comparing the amount of negative arbitrage to the potential present value savings of the refunding
 - If rates don't change as you move closer to the call date on the old bonds, the negative arbitrage shifts to savings for the issuer
- What causes negative arbitrage?
 - Difference between short-term taxable rates in the escrow versus long-term tax-exempt rates on the refunding bond issue
 - Length of time of the escrow (i.e., how long until the call date)



CONSIDERATIONS

- How do the savings compare to the total transaction costs?
- How does the negative arbitrage compare to the present value savings dollars?
 - Sensitivity analysis
 - How does waiting X months impact the economics (while recognizing the interest rate risk)?
 - How much can rates increase and still meet the savings threshold?
- Taxable refunding of a tax-exempt issue that is not eligible for an advance refunding
 - How much can tax-exempt rates move over the period until the refunding would be “current” and eligible for a tax-exempt refunding?



SENSITIVITY OF REFUNDING RESULTS

Example based on refunding \$7,015,000 of Series 2004 Bonds callable 2/15/14

	Current Market	Market rates less 0.25%	Market rates + 3 months
PV Savings (\$)	\$300,567	\$480,590	\$359,706
PV Savings (%)	4.28%	6.85%	5.13%
Negative Arbitrage	\$233,709	\$216,214	\$176,731

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REFUNDINGS GET COMPLICATED

- Structuring
 - Savings could be level (equal savings in each year), uniform (annual savings are proportional to principal amounts refunded), accelerated, or deferred
 - Restructuring to meet revenue constraints
- Determining optimal refunding candidates: savings by maturity
- Determining how much of an old issue that was part refunding is advance refundable: multi-purpose allocations
- Contributing funds on hand to the refunding
 - Debt service funds, debt service reserve funds, old unspent bond proceeds
- Escrow investments
 - Definition of allowable security can vary
 - State and Local Government Series (SLGS) vs Open Market securities

**WHAT DO WE DO NOW AND
WHO IS RESPONSIBLE FOR WHAT?**





WHAT DO WE DO NOW AND WHO IS RESPONSIBLE FOR WHAT?

▪ Represents Issuer

➤ *Financial Advisor (“FA”)*

- The FA is the liaison between the bond market and the Issuer, serving as the Issuer's advocate. The FA possesses specialized transaction, structuring and market knowledge designed to net the most advantageous financing to the Issuer. The FA is charged with coordinating the other consultants, negotiating with other service providers on behalf of the Issuer, such as bond counsel, rating services, insurance companies, paying agents, and underwriters, and preparing the bond offering document.

➤ *Bond Counsel*

- Prepares the Bond Ordinance and other legal documents governing the bond transaction
- Ensures all applicable State and Federal laws are adhered to
 - Renders the legal opinion that the bonds are exempt from Federal income taxes. This is a highly specialized area of the Federal tax code and is crucial in obtaining an attractive borrowing rate.
- May also research specific areas of State or Federal law at the direction of the Issuer and its FA in order to identify and implement effective financing and structuring options.

➤ *Disclosure Counsel*

- Hired by Issuer on complex transactions to help with disclosure associated with the offering document.



WHAT DO WE DO NOW AND WHO IS RESPONSIBLE FOR WHAT?, Cont.

■ Represents Purchaser

➤ **Underwriter**

- Charged with marketing the bonds to the ultimate holders. Purchases the bonds at either public or private sale. In traditional Issuer transactions, the underwriter is generally not involved in the implementation of the financing plan.
- Letter from the Underwriter(s)

➤ **Underwriters Counsel (negotiated sale only)**

- Hired by Underwriter to represent Underwriter's interest in transaction. Reviews offering document, conducts due diligence call/meeting and prepares the Bond Purchase Agreement.



WHAT DO WE DO NOW AND WHO IS RESPONSIBLE FOR WHAT?, Cont.

■ Other Parties

➤ *Verification Agent*

- Verify mathematical accuracy and sufficiency of escrow. Also verifies that yield on escrowed securities does not exceed the arbitrage yield on the bonds.

➤ *Auditor*

- Retained by Issuer. Pursuant to agreement with the Issuer, may or may not be requested to review offering document.

➤ *Rating Agencies*

- The more diversified the economy and revenue base, the better the bond rating is likely to be.
- Bonds attract the best interest rates when the credit quality can be adequately judged against a set of predetermined standards. Three major rating services offer credit rating services that provide this essential function.
- Credit ratings are a function of a number of factors: the diversification of the tax base or revenue source pledged to the bonds, the diversification and strength of the local and State economies, the structuring of the bond issue, and the financial operations of the issuer are key ingredients to a good bond rating.

