Bond Case Briefs

Municipal Finance Law Since 1971

Issue 99

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- And finally, The Wheels On the Bus Go Buelta y Buelta is brought to us this week by *McNair v. City and County of San Francisco*, in which school bus driver Michael McNair's professional qualifications were called into question after he (oh, so very *inter alia*) "improperly drove a group of children from San Diego, California to Tijuana, Mexico." Field trip! Mr. McNair's explanation for this little incident features the mother of all understatements, "I made a mistake and just didn't think." Appreciate the candor, but we'll be hanging on to the keys all the same.

IMMUNITY - CALIFORNIA

McNair v. City and County of San Francisco

Court of Appeal, First District, Division 4, California - November 22, 2016 - Cal.Rptr.3d - 2016 WL 6879277

Patient brought action against city and physician employed by the city's department of public health for breach of contract and violation of the California Confidentiality of Medical Information Act (CMIA).

The Superior Court granted summary adjudication on patient's intentional tort cause of action and nonsuit on his breach of contract claim. Patient appealed.

The Court of Appeal held that:

- Litigation privilege barred patient's CMIA cause of action based on physician's disclosure of patient's cognitive deficits to the Department of Motor Vehicles (DMV);
- Catchall provision of the CMIA authorized physician's disclosure of patient's cognitive deficits to the DMV; and
- Litigation privilege barred patient's breach of contract cause of action based on physician's disclosure of patient's cognitive deficits to the DMV.

The litigation privilege barred patient's cause of action under the California Confidentiality of Medical Information Act (CMIA) arising from physician's report to the Department of Motor Vehicles (DMV) that patient suffered from cognitive deficits calling into question whether it was appropriate for him to have a commercial driver's license, even assuming that the physician's report did not comply with the statute providing that a physician may report a patient's condition to a local health officer upon a good faith belief that the report will serve the public interest, since the letter to the DMV was a communication "authorized by law."

A voluntary disclosure of confidential medical information falls within the reach of the catchall provision of the California Confidentiality of Medical Information Act (CMIA) if a public policy exists encouraging such disclosure, the disclosure involves issues of public safety, and it is a communication which would otherwise be immunized by the litigation privilege.

The litigation privilege barred patient's breach of contract cause of action against city and a city-employed physician arising from physician's report to the Department of Motor Vehicles (DMV) that patient suffered from cognitive deficits calling into question whether it was appropriate for him to have a commercial driver's license, where the contract did not clearly prohibit the physician's conduct.

JUDGMENTS - CALIFORNIA

Sutter Health v. Eden Township Healthcare District

Court of Appeal, First District, Division 1, California - November 29, 2016 - Cal.Rptr.3d - 2016 WL 6958654

Nonprofit health system brought action against township healthcare district for specific performance of a written agreement to convey real property and for damages. District cross-complained for declaratory and injunctive relief.

The Superior Court granted summary judgment for health system on cross-complaint and denied district's motion for summary adjudication. District appealed. The Court of Appeal affirmed. The Superior Court denied health system's motion for attorney fees. Health system appealed, and the Court of Appeal reversed and remanded. District filed a motion to pay a judgment in up to 10 annual installments on the basis that prompt payment would impose an "unreasonable hardship." The Superior Court granted the motion, and effectively amended the judgment nunc pro tunc to decrease the postjudgment interest rate retroactively from the date the judgment was entered. Judgment creditor appealed.

The Court of Appeal held that:

- District's financial straits supported a finding of "unreasonable hardship," but
- Interest accrued prior to the trial court's grant of relief could not be reduced retroactively.

Trial court's finding that prompt payment of a $19.5 million judgment would impose an "unreasonable hardship" on township healthcare district, in authorizing payment in up to 10 annual installments, was supported by substantial evidence, including testimony of an accountant that a 10-year installment plan was necessary to avoid significantly impacting district's "ability to continue to service its residents," evidence that district was unable to borrow the funds necessary to pay the judgment in a lump sum, and evidence that a sale of assets to finance payment of the judgment would threaten bankruptcy by depriving the district of the funds required for it to operate.

Under the statutes providing that a local agency may pay a judgment in up to 10 annual installments upon a showing that prompt payment would impose an "unreasonable hardship" and that the interest rate for such judgments is the one-year United States Treasury bill rate, interest accrued prior to the trial court's grant of relief could not be reduced retroactively to the Treasury bill rate.

Township healthcare district's failure to challenge the constitutional default seven percent rate of postjudgment interest, either at the time a judgment was entered against the district or on appeal, waived any argument that the seven percent rate was not the correct rate for the trial court to impose upon the Court of Appeal's reversal of the trial court's order imposing the one-year United States Treasury bill rate retroactively under the statute authorizing a local agency to pay a judgment in up to 10 annual installments where prompt payment would impose an "unreasonable hardship."

ZONING & LAND USE - MAINE

Fryeburg Trust v. Town of Fryeburg

Supreme Judicial Court of Maine - December 1, 2016 - A.3d - 2016 WL 7010513 - 2016 ME 174

Adjacent landowner sought review of local board of appeals decision upholding local planning board's approval of neighboring private secondary school's application to use an agricultural land parcel for primarily outdoor teaching purposes and use a residential land parcel for administrative offices.

The Superior Court affirmed in part and vacated in part. All parties appealed.

The Supreme Judicial Court of Maine held that:

- Proposal to use agricultural lot as an outdoor classroom constituted using the lot as a place where courses of study that fit state education requirements were taught, and
- Proposal to use residential lot for school administrative offices concerned a task that was so integral to the functioning of the school that it was indistinguishable from the school.

Private secondary school's proposal to change use of agricultural lot and use it as an outdoor classroom instead constituted using the lot as a place where courses of study that fit state education requirements were taught, as required by local land use ordinance, despite argument that no complete courses would be taught on the lot, much less all mandated courses. School's planned courses for the lot included those in the state-required subjects of physical education and science, and nothing within the text of the ordinance required that all of the courses required by the state or the entirety of those courses be taught on each piece of property or in each building where a secondary school operated.

Private secondary school's proposal to change use of residential lot to use it for school administrative offices instead concerned a task that was so integral to the functioning of the school that it was indistinguishable from the school and, therefore, permissible under local land use ordinance governing uses by secondary schools, despite ordinance's definition of a secondary school as a "place where courses of study are taught"; administrative offices were integral to the functioning of a school.

EMINENT DOMAIN - NEBRASKA

Strode v. City of Ashland

Supreme Court of Nebraska - October 28, 2016 - 295 Neb. 44 - 886 N.W.2d 293

Husband and wife landowners brought action against city and county, alleging zoning regulation inverse condemnation and alleging that bridge load limit constituted a taking.

The District Court dismissed husband's inverse condemnation claims as time barred, and granted summary judgment for city and county. Landowners appealed.

The Supreme Court of Nebraska held that:

- As a matter of first impression, cause of action for inverse condemnation based on a regulatory taking begins to accrue when the injured party has the right to institute and maintain a lawsuit due to a city's infringement, or an attempt at infringement, of a landowner's legal rights in the property;
- City's letter to landowners providing notice of nonconforming use and the city's intention to institute legal action began running of 10-year statute of limitations on husband landowner's cause of action for inverse condemnation;
- Statute of limitations on wife landowner's separate claim for inverse condemnation began to run on date husband received letter from city; and
- Load limit on bridge to property did not constitute a "regulatory taking."

In the context of a regulatory taking, a cause of action for inverse condemnation begins to accrue when the injured party has the right to institute and maintain a lawsuit due to a city's infringement, or an attempt at infringement, of a landowner's legal rights in the property.

At the latest, city's letter to landowners providing notice of nonconforming use and the city's intention to institute legal action if landowners did not conform their use began running of 10-year statute of limitations on cause of action for inverse condemnation, as city's actions had an adverse economic impact on the landowners' right to use the property in the commercial manner that they wished.

Statute of limitations on wife landowner's separate claim for inverse condemnation began to run on date husband received letter from city providing notice of nonconforming use and the city's intention to institute legal action if landowners did not conform their use, rather than any date on which wife received actual notice of land use ordinance affecting the property, as letter constituted an infringement or attempted infringement on wife's right to use the property as she wished and gave rise to her right to institute and maintain a lawsuit.

Load limit on bridge to property did not constitute a "regulatory taking"; while load limit restricted landowner to using either semitrailer trucks that weighed less for access across the bridge or trucks of a limited height for access through railroad underpass, restriction was not an injury different in kind than injury to the general public, bridge limit did not decrease the economic value of the property, and bridge limit, which was posted prior to landowners' purchase of the property, did not interfere with any reasonable investment-backed expectations.

BONDS - NEW JERSEY

Mollica v. Township of Bloomfield

Superior Court of New Jersey, Appellate Division - October 17, 2016 - Not Reported in A.3d - 2016 WL 6068242

The Township of Bloomfield adopted Ordinance 3729 on August 11, 2014. The Ordinance appropriated $10,500,000 for the acquisition and improvement of a tract of land to be used as a public park, and authorized the issuance of $9,975,000 in Township bonds or notes to finance part of the cost. The property had previously been approved by the Township Planning Board for construction of a 104-unit townhouse development known as Lion Gate.

A group of Township residents filed an action in lieu of prerogative writs challenging the validity of the Ordinance. They also sought to enjoin the Township from issuing the bonds. The residents alleged that Councilman Nicholas Joanow had a disqualifying interest when he voted on the Ordinance under both the common law and the Local Government Ethics Law (LGEL) due to the fact that he owned a home that directly bordered the property. Joanow also cast the deciding vote approving the Ordinance.

The trial court found that Joanow did not have a disqualifying personal conflict of interest because the acquisition of the park constituted a benefit to the public.

The appeals court reversed. “Applying the statutory standards set forth in the LGEL, as well as established common law authority, we hold that Joanow’s ownership of a home directly bordering the property that the Township sought to acquire disqualified him from voting on the bond ordinance.”

The Township argued that the adoption of the bond Ordinance was a legislative act arising under the Local Bond Law, and not a judicial or quasi-judicial function involving review of a zoning application under the MLUL. However, the court found no legal or public policy basis not to apply the same conflict of interest standard regardless.

COLLECTIVE BARGAINING - PENNSYLVANIA

Americans for Fair Treatment, Inc. v. Philadelphia Federation of Teachers

Commonwealth Court of Pennsylvania - November 21, 2016 - A.3d - 2016 WL 6833073

Nonprofit organization brought action against school district and teachers’ union, seeking declaration that provision of collective bargaining agreement providing for union leaves of absence was unlawful.

School district and union moved to dismiss, for lack of standing. The Court of Common Pleas granted the motion. Organization appealed.

The Commonwealth Court held that:

- Allegations by organization were insufficient to establish associational standing, and
- Organization could not establish taxpayer standing.

Allegations by nonprofit organization were insufficient to establish associational standing to maintain an action against school district and teachers’ union to challenge a provision in collective bargaining agreement providing for union leaves of absence. Organization alleged that many of its members were teachers with lower seniority that teachers who were on leave, but complaint lacked

any factual allegation sufficient to show that this lower seniority had any direct and non-speculative, immediate effect on the organization's members.

Nonprofit organization could not establish taxpayer standing to challenge lawfulness of union leaves of absence under collective bargaining agreement. School district was better situated to assert claim that union leaves were unlawful, any teachers who were affected by the leave policy could challenge it, and organization did not allege any adverse effect on taxpayers as a whole.

ZONING & LAND USE - PENNSYLVANIA

Lower Mount Bethel Township v. Gacki

Commonwealth Court of Pennsylvania - November 30, 2016 - A.3d - 2016 WL 6993996

Township filed zoning enforcement action against landowners. The magisterial district judge entered judgment against landowners, and landowners appealed.

The Court of Common Pleas entered judgment in favor of township and awarded attorney fees. Landowners appealed.

The Commonwealth Court held that:

- Township had geographic jurisdiction over retaining wall and backfill which landowners alleged were located in the Delaware River;
- Landowners' failure to appeal zoning violation notice to zoning hearing board resulted in a conclusive determination that their retaining wall and backfill violated floodplain ordinance; Award of over $20,000 in attorney fees to municipality was reasonable;
- Permanent injunction directing landowners to remove the retaining wall and backfill was warranted; and
- Imposition of $1,200 fine was warranted.

Township had geographic jurisdiction over retaining wall and backfill which landowners alleged were located in the Delaware River, in township's zoning enforcement action. Federal law granted Commonwealth authority over the portion of the river bed that was within the Commonwealth's boundaries, boundary of township and Commonwealth was the middle of the Delaware River, and interstate compact with New Jersey extended boundary line of township to river's New Jersey shore.

If a landowner does not appeal a zoning violation notice to the zoning hearing board, the failure to appeal renders the violation notice unassailable; therefore, in the event a landowner does not appeal to the zoning hearing board and the municipality files an enforcement action with a district justice, neither the district justice nor a common pleas court may conduct a de novo review of the question of whether the landowner violated the zoning ordinance, and the only question before the district justice and the Common Pleas Court is whether the penalty imposed for the violation was proper.

Award of over $20,000 in attorney fees to municipality was reasonable in zoning enforcement action. Landowners' failure to appeal violation notice resulted in conclusive determination of their violation of ordinance, and landowners' counsel stipulated that amount of attorney fees was reasonable.

Permanent injunction directing landowners to remove the retaining wall and backfill that violated township's zoning ordinance was warranted; landowners constructed the retaining wall and backfilled the property without applying for a permit, and failed to appeal violation notice.

Imposition of $1,200 fine was warranted for landowners' violation of township zoning ordinances; landowners remained in violation of magisterial district judge's judgment that their retaining wall and backfill violated the ordinance for 687 day

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BANKRUPTCY - PENNSYLVANIA

Becker v. Bank of New York Mellon Trust Company, N.A.

United States District Court, E.D. Pennsylvania - October 5, 2016 - Slip Copy - 2016 WL 5816075

Plaintiff Leonard Becker moved to certify a class comprising holders of revenue bonds ("Bondholders") who were entitled to a distribution under the Plan for reorganization of the bond debtor, Lower Bucks Hospital ("LBH"), which Plan was confirmed under Chapter 11 of the Bankruptcy Code.

The Bondholders were awarded $8,150,000 by the Bankruptcy Court in the reorganization. That amount was distributed to The Bank of New York Mellon Trust Company ("BNYM") as the successor Indenture Trustee. None of those funds were disbursed to the ninety-five Bondholders.

