



Municipal Bond Financing “101” & Key West Charter Overview

Presented by: PFM Financial Advisors LLC & Bryant Miller Olive P.A.

September 3, 2019

PFM Financial Advisors LLC
www.pfm.com
(407) 648-2208

Bryant Miller Olive P.A.
www.bmolaw.com
(813) 222-1722



Presentation Participants

Nicklas Rocca: PFM Financial Advisors LLC

- Financial Advisor
- roccan@pfm.com

Duane Draper: Bryant Miller Olive P.A.

- Bond Counsel
- ddraper@bmolaw.com



Agenda

- I. Financing Structures**
- II. Financing Team**
- III. Credit Ratings**
- IV. City's Charter and Other Legal Considerations**
- V. Debt Financing Timeline**

Exhibits

- A. City Debt Overview**
- B. Market Update**



I. Financing Structures



Why Borrow?

- Large capital projects often can't be broken into smaller phases and funded out of annual budget
- Taxpayer / Ratepayer equity – if multiple generations of tax or rate payers benefit from a capital project, then they should all pay for it
- Mitigate rising construction costs – project costs can increase materially over 4 or 5 years while City saves funds to construct a project
- Historically speaking, interest rates for municipalities are low



Source: Thomson Reuters of August 19, 2019



What Types Of Bonds Are There?

- ◆ **Municipal Bonds**, also called “munis,” are debt securities issued by states, cities, counties and other government entities
- ◆ **Two general categories of municipal bonds**
 - **General Obligation Bonds:** backed by the full faith and credit of the issuer, which has the power to tax residents to pay bondholders (require voter referendum in Florida)
 - **Revenue Bonds:** secured by revenues from a specific project or revenue source – the revenue can be from a project (i.e. sewer system revenues) or other revenue (sales tax, tourist development tax, etc.)
- ◆ **Other financings:** lease financings, Certificates of Participation, conduit financings, etc.



Repayment of Debt

- What is the best/appropriate repayment source and security?
 - Legally available for capital purpose
 - Dedicated to repayment
 - Reliably generated
 - Note: the revenue that “secures” the financing does not have to be the same revenue used to pay the debt service
- Repayment of debt will normally take a priority position on use of revenues
- Planning should include integration of adequate revenues to cover operating and maintenance of capital project
- Current/Potential sources of security utilized by the City:
 - Ad Valorem Tax (approved via voter referendum)
 - Covenant to budget and appropriate legally available non-ad valorem revenues (CBA)
 - Sales Tax
 - Sewer Revenues



Interest Rates

◆ Fixed Rate Debt – this is by far the most common structure

- Interest rate is fixed through the final term of the loan at time of pricing
- Most new money municipal fixed rate debt is structured with semi-annual interest payments and annual principal payments over 20 or 30 years

◆ Variable Rate Debt

- Used for both long-term and short-term financings, but most commonly for short-term financings (lines of credit during a construction period, etc.)
- Interest rate resets weekly, bi-weekly, monthly or yearly based on an index or open market pricing



Tax Status of Municipal Bonds

◆ Tax-Exempt Bonds

- Interest earnings on most municipal bonds (depending on purpose of financing) is exempt from federal income tax, making them an appealing investment vehicle for institutions and high net worth individuals
- Issuance must be authorized by a governing body and proceeds must be used for state and local government purposes
- Subject to arbitrage rebate and advance refunding restrictions, per the Federal Tax Code

◆ Taxable Bonds

- Generally issued to finance a project or activity that contains a private use or function - in most cases, the federal government will not permit tax-exemption
- Sometimes used for traditional governmental projects when associated with Federally subsidized programs



Factors to Consider/Questions to ask Regarding Financing

- ◆ Can the City afford to pay the debt from existing revenues or will it require a new revenue source?
 - Will the project generate revenue to make the debt service payment?
- ◆ Does the City have legal authority per State law and City charter to pledge a certain revenue(s) to secure debt?
- ◆ If the financing requires a new revenue source, does the City have the legal authority to impose a new fee/tax or increase an existing fee/tax? If not, is the Commission willing to put a measure on the ballot?
- ◆ How much of this potentially pledged revenue does the City collect annually? Is the revenue stable from year to year? Can this revenue source be taken away by the state at any time in the future?
- ◆ What is the estimated cost of the project? How quickly are the funds needed?
- ◆ What is the most efficient financing structure given these parameters?



