Town of Mansfield

Municipal Debt Primer

Special Town Council Meeting

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Why issue debt?

- Do not wish to use current resources to finance long-term assets
- Cost of improvements exceed available resources
- Local Policy
- Maintain inter-generational equity

Characteristics of Municipal Market

- $3.7 Trillion outstanding as of November 2011
- Active secondary market
- Types of investors:
  - Institutional - Money Market & Mutual funds; Insurance companies, Banks
  - Retail - Individuals; Bank Trust Dept
- Retail investors are major participant – either through funds or direct holdings
- Investor perception of safety (low default rate)

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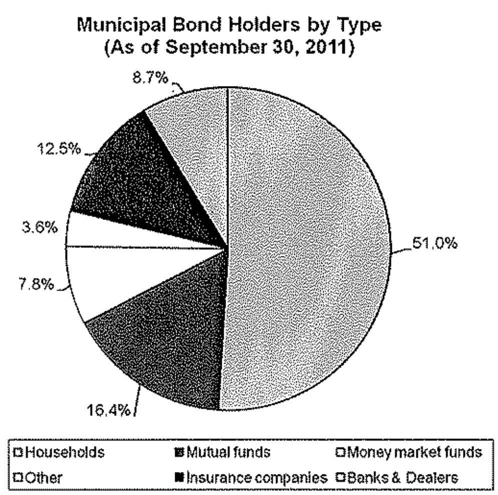
$3.7 Trillion Municipal Bond Market



Source: Federal Reserve Board, Flow of Funds Accounts

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Types of Financing Vehicles

- What security will be pledged to repay the debt?
- General Obligation Bonds:
  - ➢Unlimited pledge, full faith & credit of issuer
  - ➢Not secured by mortgage on a particular asset
  - ➢If issuer defaults on obligation, bondholders have the right to go to court to compel issuer to raise taxes sufficient to pay debt
  - ➢Typically, lowest borrowing cost

Types of Financing Vehicles

- Revenue Bonds:
  - ➢Limited pledge secured by specific revenues of a governmental enterprise. Generally, source of revenues is facility financed by bonds
  - ➢Bondholders have first lien on pledged revenues
  - ➢If issuer defaults, bondholders may foreclose on facility
  - ➢e.g. Water and sewer systems; utilities; toll roads
  - ➢Typically viewed as less secure, carries higher borrowing cost than GO

Types of Financing Vehicles

- Municipal Leases:
  - Contract, not a security
  - Subject to annual appropriation
  - Lessor retains security interest in asset
  - If issuer defaults, lessor would reposes asset
  - Typically used to finance equipment or small capital improvements when bond issues are not planned or issuance cost would be prohibitive
  - e.g. Copiers, computers, vehicles, school buses.

Long vs. Short-term Instruments

- Municipal debt can be issued as Long-term (Bonds) or Short-term (Notes) instruments
- Bonds – Either serial maturities or term bonds ranging from 1 to 30 years
- Notes – Mature in less than 2 years
  - Typically issued for 1 year, but could be shorter
  - May be renewed annually up to 10 years after initial issuance date

Structuring the Issue

- Sizing
- Term
- Maturity & payment structure
- Fixed vs. variable interest rate
- Redemption provisions

Structuring – Blended Term

PROJECT:	Project # 1	Project # 2	Project # 3	
TERM (yr):	20	15	10	
MATURITY				TOTAL
2012	-	-	-	-
2013	100,000	50,000	25,000	175,000
2014	100,000	50,000	25,000	175,000
2015	100,000	50,000	25,000	175,000
2016	100,000	50,000	25,000	175,000
2017	100,000	50,000	25,000	175,000
2018	100,000	50,000	25,000	175,000
2019	100,000	50,000	25,000	175,000
2020	100,000	50,000	25,000	175,000
2021	100,000	50,000	25,000	175,000
2022	100,000	50,000	25,000	175,000
2023	100,000	50,000	-	150,000
2024	100,000	50,000	-	150,000
2025	100,000	50,000	-	150,000
2026	100,000	50,000	-	150,000
2027	100,000	50,000	-	150,000
2028	100,000	-	-	100,000
2029	100,000	-	-	100,000
2030	100,000	-	-	100,000
2031	100,000	-	-	100,000
2032	100,000	-	-	100,000
TOTAL:	$ 2,000,000	$ 750,000	$ 250,000	$ 3,000,000

Who are the Players?

- Issuer
- Financial Advisor
- Bond Counsel
- Underwriter
- Investor
- Others
  - Registrar/Paying Agent/Trustee
  - Rating Agencies
  - Credit Enhancers

Borrowing Process

- Identify need (Capital Plan)
- Debt affordability analysis
- Determine sizing/term/structure
- Obtain legislative approval (authorization)
- Develop Prospectus (Official Statement)
- Obtain bond rating
- Obtain credit enhancement (if required)
- Sell obligations
- Closing (receive funds)

Method of Sale

- Competitive Sale
- Negotiated Sale
- Private Placement

Ratings

- Assessment of relative creditworthiness and likelihood of repayment
- Initial ratings are typically assigned just before bonds are sold
- Ratings are updated with each new parity bond sale
- Rating agencies require periodically updated information from issuer (surveillance) and can modify a rating if circumstances have changed

Ratings

- Ratings are one of many factors which affect the market price of a bond
  - Typically, higher the ratings, the lower the borrowing cost
- Major Players: Moody's, Standard & Poor's (S&P) and Fitch
- Rating categories range from AAA (Aaa) to C
- Agencies provide further gradation by assigning modifier of 1-3 or +/- (Aa1, AA+)

State Law Considerations

- Pursuant to state law municipalities can only bond for "local" or net share of project costs
  - e.g. School constructions projects – can not bond for state grant funded portion of project costs
  - Practical Matter – Only borrow what you need. Not necessarily full amount of authorization
- Authorization process is determined by CGS or by town charter for home rule charter towns

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