➤ *Insurance Companies*

PLAN OF FINANCE





PLAN OF FINANCE

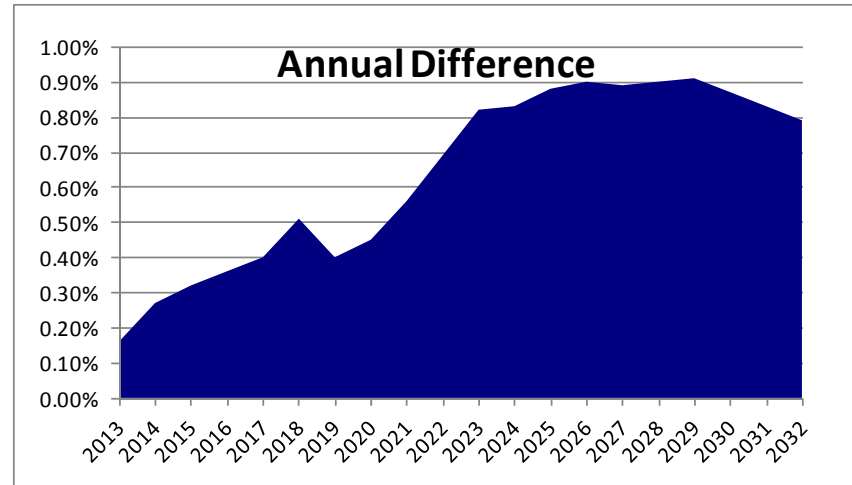
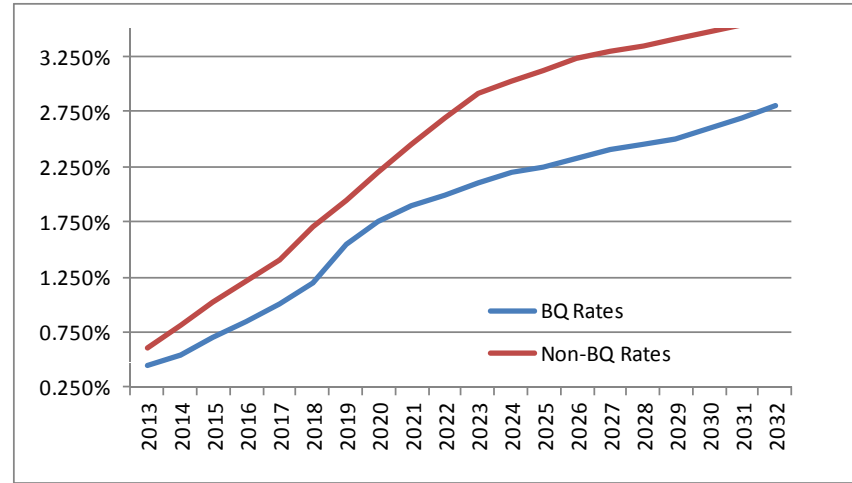
- **Evaluate refunding to be considered**
 - Involve FA and Bond Counsel
 - Determine if the refunding makes sense
 - Does it meet the City's savings target?
 - What is the amount of negative arbitrage compared to present value savings?
 - Does the City have new money needs to be financed with bonds in the near future?
 - Does the refunding fit within the Issuer's capital plan, i.e. does the City need capacity in future years for additional debt?
 - Can the refunding help in managing the I&S tax rate or water/sewer rates?
 - Other
 - Need for restructuring
 - Change in use of proceeds for the refunded bonds
 - Positive publicity with the public
 - Determine best debt instrument (W&S Revenue Refunding Bonds or GO Refunding Bonds)
- **Determine Debt Service Savings Structure**



QUALIFIED TAX-EXEMPT OBLIGATION (QTEO) BENEFIT

Bank Qualified Rates*

	"AA-/Aa3" Rated Scale	
	Bank Qualified	Non-Bank Qualified
2013	0.450%	0.610%
2014	0.550%	0.820%
2015	0.700%	1.020%
2016	0.850%	1.210%
2017	1.000%	1.400%
2018	1.200%	1.710%
2019	1.550%	1.950%
2020	1.750%	2.200%
2021	1.900%	2.460%
2022	2.000%	2.690%
2023	2.100%	2.920%
2024	2.200%	3.030%
2025	2.250%	3.130%
2026	2.330%	3.230%
2027	2.400%	3.290%
2028	2.450%	3.350%
2029	2.500%	3.410%
2030	2.600%	3.470%
2031	2.700%	3.530%
2032	2.800%	3.590%



Bank Qualified – Issuers who issue no more than \$10 million of tax exempt bonds/financings in a calendar year can designate their issue as being ‘bank qualified’ (BQ). BQ affords banks the ability to purchase tax exempt bonds and deduct 80% of their carrying cost and thereby realize the benefit of a tax exempt security.

* - Internal FirstSouthwest interest rate scales as of 1/02/2013



METHOD OF SALE

▪ **Competitive Sale**

- Bond sale is advertised at least a week prior to scheduled sale date
- Bonds are sold at a specified date and time through a “sealed bid” process
- Web-based bidding system (Parity) restricts access to bid results until sale time is passed
- Bonds are sold to the underwriter bidding the lowest borrowing cost
- Depending on amount of bonds offered, underwriters may team up in “syndicates” with one firm submitting the bid on behalf of the group
- Underwriters’ compensation is built into the interest rates bid (similar to mortgage with no points)

▪ **Negotiated Sale**

- A team of underwriters is selected by the Issuer before marketing the bonds. Issuer can ensure participation of M/WBE firms, if desired.
- Underwriters actively pre-market the bonds to investors.
- Interest rates and underwriters’ compensation are determined through negotiation with the underwriters on a specific date. FA works on behalf of the Issuer to assure market pricing.
- Bond pricing is an iterative process between FA and underwriter lasting several hours which allows for changes to bond structure during pricing.
- Underwriting expenses are typically higher due to inclusion of underwriter’s legal counsel and management fees.
- Underwriters’ compensation is paid from proceeds from bonds (like paying points on a mortgage).