II. Financing Team



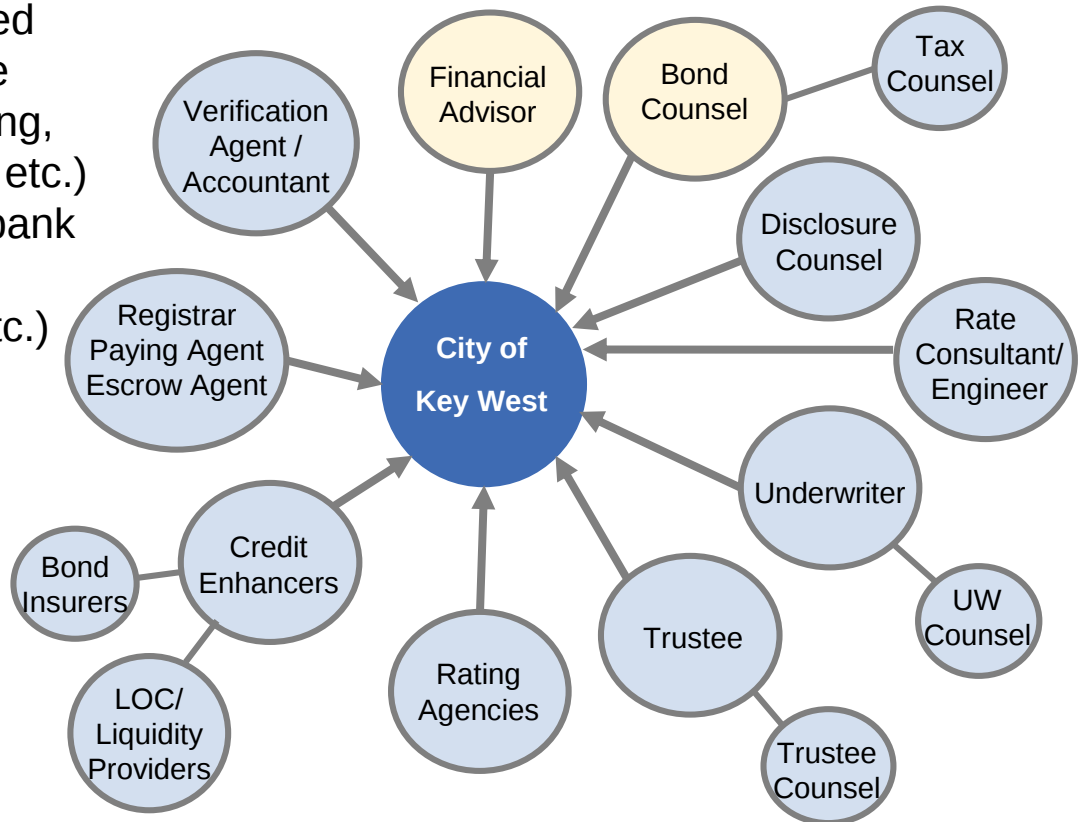
The External Financing Team

Core Team

- City staff, Bond Counsel and Financial Advisor

Transaction Dependent Team Members

- Additional members are added to the team depending on the purpose of financing (refunding, new project, enterprise fund, etc.) and the financing structure (bank loan/full public offering, fixed/variable interest rate, etc.)





Financial Advisor Duties

- ◆ Role may vary according to:
 - Expertise of issuer staff
 - Type of bonds
 - Method of sale
- ◆ Relationship may be on a transactional basis, or may be on a “retainer” basis
- ◆ Financial advisor has a fiduciary responsibility to represent the Issuer, and only the issuer, in debt financings
- ◆ Assists with capital planning, plan of finance development and transaction management tasks (including rating agency relations and bond pricing)
- ◆ Acts as extension of staff



Bond Counsel Duties

- ◆ Draft Principal Legal Documents:
 - Bond Ordinance/Trust Indenture
 - Escrow Deposit Agreement
 - Loan Agreements
 - Closing Documents
 - Opinions
- ◆ Analyze applicable federal, state and local legal issues
- ◆ Federal tax analysis
- ◆ Coordinate closing
- ◆ Issue approving opinion



III. Credit Ratings



Bond Ratings

■ What is a Bond Rating?

