

# Iowa Association of Municipal Utilities

## Municipal Utilities 2030 Conference Financing Municipal Infrastructure

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## Financial Planning Considerations

- Develop a Revenue Requirement Analysis (financial plan)
  - Reviews various sources of revenue
  - Reviews detailed operating expenses
  - Incorporates capital improvement projects
  - Incorporates current and future debt service payments and calculates the anticipated debt coverage ratios
  - Analyzes the impact on operating, capital and other designated and restricted reserves

# Financial Planning Considerations

Cash Basis for Revenue Requirements

$$\begin{aligned} &+ \text{O\&M Expense} \\ &+ \text{Taxes or Transfer Payments} \\ &+ \text{Capital Projects Financed with Revenues} \\ &+ \underline{\text{Debt Service Payments (Principal \& Interest)}} \\ &= \text{Total Revenue Requirement} \end{aligned}$$

# Financial Plan

CITY OF ANYPLACE, IOWA								
WATER ENTERPRISE FUND -								
		Audited Financial Statements-Accrual			Cash Budget	Cash Projected	Cash Projected	Cash Projected
		FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
<b>OPERATING REVENUES</b>								
<b>Total Sales Revenue</b>	1	\$24,566,224	\$23,506,747	\$25,052,990	\$25,906,887	\$27,238,012	\$28,710,587	\$30,099,611
<b>Total Service &amp; Materials, Net</b>	2	\$683,408	\$542,292	\$639,213	\$569,000	\$569,000	\$569,000	\$569,000
<b>Total Operating Revenue</b>	3	\$25,249,632	\$24,049,039	\$25,692,203	\$26,475,887	\$27,807,012	\$29,279,587	\$30,668,611
<b>NONOPERATING REVENUE:</b>	4	\$2,587,058	\$1,993,280	\$870,720	\$371,088	\$156,935	\$155,133	\$137,592
<b>SUBTOTAL REVENUES</b>	5	\$27,836,690	\$26,042,319	\$26,562,923	\$26,846,975	\$27,963,947	\$29,434,720	\$30,806,203
<b>Impact Fee Revenues</b>	6	\$1,133,595	\$863,921	\$978,180	\$500,000	\$500,000	\$500,000	\$500,000
<b>Tap Fee Revenues</b>	7	416,210	376,944	297,084	250,000	250,000	250,000	250,000
<b>TOTAL IMPACT/TAP FEES</b>	8	\$1,549,805	\$1,240,865	\$1,275,264	\$750,000	\$750,000	\$750,000	\$750,000
<b>TOTAL REVENUES</b>	9	\$29,386,495	\$27,283,184	\$27,838,187	\$27,596,975	\$28,713,947	\$30,184,720	\$31,556,203
<b>Less Federal Grant Revenue</b>	10	\$0	(\$26,000)	\$0	\$0	\$0	\$0	\$0
<b>NET REVENUES</b>	11	\$29,386,495	\$27,257,184	\$27,838,187	\$27,596,975	\$28,713,947	\$30,184,720	\$31,556,203
<b>NET OPERATING EXPENSES</b>	12	(\$14,351,136)	(\$14,425,521)	(\$14,995,077)	(\$16,183,540)	(\$16,832,284)	(\$17,508,921)	(\$18,214,744)
<b>NET REVENUES FOR DEBT</b>	13	\$15,035,359	\$12,831,663	\$12,843,110	\$11,413,435	\$11,881,662	\$12,675,800	\$13,341,459