FACTORS INFLUENCING SALE METHOD

Competitive

- **High credit quality** of bonds
- Well known/frequent issuer
- Stable bond market
- **Simple bond structure** such that bond size is not dependent on how the bonds are priced

Negotiated

- Need for **flexibility** in pricing due to structure (adv refundings or revenue constraints) and/or timing
- Need for **active pre-marketing** due to market saturation, complicated or troubled credit, or unknown credit



SELECTION OF UNDERWRITERS

- Utilize underwriting firms that:
 - Have bid on the Issuer's competitive bond sales in the past
 - Have supported the Issuer's negotiated bond sales in the past
 - Have submitted unsolicited proposals and ideas to the Issuer of value
 - Have strong Texas and national presence
 - Have strong underwriter rankings

- RFP Process
 - Broad solicitation of underwriters
 - Difficult to evaluate based on objective criteria
 - Rankings can vary depending on time period and universe (i.e., Texas versus all of the United States)
 - May not be in the Issuer's best interest to select firms based on proposed expenses or pricing



AUTHORIZATION

- Typical Resolution, Council approves final terms and conditions at council meeting at time of pricing and sale.
 - Principal
 - Coupons
 - Yields
 - Call Date

- Parameters Resolution (Delegated Sale)
 - Allowed Under Section 1207.007 Texas Government Code
 - **Council delegates final pricing authority** to selected Pricing Officer (typically City Manager and/or Director of Finance)
 - Council establishes and approves bond sale parameters in Bond Ordinance:
 - Maximum Interest Rate
 - Minimum Savings Threshold for Refundings
 - Maximum Aggregate Principal Amount of Issue
 - Final Maturity Date
 - Expiration of Delegated Authority
 - Pricing Officer can only approve sale if all parameters are met
 - Provides flexibility



TIMETABLE

Day	Event
Day 1	Provide initial draft of Preliminary Official Statement for comments and modifications
Day 7	Receive initial comments on Preliminary Official Statement
Day 9	Distribute second draft of Preliminary Official Statement for comments
Day 16	Receive comments on second draft of Preliminary Official Statement Provide draft of Preliminary Official Statement to S&P and insurance company for review
Day 23	Rating Agency call
Day 30	Receive credit rating. Receive all comments and modifications to finalize Preliminary Official Statement
Day 44	Bond Sale: Award bid and adopt Ordinance
Day 49	Prepare and distribute Final Official Statement
Day 84	Bond closing and delivery of funds Approve disbursement of Bond funds

OFFICIAL STATEMENT PREPARATION





OFFICIAL STATEMENT PREPARATION

- Official Statement is Issuer's document regardless who prepares it
- Importance of document for sale and rating
 - Investors rely on accuracy of information to determine their investment decision.
- If unaudited/year to date numbers are included, must be reasonably accurate.
- Disclosure



OFFICIAL STATEMENT PREPARATION, Cont.

- Risks pertaining to accuracy in offering documents
- Issuer: Staff and Governing Body
- FA, Bond Counsel, Underwriter, Underwriters Counsel
- Why is this so important?
 - Market Credibility
 - San Diego – errors and omissions related to pension disclosure; SEC accused City of securities fraud.



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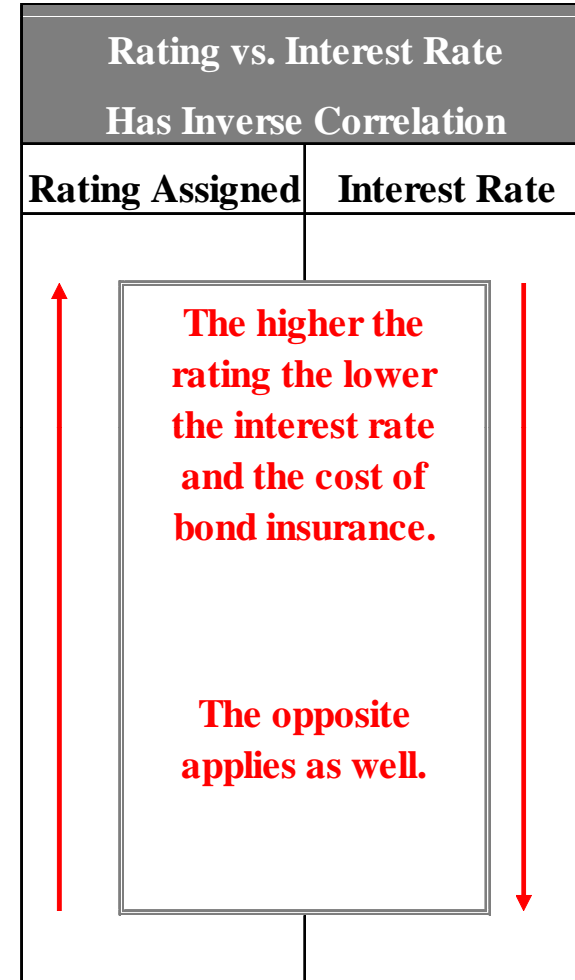
CREDIT RATINGS AND BOND INSURANCE



