Item # 32

ADDITIONAL MATERIAL

10:00 a.m. Regular Meeting
DECEMBER 12, 2017

SUBMITTED AT THE REQUEST OF

FINANCE and ADMINISTRATIVE SERVICES DEPARTMENT

FINANCE AND ADMINISTRATIVE SERVICES DEPARTMENT
115 S. Andrews Avenue, Room 513 • Fort Lauderdale, Florida 33301 • 954-357-7130 • FAX 954-357-7134 • Email: finance@broward.org

MEMORANDUM

Date: December 8, 2017

To: Mayor and Board of County Commissioners

Thru: George Tablack, CPA, Chief Financial Officer

Digitally signed by GEORGE TABLACK
Date: 2017.12.11 10:09:57 -05'00'

From: Stephen Farmer, Finance Manager
Finance and Administrative Services Department

Digitally signed by STEPHEN FARMER
Date: 2017.12.08 15:05:07 -05'00'

Subject: December 12, 2017 – Commission Meeting – Agenda Item No. 32, Half-Cent Sales Tax Revenue Refunding Bonds, Series 2017 A, B and C

Attached, please find a recommendation memorandum from the County's financial advisor, Public Financial Management, Inc., regarding the subject agenda item.

GT/ao
attachment

c: Bertha Henry, County Administrator
Robert Melton, County Auditor
Andrew Meyers, County Attorney

Broward County Board of County Commissioners
Mark D. Bogen • Beam Furr • Steve Geller • Dale V.C. Holness • Chip LaMarca • Nan H. Rich • Tim Ryan • Barbara Sharief • Michael Udine
www.broward.org

December 7, 2017

Memorandum

To: George Tablack, Chief Financial Officer
Stephen Farmer, Finance Manager

From: Public Financial Management, Inc.

RE: Half-Cent Sales Tax Revenue Refunding Bonds, Series 2017A, 2017B and 2017C – Plan of Finance Memo

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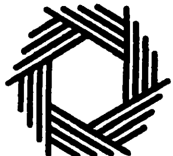
Executive Summary

In 2010, the County issued $214.69 million of Half-Cent Sales Tax Revenue Bonds, Series 2010 (the "2010 Bonds") to fund construction of the new Courthouse. Interest rates have declined since 2010 and staff, along with PFM, have determined that there is an opportunity to reduce debt service by refunding all, or portion of, the 2010 Bonds. Unfortunately, the proposed Tax Bill as currently drafted eliminates advance refunding tax-exempt bonds effective 12/31/2017. Advance refundings are defined as a refunding that occurs more than 90 days prior to the call date. This means the County needs to refund the 2010 Bonds immediately and close prior to 12/31/2017, or wait until the 2010 Bonds can be called on 10/1/2020.

The proposed Tax Bill is expected to have another negative impact on the 2010 Bonds which were issued through a unique structure that was part of the American Recovery and Reinvestment Act of 2009 (ARRA). The program promised materially lower debt service for issuers of debt if projects were financed in 2009 and 2010. (See discussion in Background section for details regarding the program). However, the Federal government has already reduced the interest subsidy as part of the Federal Sequestration program and it is expected that the Tax Bill will reduce the subsidy even further, or eliminate the subsidy completely. Elimination of the subsidy would cost the County approximately $3 million per year.

The remainder of this memorandum highlights the opportunity to refinance the 2010 Bonds for savings. Key questions and recommendations include:

- *Should the County move forward with a refunding of all or a portion of the 2010 Bonds given the constrained timetable (i.e. must close by 12/31/2017)*
    - There are three separate Series of the 2010 Bonds (2010A, 2010B and 2010C Bonds) and each offer very different savings based on current market conditions.
        - The 2010A Bonds offer significant savings since they were issued as traditional fixed rate debt.
        - The 2010B and 2010C Bonds were issued as part of the ARRA program which impacts their savings potential.
    - The County has already distributed an RFP for the refinancing. While the compressed timetable and long-term nature of the financing will likely result in debt structures that are different than traditional fixed bonds (bank loans,