- Measure of risk to bondholders
- Reflects issuer's ability & willingness to repay debt on time and in full
- Factors in expected loss and recovery
- Denotes credit quality by rating level
- Independent opinion (subjective process)
- Forward looking projection

■ A Bond Rating is Not:

- Audit
- Recommendation to buy, sell or hold a security
- Static or permanent
- Opinion of community's quality of life, or judgement of quality of service delivery
- Performance evaluation of current political leadership



Bond Ratings

- ◆ A key factor in determining the interest rate is the City's bond rating
- ◆ Generally speaking, the higher the rating, the lower the interest rate

Highest Rating



Below Investment Grade

S&P	Fitch	Moody's
AAA	AAA	Aaa
AA+	AA+	Aa1
AA	AA	Aa2
AA-	AA-	Aa3
A+	A+	A1
A	A	A2
A-	A-	A3
BBB+	BBB+	Baa1
BBB	BBB	Baa2
BBB-	BBB-	Baa3
<i>BB</i>	<i>BB</i>	<i>Ba</i>
<i>B</i>	<i>B</i>	<i>B</i>
<i>C</i>	<i>C</i>	<i>C</i>



Rating Considerations

◆ Credit considerations include, but are not limited to:

- Management, governance and business strategy
- Economy
- Financial position
- Debt and Pensions
- Legal framework

Scorecard Factor and Weights		
Broad Rating Factor	Rating Subfactor	Subfactor Weighting
Economy/Tax Base	Tax Base Size (full value)	10%
Economy/Tax Base	Full Value Per Capita	10%
Economy/Tax Base	Wealth (median family income)	10%
Finances	Fund Balance (% of revenues)	10%
Finances	Fund Balance Trend (5-year change)	5%
Finances	Cash Balance (% of revenues)	10%
Finances	Cash Balance Trend (5-year change)	5%
Management	Institutional Framework	10%
Management	Operating History	10%
Debt/Pensions	Debt to Full Value	5%
Debt/Pensions	Debt to Revenue	5%
Debt/Pensions	Moody's ANPL (3-year average) to Full Value	5%
Debt/Pensions	Moody's ANPL (3-year average) to Revenue	5%



IV. City's Charter and Other Legal Considerations



Overview of the City's Existing Charter

Bonding Legal Process

- ◆ The Florida Constitution requires that bonds payable from ad valorem taxation (pledge of the full faith and credit of the Issuer) and maturing greater than 1-year require voter approval
- ◆ Section 8.03 of the City's Charter takes this one step further:
 - **Approval by electorate required for bond issuance** – Bonds pledging the full faith and credit of the city or the revenues of the city may be issued only upon approval by a vote of the electors of the city
- ◆ It is rare for a Charter to mandate voter approval for the issuance of non-ad valorem revenue bonds or enterprise fund debt
 - None of the City's peers, or the vast majority of Florida municipalities, have this limitation



Overview of the City's Existing Charter (Continued)

- ◆ Under the existing Charter there are no exceptions for emergency funding, non-ad valorem revenue bonds, enterprise fund debt, and/or subject to annual appropriation equipment leases
- ◆ Some would argue that this puts the City at a disadvantage compared to its peer group in delivering:
 - Needed infrastructure (streets, wastewater, storm water, green space, sanitation)
 - Ensuring public safety (police and fire)
 - Supporting economic development
 - Providing needed workforce and affordable housing
- ◆ The City Charter as currently written encourages “pay go” financing of certain capital projects, which could be considered generationally unfair to current residents
- ◆ Bond financing allows “Generational Equity” for capital projects (like a city hall) as it spreads the cost of the infrastructure over time
 - The cost of the capital project isn't only borne to the current residents, but future residents as well



Process for Borrowing under Existing Charter

- An incurrence of debt under the City's Charter could potentially take a year to complete (possibly longer), which is much longer lead time than most municipalities in Florida (usually 2-3 months)
- The City's current process for borrowing debt:
 - Complete capital planning and identify the project to be financed
 - City Commission calls a bond referendum by ordinance to finance such project to be secured by taxes or revenues
 - City educates electorate (3-6 months)
 - General election or special election?
 - City validates bonds (3-4 months, best case)
 - City executes/implements the financing