RATING OF BONDS

	Fitch <u>Investors Service</u>	Moody's <u>Investors Service</u>	Standard & Poor's <u>Rating Service</u>
Highest	AAA	Aaa	AAA
	AA+	Aa1	AA+
	AA	Aa2	AA
	AA-	Aa3	AA-
	A+	A1	A+
	A	A2	A
	A-	A3	A-
	BBB+	Baa1	BBB+
	BBB	Baa2	BBB
	BBB-	Baa3	BBB-

	NON-INVESTMENT GRADE		
Lowest			



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HOT BUTTONS WITH RATING AGENCIES

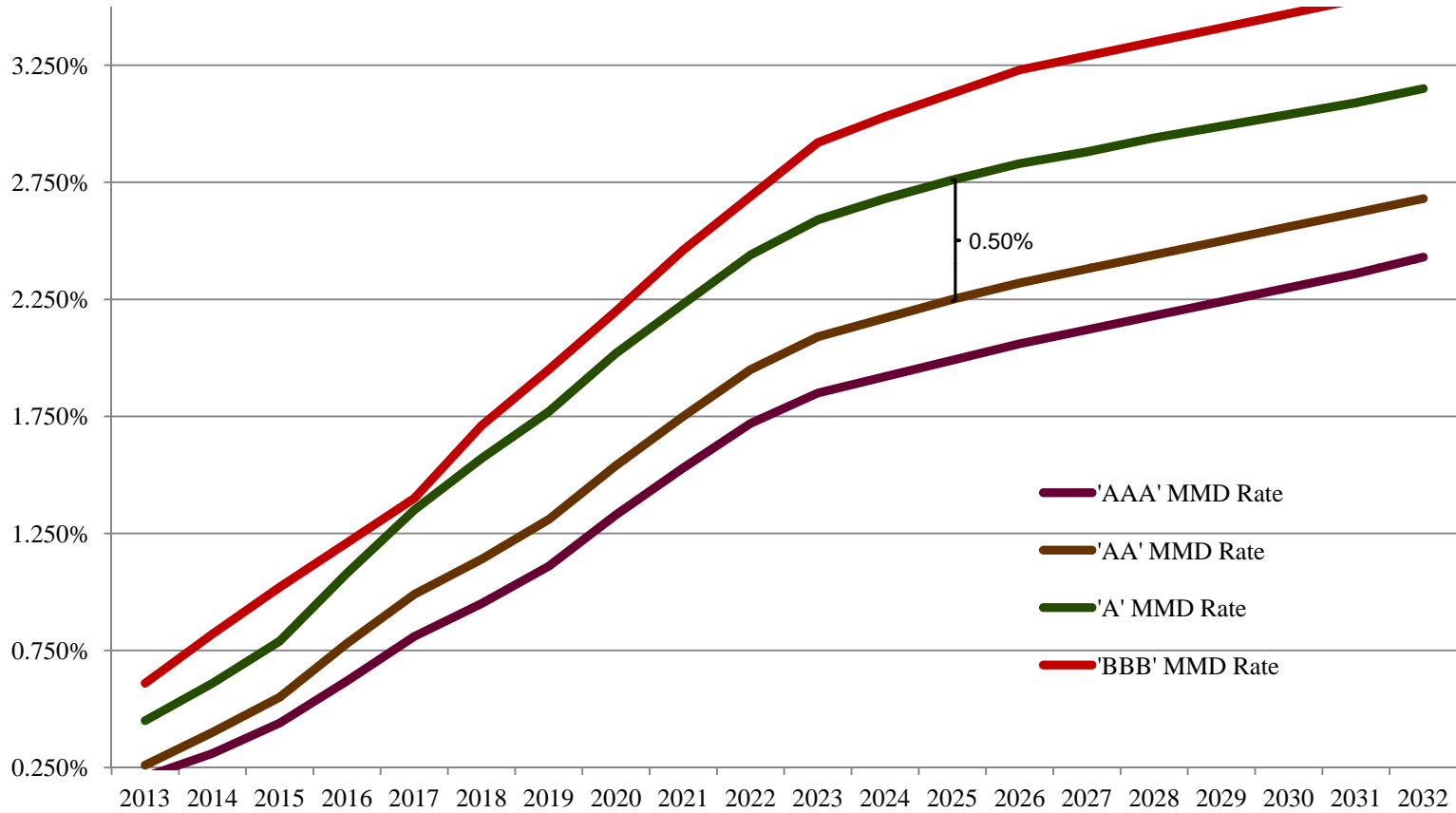
Economy	Finances
<ul style="list-style-type: none"> - Taxable assessed valuation - Residential/commercial mixture - Diversity of the City's tax base - "Health" of the City's economy 	<ul style="list-style-type: none"> - General Fund - Audit - Budget
Debt	Management
<ul style="list-style-type: none"> - Amount of debt outstanding - Future capital needs - Self-supporting debt - Derivatives, variable rate debt, liquidity facilities 	<ul style="list-style-type: none"> - Direction - Tenure - Written policy and procedures
Historical Trends	

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RATING OF BONDS, cont.