BNYM opposed certification. Its primary argument was that a finding of predominance was precluded because the proximate cause of the bondholders' alleged losses could not be proved with evidence that was common to all class members.

Plaintiff had previously sued BNYM under the multi-party agreements that created the bond financing transaction. The Complaints alleged that BNYM was negligent and breached its fiduciary and contractual duties to the Bondholders by failing to maintain perfected security interests in the property securing the bonds. Plaintiff alleged that the Bondholders were allowed less in LBH's bankruptcy than they would have been allowed if the security interests had been perfected.

Plaintiff had also sued for a declaratory judgment that the Bondholders were entitled to prompt disbursal of the funds allowed for them under the Plan, and that BNYM was not entitled to deduct from those funds any amounts that it incurred asserting its personal interests in the bankruptcy proceedings or in this litigation. Plaintiff also sued for equitable remedies — an injunction compelling BNYM to distribute the Bondholders' funds, an accounting of those funds, and damages for conversion and for money had and received.

Relevant to this litigation was the fact that the proposed pre-confirmation Plan included a stipulated third-party release of potential claims by the Bondholders against BNYM based on its alleged failure to maintain perfected security interests and liens against the property securing the bonds. Upon being made aware of the proposed release, the Bondholders objected. The Bankruptcy Court denied confirmation of the third-party release and struck it from the Plan because the release was inadequately disclosed before the Bondholders voted to accept the proposed plan.

The District Court took up the motion to certify the purported class of Bondholders.

The Court began its analysis by reviewing the facts of this case against Rule 23(a). The Court concluded that the proposed class met the requirements of numerosity, commonality, typicality and adequacy.

The Court then turned to Rule 23(b), finding that common questions predominated over any questions affecting only individual class members, as required under Rule 23(b)(3).

The Court concluded by certifying the class, certifying Plaintiff Becker as the class representative, and appointing class counsel.

Kroll Bond Rating Agency Assigns the Long-Term Rating of BBB with a Negative Outlook for the Chicago Board of Education Dedicated Capital Improvement Tax Bonds, Series 2016.

NEW YORK, NY (December 8, 2016) – Kroll Bond Rating Agency (KBRA) has assigned a BBB long-term rating and Negative outlook to the Board of Education of the City of Chicago (the "Board") Dedicated Capital Improvement Tax Bonds, Series 2016. KBRA also affirms the BBB rating and Negative outlook on the Board's Unlimited Tax General Obligation Bonds (Dedicated Revenues), Series 2016A and Series 2016B and affirms the BBB- rating and Negative outlook on the Board's Unlimited Tax General Obligation Bonds (Dedicated Alternate Revenues).

The rating is based on two KBRA methodologies, primarily the General Property Tax/Assessment Revenue Methodology and secondarily the U.S. Local Government General Obligation Rating Methodology.

To view the report, please click here.

S&P Public Finance Credit Forum.

Jan. 19, 2017 | Denver, CO

On behalf of the U.S. Public Finance team, we are pleased to invite you to our inaugural Denver U.S. Public Finance Credit Forum on Thursday, January 19th, with Keynote Speaker Arturo Perez, Director at the National Conference of State Legislatures.

Click here to learn more and to register.

S&P's U.S. Public Finance Podcast (Rating Actions on U.S. Virgin Islands & Proposed Criteria Changes for Housing Finance Agencies and Social Enterprise Lending Organizations)

Listen to the podcast.

Dec. 9, 2016

S&P: Why Massachusetts Charter Schools Haven't Damaged Municipalities' Credit Quality.

On Nov. 8, 2016, Massachusetts voters defeated a referendum to increase the number of charter

schools in the state, thus maintaining the existing cap on charter school expansion. Had it passed, the referendum would have allowed as many as 12 new charter schools to open each year regardless of the budgetary impact on cities and towns.

Continue reading.

Dec. 5, 2016

S&P: Pennsylvania School Districts Could Face More Funding Pressure Due To Sluggish State Revenue Growth, Rising Costs.

Debate over funding for public education has contributed to Pennsylvania's last two budget impasses. Generally, state lawmakers have agreed that public education spending should increase over the past two budget cycles, but given slow revenue growth and other rising required costs (e.g., pensions), they have struggled over how to increase education funding. In our view, recently projected budget deficits for fiscal years 2017 and 2018 increase the likelihood that education funding could be a key budget issue again in fiscal 2018, potentially contributing to another year of protracted deliberations. In addition to the possibility of a late budget, given limited discretionary spending, lawmakers could turn to education funding cuts to balance the budget. Both outcomes would increase credit pressure on Pennsylvania school districts.

Overview

- Education funding could again become a key budget issue as Pennsylvania grapples with projected deficits in fiscal 2017 and 2018.
- Rising pension costs will be an ongoing burden for all school districts.
- Reliance on state aid varies from district to district.

Continue reading.

01-Dec-2016

SIFMA Continuing to Work to Improve Disclosure.

The Securities Industry and Financial Markets Association will be focused on several municipal bond industry initiatives in including disclosure in 2017, the group said at its annual "State of the Industry" briefing in New York on Wednesday.

SIFMA will be working with issuers, underwriters, bond counsel, investors, auditors and credit analysts to improve transparency in the wake of the Securities and Exchange Commission's Municipalities Continuing Disclosure Cooperation initiative, said SIFMA's President and CEO Kenneth Bentsen.

"We have been working with all the various stakeholders … trying to develop an industrywide initiative to improve issuer disclosure," Bentsen said, "including having the states take a greater role in regulating and policing local government issuer disclosure."

Additionally, Bentsen said SIFMA was looking at a revisions and updates to SEC rule 15c212; disclosure regarding bank loans and direct placements; the SEC guidance with respect to the outstanding continuing disclosure agreements; and improvements to the Municipal Securities Rulemaking Board's EMMA online website.

Some of the other initiatives the group will be focused on are backing the SEC's proposal on a shortened settlement cycle (T+2), working to aid senior citizen investors with the Senior $afe Act, and promoting cyber security and preparedness, he added.

Timothy Scheve, chair of SIFMA's Board of Directors, said that he would be focused on promoting the benefits of the U.S. capital markets, pushing for a comprehensive best interest standard for retail investors, and preserving equal access for its members to all SIFMA business models.

The Bond Buyer

By Chip Barnett

December 7, 2016

New Type of Chicago School Debt Gets Investment-Grade Rating.

A new type of debt for the Chicago Public Schools (CPS) earned an investment-grade rating of A from Fitch Ratings on Thursday, based on the bonds' ability to withstand a potential bankruptcy filing by the financially struggling district.

The A rating on $500 million of capital improvement tax bonds is eight steps above the junk rating of B-plus with a negative outlook Fitch has assigned the school system's $6.8 billion of outstanding general obligation bonds.

Fitch attributed the difference to its assessment "that the pledged revenues meet the definition of 'special revenues' under the U.S. Bankruptcy Code and therefore, bondholders are legally insulated from any operating risk of the board."

The United States' third-largest public school system is struggling with pension payments that will jump to about $720 million this fiscal year from $676 million in fiscal 2016, as well as drained reserves and debt dependency. The fiscal woes have pushed its GO credit ratings deep into the junk category and led investors to demand fat yields for its debt.

The $500 million of bonds will be secured solely by a capital improvement property tax approved by the Chicago City Council last year and not by the district's GO pledge. The property tax revenue, initially totaling $45 million, can only be used to fund capital projects and not operations, and is subject to an intercept mechanism that will send the funds directly to the bond trustee.

CPS cannot currently file for municipal bankruptcy in Illinois, although there have been proposals to change state law to allow such a move.

Fitch said legal opinions for the new bonds "provide a reasonable basis for concluding that the tax revenues levied to repay the bonds would be considered 'pledged special revenues.'" The opinions on a "hypothetical bankruptcy" by CPS concluded that payments on the new bonds would not be automatically stopped by a federal bankruptcy court and that bondholders would retain a lien on the

tax revenue.

Reuters

Thu Dec 8, 2016 | 12:44pm EST

(Reporting By Karen Pierog; Editing by Jonathan Oatis)

U.S. Muni Bond Market Shrinks to $3.831 trln in Q3 - Federal Reserve.

The U.S. municipal bond market shrank slightly to $3.831 trillion in the third quarter from a revised $3.838 trillion in the second quarter, according to a quarterly report from the Federal Reserve released on Thursday.

Households, or retail investors, held $1.591 trillion of muni bonds compared with $1.598 trillion the previous quarter.

Property and casualty insurance companies bought $19 billion of munis in the third quarter after a revised $1.9 billion of acquisitions in the second quarter. Life insurance companies added $7.6 billion to their muni holdings, while U.S. banks picked up $40 billion.

U.S mutual funds bought $75.9 billion of munis in the third quarter, and exchange-traded funds added $6.2 billion.

Foreign owners bought $14 billion of muni bonds. Their third quarter holdings were $93.3 billion, the highest level on record.

Reuters

Thu Dec 8, 2016 | 12:04pm EST

(Reporting by Hilary Russ)

Final Issue Price Rules Make Allowances for Competitive Sales.

WASHINGTON – The Treasury Department and Internal Revenue Service have finalized issue price rules that contain special allowances for competitive sales.

Under the rules, which are to be published in the Federal Register on Dec. 9 and would take effect 180 days later, the issue price for competitive sales will be the reasonably expected initial offering price if several certain conditions are met, including that the issuer receives bids for the bonds from three underwriters.

The rules also clarify that, for bonds issued for money in a private placement to a single buyer that is not an underwriter or related party, the issue price is the price paid by that buyer.

In addition, the rules contain a simplified “hold-the-offering-price” anti-abuse rule, place less emphasis on certifications, and narrow the definition of an underwriter.

“We tried to respond to the comments and make the final rules more flexible and more workable,” said John Cross, Treasury’s associate tax legislative counsel.

On competitive sales, Cross said, “As a policymaker, we think that competitive sales promote competition and price transparency and we wanted to provide a workable rule to accommodate this important market sector.”

Market participants praised some aspects of the new rules, but said they have questions about and want to review other provisions more closely.

Emily Brock, director of the Government Finance Officers Association’s federal liaison center, said, “We are pleased to see the Treasury and IRS addressed our concerns with regard to competitive pricing.” She said the GFOA’s debt committee plans to discuss the three-bid requirement for competitive sales and the five-day “hold-the-offering-price” requirement with Cross at its meeting here tomorrow.

Cliff Gerber, president of the National Bond Lawyers Association, also is pleased to see the special rule for competitive sales. “And they’ve now created a modified hold-the-offering-price rule, which I think is good,” he said. But he worried that bad underwriter behavior could hurt issuers’ bonds under the final rules.

Michael Decker, managing director and co-head of municipal securities for the Securities Industry and Financial Markets Association, said, “We are pleased that the issue price rule is now final. While we are still reviewing the release, several provisions of the final rule represent welcome changes. In particular, we support the provision specifying that the general rule will apply at any time the 10-percent sales threshold is met as well as the clarification that underwriters can sell bonds at prices below the initial offering price without breaking the rule. We are also pleased about the provision for special treatment for competitive offerings.”

John Vahey, Bond Dealers of America’s director of federal policy, said, “BDA appreciates the efforts of the IRS and Treasury to adopt improvements to the issue price rule. However, we have concerns with how the final rule’s requirement to hold the initial offering price for five days will alter the market and, also, how the three-bid requirement for competitive deals has the potential to negatively impact the competitive offerings of smaller issuers.”

Issue price is important because it is used to help determine the yield on bonds and whether an issuer is complying with arbitrage rebate or yield restriction requirements. It is also used to determine whether federal subsidy payments to issuers for direct-pay bonds such as Build America Bonds are appropriate.

Under existing rules that have been in place for years, the issue price of each maturity of bonds that is publicly offered is generally the first price at which a substantial amount, defined as 10%, is reasonably expected to be sold to the public.

But tax regulators became concerned several years ago that some dealers were “flipping” bonds — selling them to another dealer or institutional investor who then sold them again almost simultaneously — with the prices continually rising before the bonds were eventually sold to retail investors. The regulators worried that the “reasonably expected” issue prices for bonds were not representative of the prices at which the bonds were actually sold.

To address their concerns, the Treasury and IRS proposed issue price rules in 2013, eliminating the reasonable expectations standard and basing the determination of issue price on actual sales. They

also proposed raising the “substantial amount” of bonds standard to 25% from 10%.

The rules were strongly criticized as unworkable by issuers and underwriters. They complained about the 25% standard and said they often don’t sell 10% or 25% of every maturity right away.

The tax regulators scrapped those rules and re-proposed them in June 2015. Under the re-proposed rules, the issue price for each maturity of bonds generally would be the price at which the first 10% of the bonds are actually sold to the public.

Issuers could use an “alternative method” of determining issue price when 10% of a maturity was not sold by the sale date. The issue price would be the initial offering price of the bonds sold to the public as of the sale date, as long as the lead or sole underwriter certified to the issuer that no underwriter filled an order from the public after the sale date and before the issue date at a higher price, unless market changes justified the higher price. The lead underwriter would then have to document any market changes that justified a higher price.

Dealers complained about the lead underwriter having to provide certifications about the actions of other underwriters.

The final rules contain a general rule under which the issue price is the price at which the first 10% of a maturity of bonds is actually sold to the public.

The rules include a special rule, under which the issue price is the initial offering price as long as the underwriter sticks with the IOP for bond sales during the five business days after the sale date (or a shorter period if 10% of a maturity of bonds is sold to the public at a price that does not exceed the IOP).

The five-day “hold-the-offering-price” provision is an anti-flipping or an anti-abuse provision. The lead underwriter must certify the IOP to the issuer, as well as provide documentation, such as the pricing wire. Each underwriter in a syndicate must agree in writing that it will not offer or sell the bonds at a price higher than the IOP for five business days after the sale date.

Under a special rule for competitive sales, an issuer may treat the reasonably expected IOP of the bonds to be sold to the public as the issue price if the issuer obtains a certification from the winning underwriter bidder as to the reasonably expected IOP upon which it based its bid.

To achieve a competitive sale: the issuer must disseminate the notice of sale in a manner reasonably designed to reach potential underwriters; all bidders must have an equal opportunity to bid; the issuer must receive bids from at least three underwriters “who have established industry reputations for underwriting new issuances of municipal bonds;” and the issuer must award the bonds to the bidder who offers the highest price or lower interest cost.

Issuers have the option of using any of these rules up until the closing (issue) date for their bond transactions.

The IRS also modified the definition of “underwriter” in response to concerns that it was vague and unworkable.

