Arizona Cardinals Stadium Debt Jeopardized by Car-Tax Challenge.

To money manager Todd Curtis, the decade-long fight over a tax that helped build the stadium for the National Football League's Arizona Cardinals didn't look good for bondholders.

Last year, a state judge ruled that a vehicle-tax that pays for about a third of the stadium's $266 million of debt is illegal. Then August brought another legal blow: The state was ordered to pay tens of millions of dollars in refunds while it appeals the case, threatening to reduce funding for the Arizona Sports & Tourism Authority, which issued the bonds. Curtis sold the securities.

"If they lose, they could probably still make their bond payments, but they couldn't pay for much else," said Curtis, a portfolio manager with Aquila Group of Funds in Phoenix who runs a $280 million Arizona bond fund. "The sports authority has always run on a very thin line."

While stadiums in cities including Indianapolis and Oakland have put taxpayers on the hook for subsidies to professional sports teams, the challenge over funding behind the Glendale, Arizona, coliseum has left another constituency at risk: Investors who bought its bonds.

Financial Toll

The loss of the car-tax money, if upheld on appeal, would put an added squeeze on the financially struggling tourism authority, whose credit rating is at risk of a downgrade from Moody's Investors Service and Fitch Ratings. The operator of the stadium, which hosted this year's Super Bowl, has already failed to bring in enough tax money to cover its operations, which include promoting tourism and assisting professional baseball teams that come to Arizona for spring training.

"If they can't collect this tax, that compounds the issue," said Heather Macre, a Phoenix attorney who represents Saban Rent-A-Car LLC and others that are challenging the tax.

The companies say that the subsidies violate the law because Arizona's constitution requires vehicle taxes to be used for roads. On Oct. 5, the companies filed a motion to put the disputed funds into an escrow account until the case is resolved, which may take years.

Pricing Risk

The legal risk has lingered in the background since not long after the first bonds were issued in 2003, and the prices of the securities were little changed after the recent court decision. On Oct. 16, the $19 million of stadium bonds maturing in 2028 traded for an average yield of 3.3 percent, about 1.7 percentage points more than benchmark securities, according to data compiled by Bloomberg. That yield is down from 3.8 percent in early August.

"Depending on what level they're at, the risk can make it more attractive," said Craig Brandon, a portfolio manager of Eaton Vance Management, which holds $29.7 billion of municipal bonds, including some of the stadium debt. "If it's not going to continue generating income, we will be concerned. From an income perspective, we're comfortable with the level we're at."

While Brandon considers the risk of default to be low, he said the bonds may be downgraded if the authority can no longer collect the rental-car tax. Fitch Ratings and Moody's Investors Service put negative outlooks on the bonds in 2014 after the first decision, a first step toward a rating cut. Fitch grades the senior bonds A, the sixth-highest investment grade. Moody's rates them A1, one step higher.

"The negative outlook is a flashing red light," said Steve Murray, an analyst with Fitch in Austin. "Until this plays out, we're watching very closely."

Victory Seen

The authority expects to prevail in its appeal, which has yet to be filed, Timothy Berg, the agency's attorney in Phoenix, said in an e-mail. The final verdict could take as much as three years if it goes all the way to the state Supreme Court, said Macre, the lawyer for the plaintiffs.

So far the case has had no impact on the state budget, said Daniel Scarpinato, a spokesman for Governor Doug Ducey. What happens if the tax is struck down will be up to the governor and state lawmakers, who so far have taken no steps to find a backup revenue source.

"I don't think the state is going to let the sports authority go under," said Curtis, the portfolio manager with Aquila Group. "But they aren't going to do anything until their back is up against the wall."

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