Current Credit Spreads



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BOND INSURANCE

December 1, 2007



Insurer	Moody's	S&P	Fitch
Ambac	Aaa	AAA	AAA
Assured Guaranty	Aaa	AAA	AAA
CIFG	Aaa	AAA	AAA
FGIC	Aaa	AAA	AAA
FSA	Aaa	AAA	AAA
MBIA	Aaa	AAA	AAA
XLCA	Aaa	AAA	AAA

December 1, 2012



Insurer	Moody's	S&P	Fitch
Ambac	Ratings Withdrawn	Ratings Withdrawn	Rating Withdrawn
Assured Guaranty/ Assured Guaranty Municipal (Formerly FSA)	Aa3*	AA-	Not Rated
Berkshire Hathaway	Aa1	AA+	Not Rated
Build America Mutual (BAM)	Not Rated	AA	Not Rated
CIFG	Rating Withdrawn	Rating Withdrawn	Rating Withdrawn
FGIC	Rating Withdrawn	Rating Withdrawn	Rating Withdrawn
MBIA (Limited municipal portfolio)	Caa2	B	Rating Withdrawn
National Public Finance	Baa2	BBB	Rating Withdrawn
Syncora (Formerly XLCA)	Ca	Rating Withdrawn	Rating Withdrawn

* Rating under review for a possible downgrade

Sources: Moody's Investors Service, Standard & Poor's Ratings Services, Fitch Ratings

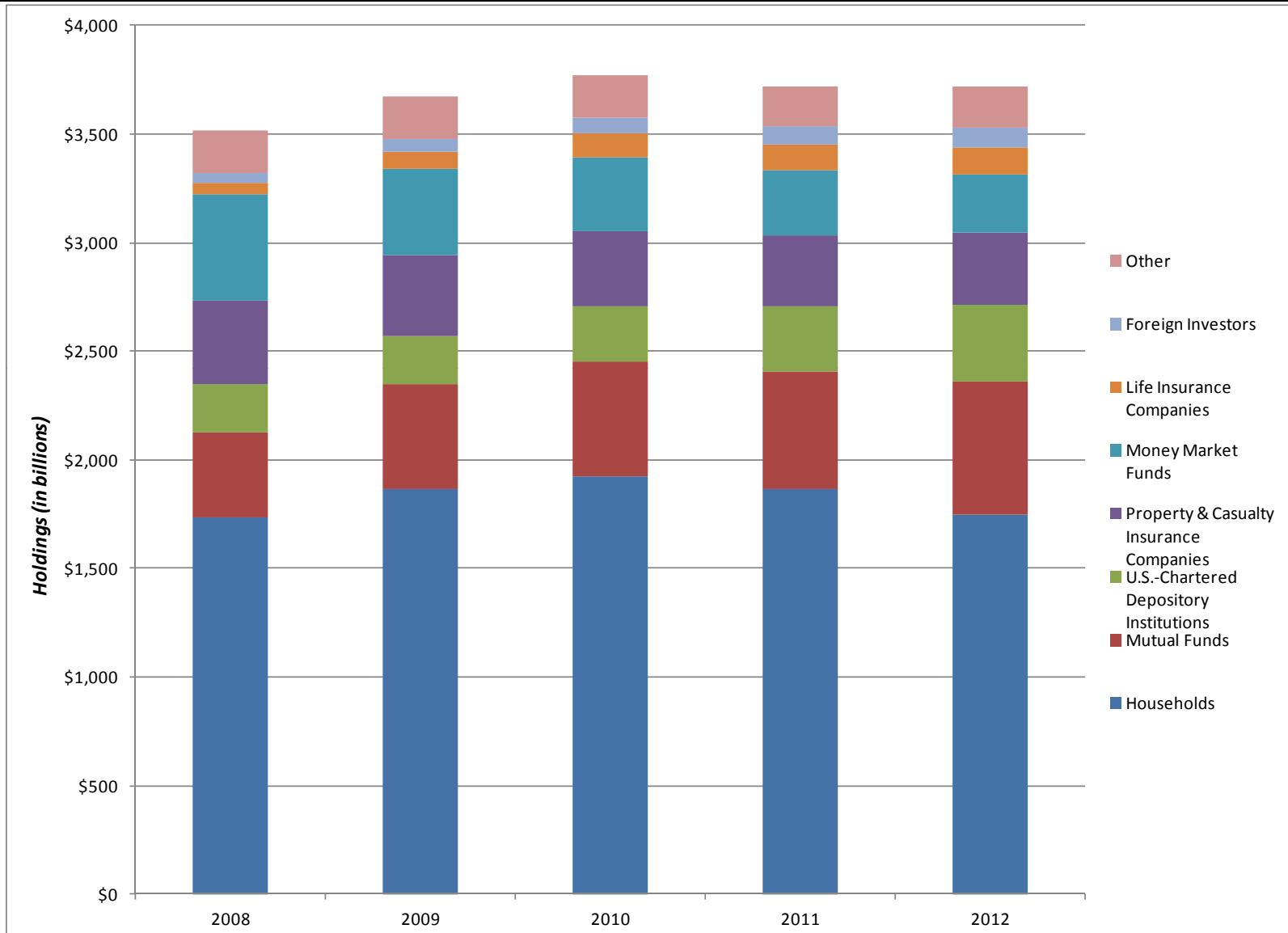


PRICING

GOVERNMENT FINANCE OFFICERS ASSOCIATION OF TEXAS



MUNICIPAL DEBT INVESTORS



GOVERNMENT FINANCE OFFICERS ASSOCIATION OF TEXAS



FACTORS IN PRICING

- Credit (Security/Pledge)
 - General obligation bonds vs. water and sewer revenue bonds
- Legal Structure
- Ratings/Insurance
- Finance Structure
- Call Feature
- Material Events
- Timing Related to the Sale
- Oversight