Charter Update Considerations

- Modifying the Charter to align with the State Constitution (and peers) by removing the voter approval requirement for bonds that do not pledge the full faith and credit of the City would provide more flexibility to issue debt in a timely fashion
- Some citizens may argue that micromanaging the City Commission through a charter limitation is essential
- Others may argue that a more appropriate remedy in a republican representative form of government is to hold elected officials accountable during the re-election process if citizens don't favor the debt
- Ultimately a policy decision for the City Commission to consider whether or not to ask voters to re-address the requirement



V. Debt Financing Timeline



Timing Considerations

- Under the City's current Charter, all bond financings must be voter approved by a referendum
- The next regularly scheduled election the City could target to approve a Bond Financing would be in November 2020
- Once the actual financing process starts, a typical bond financing takes around 3-months to complete. On the following slide is a high-level overview of the major components
 - Note that the financing timeline could be accelerated or delayed depending on numerous factors (validation proceedings (2-3months), type of project being financed, market environment, etc.)



Example of Typical Debt Financing Timeline

- Week 1 Kick-Off Meeting (Organize Team & Develop Finance Plan)
- Week 2 Draft Bond Ordinance Circulated
- Week 3 Draft Preliminary Official Statement (POS) Circulated
- Week 4 Draft Bond Financing Documents Circulated / Rating Calls
- Week 6 Receive Ratings / Finalize Bond Ordinance
- **Week 7 City Commission Approval of Bond Ordinance**
- Week 8 Finalize and Post POS for Investors to Review
- **Week 9 Pricing of Bonds**
- Week 10 Finalize Official Statement
- Week 11 Finalize Bond Financing Documents for Closing
- **Week 12 Closing of Bonds**
- ◆ As the City's Charter currently stands, an issuance for the City would need to include additional time for a referenda and validation proceeding (additional 6-9 months)



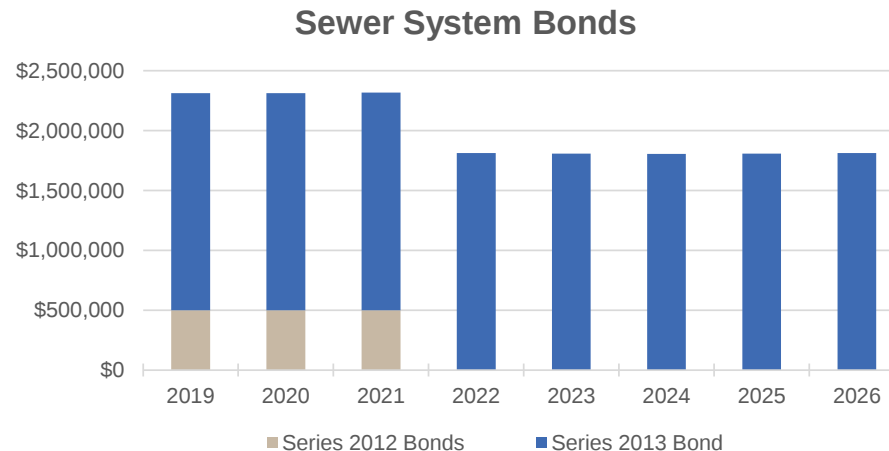
Exhibit A

City Debt Overview



Debt / Rating Overview

- ◆ The City of Key West does not currently maintain any published credit ratings due to there being no publically offered debt outstanding
- ◆ All of the City's debt is currently held privately (no securitized public debt) which does not require a credit rating
- ◆ The City may have as much as \$13.7 million of authorized but unissued sewer system revenue bonds (1999 referendum), and \$18.0 million of authorized but unissued stormwater system revenue bonds (2001 referendum), to be confirmed
 - City would need to consider if comfortable relying on votes of citizens from over 17-years ago
- ◆ There are two series of Sewer System Revenue Bonds outstanding as shown below and further detailed on the following pages