The definition still says “an underwriter is any person that contractually agrees to participate in the initial sale of the bonds to the public by entering into a contract with the issuer or into a contract with a lead underwriter to form an underwriting syndicate.”

But the final rules remove the phrase “or other arrangement” from provisions that say an

underwriter “includes any person that, on or before the sale date, directly or indirectly enters into a contract or other arrangement with any of the foregoing to sell the bonds.”

The tax regulators certified that the final rules “will not have a significant economic impact on a substantial number of small entities.

The Bond Buyer

By Lynn Hume

December 8, 2016

Michigan Municipal League Wants to Reform State Municipal Finance.

Great places make for a strong economy, and the research supports that contention. By employing community-based placemaking strategies, we strengthen both our economic and social future. On behalf of the Michigan Municipal League, I am pleased to be coming to Adrian on Monday to explain how at the heart of great places are strong cities, but in Michigan we are failing our communities.

Across the country, cities account for over 80 percent of GDP, but in Michigan we are disinvesting in this vital resource.

A recent report, “Michigan’s Great Disinvestment: How State Policies Have Forced Our Communities into Fiscal Crisis,” was prepared for the League using information from state and local records as well as census data. The report details the economic challenges facing Michigan’s communities.

Michigan is the only state where total municipal revenue declined from 2002 to 2012, an 8 percent reduction before considering inflation. Revenues remain below the 2002 level for most communities.

Michigan has cut state support for cities more than any state in the nation. Since 2002, the state has diverted from communities more than $7.5 billion in revenue sharing to balance its own budget shortfalls. For example, Lenawee County communities have seen their revenue sharing cut by $25 million over the last 14 years. Adrian’s revenue sharing has been cut by $9.4 million; other cities throughout Lenawee lost between $119,000 and $2.9 million since 2002. As a result, most communities in the county have had to reduce their police and fire forces, cut back on road and sidewalk repairs, and generally reduce their services to citizens – including rural residents who often work or play in communities from Tecumseh to Morenci.

How is this possible? State policies that hamstring cities by over constraining property tax growth, cuts in state revenue sharing and few local options for raising revenue. Michigan is one of only a handful of states that so aggressively limits the ability of local governments to raise their own revenues to address their issues, while simultaneously reducing state support.

After years of working within the existing paradigms, the League and other partners are undertaking a major legislative and policy push detailed at saveMIcity.org. This Save Michigan Cities effort is aimed at reforming municipal finance in Michigan to encourage renewed investment in our communities.

As part of this initiative, the League is traveling throughout the state discussing the state’s broken

system for funding municipalities. This statewide tour comes to Adrian for a public saveMIcity event 3:30 p.m. Monday, Dec. 12, at Siena Heights University, 1247 E. Siena Heights Drive in Adrian at Dominican Hall's Rueckert Auditorium. The event is free and open to the public.

This is intended to be an examination of how we can do things differently in Michigan to assure that local government can't just survive, but can thrive. To that end, the League is developing policy recommendations around three themes: Cost Containment, Revenue Enhancement, and Structure of Government.

We are taking this three-pronged approach to break away from the historically limiting tactic of incremental change within the context of where we are today. We also want to hear your ideas and innovative approaches, so that together we can take bold action to create a new future for communities around Michigan.

Tony Minghine is the associate executive director and chief operating officer of the Michigan Municipal League, which is involved in local government in Michigan. Minghine will speak about state municipal finance Monday, Dec. 12, in Adrian.

Michigan Municipal League

By Tony Minghine

www.mml.org

Posted Dec 9, 2016 at 9:37 AM

Third Circuit Appellate Court Rules That Post-Acceleration Payment in Bankruptcy Constitutes Optional Redemption: Mintz, Levin

The recent advisory discusses a recent Third Circuit Court of Appeals ruling that held a "make-whole" optional redemption premium to be due upon a refinancing of corporate debt following its automatic acceleration upon bankruptcy. As noted in the linked advisory, the Second Circuit Court of Appeals also is considering this issue; whether it will come to the same conclusion remains to be seen. One way or another, these decisions will have spillover effect on judicial interpretation of optional redemption provisions in municipal bond transactions, and shine a spotlight upon the discrepancies between optional redemption provisions and other early payment provisions in most municipal bond indentures.

The Third Circuit case involved a debtor, Energy Future Holdings, that filed for bankruptcy for the explicit purpose of refinancing the debt at favorable interest rates while avoiding the hefty make-whole premiums payable upon an optional redemption of the refinanced notes. The bankruptcy court and the federal district court found nothing in the applicable corporate indenture requiring payment of a make-whole following an acceleration. The Third Circuit reversed, interpreting the applicable corporate indenture's "optional redemption" provisions to be applicable to the bankruptcy-triggered acceleration followed by repayment of the accelerated debt via a refinancing.

The Third Circuit's ruling that the repayment following acceleration was an "optional redemption" may have been driven by the factual context of what could be characterized as an "optional bankruptcy" filed solely or primarily to jettison the make-whole payments and lock in lower rate replacement financing. The indenture's acceleration provision was, as is usual, a remedial provision

entirely separate from the indenture's optional redemption provisions, and, as is typical but not universal, did not specify a premium to be due upon payment of the accelerated debt. Although once the accelerated payment was due there was nothing "optional" about paying it, the appellate panel opined that the payment on the applicable date was "optional" because the issuer chose to file for bankruptcy and chose not to deaccelerate the debt after the bankruptcy triggered the automatic acceleration. The fact that the bondholders objected to repayment without a make-whole premium also seems to have factored into the court's determination that the payment by the issuer was "optional."

The federal appellate court also concluded that under New York law a "redemption" may occur at or before maturity of bonds, and that therefore a "redemption" is not synonymous with a prepayment. (Indeed, the court suggested that if the make-whole premium had been labeled a "prepayment" premium rather than an "optional redemption" premium, it may have held the make-whole inapplicable, a curious distinction that leads back to the question of under what circumstances payment of an amount that has become due can be deemed optional.) The court disregarded indenture provisions that were technically inconsistent with its determination that the payment was an "optional redemption", such as the optional redemption requirement of prior notice from the issuer to the bondholders. According to the court: "[The issuer] offers no reason why it could not have complied with [the redemption] notice procedures. In any event, it cannot use its own failure to notify to absolve its duty to pay the make-whole."

By interpreting the indenture's optional redemption provisions as applicable to the payment of the accelerated debt, the Third Circuit panel mooted and declined to address the noteholders' alternate argument that the bankruptcy court should have granted relief from the bankruptcy stay to permit the bondholders to deaccelerate the accelerated debt. Whether that would have provided a more straightforward means of getting to the same result is debatable, as debt generally is deemed accelerated upon a bankruptcy whether or not it is contractually accelerated by the terms of the indenture.

The optional redemption provisions that are typical in municipal bond indentures refute the equivalence found by the Third Circuit between an optional redemption and a payment after acceleration. In contrast to the permissibility in corporate transactions of optional redemption at any time at a make-whole premium, the norm in municipal bond transactions is a lockout period (often 10 years) during which optional redemption is impermissible, followed by a declining fixed optional redemption premium. The fact that municipal indentures permit acceleration whenever there is an event of default, including upon bankruptcy, while imposing a lockout period for optional redemption, suggests that in the municipal bond context there may be less receptiveness by courts to the notion of deemed equivalence between an optional redemption and a payment following acceleration. Accordingly, a court may be less likely to deem an optional redemption premium applicable to a post-acceleration payment on a municipal bond absent express language requiring a premium in a post-acceleration context.

Whether corporate or municipal bonds are at issue, the best way to ensure the intended result is to draft clearly and specifically. Municipal bond indentures often permit or require bonds to be paid ahead of schedule not only upon acceleration but upon a so-called extraordinary redemption. These provisions, which typically permit payment ahead of schedule at par, are infrequently deployed relative to optional redemption provisions. Use of bankruptcy as a means of avoiding a prepayment premium is less likely in the municipal context, where the prepayment premium is typically 3% or less versus the often substantially larger make-whole premium, but "default refundings" of municipal bonds have been attempted to circumvent the optional redemption lockout period. There is no difference in the economic impact to a bondholder of early payment, no matter the degree of

optionality or lack of optionality from the issuer's perspective, and whether an early payment premium is expressly provided by the indenture in cases other than "optional redemption" is primarily a risk allocation question.

Drafting acceleration provisions and/or extraordinary redemption provisions in a manner that applies an equivalent premium to the optional redemption premium upon their exercise during the post-lockout period, and a make-whole or other premium during the optional redemption lockout period, provides better protection against any perceived risk of abuse of those provisions than reliance on the courts to figure out what the parties intended and/or is equitable in borderline scenarios.

Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.

Tuesday, December 6, 2016

by Leonard Weiser-Varon

Len is active in both municipal finance and corporate finance, with an emphasis on financings for 501(c)(3) institutions, project finance, secured lending, structured finance transactions, workouts and restructurings, corporate debt, and Section 529 college savings programs.

His practice includes service as bond counsel, issuer's counsel, underwriters' counsel, and counsel to institutional purchasers and borrowers in connection with public offerings and private placements of, and defaults and bankruptcies involving, tax-exempt and taxable debt for public, nonprofit, and corporate…

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NFMA Municipal Analysts Bulletin.

The National Federation of Municipal Analysts Municipal Analysts Bulletin, Vol. 26, No.3, is now available. All officers, active committees and societies contribute to the newsletter – it's the best way to learn about what is happening at the national level and locally.

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To Prepare for the Next Recession, States Take Stress Tests.

No government can be fully prepared for every economic twist and turn. Still, some are trying.

The Great Recession was uniquely devastating for states and localities because it hit all three major tax revenue sources: income, sales and property. It was a scenario that few, if any governments,

were really prepared to absorb. As a result, governments were forced to make massive budget cuts.

Now, as the recovery trudges on longer than most, a growing number of states are making sure they aren't blindsided by the next downturn.

Enter stress testing. The idea, which was borrowed from the U.S. Federal Reserve, essentially throws different economic scenarios at a state budget to see how revenues would be impacted.

"We're in an environment where everyone is starting to think about the next downturn and what that's going to look like," said Emily Raimes, a Moody's Investors Service analyst. "A stress test is a tool for states to think about what types of programs they should commit to and how much to save now."

Credit rating agencies, in fact, are among the practice's biggest fans. Earlier this year, Moody's stress-tested budgets of the 20 most populous states and found that Missouri, Texas and Washington are in the best position to handle a recession because of their strong reserves, spending flexibility and lower revenue volatility. (Low revenue volatility means a state's income doesn't change too drastically from one year to the next. In other words, it's more predictable.)

California and Illinois, however, found themselves at the other end of the spectrum in Moody's stress test. California is endangered by its high revenue volatility and lower reserves, according to the report. And Illinois is vulnerable because of its extremely low reserves and inflexible governance.

S&P Global Ratings also stress-tests state budgets. In August, the agency performed a stress test on the top 10 borrowing states' fiscal 2017 budgets. The scenario focused on what would happen if global economies like the United Kingdom or China slowed down more than anticipated.

The results — some of which overlap with Moody's — show that Connecticut, Illinois, New Jersey and Pennsylvania are most likely to feel significant fiscal stress, while Florida, New York and Washington are best positioned for a downturn.

A few states are forging the way with their own stress-testing systems, while even more are looking into the idea.

Utah has the most robust practice, and it's something credit rating agencies have held up as an example. Last year, the state tested its budgets against a moderate and severe recession — think 2001 versus 2008. The results told policymakers that Utah has enough in reserves to weather a moderate downturn, but a severe one would likely require cutting nearly $1 billion in spending over two to three years in addition to using most of the state's reserves.

The process was so informative that Utah Office of Management and Budget Director Kristin Cox and her colleagues are developing additional scenarios to test. For instance, what happens to specific revenue streams if the state's biomedical industry slows down? Or if oil prices shoot back up? (Utah's stress testing is one of the reasons Governing recently awarded Cox with a Public Official of the Year award).

Minnesota also uses a form of stress testing to evaluate its revenue volatility and inform its rainy day fund policy. It's one of just four states that requires periodic evaluations to make sure its savings targets actually reflect the state's revenue volatility. It's also the only state to determine its risk tolerance — that is, the tolerance policymakers have for not fully covering a potential shortfall. Its current savings target is the amount deemed necessary to cover 90 percent of all possible downturn scenarios.

California, which saw its revenues drop 20 percent during the Great Recession, recently started using stress tests. The state Legislative Analyst's Office now includes estimates of what would happen to the state's budget under an economic growth scenario and a mild recession scenario. The most recent analysis concludes that, in the event of a mild recession in 2018, the state would have enough reserves to cover most of its operating deficits through the 2020–2021 fiscal year.

Of course, no government can be fully prepared for every economic twist and turn.

"We're trying to create certainty in an environment that is inherently uncertain," said Cox. "Instead our approach should be, how prepared are we to respond to different scenarios?"

The unusual recession and equally unusual recovery period has sent the message to budget officials that they can't afford to be caught unprepared. Since presenting Utah's stress-testing methods at a National Conference of State Legislatures meeting, Legislative Fiscal Analyst Jonathan Ball said he's gotten calls from Colorado, Nevada and Vermont, among others.

"It's gotten a lot of traction," he said. "We didn't know if it was going to work at first. We're kind of learning as we go and sharing our experience with other states."

GOVERNING.COM

BY LIZ FARMER | DECEMBER 12, 2016

Moody's: U.S. Local Governments Outlook Remains Stable Due To Steady Revenue Growth, Healthy Reserves.

New York, December 07, 2016 — The outlook for US local governments will remain stable as the majority of the sector is underpinned by solid property tax revenues and healthy reserves, Moody's Investors Service says. The outlook indicates fundamental business conditions over the next 12 -18 months.

Property taxes, the bedrock of local governments, remain healthy and will continue growing in 2017 owing to broader local tax base growth returns to pre-recession levels.

"A combination of property value growth and tax rate increases drove revenues 5.1% higher in the first half of 2016. We expect these factors will continue to support revenue growth of 3%-5% in 2017," according to Moody's Analyst Sarah Jensen.

Moody's says reserve levels remain healthy for most local governments and provide budget flexibility. Most local governments will continue to actively raise revenues or cut spending as needed to maintain these reserves through 2017. Reserves provide flexibility for local governments in times of unexpected economic stress and unpredictable expenditures.

While manageable for most, overall fixed costs and growing balance sheet liabilities are a long-term drag on the sector. Fixed costs such as pension liabilities, debt service and other post-employment benefit (OPEBs) contributions could, if unaddressed, begin to crowd out essential services.