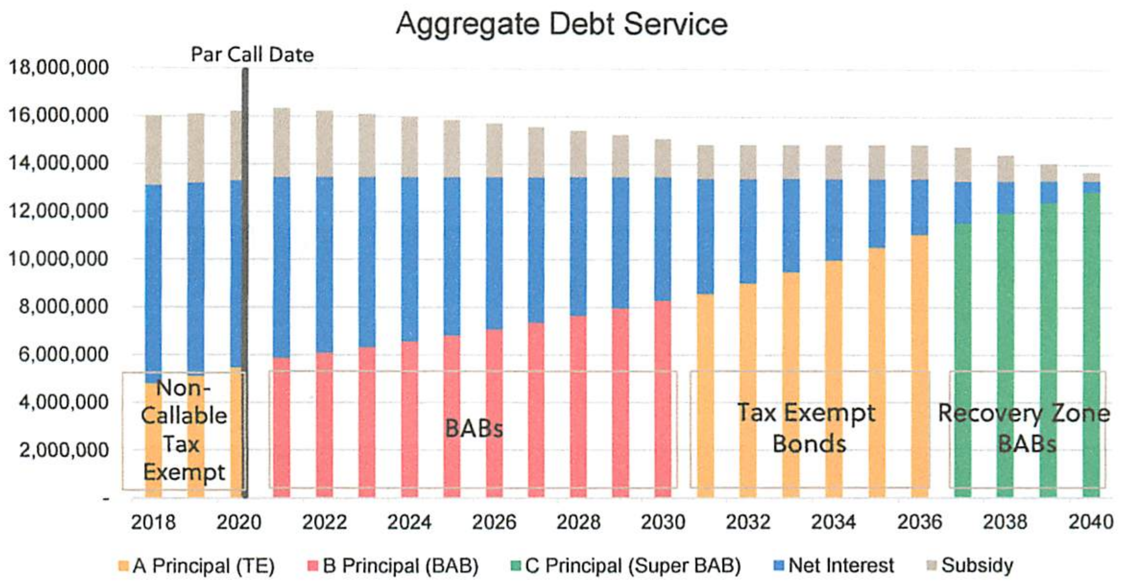
forward purchase bonds, etc.), it is reasonable to expect that proposals will offer material savings.

- Impact of the potential loss of subsidy – The most difficult decision in front of the County is the uncertainty regarding the loss of the interest rate subsidy which impacts the 2010B and 2010C Bonds. *This raises the question of whether the County should refund all the Bonds now, even if there is a loss.* This is a far more complicated question since (1) the subsidy has not been eliminated yet and (2) since the Bonds are not callable *at par* until 2020, the County would have to cover the cost of the reduced/eliminated subsidy between now and 2020.
    - The refunding of the 2010B and 2010C Bonds will NOT address the loss of the subsidy because the original debt will not be called (paid off) until the call date in 2020. So, between now and then, the County is exposed to reduction/loss of subsidy. But, completing the refunding now does put an end date to the loss of the subsidy at no later than 2020 while locking in today's low interest rates. The point is that the refunding would reduce debt service AND eliminate the exposure to the Federal government reducing the subsidy in the long-run, but does not eliminate that risk between now and 2020.
- Under the assumption that reasonable proposals are received, PFM recommends that the County:
    - Move forward with refunding the 2010A Bonds
    - Move forward with refunding the 2010B and 2010C Bonds if there is material savings. If there is dissavings associated with refunding either or both the 2010B and 2010C Bonds, evaluate the risk/reward based on comparing the potential cost of the loss in subsidy ($3 million per year) to the risk of having to refund the Bonds at a later date (2020) when interest rates may be materially higher.