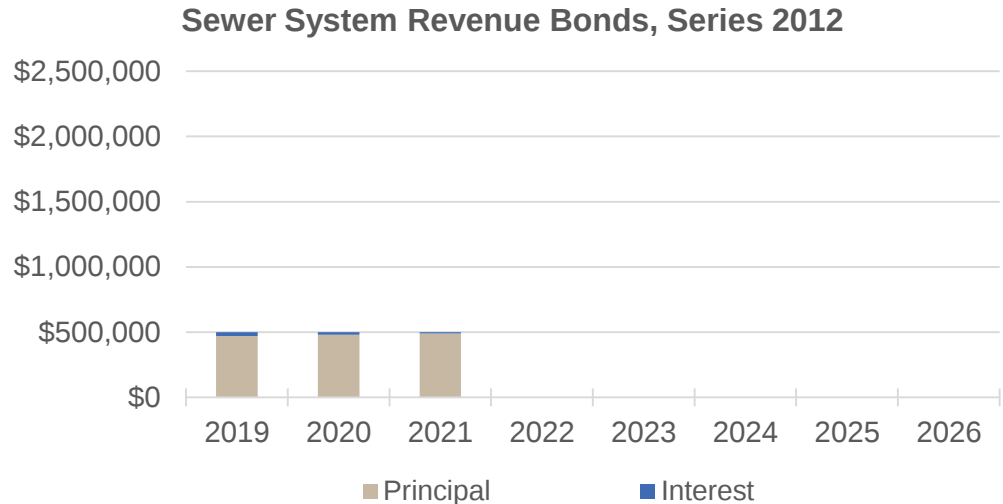




Sewer System Revenue Bonds, Series 2012

- ◆ The Sewer System Revenue Bonds, Series 2012 were issued via a Bank Loan on February 14, 2012
- ◆ Purpose: Repay a grant from the State of Florida Department of Emergency Management
- ◆ Security: Net Revenues of the City's sewer system

Series 2012 Bonds Debt Summary	
Total Outstanding Debt	
Original Principal Amount	\$4,065,000
Principal Outstanding	\$1,440,000
Final Maturity	10/1/2021
Maximum Annual Debt Service	\$500,143,000
Interest Rate(s)	2.07%
Refunding Breakdown	
Call Date	Anytime*
Refundable Debt	\$1,440,000
Non-callable Debt	-
*Currently Prepayable anytime without penalty	

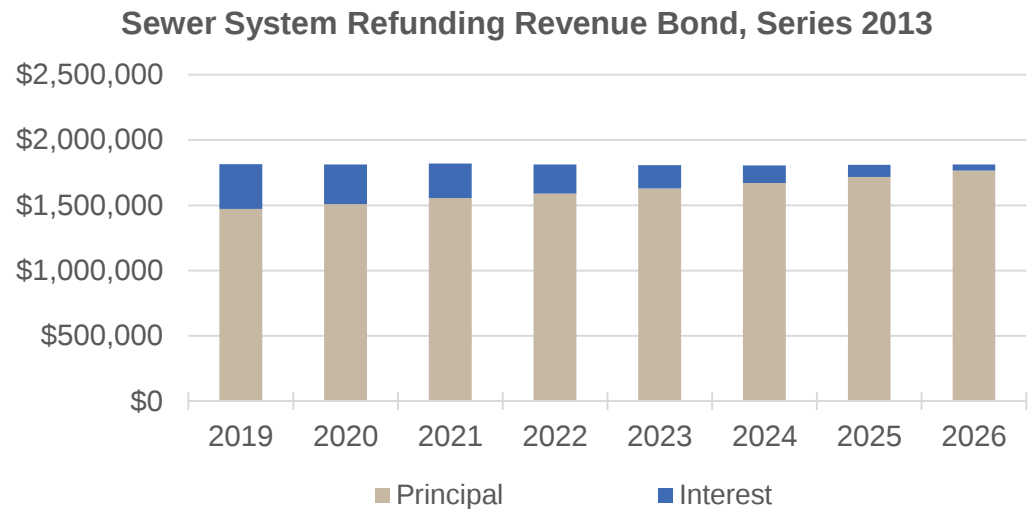




Sewer System Refunding Revenue Bond, Series 2013

- ◆ The Sewer System Refunding Revenue Bond, Series 2013 were issued via a Bank Loan on August 23, 2013
- ◆ Purpose: Refund the Sewer System Refunding Revenue Bonds, Series 2003
- ◆ Security: Net Revenues of the City's sewer system

Series 2013 Bond Debt Summary	
Total Outstanding Debt	
Original Principal Amount	\$19,963,753
Principal Outstanding	\$12,909,386
Final Maturity	10/1/2026
Maximum Annual Debt Service	\$1,819,142
Interest Rate(s)	2.65%
Refunding Breakdown	
Call Date	Anytime*
Refundable Debt	\$12,909,386
Non-callable Debt	-
*Currently Prepayable anytime without penalty	





Can the City Support Additional Debt?