COMPONENTS OF PRICING

- Par Amount
- Coupon
 - Interest rate on a bond
 - Calculation of debt service
- Yield
 - Actual return realized by an investor if the security is held to maturity
- Price
 - Function of the Coupon, Yield, Duration and Call Feature
- Yield and Price have an inverse relationship

General Types of Bonds			
	Premium Bond	Par Bond	Discount Bond
Coupon	4.00%	4.00%	4.00%
Yield	3.00%	4.00%	5.00%
Price (Example)	105.00	100.00	95.00



PRICING

- Competitive Sale
 - Notice of Sale (“NOS”)
 - Contains the general initial structure of the bonds
 - Also contains the parameters under which bids will be accepted
 - i-Deal/Parity
 - Electronic database and bid platform
 - Structuring
 - Generally set prior to the pricing of the bonds
 - Underwriters Compensation
 - Award
 - AG Review
 - Closing
- Negotiated Sale
 - Underwriters Counsel –
Second set of eyes
 - Interaction with Underwriter and Desk
 - Structuring
 - Greater flexibility for change during the pricing process
 - Process – How do I get a fair Price?

 - Components of spread?
 - Award
 - AG Review
 - Closing



PRICING, Cont.

▪ Negotiated Bond Allocation Process

➤ Net Designated Orders

- Institutional orders where the order is split between syndicate members as designated by the bond purchaser. Generally, we require three firms to be designated, with no more than 50% to any one firm. Most Net Designated Orders are placed with the Senior Manager.

➤ Group Net Orders

- Each order is shared based on liability (% of transaction each firm responsible for) of each syndicate member. Most Group Net Orders are placed with the Senior Manager.

➤ Member Orders

- All of the commission goes to the firm entering the order. Member orders generally have last priority and often do not get filled.
- Majority of Competitive deals are on member order basis.

▪ Underwriters' Compensation (Negotiated Sale)

➤ Total compensation is also call the “underwriting spread”

➤ Components of the spread:

- Expenses – also includes Underwriters' Counsel, Municipal Advisory Council (MAC) fee
- Takedown – commission paid to sales force
- Management fee – “origination fee” paid to relationship banker

➤ If the takedown is considered below market when compared to similar bond issues, the sales force may not work as hard to sell the bonds. This can translate into cheaper prices (higher rates) offered which means higher interest rates to the Issuer.

CONTINUING DISCLOSURE





CONTINUING DISCLOSURE OBLIGATION

- SEC Rule 15c2-12 – A Brief Timeline
 - **1930s** Securities Acts of 1933 and 1934
 - The “anti-fraud provisions” of the securities laws
 - Securities and Exchange Commission (SEC) created
 - Municipal securities exempt from registration
 - **1970s** New York City Fiscal Crisis
 - **1975** Municipal Securities Rulemaking Board (MSRB) created
 - Tower Amendment, don’t have to file with SEC, like Corporate offerings
 - **1983** The Infamous “Whoops” (WPPSS)
 - Washington Public Power Supply System
 - **1989** SEC adopted Rule 15c2-12 (the “Rule”) to regulate primary offerings of municipal bonds



CONTINUING DISCLOSURE OBLIGATION, Cont.

- **1994** SEC amended the Rule to require that issuers file secondary market disclosure information
- **July 3, 1995** Amended Rule became effective for all obligated issues
- **November 14, 2006**
 - SEC filed fraud charges against San Diego, CA
- **December 8, 2008**
 - SEC amended Rule 15c2-12 (EMMA) - effective **July 1, 2009**
- **May 26, 2010**
 - SEC amended Rule 15c2-12 (Material Events must be filed within 10 business days of event) – effective **December 1, 2010**



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Disclosure Reporting Requirements

➤ Rule 15c2-12 (the “Rule”)

- Became effective in **July 1995**
- Requires issuers to obligate filing of annual financial information and notices of material events in a timely manner to improve disclosure in the secondary market

■ Current Requirements

➤ **All non-exempt municipal issuers with aggregate debt of \$1,000,000 or more and that have issued at least one debt offering in the par amount of \$1,000,000 or more are required to:**

- Prepare and file updated annual financial information
 - Generally within 6 to 9 months of their fiscal year end
- Provide notices of material events
- File documents with the MSRB and state depository (if applicable) each year for as long as the obligated debt remains outstanding



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Disclosure Information Repositories

➤ Prior to July 1, 2009

- State Information Depositories (SIDs)

- Texas (the M.A.C.), Michigan, Ohio and the Carolinas

➤ Nationally Recognized Municipal Securities Information Repositories (NRMSIRs)

- Bloomberg

- DPC Data Inc.

- FT Interactive Data

- Standard & Poor's

Note: www.DisclosureUSA.org was the previously designated disseminator to the SIDs and NRMSIRs and contains date records of documents posted for years 2005-2009



CONTINUING DISCLOSURE OBLIGATION, Cont.

- **EMMA – Electronic Municipal Market Access**
 - **SEC modified Rule 15c2-12 effective July 1, 2009**
 - Eliminated previous NRMSIRs and SIDs as official repositories for secondary market disclosure documents and material events
 - Created a central repository for all municipal issuers (EMMA)
 - The MSRB via the EMMA system is the sole “NRMSIR”
 - www.emma.msrb.org is a free online system operated by the MSRB
 - Past disclosure obligations must be honored until expired (e.g. SID)



CONTINUING DISCLOSURE OBLIGATION, Cont.