Background
The County's $214.69 million 2010 Bonds were issued to fund construction of the new Courthouse. The initial plan of finance called for issuing traditional tax-exempt bonds secured by the County's Half-Cent Sales Tax. However, as part of the American Recovery and Reinvestment Act of 2009 (ARRA) the Federal government created the Build America Bond (BAB) and the Recovery Zone Economic Develop Bond (known as "Super BABs") programs to incentivize local governments to invest in infrastructure to spur economic activity and help lead the economy out of the Great Recession. The programs required that local governments issue taxable bonds to fund infrastructure needs and then the Federal government would rebate back to the local government a portion of the interest expense, with the net result being debt service that was materially lower than traditional tax exempt debt. BABs provided a 35% subsidy and Super BABs provided a 45% subsidy. As an example, if the County issued taxable bonds at 5.5%, the 35% subsidy would result in a net interest rate of approximately 3.5% and the 45% subsidy would result in a net interest rate of approximately 3.0%, compared to a tax exempt interest rate of 4.0%. For a $50 million financing the savings derived from the 45% subsidy would be $500,000 per year. Due to the material savings, the County issued the 2010 Bonds in three pieces:

- 2010A Bonds - $95.96 million of traditional tax-exempt bonds
- 2010B Bonds - $69.95 million of BABs
- 2010C Bonds - $48.78 million of Recovery Zone Economic Development Bonds

The 2010 Bonds were issued in three pieces because market factors were such that BABs only provided savings in certain maturities. So, traditional tax-exempt bonds (2010A Bonds) were issued for maturities through 2020 and then from 2031 to 2036. Also, the Federal government allocated limited amounts of Super BABs to each region, so the County issued the maximum amount available, $48.78 million. Since Super BABs offered the largest savings, the Super BABs (2010C Bonds) were structured as the last maturities (2037 through 2040). The 2010B Bonds were issued as BABs with maturities between 2021 and 2025 and then again from 2031 through 2036. This structure was designed to result in generally level debt service of approximately $13 million per year. The actual debt service was approximately $16 million per year (follow the top of the grey bars on the graphic on the following page), but the BAB and Super BAB subsidies of $1.47 million and $1.44 million, respectively, totaled $3 million. So, the net debt service was $13 million (follow the top of the blue bars across the graphic on the following page).



Call/Prepayment provisions

Most traditional, tax exempt debt is issued with a call at par, 10 years after the issuance of the debt, which enables the issuer to refinance and reduce debt service. However, taxable obligations are typically non-callable or include a "Make Whole" call. Fortunately, to protect the County, the 2010B and 2010C Bonds included BOTH a Make Whole call at any time and a par call on 10/1/2020. While this carried a slight cost back in 2010, it limited the County's exposure to the potential that the Federal government reduced the subsidy; the precise situation that the County faces today. While the Make Whole call allows the County to call the Series 2010 B & C Bonds at any time, the Make Whole provisions require that the County make the investor whole (thus the name) for the original yield the investor expected. The way the math works, Make Whole calls require a larger and larger prepayment penalty as current interest rates go lower and lower. Since interest rates are materially lower today than in 2010, the prepayment premium would be approximately $15,080,993 for the 2010B Bonds and $22,262,398 for the 2010C Bonds if the Tax Bill effectively alters the subsidy payments. Clearly this is cost prohibitive today leaving the County in the position that the optimal structure is to utilize the 2020 par call to refund the 2010 Bonds.

Estimated Results of Refunding the Series 2010 Bonds

As discussed previously, the 2010 Bonds were structured as three different series of bonds and can be refunded independently. Since the bonds have different maturities, different tax status and different subsidies, the potential savings from refunding the bonds varies materially. As shown below:

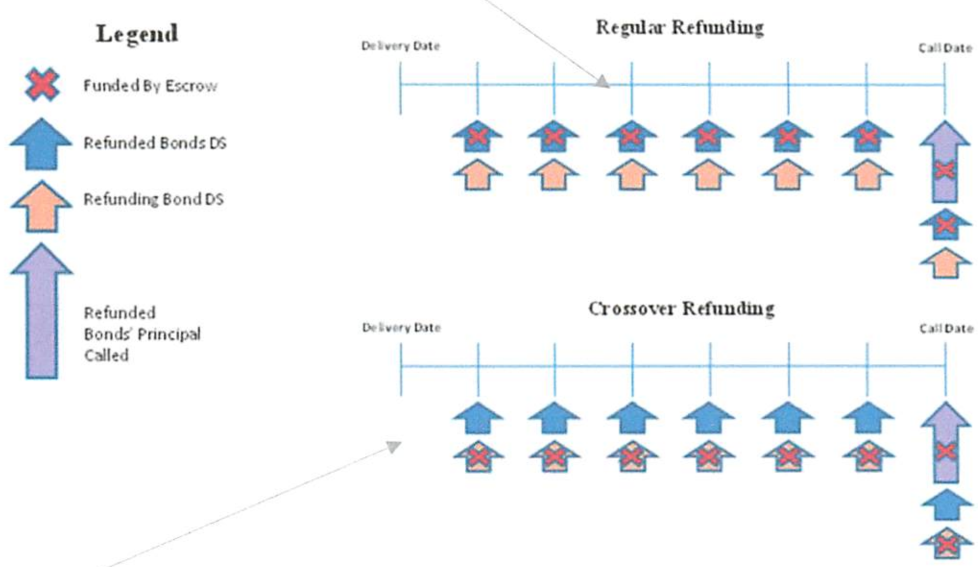
- Refunding the 2010A Bonds is estimated to result in approximately $10.13 million in net present value debt service savings when compared to the current debt service,
- Refunding the 2010B Bonds is estimated to result in approximately $2.27 million in net present value debt service savings when compared to the current net debt service, and
- Refunding the 2010C Bonds is estimated to result in approximately $1.02 million in net present value debt service savings when compared to the current net debt service.

	2010A	2010B	2010C	Total
	Tax-Exempt	BAB - 35%	BAB - 45%	
Refunded Par	58,625,000	69,950,000	48,780,000	177,355,000
Full Subsidy				
NPV Savings ($)	10,131,764	2,265,269	1,024,856	13,421,889
Savings as a %	17.28%	3.24%	2.10%	7.57%
FY18 Sequestration (6.60%)		BAB - 32.69%	BAB - 42.03%	
NPV Savings ($)	10,131,764	2,744,378	2,240,681	15,116,823
Savings as a %	17.28%	3.92%	4.59%	8.52%
Make-Whole Call Premium (100 bps)	-	15,080,993	22,262,398	37,343,391
Make-Whole Call Premium (35 bps)	-	18,939,467	28,634,096	47,573,563

Since the debt service used to estimate the savings is compared to the net debt service (i.e. including the subsidy), if sequestration continues, the cost to the County increases. As an example, even the relatively modest impact of sequestration that is already in place increases the savings on the 2010B Bonds refunding from $2,265,269 to $2,744,378. *It is important to note that the savings estimates assume the 2010 Bonds remain outstanding to maturity. This is the typical way issuers estimate savings from refundings. As a practical matter, if the subsidy were to go away in the future (for example, in 2025), at that point in time the County would convert the 2010B and 2010C Bonds from taxable to tax-exempt bonds. But, this would be done at interest rates at that point in time, which could be materially different than today; higher or lower.*

Other Factors for Consideration

Cross over refunding - The IRS has advised issuers that if BABs are legally defeased using a traditional advance refunding, the subsidy will be eliminated. Therefore, a crossover refunding is recommended by bond counsel so that the subsidy would stay in place until the bonds are called. How is an advance refunding different from a crossover refunding? For a typical advance refunding, the new bonds (2017 Bonds in this case) fund an escrow that pays the debt service on the prior bonds (2010B and 2010C Bonds in this case) until the bonds are called. The vast majority of advance refundings are completing with this structure. But, the Tax Code specifically allows for another type of advance refunding, called a crossover refunding.



For a cross over refunding, conversely, the escrow pays the interest on the new bonds (2017 Bonds) until the old bonds (2010B and 2010C Bonds) are called. Legally, both series of bonds are outstanding between now and the call date. Additionally, there is no cashflow relief until after the call date. From a present value savings perspective, the difference between a traditional advance refunding and a crossover advance refunding is not material. But, debt service coverage is lower since both bonds would technically be outstanding—although the coverage for the Sales Tax Bonds would still be very high.