Infrastructure needs are becoming more pressing, and rising fixed costs could hamper the ability to issue debt to address this issue.

Despite general stability across the sector, there is a growing portion, roughly 5% -10% of issuers, facing numerous challenges pressuring their credit profiles. These local governments face revenue stagnation combined with growth in fixed costs, leading to a trend of credit deterioration.

Moody's would change the outlook on the sector to positive if strong property tax revenue growth continues at 4%-5% and is accompanied by a stabilization of fixed costs and maintenance of healthy reserves. The sector outlook could change to negative if property tax revenue growth weakens to 1-2% or growth is outpaced by the increase in long-term liabilities and fixed costs.

"Financial challenges at the state level, particularly in states hit by low energy prices or budget imbalances, could impact some municipalities and school districts as states could either cut aid or shift fiscal responsibilities to local governments," said Jensen.

"Local Governments — US: 2017 Outlook – Strong Tax Revenues, Healthy Reserves Drive Stability for Most." Is available to Moody's subscribers at

https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBM_1045982.

This report is part of a series of 2017 Credit Outlooks that provide insight into next year's credit conditions across all sectors. See more at www.moodys.com/2017outlooks

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The Week in Public Finance: Federal Budget Chaos, a Bankruptcy Win and Pension Portfolios.

A roundup of money (and other) news governments can use.

The Week in Public Finance.

GOVERNING.COM

BY LIZ FARMER | DECEMBER 9, 2016

LAX's Makeover Inspires Airport Changes Around the Country.

Los Angeles is spending billions to revamp its airport. The move is spurring other cities to make similar investments.

Twenty miles from downtown Los Angeles, squeezed between the Pacific Ocean and one of Southern California's busiest freeways, sits 3,400 acres of bare pavement and neglected jet-age architecture that make up Los Angeles International Airport. These features are the first glimpse travelers get of a city with lofty aspirations. It's not a pretty sight.

For decades, LAX has been known for crowded gates, drab terminals, scarce amenities and ungodly traffic. It's a place that international visitors and lifelong Angelenos alike avoid if at all possible. That's a troubling prospect for a region that thrives on tourism, international trade with Asia and Latin America, and industries such as defense and aerospace manufacturing that are heavily intertwined with global travel.

“There is no calling card like it to people who will invest, who will travel, who will study in your city than an airport,” says Los Angeles Mayor Eric Garcetti. “It is the first taste, the last taste, the first view, the last view. If you’re greeted with traffic, cigarette smoke, honking cars, people giving tickets and gridlock, you’ll say, ‘Oh, I guess this is what L.A. is like.’” That’s not the impression the mayor wishes to leave. Garcetti wants to refashion the airport around enhanced customer experiences that could put LAX in the top tier of airports globally, right next to Hong Kong, Munich, Seoul, Singapore and Tokyo. It is an incredibly ambitious goal, considering LAX ranks near the bottom of the world’s 100 biggest airports in passenger satisfaction. Nevertheless, Garcetti is undertaking a near-total transformation of the much-maligned but vital facility.

The first step in the process was a complete overhaul of LAX’s Tom Bradley International Terminal, a job which was finished three years ago. The revamped terminal includes 18 gates, half of which can handle the massive double-decker Airbus A380 jets, and a great hall the size of three football fields. The jagged roof, meant to evoke the waves of the Pacific Ocean, reaches heights of up to 110 feet. That allows arriving passengers to look out onto the light-bathed space from glass-enclosed passageways below as they travel to customs. In the great hall, huge LED screens project images of California scenery and digital art, as well as the usual advertisements and flight information. Passengers can while away their time at upscale shops including Armani and Porsche, or eat at one of 20 restaurants that run the gamut from KFC to a steakhouse with $51 ribeyes.

The last time LAX updated its international terminal was when the city hosted the 1984 Summer Olympic Games. By the time the torch is lit for the 2024 Olympics, which L.A. hopes to host, almost every corner of the airport is expected to be upgraded. The ongoing $14 billion plan includes expanding the international terminal, remodeling all the other terminals, potentially adding new domestic concourses, finishing up runway work, introducing more efficient security checkpoints, installing new baggage carousels, consolidating rental car facilities, building new parking structures and finally, after decades of promises, connecting LAX to L.A. Metro’s growing light rail network.

Los Angeles will have plenty of competition as it tries to build the best airport in the United States. After years of coping with cost-conscious airlines and accommodating ever-changing security processes, U.S. airports are turning their focus back to improving their product. Overall spending on airport capital improvements is expected to reach $13 billion a year by 2019, a 30 percent increase compared to the previous five-year period.

From LAX and San Francisco to New York and Atlanta, airport authorities hope better facilities can attract new customers, provide for bigger aircraft and shore up their bottom lines. And, if all goes according to plan, perhaps the remade airports will even boost the fortunes of the regions they serve.

Unlike other major airports, LAX is not dominated by any single airline. Each of the four major U.S. carriers claims at least one terminal there, but none has more than a fifth of the airport’s traffic. Still, LAX is being buffeted by the forces of consolidation that have reshaped the airline industry over the last two decades. Until recently, those forces have pushed terminal modernization and other airport improvements far down on the list of airline priorities.

The carriers shoulder the bulk of the cost of running airports, by renting terminal space and by paying weight-based landing fees for incoming flights. But the carriers also have a lot of say over infrastructure improvements. If they choose to, they can block new construction. Or they can cooperate and, as with many of the LAX improvements, even provide the initial money to pay for big projects (which the airport will pay back over time).

Since the turn of this century, airlines have had to contend with two recessions and sky-high oil

prices. Bankruptcies and mergers have left four dominant domestic airlines: American, Delta, United and Southwest. As the airlines have tried to climb back to solvency, they've focused on becoming more efficient. One result of that has been further concentration of flights to major hubs such as Atlanta, Chicago, Dallas and Los Angeles.

But it's not flight destinations that have forced airlines and airports to take a new look at their facilities: It's the way flights are operated. To save money on their two biggest expenses — labor and fuel — airlines are flying bigger, fuller planes, but fewer of them. So a city that once had three flights a day to its hub airport, served by 50-seat regional jets, might now have only two flights a day on larger aircraft. The arrangement helps the airline save money on jet fuel, pilots and baggage handlers. In many cases, though, the airlines have also trimmed the excess capacity that they once provided in hopes of gaining a competitive advantage. With so much consolidation in the industry, they face less competition from one another. There's no sense losing money on empty seats, so the airlines are basically scheduling only flights they can fill.

Airlines might have been expected to increase the number of flights with the steep drop in oil prices over the last couple of years, but this has not happened. One reason, says Earl Heffintrayer, lead airport analyst for Moody's Investors Service, is a worsening pilot shortage caused by increased training requirements for new co-pilots and the mandatory retirement of baby boomer pilots at age 65. "If you have a limited supply of pilots, you want to fly them on larger planes. Smaller planes are the ones that are falling out, because you can make more money on the bigger ones," Heffintrayer says.

What all this means is that many larger airports, including LAX, are handling more passengers than ever, even though they have fewer flights going in and out than they did before the Great Recession or even before the 2001 terrorist attacks.

As a result, many of their existing gates are now inadequate. If a waiting room that was designed to accommodate 50-seat shuttles now suddenly starts handling 70- or 110-seat jets, there aren't enough places for people to sit with their carry-on baggage. Boarding lines spill beyond the gate area. Waiting times increase for nearby bathrooms and restaurants. The consequence is that many airports are having to remodel their terminals to handle the more concentrated bunches of passengers.

They are also adding new gates. "The capital improvements we saw over the last four to five years have been fixing existing facilities, making them look more modern and having a better passenger experience," Heffintrayer says. "The next wave of capital, which is really looking to take off next year, is going to start with gate expansions. We're seeing a real change in what airports are spending their money on going into the next year."

Although many of the improvements were in the works for years, the recent financial strength of the airline industry is also fueling the building spree, says Khalid Usman, a vice president with the consulting firm Oliver Wyman who has worked on airport renovations. "In 2015, the U.S. airline industry's combined profitability was $25 billion. That's historically the highest number we've ever seen in the entire history of U.S. aviation," says Usman. "That kind of profit is unknown in this type of industry. If you look at the prior 17 years [combined], that was actually negative $32 billion. It's an industry that is very cyclical."

With the return of airline profitability, San Francisco International Airport, which has seen more than a 50 percent annual traffic increase over the last nine years, has launched a five-year, $5.7 billion plan for adding and refurbishing gates, consolidating rental car facilities and extending its AirTrain. Atlanta's Hartsfield-Jackson International, the busiest passenger airport in the world, is

planning for more growth with a $6 billion effort that will add 15 gates, renovate parking garages and remodel its concourses to bring more sunlight into the buildings. Charlotte Douglas International Airport in North Carolina, which is also benefiting from surging traffic, is building nine new gates along with an expanded pre-security lobby, a new runway and a new traffic control tower.

For Los Angeles, the catalyst for the recent wave of upgrades was the arrival of the Airbus A380 in 2007. Nearly 100 Southern California suppliers contributed to the construction of the world's largest jumbo jet, which is as tall as an eight-story building and has wings 260 feet across. Despite an early commitment to LAX, Airbus later said the A380 would make its U.S. debut at John F. Kennedy International Airport in New York City. Los Angeles protested, and Airbus settled on a compromise: Two A380s touched down simultaneously at JFK and at LAX.

But LAX didn't have any good place to put the A380s once they landed. LAX crews were able to widen taxiways and make other improvements to the airfield to handle the jet's size, but there was nowhere to park them at the terminals. Because the double-decker planes are so big, they require three jet bridges for passengers to board or disembark. The large wingspans also require a lot of space between gates. So the new jets had to park at remote gates at a far corner of the airfield. "A passenger is getting on an A380 in Dubai or Abu Dhabi in what could be a 'gold-plated' boarding bridge," says Roger Johnson, the LAX official overseeing the physical improvements to the airport. "Then at LAX, they arrive in a concrete bunker, walk onto a concrete ramp and get onto a bus to get to a tunnel. That was one of the driving forces behind the Tom Bradley International Terminal."

The stakes were high. Los Angeles' economic development agency concluded in 2007 that the A380 and Boeing's Dreamliner 787 were "competitive threats" to the entire region. Airlines operating the 550-seat A380s would send the jets to airports that could handle them. Meanwhile, the fuel efficiency of Boeing's new long-haul jet, which carries half the passengers of the A380, could make it easier for overseas flights to skip over LAX completely. That was especially bad news, because overseas flights are highly lucrative. The economic development agency estimated that scheduling one daily transoceanic flight to LAX in 2006 generated $156 million in wages and added $623 million a year to the region's economic output. "Southern California," the agency concluded, "can ill afford to lose the competition for overseas routes."

Luckily for Los Angeles, the A380 arrived at about the same time the airport settled long-disputed lawsuits over its master plan. Finally, the airport could start building. The first task was replacing most of the international terminal.

Garcetti now uses the new international terminal as a selling point to lure even more international flights to LAX. "We would fall all over ourselves to bring a company that would produce $300 million a year here. It'd be all over the news," Garcetti says. "But people forget that one flight is worth about $1 billion a year." Airlines seem to like L.A.'s pitch. LAX now handles more A380 flights (14 a day) than any other airport in this country. It is the only U.S. airport with three daily nonstop flights to and from China. And LAX has surpassed its rival JFK in connections to Asia, with 207 flights a week as of last year, compared to 121 for the New York airport.

Many of the flashy features in the Tom Bradley International Terminal are being included in renovations to the airport's other terminals. They aren't just designed to show off. Most of them have practical purposes as well.

As part of United Airlines' renovation of its terminal at LAX, it is including "smart lanes" at its TSA security checkpoint. United is taking a page out of the playbook of Delta, which first tested the idea in Atlanta. With smart lanes, passengers each get their own counter space, side-by-side with those of other passengers, to load their items into bins. The system allows people to go at their own pace,

because they're not stuck in line behind someone who might be slower. United officials say the smart lanes will reduce security wait times by 25 percent.

LAX is also one of a few dozen airports currently working with U.S. Customs and Border Protection to use technology to speed up the process of clearing customs. The automated passport control system lets arriving passengers use kiosks for their initial screening.

Airport managers hope better use of technology, among many other things, will help boost the customer experience. Last year, LAX trailed only LaGuardia and Newark airports in J.D. Power's rankings for lowest customer satisfaction among U.S. airports. Mike Taylor, a J.D. Power airport analyst, says technology is one way to make customers happier. "The highest-rated portion of the airport experience is check-in," he says, "because it's become more and more automated over the years."

But terminal improvements can only go so far in making customers happier. Only 30 percent of passengers' satisfaction is associated with the structure itself. "A new building will not solve all of your problems," Taylor says. "It won't solve all your problems because the same traffic pattern is present when you step outside the building, the same congestion." The frustration with getting in and out of airports is only getting worse as airports become more crowded.

That's what the next phase of LAX's improvements is meant to address.

LAX is the third-busiest airport for passengers in the country, but that doesn't tell the whole story. Atlanta and Chicago's O'Hare airports handle more people, but many of them simply pass through as they transfer to other flights. LAX, on the other hand, is the top airport in the country for starting and ending trips. In other words, it has to get more passengers in and out than any comparable facility in the country.

The traffic problems at LAX are made worse by the fact that just about the only way to get to the terminals is with a car, bus or van, and all of those vehicles follow the same double-decker road in a U-shape past all nine terminals. Forty percent of the vehicles are commercial shuttles for hotels, rental car agencies or parking lot operators. One trip around the loop can easily take more than half an hour.

The growing popularity of air travel is making the traffic worse. Vehicles made more than 90,000 trips a day through LAX's main terminal loop this summer, and that number grew to nearly 95,000 on holiday weekends. "It's reached a state where it's untenable," says Deborah Flint, the CEO of Los Angeles World Airports, the agency that runs LAX. "The only real, effective option is to bring the mass transit connections to the airport."

So Los Angeles is joining a growing list of cities building new rail connections to their airports. Denver; Oakland, Calif.; Phoenix; and Washington, D.C.'s Dulles Airport all either completed rail connections recently or are building them now. Garcetti says one reason he pushed to bring in Flint, who previously led the Oakland Airport, and L.A. Metro CEO Phillip Washington, who headed Denver's transit system, is that both had experience creating rail connections to their respective airports.

LAX's rail connection will be especially ambitious, because it depends on both the construction of an automated "people-mover" train at the airport and the completion of a new north-south light rail route by L.A. Metro.