- ◆ The City has a very low debt burden

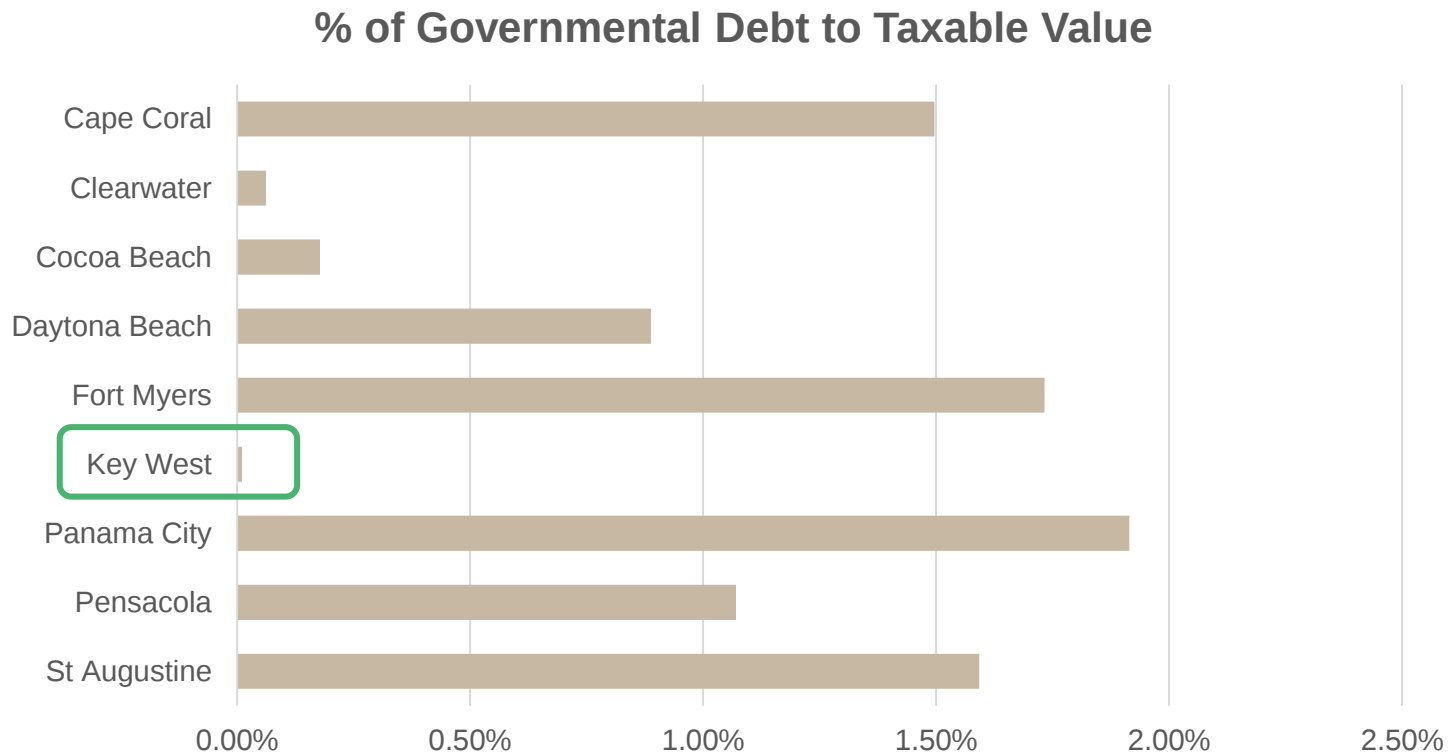




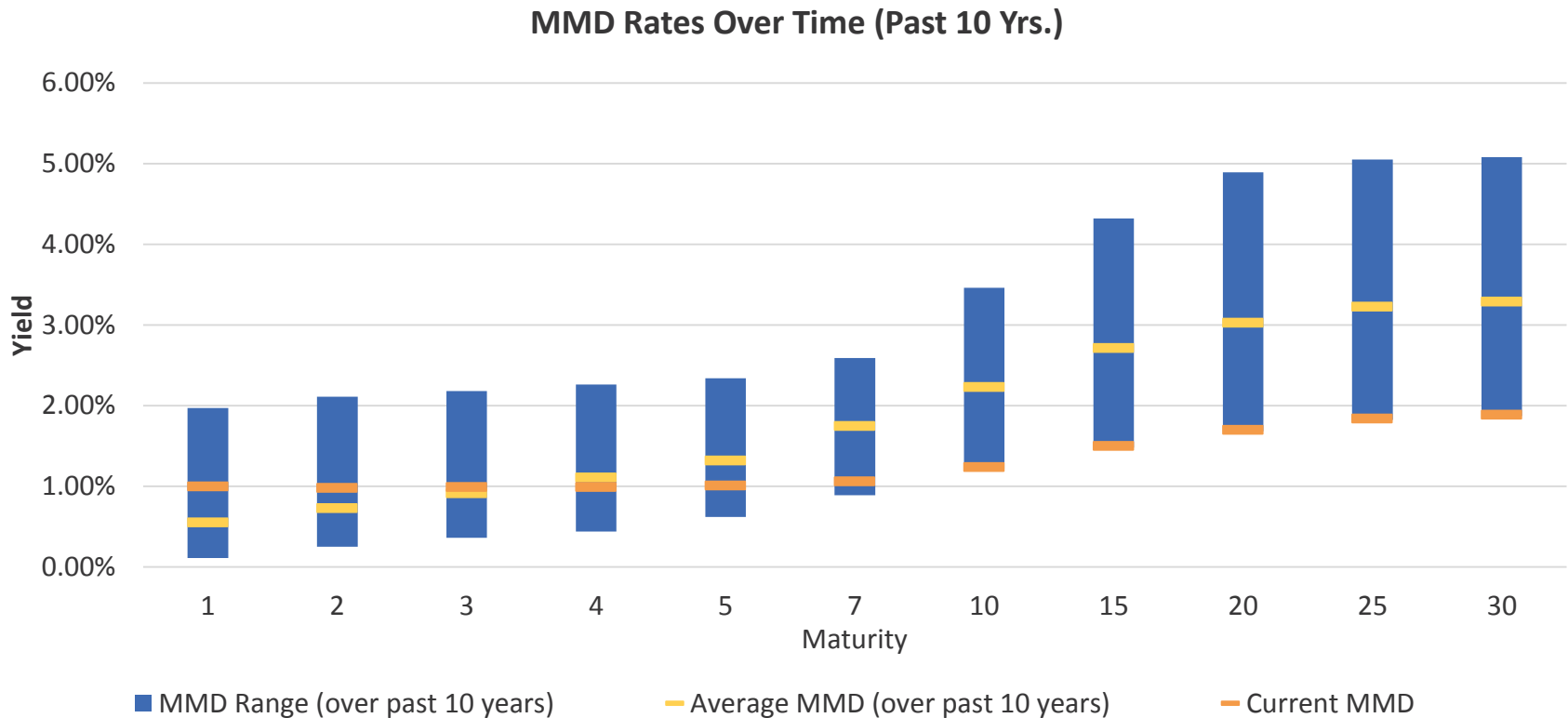
Exhibit B

Market Update



Long-Term Rate History

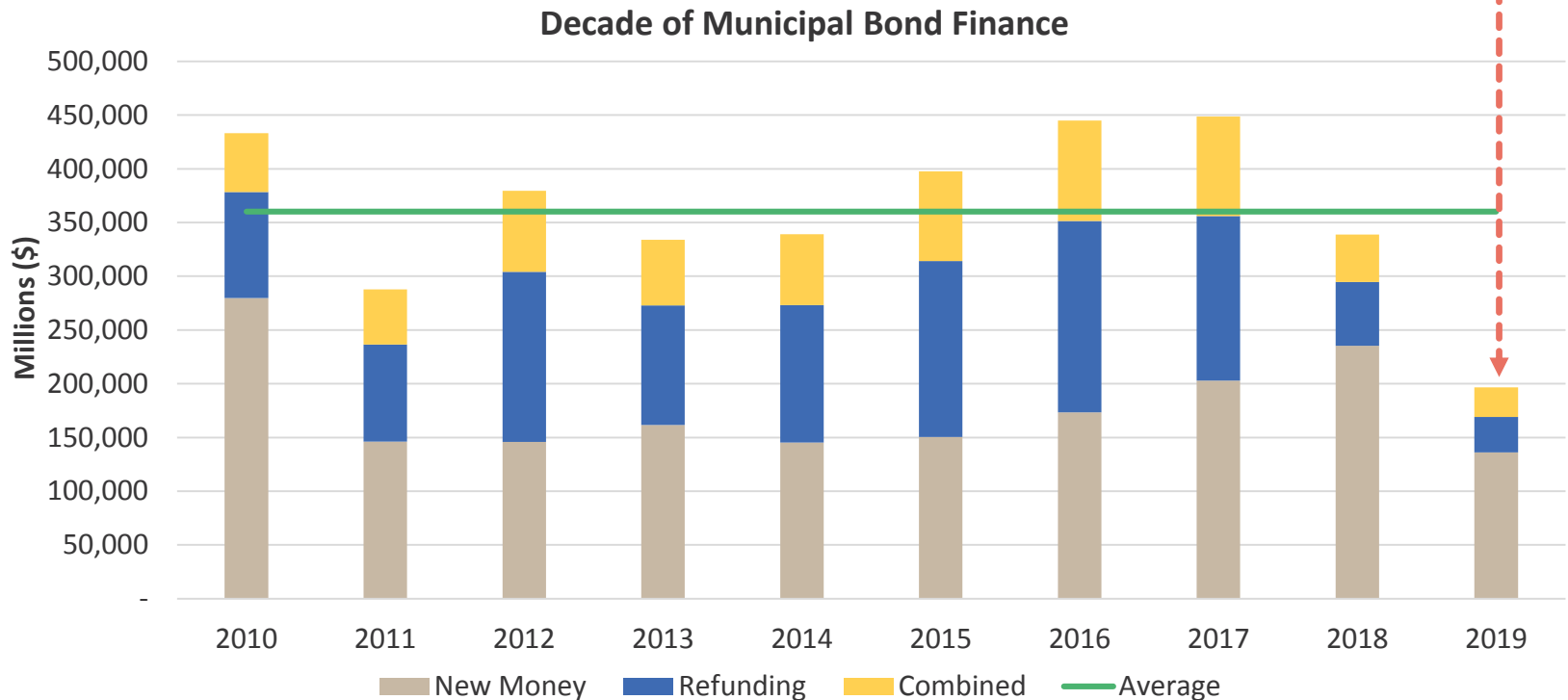
- Continued flattening of the yield curve as short-term rates have risen but long-term rates are currently at historic lows





Municipal Market Issuance

- Over the last decade municipal market issuance has been volatile year-to-year
- 2019 volume is on track to exceed the average since 2010 (volume through the 1st half of the year shown below)





Interest Rate Forecast

- Based on economists surveyed by Bloomberg, the chances of at least one rate cut by the Federal Reserve is:
- 62% probability by September 2019 meeting (38% probability of inaction)
 - 83% probability by October 2019 meeting
 - 90% probability by December 2019 meeting
 - 98% probability by January 2020 meeting