# Financial Plan

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		FY 2006-07	FY 2007-08	FY 2008-09	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13
<b>NET REVENUES FOR DEBT</b>	13	\$15,035,359	\$12,831,663	\$12,843,110	\$11,413,435	\$11,881,662	\$12,675,800	\$13,341,459
Total Water Parity Debt	14	\$8,952,001	\$8,931,201	\$8,923,414	\$9,508,096	\$9,501,858	\$9,605,055	\$8,086,992
Subordinated Water Debt	15	0	0	0	0	0	0	0
<b>TOTAL WATER DEBT</b>	16	\$8,952,001	\$8,931,201	\$8,923,414	\$9,508,096	\$9,501,858	\$9,605,055	\$8,086,992
<b>Debt Service Coverage: <sup>1)</sup></b>								
Net Revenues/ Revenue Debt	17	1.68	1.44	1.44	1.20	1.25	1.32	1.65
Net Revenues / All Debt	18	1.68	1.44	1.44	1.20	1.25	1.32	1.65
<b>CASHFLOW AFTER DEBT</b>	19	\$6,083,358	\$3,900,462	\$3,919,696	\$1,905,339	\$2,379,805	\$3,070,745	\$5,254,468
Capital Improvements	20	(\$11,116,135)	(\$25,438,740)	(\$17,815,271)	(\$9,128,930)	\$0	(\$11,210,000)	(\$11,470,000)
Capital Replacement	21	0	0	0	(400,000)	(2,560,000)	(12,215,000)	(5,315,000)
Bond Proceeds	22	0	0	15,248,642	0	0	17,240,000	9,590,000
Misc Cash Adjustments <sup>2)</sup>	23	\$8,840,194	\$10,497,188	(6,463,158)	9,179,764	1,125,456	3,207,769	1,880,000
<b>ANNUAL SURPLUS/DEFICIT</b>	24	\$3,807,417	(\$11,041,090)	(\$5,110,091)	\$1,556,172	\$945,261	\$93,514	(\$60,532)
<b>BEG. CASH BALANCE</b>	25	\$15,688,023	\$19,495,440	\$8,454,350	\$3,344,258	\$4,900,431	\$5,845,692	\$5,939,206
<b>ENDING CASH BALANCE</b>	26	\$19,495,440	\$8,454,350	\$3,344,258	\$4,900,431	\$5,845,692	\$5,939,206	\$5,878,674
Days Cash on Hand	27	496 days	214 days	81 days	111 days	127 days	124 days	118 days
Cash % of O & M (net of depr)	28	136%	59%	22%	30%	35%	34%	32%
<b>SELECT CREDIT RATIOS</b>								
↓ Operating Ratio (%)	29	48.84%	52.92%	53.87%	58.64%	58.62%	58.01%	57.72%
↑ Net Take-Down (%)	30	51.16%	47.08%	46.13%	41.36%	41.38%	41.99%	42.28%
Debt Service Safety Margin (%)	31	20.70%	14.31%	14.08%	6.90%	8.29%	10.17%	16.65%
↓ Debt Ratio (%)	32	28%	23%	26%	24%	22%	26%	29%
↓ Debt per No. of Meters	33	\$938	\$859	\$977	\$897	\$808	\$965	\$1,038
↓ Debt per Capita	34	\$299	\$268	\$305	\$279	\$252	\$303	\$327

## Financial Policies

- Develop Informal/Formal Policies
  - Operating ratio % (operating expenses/revenues)
  - Liquidity position (% of O&M or days cash on hand)
  - Debt Service Coverage Ratio
  - Debt Ratio (debt outstanding/net plant)
  - Capital projects funded with operating revenues versus debt proceeds