The 2.25-mile people-mover route would run down the center of the U-shaped terminal area, so

passengers from both sides would be able to cross over pedestrian bridges to get on at one of three stations. The free trains would arrive every two minutes.

The automated people-mover trains would stop at an intermodal center, which would have parking and shuttle services. It would be convenient to reach by car. But drivers could turn around or park before they get trapped in traffic near the terminals. Once they're at the facility, passengers would be able to check in, print their boarding passes and get information before they catch the people-mover to the terminals. From the intermodal center, the people-mover would then go to the Metro station, which would also offer several bus connections. Work is already halfway completed on the 8.5-mile rail line, which is part of a much larger Metro expansion effort that began in 2008. The first trains are scheduled to start running along the Crenshaw/LAX line in 2019.

Finally, nine minutes after leaving the first station, the people-mover would stop at a consolidated rental car facility, which would bring some two dozen of LAX's far-flung rental car lots under one roof. Both the automated people-mover and the rental car facility would be operated as public-private partnerships.

The overarching idea of the $5 billion project is to move as much traffic as possible away from the central terminal area. Just relocating the commercial shuttles to one of the intermodal facilities could have a huge impact, since they make up so much of the traffic that circles the terminals now. Rental car companies alone currently account for 3,200 shuttle trips a day around the loop, which would be eliminated.

Giving passengers transportation options is key to attracting the most desirable customers, especially those coming from overseas. "International passengers — there were over 20 million of them [at LAX] last year — expect an international city gateway that is connected to many different transportation options," says Flint. "It's par for the course for a major city like Los Angeles."

For Garcetti, who has made infrastructure projects big and small a major focus of his administration, there is also an element of pride at stake in connecting LAX to a rail line, something that's been promised for generations. "When I was campaigning and saying I would, after 50 years of talk, finally bring public transportation to the airport, it was an applause line from the furthest point away from the airport in the city to the next-door neighbors," he says. "It's not only an amenity, it's a symbol of what we couldn't do and we wondered if we ever would do. Are we capable of big projects? Are we capable of building again? That was a core part of our identity, but it was slipping through our fingers. I think this is a way of solidifying that."

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BY DANIEL C. VOCK | DECEMBER 2016

P3 Digest for Week of December 6, 2016

Powered by P3 INGENIUM the most comprehensive source for P3 project updates in North America.

Read the Digest.

NCPPP

December 6, 2016

TAX - PENNSYLVANIA

City of Philadelphia v. Lerner

Supreme Court of Pennsylvania - November 22, 2016 - A.3d - 2016 WL 6873039

City brought collection action against taxpayer. Following a bench trial, the Court of Common Pleas found taxpayer waived his right to challenge net profits tax and/or business income and receipts tax assessments, and awarded city $280,772.67, which included principal liability of $74,907, $85,828.05 in interest, and $120,037.62 in penalties.

Taxpayer appealed. The Commonwealth Court affirmed. Taxpayer appealed.

The Supreme Court of Pennsylvania held that taxpayer waived for purposes of appeal his argument that his failure to exhaust administrative remedies within the Department of Revenue did not prevent him from challenging city's assessments, where taxpayer failed to raise the issue in the trial court.

COUNTIES - ILLINOIS

Blanchard v. Berrios

Supreme Court of Illinois - December 1, 2016 - N.E.3d - 2016 IL 120315 - 2016 WL 7007820

County inspector general brought action against county assessor for declaratory judgment that it was obligated to comply with inspector's investigation into circumstances surrounding grant of exemptions from property tax and to comply with subpoena.

The Circuit Court entered order requiring assessor to produce subpoenaed documents. Assessor appealed. The Appellate Court affirmed. Assessor's leave to appeal was granted.

The Supreme Court of Illinois held that:

- County ordinances creating office of inspector general and imposing duty on elected county officials to cooperate with investigation by inspector general were proper exercise of county board of commissioners' constitutional authority to exercise those duties, powers and functions provided by law and those provided by county ordinance";
- Ordinances were proper exercise of board' statutory authority to "alter any other duties, powers or functions or impose additional duties, powers and functions upon county officers";
- Assessor did not have authority to oversee or supervise its office free from oversight or investigation by inspector general;
- Ordinances did not impermissibly conflict with county assessor's home rule authority to assess property taxes and grant exemptions from same;
- Board had home rule authority to enact ordinances creating office of inspector general and imposing duty on elected county officials to cooperate with investigation by inspector general; and
- County assessor, as elected official, was not separate from county, as local unit of government recognized under Illinois Constitution, and thus, was subject to ordinances enacted by board.

What Happens When the IRS and Issuer Agree to Disagree?

My last blog post was about how, as a result of a change in the Internal Revenue Code (the "Code"), the IRS will be altering the manner in which it audits many partnerships (and limited liability companies that are taxed as partnerships under the Code). In a nutshell, for tax years beginning on or after January 1, 2018, the IRS may assess a tax deficiency against certain partnerships rather than flowing the taxable income adjustment at the partnership level through to the individual partners and then collecting the additional tax from each individual partner. This change in the Code was deemed to be a revenue raiser due to the increased efficiency in assessing the tax against the partnership rather than the individual partners. This streamlined partnership audit process is similar to the IRS being permitted to settle an IRS audit involving tax-exempt bonds with the issuer or conduit borrower rather than having to assess a tax deficiency against the various bondholders and collecting the tax from each individual bondholder. This got me thinking . . . what happens if the issuer or conduit borrower and IRS cannot agree to a resolution when the IRS believes the tax-exempt bonds are taxable?

As you know, the IRS treats the issuer as the "taxpayer" when it begins an audit of tax-exempt bonds even though the bondholders will ultimately be the "taxpayers" if the tax-exempt bonds become taxable. For example, under IRS guidelines, the IRS sends the information document requests ("IDRs") to the issuer of the tax-exempt bonds and is authorized to reach a settlement with the issuer. In addition, it is the issuer of the tax-exempt bonds that has the ability to either (a) request a technical advice memorandum ("TAM") from the IRS national office with respect to one or more issues relating to the tax-exempt bonds, or (b) after receiving a proposed adverse determination from the IRS agent, request that the matter be referred to the IRS' Office of Appeals ("Appeals"). Although the goal of Appeals is to settle cases with the Appeals' officer acting as an independent reviewer, sometimes the parties cannot agree. If settlement attempts at Appeals between the IRS agent and issuer are unsuccessful, the IRS will issue a final adverse determination that the tax-exempt bonds are now taxable. If the IRS has not already done so, around the same time that the IRS issues the final adverse determination, the IRS will contact the trustee for the subject bonds and request the names and address of all bondholders thereof.

Once the final adverse determination is made that the tax-exempt bonds are taxable, the issuer no longer has any rights in the audit process. Rather, the IRS will begin treating the bondholders as the "taxpayer" from that point until final resolution of the tax controversy. In general, the IRS has three years from the date that a bondholder filed his or her income tax return reporting tax-exempt interest to assess a tax on the now allegedly taxable interest. The IRS will assess this tax by sending each bondholder a statutory notice of deficiency that is oftentimes referred to as a "90 Day Letter." The 90 Day Letter sent to each bondholder will set forth the basis for the tax deficiency and will also set forth the amount of tax, interest and penalties owed by such bondholder. The bondholder will have 90 days to respond by filing a petition challenging the assessment in the U.S. Tax Court. In the alternative, the bondholder could pay the assessed tax, interest and penalties due, but then file a claim for refund. At this point, the bondholder could attempt to reach a settlement with the IRS, although there is no formal procedure in place to do so. The incentive for both the bondholder and IRS to settle, however, would be to avoid the costly litigation process discussed below.

After the bondholder's refund is denied by the IRS (which it presumably would be), the bondholder could then file a claim for refund in the U.S. district court with jurisdiction over his or her tax residence or in the U.S. Court of Federal Claims located in Washington D.C. If the bondholder was to lose at the district court or Tax Court, the bondholder could appeal to the appropriate U.S. Court of Appeals. Similarly, if the bondholder was to lose at the U.S. Court of Federal Claims, he or she could appeal to the U.S. Court of Appeals for the Federal Circuit, which is also located in Washington D.C.

If the bondholder then loses at the appellate level, the bondholder could appeal to the U.S. Supreme Court. However, as you know, the U.S. Supreme Court could decide not to hear the case (i.e., by denying the taxpayer's writ of certiorari), thus affirming the appellate court's decision.

Assuming that the bondholder hires legal counsel to help navigate the above-described litigation, the process could become very costly for the bondholder even if he or she ultimately wins the case. This bondholder-by-bondholder litigation process would also be very expensive for the IRS. Accordingly, it is a good thing that the vast majority of tax controversies involving tax-exempt bonds are settled by the issuer and IRS before a final adverse determination is issued by the IRS. This is because the issuer has a very strong incentive to settle with the IRS so that the marketplace does not react negatively the next time the issuer wants to issue tax exempt bonds. In addition, from the IRS' standpoint, it is far more efficient to settle with the issuer than to pursue each bondholder. Therefore, thankfully, it is very rare for the IRS and issuer to agree to disagree.

Squire Patton Boggs

The Public Finance Tax Blog

By Cynthia Mog on December 7, 2016

The Supreme Court Case That Could Bankrupt Religious Schools and Hospitals.

Advocate Health Care Network v. Stapleton pits financially strained organizations against their own workers, who fear their promised pensions may not be there when they retire.

A new case on the U.S. Supreme Court's docket could potentially involve millions of American employees and lead to billions of dollars' worth of litigation. The justices' decision could affect the viability of religiously affiliated orphanages, hospitals, schools, and nursing homes, and it could also threaten the financial security of a generation of their workers, fast heading toward retirement.

On its face, *Advocate Health Care Network v. Stapleton* and the two other cases it's consolidated with may seem boring—after all, they're about federal regulations on pension plans for church-affiliated hospitals. But these cases are actually the culmination of a new, vicious fight over the rights of employers that are loosely affiliated with religious institutions, and how they should have to pay retirement benefits to their employees in accordance with federal law.

The three consolidated cases in question seem likely to turn on something deceptively simple: the single word "established." In 1974, Congress passed a law called the Employee Retirement Income Security Act, or ERISA, which, among other things, created guidelines for defined-benefit retirement plans, otherwise known as pensions. The two most relevant requirements in these cases have to do with good planning and risk mitigation: Employers have to put money into their employees' retirement plans in a responsible way, so that they can afford to pay out big sums of money once those employees get old. But, if a company is in financial trouble when it comes time to pay out the promised benefits, there's a safety net: ERISA established the Pension Benefit Guaranty Corporation, or PBGC, which is effectively a government insurance agency for underfunded pension plans.

These rules do not apply to houses of worship. Benefit plans "established and maintained" by these groups are exempt. The reasons for this are a bit opaque, said Norman Stein, a professor at Drexel

University's Kline School of Law, but an early draft of the law suggests Congress "didn't want churches to have to open their books to the government." Legislators also figured religious groups weren't the problem: "People felt that it's the church—it's not going to let its plan fail and screw its employees," he said. "Some of the writing about the statute has speculated that this was a reason, too—churches are moral institutions that are going to stand behind their promise [to pay for people's pensions], because that's what religions do."

When ERISA first passed, it wasn't clear whether this exception would apply long-term to religious organizations that weren't houses of worship, like Jewish day schools or Catholic hospitals. In 1980, Congress amended the law to clarify that religiously affiliated groups can also maintain what's called a "church plan," so long as they satisfy certain requirements. For years, the IRS allowed religiously affiliated groups to offer these "church plans" without much controversy. Since 1982, according the hospitals' Supreme Court petition, it has sent over 500 letters granting ERISA exemptions to organizations as diverse as the Princeton Theological Seminary and the Little Sisters of the Poor, an order of nuns.

Three years ago, employees across the country began filing lawsuits claiming that these organizations shouldn't be exempt, after all. Current and former employees of three health-care systems filed suit against their employers: Dignity Health in California and Saint Peter's Healthcare System in New Jersey, which are both associated with the Roman Catholic Church; and Advocate Health Care Network in Illinois, which is jointly associated with the the Evangelical Lutheran Church in America and the United Church of Christ. This is where everything comes back to "established": Because these pension plans weren't "established" by actual churches, the employees argue, they shouldn't be exempt from ERISA.

The conflict matters for a few reasons. First, both sides arguably stand to lose incredible amounts of money. The Pension Rights Center, which supports the hospital employees, has identified at least three cases of allegedly failed church plans. When the owners of St. Anthony Medical Center in Illinois terminated one of its pension plans in 2012, the president and CEO told employees she was "very sorry for this surprising and disappointing news." In 2013, the president and CEO of St. Mary's Hospital in New Jersey wrote a letter to employees stating that "there simply are no funds remaining in the retirement plan's trust." And something similar happened last month at the now-closed St. James Hospital in New Jersey—the liability in that case is still murky.

Because these plans were not insured by the PBGC, they have left or may leave huge numbers of workers with less retirement money than they were promised. Hospital employees and their allies argue that church plans are a way for large employers to avoid complying with federal regulations—ones that were explicitly put in place to protect workers. Under church plans, a "[pension] promise is only as good as the word of the hospital," Stein said. "If the hospital gets into financial trouble and the plan is not well-funded, you're not going to get paid your benefits."

But if these hospitals lose, they will also face intense financial consequences—and so will other religiously affiliated organizations across the country. Two appellate courts, the Third and Seventh Circuits, recently ruled against them, and "it is hard to overstate the burden and havoc these two decisions have created," the hospitals wrote in their petition to the Supreme Court. If the lower-court rulings are affirmed, "this will mean renegotiating contracts with employees whose benefits are covered by collective-bargaining agreements, revamping benefit structures, redesigning pension-funding policies, and overhauling budget plans."

There will also be future consequences: Under ERISA, employers are required to pay premiums to the PBGC and fund their pension plans at certain levels. When the law was created, "There was … a feeling that these kinds of church groups could not afford the cost of an ERISA plan," said Howard

Shapiro, a lawyer at Proskauer Rose in New Orleans, who has defended a number of hospitals that are being sued over their church plans. If these organizations are retroactively forced to comply with ERISA, they could face significant, and potentially ruinous, financial hardships.

The irony is that both religious groups and their employees could end up suffering if these hospitals lose at the Supreme Court. The church plans at issue "are still the old style of defined-benefit plans which everyone wishes they still had but don't have anymore," said Colleen Medill, a law professor at the University of Nebraska and counsel at the Koley Jessen law firm. "If [the hospitals] lose, and they pay whatever they have to pay in damages, they will probably, as a pure financial decision, freeze or terminate these plans and move over to a defined-contribution kind of plan."