- **SEC Modified Rule 15c2-12**

- **Effective December 1, 2010**

- **Material Events** increased from **12 to 16**
 - Materiality determination was removed for certain material events
 - **Material Events must be filed** within **10 BUSINESS DAYS** of occurrence
 - The Rule was expanded to include additional types of municipal securities
 - Variable Rate Demand Obligations (“VRDOs”)
 - SEC reaffirmed underwriters’ responsibilities to have a reasonable basis for recommending any municipal securities



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Required Material Events

The following must be filed regardless of materiality:

- Principal and interest payment delinquencies
 - Unscheduled draws on debt service reserves reflecting financial difficulties
 - Unscheduled draws on credit enhancements reflecting financial difficulties
 - Substitution of credit or liquidity providers, or their failure to perform
 - Adverse tax opinions
 - Defeasances
 - Rating changes
 - **The issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the securities***
 - **Tender offers***
 - **Bankruptcy, insolvency, receivership or similar proceeding***
- * Newly required material events for issuances on or after December 1, 2010**



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Required Material Events, Cont.

The following must be filed if deemed necessary:

- Non-payment related defaults
- Modifications to rights of security holders (changes to bond covenants or the continuing disclosure agreement)
- Bond Calls
- Release, substitution, or sale of property securing repayment of the securities
- **Mergers, consolidations, acquisitions, the sale of all or substantially all of the assets of the obligated person or their termination***
- **Appointment of a successor or additional trustee or the change of the name of a trustee***

*** Newly required material events for issuances on or after December 1, 2010**



CONTINUING DISCLOSURE OBLIGATION, Cont.

- **What Type of Debt Obligations are Exempt?**
 - **Exempt from disclosure filing requirements:**
 - Bond or note offerings with a par amount of \$1 million or less
 - Bond or note offerings issued in denominations of \$100,000 or more, if:
 - Sold to no more than 35 persons deemed capable of evaluating risk
 - Maturity of 9 months or less
 - **Exempt from filing annual information ONLY but not material event notice disclosure:**
 - Issues maturing within 18 months (i.e. interim financings/cash flow obligations)
 - **Issuers with less than \$10 million in aggregate debt outstanding “Small Issuer Exemption”**
 - Must provide annual financial information that is “customarily prepared and publicly available” (e.g. audited financial statements only)
 - Material Event Notice disclosure
 - Prior to July 1, 2009 issuers could choose to provide information upon request or to the SID only
 - This requirement still applies until the older issues are expired



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Consequences of Non-Compliance

➤ What Happened in San Diego and Miami

- **First government accused of securities fraud by the SEC for inaccurate pension disclosure**
 - City could not fund increased Annual Pension Liability
 - By not funding pension benefits, the contribution was slated to grow from a manageable amount to a multi-billion dollar liability by 2010
- **Liability was not disclosed in offering documents to investors, rating agencies, and other participants in the municipal market**

■ Consequences

➤ San Diego

- November 2006, SEC charged City with securities fraud
- Restatement of audited financial statements for FYE 2003 – 2005
- Implementation of 150-item plan set forth by SEC to improve disclosure
- City could not publicly issue debt for four years
- Credit ratings were decreased
- April 2008, five former city officials charged individually with securities fraud
- *Liability was not significantly different than that which other municipal issuers are facing*

➤ Miami

- SEC Filed in July of 2012 against Miami for failing to disclose serious budget problems
- They received “Wells Notice” for securities violations
- This is their second enforcement action since 2003



CONTINUING DISCLOSURE OBLIGATION, Cont.

■ Consequences:

- According to the Rule, underwriters/institutional investors cannot bid on transactions until all required information is filed and a notice of late filing (if applicable) is made
- Non-compliance language must be included in any public offering documents for five years
- Serious or ongoing non-compliance issues could limit access to the capital markets, which may increase borrowing costs
- Serious non-compliance could also lead to lower bond ratings or negative rating actions
- Inaccurate statements in the offering documents is considered securities fraud (e.g. San Diego, Miami)



CONTINUING DISCLOSURE OBLIGATION, Cont.

- **Increased Disclosure for Greater Transparency:**
 - OPEB Liabilities (GASB 45)
 - Significant health care costs that impact Issuer's financial position
 - Variable Rate Debt, Derivative Instruments, and Auction Rate Securities
 - More Recently:
 - Insurance or enhancement provider credit rating and outlook
 - **As of February 14, 2011, underwriters required to indicate disclosure requirements for primary offerings, post on EMMA**
 - **MSRB encouraging voluntary disclosure** of other information (bank loans, private placements, etc.)



CONTINUING DISCLOSURE OBLIGATION, Cont.