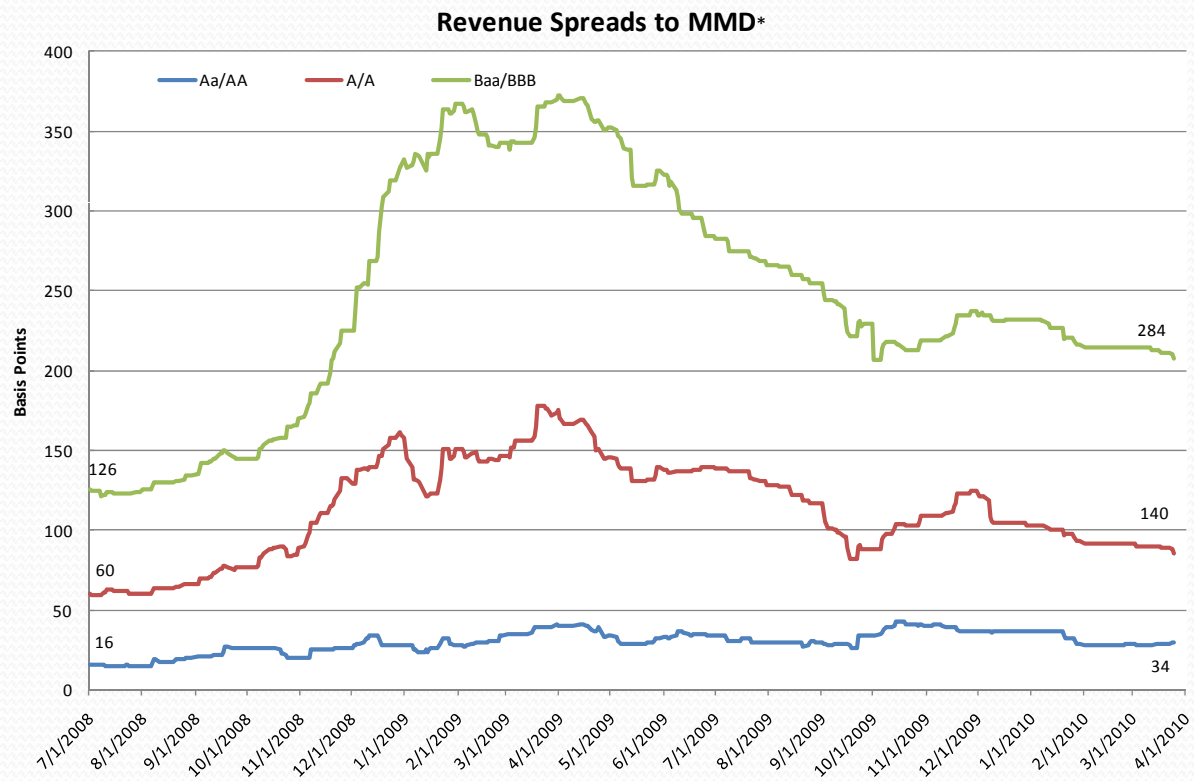
## Recalibration of Credit Ratings

- In March 2010, Moody's Investor Service and Fitch Ratings announced the recalibration of their U.S. municipal bond issues and issuers to its global rating scale.
- This was done to enhance the rating comparability between municipal and non-municipal sectors.
- Historically, municipal ratings were calibrated on a separate rating scale that emphasized the ordinal ranking of credit risk with the municipal sector only and measured the distance to distress.
- The global rating will provide ordinal rankings of credit, both within and across sectors, industrial, assets classes and geographies as well as a measure of the distance to distress.
- The global rating seeks to measure expected loss, which is the product of default probability and the loss that would occur following the default.
- The recalibrations are not upgrades but a shift to a different scale.

# Recalibration of Credit Ratings

Moody's (GRS) Shifts		Fitch's (GRS) Shifts	
<u>Current Ratings</u>	<u>Global Ratings</u>	<u>Current Ratings</u>	<u>Global Ratings</u>
Aaa	Aaa	AAA	AAA
Aa1	Aa1-Aaa	AA+	AAA
Aa2	Aa1	AA	AA+
Aa3	Aa2	AA-	AA
A1	Aa2	A+	AA-
A2	Aa3	A	AA-
A3	A1	A-	A+
Baa1	A1	BBB+	A
Baa2	A2	BBB	A-
Baa3	Baa1-A3	BBB-	BBB+

# Borrowing Credit Spreads



Source: TM3 Rates current as of 3/26/2010 \*10 Year Maturity

# Revenue Bond Interest Rates as of March 26, 2010

Years to Maturity	GM Revenue Aaa/AAA	GM Revenue Aa/AA	GM Revenue A/A	GM Revenue Baa/BBB
1	0.35	0.42	0.77	2.07
2	0.79	0.91	1.31	2.71
3	1.13	1.28	1.74	3.08
4	1.5	1.66	2.12	3.47
5	1.85	2.02	2.5	3.82
6	2.31	2.48	2.97	4.28
7	2.62	2.79	3.3	4.61
8	2.84	3.01	3.55	4.85
9	3.04	3.22	3.76	5.03
10	3.18	3.36	3.92	5.14
11	3.27	3.46	4.06	5.24
12	3.36	3.56	4.16	5.3
13	3.46	3.66	4.26	5.36
14	3.54	3.74	4.34	5.41
15	3.63	3.83	4.43	5.47
16	3.71	3.91	4.51	5.51
17	3.79	3.98	4.57	5.54
18	3.86	4.04	4.62	5.57
19	3.93	4.11	4.67	5.59
20	4	4.18	4.72	5.62