Defined-contribution plans typically include options like 401 (k) features, which have become much more popular in recent years—if you look at graphs of the number of organizations that have switched over to these plans, "they kind of look like the Nike swoosh," said Medill. The reason behind this rise is straightforward: Defined-contribution plans shift the burden of bad economic times from employers to employees. A 401 (k) plan is great when the stock market is doing well, but "when the market goes down, maybe you don't love that 401(k) plan so much because you bear the risk of market volatility," Medill said. "In terms of retirement-income security, is it better to have an account that goes up and down every day with the market? Or is, it better to know that when I retire, I'll get $3000 a month for life?"

In some ways, it's surprising that all these issues are coming out now—ERISA has been around for 42 years, and Congress clarified the nature of church plans in 1980. In part, the delay is due the nature of retirement plans: People pay in over a long period of time, and they might not realize the consequences of being part of an uninsured pension plan until they're about to hit 65 and realizing they don't have the money they need to live.

But the delay also has to do with the way the IRS has dealt with religiously affiliated groups, Stein argued. "This went on for as long as it did [because] there was no regulation, no formal rule-making," he said. During the 1990s and into the 2000s, a large number of religiously affiliated organizations won permission from the IRS to convert their pension plans into church plans. There were big incentives to do so: If they won church-plan status, the PBGC would refund a portion of the premiums they had paid in the past, which meant anything from a few thousand dollars to millions. Groups would get a private-letter ruling from the IRS, a form of guidance that does not set precedents for other taxpayers. But until 2011, when the agency began facing media scrutiny for what one amicus brief called "church-plan conversions," organizations weren't required to tell employees about the changes to their benefits plans. "By and large, employees didn't even know it was happening—churches didn't write a letter saying, 'By the way, we just decided to screw you,'" said Stein.

Around the time a handful of plans began failing, a wave of lawsuits began—dozens have been filed since 2013, according to court documents. "There's a whole movement among class-action lawyers where they see the potential to sue a very large plan and collect a lot of money in attorney's fees and have some benefits for the employees," said Medill. If the hospital employees win, "these employers are going to have to come up with a lot of money to fund these plans to come into compliance with ERISA."

Not all churches and religious organizations dislike ERISA—in fact, any house of worship or religiously affiliated group can voluntarily choose to be subject to the law. "There are reasons to do that—namely to take advantage of federal preemption of state laws," said Medill. ERISA limits the scope of what plaintiffs can win in a lawsuit, for example—if they operate in states that are more permissive, employers might find ERISA's limited legal liability attractive. But that's not what's

happening in these cases. “The real issue here is the funding requirement for the pension plans. If the plans were subject to ERISA, the employers would have to pay a lot more to fund these plans,” Medill said.

It’s hard to know how extensive the consequences of this Supreme Court decision could be. But they may not just be financial—Shapiro also sees the potential for religious-freedom conflicts. Under their church plans, religiously affiliated organizations can choose how they invest their money—pacifists can avoid putting money behind ammunitions companies, for example, or pro-life faiths can steer clear of investments related to abortion. Because ERISA imposes specific investment responsibilities on employers, Shapiro said, compliance “[could] actually conflict with some religious principles that are very important to these entities.”

These cases don’t break down along clear lines of good vs. evil. Various sides are trying to protect people who have compelling, conflicting needs, including employees who want to be able to survive retirement and hospitals with missions to follow their teachings and serve the poor. Everyone involved likely has some religious stake—many people who spend their lives working for religious hospitals are probably just as faithful as the organizations that employ them. There’s only one group that will really walk away victorious: As Medill put it, “This will be good for employment for ERISA lawyers.”

THE ATLANTIC

BY EMMA GREEN

A Roadmap For Muni Investors On Public-Private Infrastructure Partnerships.

- For municipal bond investors, the private sector’s increasing role in financing public transportation projects may provide an opportunity.
- Also known as P3s, these partnerships are increasingly using muni bonds as a cornerstone of their capital structures.
- Here’s a primer on how P3s work and how the muni bonds used to finance these projects could potentially offer yield and diversification opportunities.

The increasing role of the private sector in financing public transportation projects may provide an investment opportunity for municipal bond investors. In fact, President-elect Donald Trump has called for $1 trillion investment in infrastructure, much of which will depend on public-private investment for funding. Below is a review of these types of infrastructure projects, known as private-public partnerships (P3s), which have been a response to chronic funding shortages at the governmental level, and which are increasingly using municipal bonds as a cornerstone of their capital structures. These types of municipal bonds may offer incremental yield and portfolio diversification for municipal bond portfolios.

Continue reading.

Wells Fargo Asset Management

By Lyle Fitterer, CFA, CPA

Dec. 4, 2016 3:57 PM ET

Report: Michigan Needs $4 Billion More Per Year to Close Infrastructure Spending Gap.

New study from Snyder-appointed commission suggests state needs better inventory management, planning

LANSING — Michigan needs to come up with nearly $4 billion more per year if the state is to close a gap in spending on its infrastructure needs, according to a report released Monday by a commission formed to study the issue.

The 21st Century Infrastructure Commission, appointed by Gov. Rick Snyder, found that the state would need to spend in excess of $60 billion more over 20 years just to fix existing infrastructure systems. (That would come to about $3 billion per year; the report did not indicate how much more than $60 billion would be required over the next two decades. A spokesman for Snyder said the annual $4 billion investment figure could fluctuate.)

Continue reading.

December 05, 2016 8:00 a.m.

Fitch Rates $500MM Chicago Board of Ed (IL) Bonds 'A' on Special Revenue Analysis; Outlook Stable.

Fitch Ratings-New York-08 December 2016: Fitch Ratings has assigned an 'A' rating to the following Chicago Board of Education, IL bonds:

–$500 million dedicated capital improvement tax bonds, series 2016.

The bonds are expected to price the week of Dec. 12. Proceeds will finance specific capital projects listed in the authorizing resolution.

The Rating Outlook is Stable.

The Board of Education's Issuer Default Rating (IDR) is 'B+' with a Negative Rating Outlook. The distinction between the 'A' rating on the series 2016 bonds and the 'B+' IDR reflects Fitch's assessment that the pledged revenues meet the definition of "special revenues" under the U.S. Bankruptcy Code and therefore, bondholders are legally insulated from any operating risk of the board.

SECURITY
The bonds are secured by a first priority lien on revenues from the capital improvement tax (CIT), a district-wide property tax.

KEY RATING DRIVERS

SPECIAL REVENUE ANALYSIS: The 'A' rating on the dedicated CIT bonds is based on a dedicated tax analysis without regard to the board's financial operations. Fitch has been provided with legal opinions by board counsel that provide a reasonable basis for concluding that the tax revenues

levied to repay the bonds would be considered ‘pledged special revenues’ under Section 902(2)(e) of the U.S. Bankruptcy Code in the event of a board bankruptcy.

PREDICTABLE REVENUES: Growth in the levy (currently $47.9 million) is set by state statute at the rate of inflation; however, the levy jumps up in 2033 by $142.5 million, then resumes inflation-based growth. Debt service schedules are sized to the minimum levy, without assuming inflationary increases.

STRONG RESILIENCE OF PLEDGED TAX SECURITY: A multi-year levy with pre-determined minimum amounts combined with limited volatility in historical property tax collection rates support strong financial resilience for debt service coverage throughout economic declines.

RATING SENSITIVITIES

PROPERTY TAX COLLECTION RATES: The rating is sensitive to declines in property tax collection rates of a scale that would materially erode the protection inherent in the expected coverage ratios, given the fixed-dollar levy, 1.1x additional bonds test and moderate historical delinquency experience.

CREDIT PROFILE
The Chicago Board of Education provides preK-12 education to over 390,000 students within the city of Chicago. Its taxing jurisdiction is coterminous with the city of Chicago. The Chicago Public Schools (CPS) manages the school system, which is composed of 673 school facilities.

CIT VIEWED AS SPECIAL REVENUES
The specific features of the bonds meet Fitch’s criteria for rating special revenue obligation debt without consideration of the board’s general credit quality. Fitch believes bondholders are effectively insulated from the operating risk of the board as expressed in its IDR.

Fitch sets a high bar for considering local government tax-supported debt to be secured by special revenues, which provide security that survives the filing of a municipal bankruptcy (in preservation of the lien) and benefit from relief from the automatic stay provision of the bankruptcy code. We give credit to special revenue status only if, in our view, the overall legal framework renders remote a successful challenge to the status of the debt as secured by special revenues under Section 902 (2) (e) of the U.S. Bankruptcy Code.

Fitch has identified a number of elements we consider sufficient to reduce the incentive to challenge the special revenue status given the definitions outlined in the bankruptcy code. These include clear restrictions on the use of pledged revenues for identified projects and clear separation from the entity’s operations. Fitch has undertaken an extensive review of the statutory provisions that govern the use of the CIT. Those provisions, along with the legal documents governing the bond issuance, provide sufficient strength for Fitch to rate the CIT bonds higher than the IDR.

The bonds are secured by a first priority lien on CIT revenues. The board is authorized under the Illinois School Code to levy the CIT on all taxable property within the district, which is coterminous with the city of Chicago. State statute limits the permitted uses of CIT revenues to include construction, acquisition and equipping of school and administrative buildings, and site improvements. The board has identified specific capital projects in the bond resolution that may be funded either by bond proceeds or by residual CIT revenues. Any amendments to the project list must be passed by board resolution. The revenues legally cannot be used for general operations of the board.

STRONG RESILIENCE OF PLEDGED CIT SECURITY

The multi-year levy supporting debt service on the bonds required and received approval by the Chicago city council; however, no further approvals are necessary for the levy to be extended and collected for the life of the bonds. The multi-year levy is set by resolution at the time of bond issuance and no policy action is required to offset potential declines in assessed value. Importantly, the minimum amount of the levy is knowable in advance and the debt service schedule is sized to that, allowing for a minimum of 1.1x coverage. This leaves only the risk of diminishing collection rates, which historically have been well within the norm for U.S. municipalities.

To evaluate the sensitivity of the dedicated revenue stream to cyclical decline, Fitch considers both revenue sensitivity results (using a 1% decline in national GDP scenario) and the largest decline in revenues over the period covered by the revenue sensitivity analysis. Since the CIT revenue history is insufficient to conduct this analysis, Fitch uses a proxy of overall property tax collection rates, which it believes approximates future risk to CIT revenue sufficiency.

Based on historical property tax collection rates, Fitch's Analytical Sensitivity Tool (FAST) generates a fairly modest 1.7% scenario decline in pledged revenues. The largest cumulative decline was a 2.7% decline during the recession between 2008 and 2009.

Given the 1.1x coverage, pledged revenues could withstand a 9% decline before they were insufficient to fully cover debt service. This is 3.3x the largest actual cumulative decline, or 5.3x the recessionary impact estimated in Fitch's FAST scenario. Recent tax increases by Chicago-area governments could contribute to delinquencies beyond historical experience in a recession, but even so, Fitch believes collection rates would continue to support financial resilience consistent with an 'A' rating.

Chicago acts as the economic engine for the Midwestern region of the United States. The city's residents are afforded abundant employment opportunities within this deep and diverse regional economy. The city also benefits from an extensive infrastructure network, including a vast rail system, which supports continued growth. The employment base is represented by all major sectors with concentrations in the wholesale trade, professional and business services and financial sectors. The city's economic indicators are mixed with elevated individual poverty rates and average per capita income levels, but strong educational attainment levels. Recovery from the recession has been slow but steady. The unemployment rate is almost half of its recessionary peak but remains elevated relative to the state and nation. Population losses appear to have reversed.

ADEQUATE STRUCTURAL PROVISIONS

The additional bonds test dictates that projected CIT revenues must provide at least 1.1x coverage of annual debt service in each bond year. Projections may not include assumptions for inflationary increases prospectively. Fitch's analysis assumes the pledged revenues would be leveraged to the full extent allowable under the additional bonds test.

Under the flow of funds, the CIT revenues are collected by the county collectors of Cook and DuPage Counties. The board has directed the collectors to transmit the CIT revenues directly to an escrow agent. The escrow agent transfers revenues needed for payment of debt service to the bond trustee daily. Revenues in excess of those required to meet annual debt service may be available to reimburse CPS for authorized capital expenditures.

The board covenants not to revoke the direction to the county collectors as long as the bonds are outstanding. Based upon review of bond counsel opinions Fitch believes that any future attempt to revoke the direction to the county collectors would be contrary to state statute.

The debt service reserve requirement of 14% of maximum annual debt service (MADS) will be

funded with bond proceeds.

The board's 'B+' IDR with a Negative Outlook reflects CPS's chronic structural imbalance, slim reserves and weak liquidity position which are exacerbated by rising long-term liability costs, an historically acrimonious labor relationship and the lack of an independent ability to raise revenues. For more information on the board's IDR, please see 'Fitch Rates $426MM Chicago Board of Education (IL) ULTGOs 'B+'; Outlook Negative' dated Nov. 7, 2016.

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GFOA Debt 101 Resource Center.

Governmental entities have been using debt for more than 200 years to fund public infrastructure such as government buildings, water distribution systems, schools, police stations, and many other projects that require significant capital investment. When a government issues debt, it receives an infusion of cash to build a project; in return, the government repays the bond purchasers over time, plus interest. The use of debt allows a government to complete a capital project with a repayment schedule that spreads the cost of that project over its useful life, and the bond purchaser receives a reasonably reliable source of investment income.

Before issuing debt, a government needs to consider many factors. Appropriate planning and understanding help provide the most favorable results to the issuer while avoiding unnecessary risks and negative consequences. Debt issuance requires working with a number of partners, each with a specific role. The debt issuance will result in a financing agreement that is legally binding, and it is critically important that government officials understand the basic terms of the agreement and what the agreement commits them to do.

To ensure that issuers have all the information they need, the GFOA's Committee on Governmental Debt Management has created two new resources. Debt 101, Volume 1, provides a high-level outline of the debt issuing process and important considerations, and is intended to be a resource for the first-time or infrequent bond issuer. Debt 101, Volume 2, discusses what needs to happen after the issuance is completed.

Debt 101 (Volume 1) – Issuing a Bond

Debt 101 (Volume 2) – Responsiblities After Issue

New Issue Calendar Coming to EMMA.