- ***“The provisions of Rule 15c2-12 set a floor, not a ceiling. Common-sense approaches to disclosure also serve ethical considerations and the issuers’ self-interests, in keeping their investors and constituents alike current and fully informed.”***

-Stephen J. Weinstein, from the Office of Municipal Securities of the Securities and Exchange Commission

NEW REGULATORY ENVIRONMENT





NEW REGULATORY ENVIRONMENT

▪ Recent Headlines from The Bond Buyer

- "Tax Exemption Faces Real Threat, Tax Panelists Agree"
- IRS urged Congress to reconsider tax-exemption, including municipal tax-exemption
- "House Passes Muni Advisor (MA) Bill, Drawing Mixed Reviews"
- "Muni Office Now Reporting to SEC Chairman; Defining MA Top Priority"
- "SEC to Pursue Securities Charges again Miami"
- "SEC Could Tighten Underwriters Oversight or Form 3-Strike System for Issuers"
- "Sequestration Would Cut BAB Payments by \$255 Million"
- "IRS Audits Bond Issues in Louisiana and Oklahoma"



REGULATORY CHANGES

- Topics
 - Dodd Frank Wall Street Reform Act
 - SEC
 - MSRB
 - IRS

GOVERNMENT FINANCE OFFICERS ASSOCIATION OF TEXAS



DODD FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT

- **Broad based** changes to financial regulations; approved in **July 2010**
- **Has specific** impact on municipal issuers and municipal bond **market** as carried out by the SEC and MSRB
- **Regulates credit rating agencies**
 - The SEC can now require agencies to submit their methodologies for review and can suspend or revoke the registration of an agency with respect to a certain class of securities should there be faulty ratings over a sustained period



SECURITIES EXCHANGE COMMISSION (SEC)

- **Currently, SEC doesn't directly regulate municipal issuers**
 - But does require dealers to verify 15c2-12 filings of municipal issuers in order to sell their bonds

- **SEC is charged with implementing Dodd Frank**

- **Definition of "municipal advisor" is still in the works**
 - H.R. 2827 passed in September narrowed municipal advisor definition to include only those engaged for compensation and clarified those covered by the rule by exempting nine categories of professionals (e.g. engineers, attorneys, swap advisors)

 - SEC then extended the sunset date to September 30, 2013 for the rules of temporary registration of municipal advisors and the date by which the SEC must take action on its final rules, and now expects to finalize definition "early next year"



SEC'S REPORT ON THE MUNICIPAL SECURITIES MARKET

- 165 page report issued on July 31, 2012
- SEC recommends legislative changes to provide additional authority for the SEC to regulate the municipal market
- Focus on improving muni bond trade transparency
- Could establish disclosure standards for primary offering documents (**repeal the Tower Amendment**)
- Could enforce compliance of continuing disclosure agreements with municipal issuers
 - Recently suggested the idea of a 3 strike system for issuers who fail to comply
- Could require municipalities to have audited financial statements and/or more timely financial reporting requirements



MUNICIPAL SECURITIES RULEMAKING BOARD (“MSRB”)

MSRB’s Six Things to Know When Issuing Municipal Bonds

1. MSRB registration is required for underwriters and financial advisors.
2. Underwriters and advisors must provide accurate information related to the sale of bonds.
3. Advisors owe a fiduciary duty to their state/local government issuer clients.
4. State/local governments can use different approaches to financing capital projects to borrow at the lowest possible cost.
5. State/local government issuers can use the EMMA system to communicate important information directly to investors.
6. State/local government issuers can use EMMA to track bond trading.

Source: <http://www.msrb.org/MSRB-For/Issuers/Issuer-Toolkit.aspx>



MSRB RULES/INTERPRETATIONS

- Rule G-17 relates to fair dealing
 - **Senior Manager:** letter to issuer defining role in transaction with compensation disclosure, conflicts disclosure and separate risk disclosure
 - **Co-Managers:** separate letters defining role in transaction with conflicts disclosure
 - Issuer needs to acknowledge receipt of the letters
 - <http://www.msrb.org/msrb1/pdfs/MSRB-Rule-G-17-For-Issuers.pdf>

- Rule G-23 relates to role switching
 - Dealers are prohibited from acting as a financial advisor and underwriter on the same transaction. Prohibition applies to both negotiated and competitive sales. Private placements are treated as underwritings for purposes of G-23.

- Rule G-20 relates to gifts
 - Gifts or anything of value limited to \$100 per person per year (excludes "occasional gifts of meals or tickets to theatrical, sporting and other entertainments hosted by the dealer")



MSRB RULES/INTERPRETATIONS

- Rule G-37 relates to political contributions
 - Addresses "pay to play" by limiting contribution to \$250 per election and only for elections in which the municipal finance professional/dealer is eligible to vote

- MSRB created a State and Local Government Toolkit at <http://www.msrb.org/MSRB-For/Issuers/Issuer-Toolkit.aspx> that includes educational resources:
 - Understanding and using the EMMA system (submitting disclosure information and trade monitoring)
 - Roles and responsibilities of financing team
 - Publications for issuers:
 - ***What to Expect from Your Underwriter***
 - ***Understanding Municipal Market Indices, Yield Curves and Benchmarks***
 - ***LIBOR and the Municipal Market***



IRS

- IRS is becoming more active in reviewing tax-exempt bond transactions for compliance
- Form 8038-G was amended in September 2011 and now includes a question as to whether or not the issuer has written procedures for post-issuance compliance and record retention practices
 - No legal requirement to have procedures but the IRS believes there's a strong correlation between having procedures and compliance
- Primary focus is on use of proceeds
 - Use needs to remain governmental
 - Check with bond counsel before leasing or selling assets financed with tax-exempt bonds or entering into management agreements



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