## Utility Revenue Debt

- Publicly Sold Revenue Debt
  - Requires debt reserve fund, minimum 1.25x debt coverage for documents and 1.35x – 1.50x debt coverage demanded by investors
- Iowa Finance Authority (SRF) Loans @ 3.00%
  - No debt reserve fund, minimum 1.10x debt coverage
  - Subject to Davis Bacon wage requirements
  - For cities >10,000, SRF loans can be designated as a Build America Bond through December 31, 2010 and apply for a 35% interest rate subsidy
  - Should expect an IRS compliance questionnaire and possible examination of issuer's records to ensure compliance with the rules
  - Additional bonds test considerations

## BAB Developments

- Reoffering Limit – De Minimis
- Costs of Issuance – Less than 2%
- Spending for Capital Expenditures
- Questionnaire
- SRF: Over 10,000 population – up to \$20,000,000
- Exempt from Davis-Bacon Requirements unless issued to SRF

## De Minimis

### Re-offering Premium limitations:

Not more than a *de minimis* amount of premium may be charged by underwriters in secondary market sales.

De minimis amount of premium is an amount that is not greater than  $\frac{1}{4}$  of 1 percent of the stated redemption price at maturity for the bond, multiplied by the number of complete years to the earlier of the maturity date for the bond or the first optional redemption date for the bond, if applicable.

# Verification Certificate

## EXHIBIT "A"

### VERIFICATION CERTIFICATE OF THE PURCHASER

The undersigned, \_\_\_\_\_ an officer of \_\_\_\_\_, (the "Purchaser"), hereby certifies as follows:

1. The Purchaser and the County of \_\_\_\_\_ (the "Issuer"), have entered into an Agreement dated September 29, 2009 (the "Bond Purchase Agreement"), providing for the purchase of \$5,000,000 General Obligation Taxable Bonds, Series 2009 (Build America Bonds - Direct Pay), of the County dated October 27, 2009 (the "Bonds").

2. The Agreement is in full force and effect and has not been repealed, rescinded or amended.

3. None of the interest rates on the Bonds, the Purchaser's spread, or the production or profits in connection with the purchase and sale of the Bonds is unreasonably high and the initial public offering price as set forth below does not exceed the fair market value of the Bonds on the date of the Bond Purchase Agreement.

4. The Purchaser hereby confirms, as set forth below: (a) the initial public offering price of each maturity of the Bonds (not including bondhouses and brokers or similar persons or organizations acting in the capacity of underwriters or wholesalers) at which price a substantial amount of the Bonds (not less than 10% of each maturity) were sold to the public; or (b) for those maturities where less than 10% of such maturity has been sold at the initial public offering price, the price for that maturity is determined as of the date of the Bond Purchase Agreement based upon the reasonably expected initial offering price to the public:

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# Verification Certificate Cont.

Year	Principal Amount Issued	Principal Amount Sold	Reoffering Yield	Reoffering Price (% of par) (do not include accrued interest)	Maximum Permitted Reoffering Price	Aggregate Dollar Reoffering Price (do not include accrued interest)
2011	\$ 440,000					
2012	\$ 445,000					
2013	\$ 455,000					
2014	\$ 465,000					
2015	\$ 480,000					
2016	\$ 500,000					
2017	\$ 515,000					
2018	\$ 540,000					
2019	\$ 565,000					
2020	\$ 595,000					
Total	\$5,000,000					

In addition, accrued interest in the total amount of \$ -0- will be paid by the investors purchasing the Bonds. The aggregate initial offering price to the public not including accrued interest is \$5,000,000.

IN WITNESS WHEREOF, the Purchaser has caused this Verification Certificate to be executed by its duly authorized officer this \_\_\_\_ day of \_\_\_\_\_, 2009.

PURCHASER

By: \_\_\_\_\_  
 Title: \_\_\_\_\_

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## Costs of Issuance Limitation

Cost of issuance limitation. Not more than 2% of the bond proceeds can be used to pay costs of issuance. If costs exceed this limit, funds from sources other than proceeds must be used.