Sensitivity related to changes in interest rates over time – The table on page 5 highlights that refunding the 2010A Bonds should be accomplished if possible in the short time frame between now and year-end. The refunding of the 2010B and 2010C Bonds offers savings, but is not as favorable as refunding the Series 2010A Bonds. However, we expect the firms responding to the proposal to provide alternatives that may change the estimated savings. For example, most banks do not offer loans for 20+ years. So, they will most likely offer a loan that has a fixed rate, but the rate would be reset after 10 or 20 years. This would most likely increase the estimated savings, but leave the County exposed to interest rate changes. This is offset by the fact that most of the principal will be paid off by the time that the interest rates would be reset. PFM will perform a sensitivity analysis of the proposals to assist staff ascertain whether the proposals offer enough benefit to offset the potential for higher interest

rates in the future. In the end, the County will need to decide whether the risk and cost associated with the potential/likely reduction/loss of the subsidy is greater than the risk of higher interest rates in 10 or 15 years.

Example of sensitivity analysis that will be applied to proposals
The most straightforward assessment of risk/reward is to consider the impact of potential changes in interest rates between now and the call date in 2020. The table below shows how much interest rates could increase between now and 2020 and obtain the same results today. Typically if the change in interest rates is relatively small, it is best to complete the refinancing now. The increase in interest rates from today that would result in the same outcome is 36bps, 49.5bps and 27bps for the 2010A, 2010B and 2010C Bonds, respectively, suggesting that the County should move forward. For the refunding of the 2010C Bonds, the analysis is more complex because the refunding offers limited savings. (In fact, until interest rates dropped materially in the last week, there was actually dissavings.)

	Series 2010A (Advance Refunding)	Series 2010B (Crossover Refunding)	Series 2010C (Crossover Refunding)
Par Amount Refunded	58,625,000	69,950,000	48,780,000
Value of Negative Arbitrage	2,084,543	1,651,421	1,676,207
PV01	77,823	53,320	77,027
Advance Refunding @ Current Rates			
NPV Savings ($)	10,131,764	2,265,269	1,024,856
Savings (%)	17.28%	3.24%	2.10%
Increase in rates that could occur between now and 2020 that results in the same savings	36 bps	49.5 bps	27 bps

*All Cashflows are discounted back to 12/28/2017

**Assumes Full Subsidy

Summary and Recommendations

The County faces both an opportunity and a challenge related to the 2010 Bonds. The Tax Bill, and ramifications of the Tax Bill, create significant uncertainty related to the receipt of the $3 million per year subsidy for the 2010B and 2010C Bonds and forces the County to decide whether to refund the bonds now, or wait until 2020. At the same time, interest rates are such that refunding a portion of the 2010 Bonds offers the County significant savings, although the County will need to accomplish the refunding very quickly. Assuming the actual financial results are similar to the estimates shown above, PFM recommends that the County (i) move forward with the refunding of the 2010A Bonds and the 2010B Bonds and (ii) only move forward with the refunding of the 2010C Bonds if the final sensitivity analysis suggests refunding results in a materially better outcome than waiting until 2020. Regarding both the 2010B and 2010C Bonds, significant assumptions will need to be made regarding future action of the Federal government and interest rates, so the outcomes will most likely be different than estimated.

Jardine, Arlene

From: Cassini, Gretchen
Sent: Monday, December 11, 2017 10:45 AM
To: Pelkey, John; Jardine, Arlene
Cc: Cassini, Gretchen
Subject: RE: Organizational Development

Looks fine! Arlene please reschedule.

GRETCHEN M. CASSINI
BROWARD COUNTY ADMINISTRATION
(954) 357.7579

-----Original Appointment-----
From: Pelkey, John
Sent: Monday, December 11, 2017 10:03 AM
To: Jardine, Arlene
Cc: Cassini, Gretchen
Subject: New Time Proposed: Organizational Development
When: Thursday, December 14, 2017 11:00 AM-12:00 PM (UTC-05:00) Eastern Time (US & Canada).
Where: Gretchen's office

We have our HR Retreat on Thursday. I hope this time works for you. Thanks!