Beginning in January 2017, the Electronic Municipal Market Access (EMMA®) website will provide free, convenient access to a new issue calendar enabling individual investors, issuers and other market participants to see new bond issues coming to market as well as final pricing scales for bond issues sold through competitive and negotiated sales.

Individual investors can use the calendar to locate upcoming bond offerings of interest. The new issue calendar provides issuers that may be planning on issuing a new security the ability to identify, monitor and compare prices of similar issues that are coming to market or have been recently sold. The Municipal Securities Rulemaking Board (MSRB) is providing the calendar to help all market participants make decisions that are right for them.

Learn more about other tools and resources on EMMA.

IRS Publishes Issue Price Definition for Tax-Exempt Bonds.

Final issue price regulations in Treasury Decision 9801 were publicly filed with the Federal Register on December 8 and have been published as of December 9. The effective date will be 180 days after publication of the final regulations.

The final regulations include a special rule for competitive sales.

Federal Register Final Regulations

Muni Disclosure Responsibility Would Shift to Issuers from Underwriters in New Bill.

Rep. Gwen Moore (D-WI) has introduced a bill that would make state and local government issuers or borrowers responsible for bond-related information disclosure, rather than underwriters. Under current SEC rules, muni issuers are not regulated with regards with muni disclosures. The bill would also allow the SEC to establish baseline mandatory disclosure requirements for primary offerings.

Bill Text

How Big-Box Retailers Weaponize Old Stores.

Merchants such as Walmart are using a novel legal tactic to sharply lower their property taxes.

Tucked away on the northern edge of Michigan's rugged Upper Peninsula, Sault Ste. Marie is bracing for the battle of its life. The tourist town is heading to court in early 2017 to fight Walmart Stores, which seeks to cut $286,000 off its annual property tax bill on a local store. Using what critics call the "dark store loophole," Walmart is following in the footsteps of big-box merchants including Lowe's and Target by arguing that its bustling store should be assigned about the same value for tax purposes as one that's been vacant for years, hundreds of miles away.

The financially strapped town of 14,000 faces legal bills of about $100,000 to take on the retailing giant. The cost of the battle that started in 2014 already has forced local authorities to slash budgets for everything from senior meals and the local animal shelter to police and fire pensions. Now its leaders have decided they've been pushed around long enough. "It is like David and Goliath," says Jim German, the county administrator in Chippewa County, which includes Sault Ste. Marie. "We are going to give it our best shot, because it isn't fair."

The city has tried for years to keep the dispute out of court to avoid the legal fees, agreeing with Walmart in 2014 and 2015 to lower the store's local taxes by a total of $103,000. This year, Walmart has gone too far, German says. It wants its store, currently assessed at $63 a square foot, to be valued at $16 a square foot based on sales of similar-size vacant properties across the state—less than what some local small businesses pay. Chippewa County is hedging its bets in case of a loss, freezing salaries for all nonunion employees.

Walmart, which annually pays $3.3 billion in property taxes, state income taxes, and franchise taxes plus $15 billion in state and local sales taxes, says it pays its "fair share" of property tax in Michigan based on standard appraisal methodology. "When we can't reach an agreement, we seek clarification through the legal process for a fair market value of our property," says Walmart spokesman Lorenzo Lopez.

The dark store tax argument has been gaining use since a Michigan court accepted it in 2010. In that case, the judge agreed that a Target store in a depressed Detroit suburb was worth about half the city's valuation. From that one ruling, which turns on its head the traditional way municipalities value businesses based on the cost of acquiring the land and building the structure, big-box retailers including Lowe's, Best Buy, and Menards have spread out across the country, taking to court more than 100 townships, cities, and counties in at least a dozen states over the past four years. In most cases the stores have prevailed, saving millions of dollars in property taxes, according to the National Association of Counties. Two-thirds of Michigan's counties have lost more than $75 million in property taxes since 2012 as a result of the ruling. Indiana estimates it could lose $120 million in tax revenue annually if the strategy takes hold.

That's left many municipalities scrambling to cope with lost revenue. Library hours have been curtailed, roads have gone unpaved, and police and fire departments have made do with aging equipment. County officials in Alabama and Texas, where Lowe's only recently began filing dark store suits, say they fear a similar fate.

"If the big-box folks do this, then you'll have it spill down to the banks, the fast-food places, the drugstores," says Don Armstrong, property tax commissioner for Shelby County, Ala., where Lowe's

is pursuing a challenge. “It would just multiply and have a domino effect.”

Target, noting that it wants to ensure its properties are assessed at fair market value, said in a statement that it “remains committed to supporting the communities in which we do business, and this includes paying a fair share of property taxes.”

Michael Shapiro, a Detroit real estate tax attorney who pioneered the dark store argument, says he’s not insensitive to the financial needs of communities, but “whether it is unfair or not doesn’t have anything to do with me. I’m just looking at what the law is.” For more than 40 years, Shapiro has made a career out of helping businesses challenge property tax bills. A lawyer with the Detroit firm Honigman Miller Schwartz and Cohn, he made a name for himself representing car companies, successfully arguing their plants’ taxes should be based on the values of closed factories. Years later, he saw a similar opportunity in big-box stores. He made his first such successful case in 2010.

Typically, local property tax assessors set values of such stores based on the purchase price of the land plus the cost of construction, less depreciation. Shapiro believed a more accurate way to measure the value was to use comparable sales of similar properties, the way a house is valued for tax purposes.

He began amassing comparable sales data to make a case that the value of a big-box store on the market was far lower than what tax assessors had determined because they were built to suit the needs of a specific owner—the way “a suit would lose its value once it was tailored to a specific person,” says Shapiro.

There’s now a thriving cottage industry of lawyers, tax representatives, and appraisers helping retailers initiate dark store challenges. Larry Clark, director for strategic initiatives at the International Association of Assessing Officers in Kansas City, Mo., says lawyers and tax representatives typically target smaller towns that are less able to mount a vigorous defense. “They pick the low-hanging fruit,” he says. “It probably costs $50,000 or more to litigate one big-box chain,” says Jack Van Coevering, who’s represented small towns in Michigan that have faced big-box valuation challenges. “If you are a township with a whole bunch of these properties, imagine that.”

Towns can find it hard to attract companies to fill vacant buildings that bring down valuations. Often a closed store has deed restrictions that prevent another big-box retailer from moving in, sometimes for years, significantly limiting the pool of potential buyers. Buildings can sit vacant for years and deteriorate or end up repurposed for low-revenue uses such as roller-skating rinks or flea markets.

Probably no community has suffered more from Shapiro’s brainchild than Marquette, a three-hour drive west of Sault Ste. Marie. In 2012, Lowe’s argued that its two-year-old store there, which cost about $10 million to build, was worth just $3.5 million based on the resale value of shuttered big-box stores in other parts of the state. A judge with the Michigan Tax Tribunal agreed, and Lowe’s tax bill was slashed by two-thirds, forcing Marquette to pay the company nearly $450,000 in back taxes and lowering its tax bill by more than $150,000 a year going forward.

“Lowe’s pays property tax, income tax, sales and use tax, and, just like homeowners, we want to be taxed on the fair value of our buildings and land,” the retailer said in a statement. “It’s Lowe’s intention to always pay our fair share of taxes.”

The home center chain’s suit opened the floodgates for Marquette’s other retail chains. Even car dealerships made the same case. In the almost five years since, the timber and mining community on the edge of Lake Superior has lost more than $2 million in property tax revenue from retailers including Target, Best Buy, and Kohl’s.

Shortly after the ruling, a county-funded group home for troubled teens was forced to close, and the local library has slashed its hours. Ron DeMarse, the township's fire chief, worries his 23-year-old fire truck and battered two-way radios won't weather another winter. That would be a disaster, since he has no money left to replace them. DeMarse says the $56,000 he's lost in this year's budget from Lowe's tax challenge would have been enough to cover annual payments on a new engine to replace his aging one—the only truck the department has with a pump and ladder large enough to put out a fire at a building the size of Lowe's. Now his only option is a ballot initiative that would raise the needed money from the township's residents. "Maybe we just won't replace it," he says, and Lowe's might be forced to pay higher insurance premiums. "Maybe that would be fair."

Sentiments are equally raw in Sault Ste. Marie, where civic leaders are gearing up to keep its tax dollars in town rather than hand them back to Walmart. "It is an attack on all the services we provide: the sheriff's department, the health department, the schools, everyone is going to suffer here," Chippewa County Commissioner Jim Martin told residents at a recent county meeting. "That money will leave our community and go to their corporate offices."

The bottom line: *Big-box retailers are often thriving businesses. Now some are petitioning to pay the same property tax as shuttered stores.*

Bloomberg

by Shannon Pettypiece

December 8, 2016 — 5:01 AM EST December 8, 2016 — 9:47 AM EST

Dallas Bankrupted by Pensions? Bond Market Doesn't Think So.

- City's G.O. bonds due 2025 closely tracking 10-year benchmark
- Police and fire pension fund projected to go broke by 2030

Dallas's police and fire pension system may be going broke, but you'd never know it by looking at the municipal-bond market. The city's general obligations due in 2025 yield 2.46 percent, less than even top-rated 10-year debt, according to data compiled by Bloomberg.

That's despite Mayor Mike Rawlings telling a state board last month that the city's $7 billion debt to the retirement fund has left it walking into "fan blades" that look like bankruptcy.

"There's a lot of positive aspects absent of the pension issues that, given the right spreads and the right market context, would certainly make me look toward Dallas as a name to invest in," said Eric Kazatsky, municipal credit analyst at Janney Montgomery Scott. "The pension issue wouldn't prohibit me from adding it to a portfolio."

Bond market investors, known for enforcing financial discipline on governments by stanching the flow of capital and demanding higher interest rates, sometimes respond slowly the fiscal distress of local governments, which rarely default or go bankrupt.

But in Dallas, the pension fund's shortfall contrasts with an otherwise prosperous city, with rapid employment growth, a strong tax base and a population that swelled by nearly 100,000 since 2010 to 1.3 million last year. The city's fiscal 2016 tax rate is 7 cents per $100 of assessed value, with ample room to grow before hitting the $2.50 statutory cap.

Dallas's city council is scheduled Wednesday to discuss plans to save the fund. A briefing posted on Friday has few specifics, though it makes it clear that the city won't chip in the $1.1 billion requested by pension officials.

The scale of the city's pension debt — which is twice the size of its annual budget — prompted Fitch Ratings in October to downgrade Dallas one step to AA, the third-highest investment grade. The fund is projected to become insolvent by 2030.

The fund's leadership has tried to stem the bleeding by proposing a package of benefit rollbacks that will cut costs. A vote on the measures is scheduled to close on Dec. 17, according to the fund's website, after a judge refused a bid by workers to halt the proceedings.

Despite the drama, the strength of the city's financials has bondholders seemingly at ease.

"It's a holding that lets me sleep well at night," said Doug Benton, senior municipal credit manager for Canaval Hill Investment Management, which manages about $7.5 billion, including the city's debt. "I've got things that keep me up, but this is not one of those."

Bloomberg

by Katherine Greifeld

December 5, 2016 — 2:54 PM EST December 6, 2016 — 11:05 AM EST

Bloomberg Brief Weekly Video - 12/08

Taylor Riggs, a contributor to Bloomberg Briefs, talks with Joe Mysak about this week's municipal market news.

Watch video.

December 9, 2016

Bloomberg News

Judge Authorizes San Bernardino to Exit Bankruptcy.

California city to emerge from bankruptcy after more than four years with a plan to eliminate millions of dollars in debt

A federal judge on Tuesday ruled that San Bernardino, Calif., can leave bankruptcy even though city leaders said they won't have enough money to fully fund a police department that is fighting a rise in violent crime after last year's terror attack.

U.S. Bankruptcy Judge Meredith Jury cleared the 200,000-resident city to emerge from bankruptcy after more than four years with a plan to eliminate millions of dollars in debt. The plan, however, would pay just a portion of the $56.5 million sought by the police department for the next five years.

“The city infinitely could use more funds” for its police department, Judge Jury said. “Anybody who lives in the area knows that the crime problem in San Bernardino is substantial.”

San Bernardino police officers were lauded for their response to the Dec. 2, 2015, attack in which Syed Farook and Tashfeen Malik shot and killed 14 people, injuring 22 others, at a gathering of county workers.

Now the same department is battling a crime wave with 220 officers, down nearly 40% from before the bankruptcy.

“It wasn’t like crime decided to take a vacation when we lost those positions,” said Lt. Mike Madden. “We’re chasing our tails; we’re not being as proactive and stopping crime before it’s committed.”

The city outside of Los Angeles has recorded 60 homicides so far this year, Lt. Madden said. There were 44 murders last year, including the 14 people killed in the attack at the Inland Regional Center.

“If the homicide rate continues, the city will have more murders this year than in any year since 1995,” Chief of Police Jarrod Burguan warned in papers filed in the city’s bankruptcy case.

Gary Saenz, the city’s lawyer, said that while the restructuring will balance the city’s budget for the next 20 years, the city plans to pay only about 40% of what is necessary to fund the city’s police needs. The city won’t be able to provide all of the services that citizens need, he said.

“Given where we are financially, this is what we can afford,” Mr. Saenz said, adding that the plan will provide an “adequate” level of public safety.

During the bankruptcy, the city’s staffing fell to 600 people from 1,140. Its finance department can’t recruit workers to work at below-market wages, city officials said in court papers.

The city also won’t be able to fund the $180 million needed for street repairs and $130 million for building repairs. It can’t afford to replace the 60 public computers at its library system that are all more than seven years old.

San Bernardino filed for bankruptcy on Aug. 1, 2012, projecting it would run out of money in less than two months. The city that sits about 60 miles east of Los Angeles has suffered from double-digit unemployment and lower tax revenue from fallen property values.

Throughout the case, San Bernardino officials found ways to save money aside from cutting the amount of debt it faced. The city began using county-employed firefighters instead of its own and contracted out solid-waste disposal, recycling and sweeping services.

City leaders stopped paying retiree health benefits, though they will continue making full payments into the pension fund run by California Public Employees’ Retirement System, also known as Calpers. The system distributes payments to thousands of retired city workers—often their lone source of income, court papers said.

The city decided to make pension payments even though federal judges in charge of other large municipal bankruptcy cases ruled that pensions could indeed be cut.

The restructuring plan also doesn’t call for any immediate tax increases on its residents.

“The city came in in financial chaos, and it’s leaving in much better shape,” Judge Jury said Tuesday.

