

Council Finance/Audit Committee Overview of Refunding Opportunities

11/13/17

FINANCIAL MANAGEMENT POLICY STATEMENT GUIDANCE

Debt Refunding

The City's financial advisor shall monitor the municipal bond market for opportunities to obtain interest savings by refunding outstanding debt. As a general rule, the net present value savings of a particular refunding should exceed 3.0% of the refunded maturities unless (1) a debt restructuring is necessary or (2) bond covenant revisions are necessary to facilitate the ability to provide services or to issue additional debt.

Sale Process

The City shall use a competitive bidding process in the sale of debt unless the nature of the issue warrants a negotiated sale. The City will utilize a negotiated process when the issue is, or contains, a refinancing that is dependent on market/interest rate timing. The City shall award the bonds based on a true interest cost (TIC) basis. However, the City may award bonds based on a net interest cost (NIC) basis as long as the financial advisor agrees that the NIC basis can satisfactorily determine the lowest and best bid.

Underwriting Syndicates

In response to the MSRB Rule G-17, which recognizes that the motivations of an underwriter may not be consistent with the best interest of the City, the City shall refer underwriters to its Municipal Advisor to review potential refunding opportunities. The City's municipal advisor is prohibited from underwriting the City's bonds while under contract with the City for municipal advisory services, and for a period of one year after termination of the municipal advisory contract.

The City will consider the recommendation of the Municipal Advisor when engaging one or more firm to underwrite a negotiated bond transaction.

TIMING OF POTENTIAL REFUNDING

Current Refunding – delivery of funds no earlier than 90 days prior to call date

Advance Refunding- delivery of funds 90+ days prior to call date. IRS regulations allow advance refunding only once, but bonds can be currently refunded multiple times if savings are available.

Tax Reform Act- as currently proposed, both the House and Senate versions of the tax reform bill eliminate the ability for state and local issuers to advance refund with tax-exempt bonds, for any issues after December 31, 2017. The IRS considers an issue completed upon delivery of funds.

GO REFUNDING

There is one issue that we have been monitoring for several years for an advance refunding opportunity. This issue funded construction of the Surface Water Treatment Plant, improvements to groundwater plants and distribution lines. The original issue, 2011 Certificates of Obligation, were for \$98.5 million in principal with a 30-year maturity. The bonds are callable February 15, 2020.

<i>Series</i>	<i>Call Date</i>	<i>Maturities</i>	<i>Coupon</i>	<i>Principal</i>
2011 Certificates of Obligation	2/15/20	2021-41	3.25-5.0%	80,935,000
Total Principal to Refund				\$ 80,935,000

Potential savings based on 11/6/17 market conditions with a delivery date of 12/28/17:

<i>Criteria</i>	<i>Amount</i>
Net PV Savings	\$ 9,263,974
PV Savings as a % of Refunded Bonds	11.4462%
Savings Period	22 years
Average Coupon to be Refunded	4.24%
True Interest Cost	3.22%
Est. Debt Service Savings	\$13,592,906
Average Annual DS Savings	\$ 617,859

The savings from this refunding should help the City reduce the magnitude of future surface water rate increases, and accumulate funding that will be necessary to meet the 60% groundwater reduction requirement in 2025.

STAFF RECOMMENDATION

Due to the timing needs associated with the GO refunding issues, particularly with an extremely tight window to beat the potential tax reform act deadline, I am recommending that the City Council approve a parameter sale in advance of the transaction date. A preliminary official statement will be distributed today to rating agencies to allow scheduling of ratings calls the week of November 20.

Under a Parameter sale, the City Council approves an ordinance authorizing the transaction to refund the bonds within parameters or minimum levels of savings and authorizing representatives to execute the transaction within those parameters, and naming a pricing officer who is authorized to approve the transactions. The City has utilized this method successfully with past refunding transactions.

The following table shows the top 3 bidders on competitive bond sales the city has conducted in the last two years:

Date	Amount	Type of Bond	Bidders	True Interest Cost (%)	Rank
Oct-16	7,345,000	General Obligation Bonds	Robert W. Baird & Co.	2.6492	1
Oct-16	7,345,000	General Obligation Bonds	Hutchinson, Shockey, Erley & Co.	2.704758	2
Oct-16	7,345,000	General Obligation Bonds	Citigroup Global Markets Inc.	2.707251	3
Mar-17	19,825,000	Waterworks & Sewer System Revenue Bonds	Citigroup Global Markets Inc.	3.1412	1
Mar-17	19,825,000	Waterworks & Sewer System Revenue Bonds	Robert W. Baird & Co.	3.204301	2
Mar-17	19,825,000	Waterworks & Sewer System Revenue Bonds	Coastal Securities, Inc.	3.21517	3
Apr-17	21,710,000	Certificates of Obligation	JP Morgan Securities LLC	2.7807	1
Apr-17	21,710,000	Certificates of Obligation	Fidelity Capital Markets	2.804169	2
Apr-17	21,710,000	Certificates of Obligation	Citigroup Global Markets Inc.	2.80539	3

Based on the size of this issue, I recommend that we work with Citigroup Global Markets and JP Morgan Securities as the underwriters on this deal. Due to the size of the refunding and its natural AAA rating, it will be appealing to institutional investors and should garner significant market interest on the retail side as well.

I recommend that we take a parameter ordinance to City Council on November 21, outlining the conditions under which the refunding transaction can take place. Due to requirements for due diligence (and compliance with HB 1295 disclosure requirements which were effective January 1, 2016) we recommend a negotiated transaction so that the City knows who it is doing business with and can get all disclosure and due diligence taken care of up front.

While the issue will be a GO refunding, the Surface Water Fund will continue to pay the debt service payments on the issue. The parameter authorization gives the City Manager authority to sign the pricing certificates that will execute the refunding and schedule delivery upon completion. This option allows the underwriter to market the bonds prior to the actual pricing date, and allows for a short process including pre-filing of documents with the Attorney General's office to allow for delivery of funds prior to year-end.

The November 21 Council Agenda will contain an ordinance to consider the following items, my recommendations are filled in, they are subject to change based on committee input:

Sale Parameters	GO Refunding
Minimum % NPV Savings of Refunded Bonds	8%
Maximum Principal Amount to be Refunded	\$81M
Recommended Underwriters	Citigroup Global Markets and JP Morgan Securities

Finance staff are already working with First Southwest (Hilltop Securities) and Andrews Kurth Kenyon to prepare the bond offering documents, schedule rating calls, allow for due diligence by the underwriters and get the refunding to the market on a very aggressive schedule, to ensure that the City does not lose this opportunity due to potential changes from the Tax Reform Act.