Bond Case Briefs

Municipal Finance Law Since 1971

Commentary BDA Calls on Michigan Legislature to Promote Investment, Not Hamper Growth.

Michigan municipalities' statewide have turned the corner since the 2008 recession. According to the Center for Michigan, since 2009 the state has the nation's seventh fastest growing economy. Investment is flowing back into the state including Metro Detroit where the economy accounts for over half of the state's GDP.

Recently State Treasurer Nick Khouri announced that for the first time in nearly two decades, no Michigan municipality or school district was under state financial oversight. This feat is an incredible accomplishment by issuers in the state and demonstrates most issuers across Michigan are quite capable of managing their finances prudently.

As cities continue to build upon their fiscally stable condition, a Michigan Senate bill was introduced that could hamper the continued growth and force residents – all taxpayers – to pay more for daily services and infrastructure, while limiting the ability of municipalities to finance vital capital infrastructure including roads, bridges, schools and more.

Senate Bill No. 1054, the Revised Municipal Finance Act, would be detrimental to this recovery. This bill will create unintended consequences by increasing debt costs for municipalities, school and water districts, extending timely access to the capital markets, and isolating municipalities from much of the municipal securities market.

If passed, the bill would prohibit issuers from negotiated underwritings of municipal bonds, limiting their choice and forcing issuers of public debt to sell their debt in competitive underwritings in nearly all cases, removing a critical issuance option and isolating municipal issuers in Michigan.

What is the difference between competitive and negotiated underwritings you may ask? The Bond Dealers of America is the trade association in Washington, DC representing the U.S. bond markets and while the BDA is not advocating in favor of one or the other, it is essential to understand the difference and the important role each can play for municipalities.

In a competitive sale of municipal bonds, an issuer publishes a notice of sale and seeks bids on its bonds from underwriters across the marketplace. Issue size and structure is predetermined, and the bond issue is awarded to the bidder offering the lowest interest cost. In a negotiated sale, an issuer selects an underwriter or group of underwriters to purchase its bond issue. The selected underwriter works closely with the issuer to structure and market the bonds, and the terms of the issue are tailored to the needs of the issuer and the demands of investors.

Many observers of the municipal marketplace have debated whether competitive or negotiated underwritings are more cost-effective for municipal issuers, and the BDA is not taking a position in that debate. However, what is beyond debate is that categorically eliminating the ability of Michigan municipalities to access the marketplace through negotiated underwriting will limit their ability to respond to market conditions, create unnecessary hurdles to market access, and diminish the cost-effectiveness of their bond issuances. The end result will be increased costs to the taxpayer, especially for those constituents of issuers whose bond offerings are more complex, whose credit quality is less than ideal, or who sell public debt in distressed or volatile market environments.

Municipal bond financing is working well for local governments in Michigan, so why limit the tools available to issuers by prohibiting one of the ways in which bond issuances are transacted?

We call on the Senate to reject Senate Bill No. 1054 and allow municipalities to be able to continue to issue debt in the manner that works best for them, and not to force a one-size-fits-all methodology that will cost taxpayers more of their hard-earned money.

Bond Dealers of America

August 31, 2018

By Michael Nicholas