The plan aims to pay 1% of $209.3 million owed to retirees for health-care claims, families who have won police brutality lawsuits and other unsecured debts.

A European bank owed $51 million in bond debt will be paid 40% of its claim over 30 years. The bank's lawyers argued that, by law, the bonds should be paid at a higher rate. City officials disagreed.

Lawyers who handled the bankruptcy of Detroit, the largest city in U.S. history to file for chapter 9 municipal bankruptcy, had to similarly balance cutting debts between retirees and certain Wall Street firms who stood, by law, to be paid a better rate. Detroit leaders reached a deal with all of the major creditors before emerging from bankruptcy in December 2014.

THE WALL STREET JOURNAL

By KATY STECH and ZUSHA ELINSON

Dec. 6, 2016 7:01 p.m. ET

Write to Katy Stech at katherine.stech@wsj.com and Zusha Elinson at zusha.elinson@wsj.com

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Judge Slashes SEC's Proposed Fine for Ex-Miami Budget Director.

NEW YORK — A federal judge has rejected the U.S. Securities and Exchange Commission's request for a record $450,000 penalty against a former Miami budget director found liable for misleading municipal bond investors, fining the man $15,000 instead.

In an order on Monday, U.S. District Judge Cecilia Altonaga said the SEC has already made an example of former budget director Michael Boudreaux in its first municipal securities fraud case to go to trial.

Boudreaux and the city of Miami were found liable by a jury in September for shifting money among accounts to hide the city's worsening financial condition from investors who bought over $150 million of Miami's bonds in 2009.

Though a jury found Boudreaux acted with severe recklessness, he did not gain financially from his conduct, Altonaga said, adding that the fine the SEC was seeking appeared "overreaching and punitive."

The SEC's 2013 lawsuit alleged the city's "shell game" helped it win favorable ratings for its bonds and exposed bondholders to substantial risk of losses.

Penalties were not part of the jury trial. Miami reached an agreement with the SEC in October to pay $1 million to settle its case.

A $450,000 penalty against Boudreaux would have been the largest ever against a municipal official by the SEC. In a motion in October, the SEC said the penalty was justified because Boudreaux orchestrated the fraud and directed multiple transfers of money over a two-year period.

In a statement on Monday, Boudreaux's lawyer Benedict Kuehne said his client was relieved by the reduced penalty.

SEC spokesman Ryan White declined comment.

In a motion in November, Kuehne had argued that the proposed penalty was “massively unfair.” Boudreaux had already been financially ruined by the SEC’s case and could no longer find work in municipal government, his lawyer said.

In Monday’s order, Altonaga said the SEC failed to present any evidence that Boudreaux’s conduct caused investor losses or a substantial risk of losses. It was also unreasonable to expect Boudreaux to individually pay almost half the amount paid by the city itself, she said.

The judge also rejected the SEC’s request for a permanent injunction barring Boudreaux from future violations of securities laws, saying there is “little to no chance” he will ever work for a municipality again, let alone with securities or bonds.

The case is Securities and Exchange Commission v City of Miami, U.S. District Court, Southern District of Florida, No. 13-22600

By REUTERS

DEC. 6, 2016, 11:39 A.M. E.S.T.

(Reporting by Dena Aubin; Editing by Anthony Lin and Tom Brown)

Junk-Rated Chicago Schools Plan New Kind of Bond Issue.

CHICAGO — Chicago’s public school (CPS) system plans to sell a new type of bond issue in an attempt to separate the debt from the district’s severe financial woes and protect it in a potential bankruptcy filing, according to a document released by the district on Tuesday.

The preliminary prospectus for the debt indicates the Chicago Board of Education will issue $500 million of bonds secured solely by a capital improvement property tax and not by the district’s general obligation pledge.

That pledge currently covers about $6.8 billion of existing bonds that are rated junk by Moody’s Investors Service, S&P, and Fitch Ratings.

CPS, the nation’s third-largest public school system, is struggling with pension payments that will jump to about $720 million this fiscal year from $676 million in fiscal 2016, as well as drained reserves and debt dependency – factors that have pushed its GO credit ratings deep into the junk category and led investors to demand fat yields for its debt.

Illinois Governor Bruce Rauner last week vetoed a bill to give CPS a one-time $215 million state payment to help cover pension costs.

Ratings for the new bonds, backed by a $45 million a year property tax levy approved by the Chicago City Council in 2015, were not available. Because that tax revenue can only be used to fund capital projects and not operations, CPS is hoping bondholders will consider the debt a safer bet than the district’s GO bonds.

A CPS spokeswoman could not immediately be reached for comment.

CPS cannot currently file for municipal bankruptcy in Illinois, although there have been attempts to change state law to allow such a move. The prospectus includes legal opinions on a “hypothetical bankruptcy” by CPS that conclude payments on the new bonds would not be automatically stopped by a federal bankruptcy court and that bondholders would retain a lien on the tax revenue.

The prospectus was released a day before the schools’ governing board, appointed by Chicago Mayor Rahm Emanuel, votes on an amended fiscal 2017 budget to account for a new contract with teachers. The bond issue is tied to a bigger capital plan CPS announced last week.

The bonds, to be priced through Barclays and J.P. Morgan, carry term maturities in 2036 and 2046.

By REUTERS

DEC. 6, 2016, 6:36 P.M. E.S.T.

(Reporting by Karen Pierog; Editing by Matthew Lewis)

Judge Approves San Bernardino, California's Plan to Exit Bankruptcy.

SAN FRANCISCO — The judge overseeing San Bernardino, California’s municipal bankruptcy said on Tuesday she would approve the city’s plan to restructure its finances, according to a spokeswoman for the city.

An official confirmation order is expected by late January, spokeswoman Monica Lagos added in an email to Reuters.

U.S. Bankruptcy Judge Meredith Jury in recent months has been signaling support for the Southern California city’s plan to emerge from Chapter 9 bankruptcy after four years.

The plan involves slashing bondholder debt and retiree healthcare costs while protecting pensions.

San Bernardino’s financial restructuring also includes folding its fire department into San Bernardino County’s fire services district as a cost-cutting measure.

Hit by the 2008 financial and housing foreclosure crises as well as years of budget mismanagement, San Bernardino declared bankruptcy in July 2012 with a $45 million deficit.

The case is In re City of San Bernardino, in U.S. Bankruptcy Court, Central District of California, No. 12-28006

By REUTERS

DEC. 6, 2016, 7:12 P.M. E.S.T.

(Reporting by Jim Christie; Editing by Bernard Orr)

Chicago School Board Approves Revised Budget With $215 Million Hole.

CHICAGO — The Chicago Board of Education on Wednesday approved a revised fiscal 2017 budget that accommodates a new teachers' contract, but contains a $215 million funding gap for pensions.

The spending plan for the fiscal year that began on July 1 was increased by $55 million to $5.5 billion to reflect an additional contribution of surplus tax increment financing money from the city of Chicago. That money will cover higher costs from a new four-year contract with the Chicago Teachers Union that the board ratified on Wednesday.

Chicago Public Schools (CPS), the nation's third-largest public school system, is struggling with pension payments that will jump to about $720 million this fiscal year from $676 million in fiscal 2016, as well as drained reserves and debt dependency. The fiscal woes have pushed credit ratings on the district's $6.8 billion of general obligation bonds deep into the junk category and led investors to demand fat yields for its debt.

Illinois Governor Bruce Rauner last week vetoed a bill to give CPS a one-time $215 million state payment to help cover pension costs.

CPS officials on Wednesday blasted Rauner's action, while contending there is still time to pressure the governor and state lawmakers to restore the money.

"We will not allow Chicago students, most of them poor and minority, to be held hostage," said CPS Chief Executive Officer Forrest Claypool.

If the effort fails, School Board President Frank Clark said the district was prepared to deal with the budget gap in January.

The board also reaffirmed its approval for issuing up to $840 million of bonds backed by a new $45 million a year property tax levy earmarked solely for capital expenses.

On Tuesday, CPS released a preliminary prospectus for a $500 million bond sale secured by that revenue stream and not the district's junk-rated general obligation pledge. A CPS spokeswoman said the timing for the bonds' pricing is subject to market conditions.

Richard Ciccarone, president and CEO of Merritt Research Services, an independent municipal bond research and data provider, said the new type of CPS credit could attract investors who have avoided the district's GO bonds.

"The buyers are still going to demand a higher rate," Ciccarone said.

By REUTERS

DEC. 7, 2016, 6:21 P.M. E.S.T.

(Reporting by Karen Pierog; Editing by Matthew Lewis)

Fund Manager Q&A: What Should Muni Bond Investors Do Now?

NEW YORK — The past year has meant a wild ride for investors in municipal bond funds.

Between September 2015 and this past October, municipal bond funds had 54 straight weeks of inflows, with investors pouring some $68 billion into them. Muni fund owners were rewarded

handsomely: In the first six months of 2016, the BlackRock Strategic Municipal Opportunities fund returned 4.7 percent, for example. The 10-year yield on the AP Municipal Bond index, which moves inversely to bond prices, hit a low of 1.69 percent in July.

Then the bear came out roaring.

In early October, the flow of dollars into muni funds stalled as bets increased that the Federal Reserve would raise interest rates late this year. Selling accelerated after Donald Trump's surprise victory on expectations that his plans to boost economic growth would hurt the price of bonds. In November alone, investors yanked over $10 billion from muni funds, according to the Investment Company Institute. BlackRock's Strategic Municipal Opportunities fund fell 4.4 percent.

Peter Hayes, co-manager of the $4.7 billion BlackRock Strategic Municipal Opportunities fund, recently talked about the about-face for munis, and how investors can best navigate the current uncertainties. Answers have been edited for length and clarity.

Q: Muni bonds have just undergone an intense sell-off. Do you think it has gone too far?

A: Well, every big sell-off winds up being a good long-term buying opportunity, at some point. It's a question of finding the right entry point.

This sell-off has been so dramatic that it created value in a short amount of time. Municipal bonds are yielding more than Treasurys right now, and last week we began to see some stabilization of the market.

But given the headwinds, I'm not sure we are completely out of the woods yet.

Q: Which headwinds worry you the most?

A: Interest rates continue to be a concern. If rates go higher, that will scare investors from long-term assets.

Q: What about tax rates? Some believe that the Trump administration will slash tax rates for higher earners, which would diminish the value of muni bonds' tax-free income.

A: That's a potential headwind as well, but it's much longer term. I think we need to get past the inauguration and see what the new administration is really most concerned with.

Q: With all the talk of tax reform, some have wondered if the municipal tax exception could be at risk.

A: We emphatically don't believe that we will lose the muni tax exemption. Taxes are a bit of an overhang to the market, but a lot of that's already been factored into the price of the bonds today.

Q: Sounds like taxes are a wildcard. But it does seem likely that President-elect Trump will try to boost infrastructure spending. How do you think that will impact the muni market?

A: The initial reaction to the infrastructure proposals was that it would be negative, because it would mean more issuance in the muni market. That is usually a headwind for performance, given that we don't know what the demand is going to be.

But if you really look at the Republican proposals, they're talking about an infrastructure bank and private tax credits. That doesn't translate into increased muni issuances.

It’s also important to keep in mind that this year, about 60 percent of new issuance was related to issuers that were refinancing their debt.

If rates move higher, refunding will be less attractive. So I don’t see the current proposal as we know it today translating into higher issuance in the muni market in 2017, especially if the first half of the year is driven by all this insecurity around tax policy. Altogether, I don’t see infrastructure as a big headwind.

Q: So what’s the best strategy for investors right now?

If you already own munis, don’t sell. The market has already sold off significantly.

If you need a bit of income and want to take a position, shorter-term bonds look cheap. For the most part, stay in the three- to five-year range, where you will be less exposed to a change in tax policy and a potential rise in longer-term interest rates. Because the correction has been so large, those looking for more income might want to put a portion of their money in the 10- to 15-year part of the curve.

Otherwise, I suggest waiting on the sidelines. The severity and size of the move is likely to have scared investors. The next several weeks are very important. If the fund flows continue to be very negative, we have to be cautious. If they stabilize, then I think we can be more confident that the worst is over.

By THE ASSOCIATED PRESS

DEC. 8, 2016, 1:22 P.M. E.S.T.

Chicago Schools' New Debt Deal Tops U.S. Muni Sales Next Week.

CHICAGO/NEW YORK — The financially struggling Chicago Board of Education next week will sell a new type of debt, armed with an investment grade rating from Fitch Ratings based on the bonds’ ability to withstand a bankruptcy filing.

The $500 million of capital improvement tax bonds slated to price through Barclays Capital are secured by a new property tax levy earmarked exclusively for capital spending and not by the school district’s junk-rated general obligation pledge.

That money would be considered special revenue in a “hypothetical” municipal bankruptcy by the district, allowing debt service payments to continue as bondholders retain a lien on the tax collections, according to the debt issue’s legal opinions. The Chicago Public Schools cannot file for bankruptcy under Illinois law.

Fitch assigned the bonds an A rating, eight steps above the district’s B-plus junk rating with a negative outlook.

Alan Schankel, a municipal bond strategist at Janney Capital Markets, said the new bonds should fetch lower yields than the district’s February GO bond sale, when yields hit a whopping 8.5 percent.

“I suspect pricing will still be well into high yield territory given lack of Moody’s and S&P ratings as well as relative novelty of Fitch’s rating approach,” he said.

Earlier this week some of the school system's longer-dated GO bonds yielded as much as 380 basis points over Municipal Market Data's benchmark triple-A scale, according to MMD.

The deal is the largest of the $4.3 billion of U.S. muni bond and note sales scheduled next week.

The light issuance could help stabilize the market near term, especially with December redemptions on track to be the largest in 25 years, Barclays analysts wrote on Friday.

Munis suffered in the wake of the presidential election, with the 30-year yield jumping 82 basis points to 3.35 percent between Nov. 7, the day before the election, and Dec. 1.

Yields have since dropped, closing at 3.12 percent on Friday.

"This week's massive rally is at the very least a little puzzling to us and feels artificial," Barclays wrote.

The rally is "too far, too fast" because concerns remain about how munis would be affected by changes to tax policies and the Affordable Care Act under President-elect Donald Trump.

Barclays said fund outflows are the biggest threat to the market. Investors drained $9.5 billion from muni funds over the last four consecutive weeks, according to data from Thomson Reuters' Lipper service.

By REUTERS

DEC. 9, 2016, 4:54 P.M. E.S.T.

(Reporting by Karen Pierog in Chicago and Hilary Russ in New York; Editing by Daniel Bases and James Dalgleish)