"Cost of Issuance" shall mean costs to the extent incurred in connection with, and allocable to, the issuance of an issue within the meaning of Section 147(g). For example, issuance costs include, but are not limited to, the following costs to the extent incurred in connection with, and allocable to, the borrowing: loan initiation fees; underwriters' spread; counsel fees; financial advisory fees; rating agency fees; trustee fees; paying agent fees; Note registrar, certification and authentication fees; accounting fees; printing costs for Notes and offering documents; public approval process costs; engineering and feasibility study costs; guarantee fees, other than for qualified guarantees (as defined in §1.148-4(f)); and similar costs.

## Capital Expenditures

Capital Expenditures - Proceeds must be used to pay for capital expenditures (chargeable to a capital account under IRS guidelines). The issuer must document the expenditures to prove compliance.

"Capital Expenditure" shall mean any cost of a type that is properly chargeable to capital account (or would be so chargeable with a proper election or with the application of the definition of placed in service under §1.150-2(c)) under general Federal income tax principles. For example, costs incurred to acquire, construct, or improve land, buildings, and equipment generally are capital expenditures. Whether an expenditure is a Capital Expenditure is determined at the time the expenditure is paid with respect to the property. Future changes in law do not affect whether an expenditure is a Capital Expenditure.

# IRS BAB Questionnaire

Form <b>14127</b> (January 2010)	Department of the Treasury — Internal Revenue Service <b>Direct Pay Bonds Compliance Check Questionnaire</b>	OMB No. 1545-2071
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We are asking for information regarding your Direct Pay Bonds, post-issuance bond compliance and record retention practices. Please complete the questionnaire and follow the instructions in the accompanying letter for returning it to us. Please note that section references in this questionnaire are to sections of the Internal Revenue Code unless otherwise indicated. For all accompanying documentation, please clearly label the question to which it relates.

Name of Governmental Entity: \_\_\_\_\_

Employer Identification Number: \_\_\_\_\_

1. Do you have written procedures to ensure that none of the maturities of your Direct Pay Bonds are issued with more than a de minimis amount of premium as required by section 54AA(d)(2)(C)?  Yes  No

If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)

If Yes, describe in detail your procedures for ensuring compliance with such de minimis rule and how you implement such procedures, including dates of revisions, if any. In lieu of the above description, you may attach a copy of your written procedures. If you have no written procedures, explain what guidelines you have in place and from what source these guidelines are derived that ensure Direct Pay Bonds issued with premium fall within the de minimis rule. (Attach sheet with description)

2. Are records of secondary market trading activity for your Direct Pay Bonds available through the Municipal Securities Rulemaking Board's Electronic Municipal Market Access System (see <http://www.emma.msrb.org>)?  Yes  No  Do not know

If Yes, did you or a consultant to the issuer, other than the underwriter or initial purchaser of the Direct Pay Bonds, review the records of the secondary market trading activity for the Direct Pay Bonds after the sale date of the bonds but before the bonds were delivered on the date of issue?  Yes  No  Do not know

If Yes, that is, if such records were reviewed as described above, did any of your Direct Pay Bonds trade at a price greater than the issue price prior to the delivery of those Direct Pay Bonds on the date of issue?  Yes  No  Do not know



# IRS BAB Questionnaire Cont.

3. Do you have written procedures to ensure that your Direct Pay Bonds remain in compliance with the following Federal tax requirements after the bonds are issued:

- a. Timely expenditure of bond proceeds?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- b. Correct calculation of Available Project Proceeds (See section 54A(e)(4))?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- c. Use of 100% of Available Project Proceeds less amount in a reasonably required reserve fund only for capital expenditures (See section 54A(d)(2)(A))?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- d. Arbitrage yield restriction and rebate?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- e. Costs of issuance financed by the issue do not exceed 2% of the proceeds of sale (See section 54A(e)(4)(A)(ii))?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- f. Proper determination of the amount of interest payable on each interest payment date?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- g. Proper amount of refundable credit reported on Form 8038-CP?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- h. Timely filing of Form 8038-CP?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)
- i. Payment of refundable credit will be made to the proper person?  Yes  No  
If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)

If Yes, describe in detail your procedures for each of the above items (a-i) and how you implement such procedures, including dates of revisions, if any. In lieu of the above descriptions, you may attach a copy of your written procedures. If you have no written procedures, explain what guidelines you have in place and from what source these guidelines are derived that ensure bond financings are in compliance with Federal tax requirements. (Attach sheet with description)