 - 90% probability by March 2020 meeting

Street Median Forecast							
Metric	Market Yield	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020
3-Month LIBOR	2.14%	2.12%	2.02%	1.94%	1.88%	1.88%	1.88%
2 Year T-Bond	1.52%	1.71%	1.74%	1.75%	1.77%	1.79%	1.82%
10 Year T-Bond	1.48%	1.91%	1.98%	2.06%	2.11%	2.14%	2.17%
30 Year T-Bond	1.95%	2.46%	2.49%	2.55%	2.59%	2.61%	2.63%



Disclosures

ABOUT PFM

PFM is the marketing name for a group of affiliated companies providing a range of services. All services are provided through separate agreements with each company. This material is for general information purposes only and is not intended to provide specific advice or a specific recommendation.

Financial advisory services are provided by PFM Financial Advisors LLC and Public Financial Management, Inc. Both are registered municipal advisors with the Securities and Exchange Commission (SEC) and the Municipal Securities Rulemaking Board (MSRB) under the Dodd-Frank Act of 2010. Investment advisory services are provided by PFM Asset Management LLC which is registered with the SEC under the Investment Advisers Act of 1940. Swap advisory services are provided by PFM Swap Advisors LLC which is registered as a municipal advisor with both the MSRB and SEC under the Dodd-Frank Act of 2010, and as a commodity trading advisor with the Commodity Futures Trading Commission. Additional applicable regulatory information is available upon request.

Consulting services are provided through PFM Group Consulting LLC. Institutional purchasing card services are provided through PFM Financial Services LLC. PFM's financial modelling platform for strategic forecasting is provided through PFM Solutions LLC.

For more information regarding PFM's services or entities, please visit www.pfm.com.