# IRS BAB Questionnaire Cont.

4. Do you have written procedures to ensure timely identification of violations of Federal tax requirements after your Direct Pay Bonds are issued and the timely correction of any identified violation(s) through remedial actions described in the Treasury Regulations or through the Tax Exempt Bonds Voluntary Closing Agreement Program described under Notice 2008-31?  Yes  No

If Yes, date they were implemented? \_\_\_\_\_ (dd/mm/yyyy)

If Yes, describe in detail your procedures for timely identification and correction of any such violations and how you implement such procedures, including dates of revisions, if any. In lieu of the above description, you may attach a copy of your written procedures. If you have no written procedures, explain what guidelines you have in place and from what source these guidelines are derived that ensure timely identification and correction of any violations of Federal tax requirements. (Attach sheet with description)

5. Do you maintain records necessary to support the status of the bonds as qualified to receive the tax advantaged treatment described in section 54AA(g)?  Yes  No

If yes, for how long?

- Less than life of bonds
- Life of bonds
- Life of bonds plus 3 years

6. How do you maintain your bond records?

- On Paper
- Electronic media (e.g., CD, disks, tapes)
- Combination of paper and electronic

# IRS BAB Questionnaire Cont.

Under penalties of perjury, I declare that I have examined this completed questionnaire, including accompanying documents and statements, and to the best of my knowledge and belief, the completed questionnaire contains all the relevant facts relating to the answers to the questionnaire, and such facts are true, correct, and complete.

Signature: \_\_\_\_\_ Date: \_\_\_\_\_

Printed Name: \_\_\_\_\_

Title: \_\_\_\_\_

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The IRS may not conduct or sponsor, and an organization is not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB number. Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103 and 6104.

Catalog Number 54588D

[www.irs.gov](http://www.irs.gov)

Form 14127 (Rev. 01-2010)

# Recovery Zone Economic Development Bonds

The term “recovery zone” means:

- Any area designated by the issuer as having
  - 1) Significant poverty,
  - 2) Unemployment,
  - 3) Rate of home foreclosures or general distress;...
- Any area for which a designation as an empowerment zone or renewal community is in effect as of the effective date of February 17, 2009.

Designations of Recovery Zones: any state, county or large municipality may make these designations of recovery zones in any reasonable manner as it shall determine in good faith in its discretion

# Recovery Zone Economic Development Bonds

Used to finance certain “qualified economic development purposes”

## Definition of Qualified Economic Development Purpose:

means any expenditures for purposes of promoting development or other economic activity in a recovery zone, including:

- Capital expenditures paid or incurred with respect to property located in the recovery zone,
- Expenditures for public infrastructure and construction of public facilities, and
- Expenditures for job training and educational programs.



## Recovery Zone Economic Development Bonds

ARRA imposes the Davis-Bacon labor standards to projects financed with Recovery Zone Economic Development Bonds.

## BAB-ification of CREBS

- HR 2847 – signed on March 18, 2010
- Applies to Clean Renewal Energy Bonds (“CREBs”) and Qualified Energy Conservation Bonds (“QESBs”)
- Direct payments to the issuer
- Approximately 70% of interest cost
- Davis-Bacon applicable?

## Tax Issues

- Used Equipment (See IRC Section 141(d))
  - Acquisition of nongovernmental output property by a governmental entity
  - Private activity bond – includes any bond issued the proceeds of which are to be used directly or indirectly to acquire used property
  - Limited exceptions to this rule
- Purchase Power Agreements
- Management Contracts
- Public-Private Facilities

# Contracting Issues

## Thresholds:

- Full Bidding/Competitive Bid: \$100,000 regardless of type of issuer
- Proposals/obtaining a competitive “quote”:
  - Cities or other governmental entities with population less than 50,000: \$45,000
  - Cities or other governmental entities with population of more than 50,000: \$65,000
  - Counties: \$85,000
- No bidding
- Plans/Specs – prepared by Engineer or Architect licensed in Iowa
- Utility equipment – if packaged with installation probably a public improvement
- Cannot divide contract to avoid bidding laws

Thresholds discussed above apply to vertical infrastructure.