HOUSING - NEW YORK

County of Westchester v. U.S. Dept. of Housing and Urban Development

United States Court of Appeals, Second Circuit - September 25, 2015 - F.3d - 2015 WL 5616304

County brought action against United States Department of Housing and Urban Development (HUD) challenging its decision to withhold funds under grant programs as a violation of the Administrative Procedure Act (APA). The United States District Court granted summary judgment to HUD. County appealed.

The Court of Appeals held that:

- HUD's decision to reject county's analysis of impediments, submitted to HUD as required part of its certification that it would affirmatively further fair housing with HUD grant funds it was applying for, was not arbitrary or capricious, and
- HUD's decision to reject county's analysis of impediments did not ever condition the release of grant funds on certain municipalities changing their zoning laws, and thus did not violate statutes that prohibiting HUD from denying funds based on the adoption, continuation, or discontinuation of any policy or law.

Department of Housing and Urban Development's (HUD) decision to reject county's analysis of impediments, submitted to HUD as a required part of its certification that it would affirmatively further fair housing with HUD grant funds it was applying for, was not arbitrary or capricious under Administrative Procedure Act (APA), and thus HUD's decision to withhold county's funds based on rejection of the analysis of impediments was also permissible under APA, where exclusionary zoning could violate the Fair Housing Act (FHA), HUD was required to further the policies of the FHA, HUD's conclusion that the county's analysis of impediments was flawed and incomplete was based on detailed reports of consent decree monitor that determined that several municipalities' ordinances were exclusionary, and HUD provided a written explanation grounded in the evidentiary record, giving county multiple opportunities to make changes and submit a revised analysis of impediments.

Department of Housing and Urban Development's (HUD) decision to reject county's analysis of impediments, submitted to HUD as a required part of its certification that it would affirmatively further fair housing with HUD grant funds it was applying for, did not ever condition the release of grant funds on certain municipalities in county changing their zoning laws, and thus HUD's rejection of county's analysis and withholding of grant funds on that basis did not violate statutes that prohibited HUD from denying funds based on the adoption, continuation, or discontinuation of any policy or law. HUD's rejection of county's analysis was based on the county's failure to assess and analyze whether certain zoning laws in the jurisdiction impeded fair housing, its refusal to

acknowledge the connection between zoning restrictions and the availability of affordable housing, and its failure to identify a plan to overcome the effects of such impediments.

MUNICIPAL ORDINANCE - PENNSYLVANIA

Kuziak v. Borough of Danville

Commonwealth Court of Pennsylvania - September 29, 2015 - A.3d - 2015 WL 5687678

Landlord sought judicial review of decision of borough residential rental registration and property maintenance hearing board, which directed him to pay rental registration fees. The Court of Common Pleas denied appeal. Landlord appealed.

The Commonwealth Court held that:

- Trial court did not abuse its discretion by failing to conduct a de novo hearing;
- Trial court did not abuse its discretion in dismissing landlord's argument that ordinance requiring payment of fees was not properly advertised; and
- Ordinance specifying due date of fees for the next calendar year was not retroactive, and thus borough could proceed under new or prior ordinances to collect outstanding fees.

Trial court did not abuse its discretion by failing to conduct a de novo hearing on landlord's appeal from decision of borough residential rental registration and property maintenance hearing board directing him to pay rental registration fees. Landlord testified at hearing before board and was provided with a full opportunity to address any arguments he wished to raise and to present evidence, landlord opted to limit his testimony regarding allegations of illegality and unconstitutionality of ordinances requiring payment of fees and did not present any evidence during hearing, and trial court conducted its own hearing and directed parties to address issues by way of briefs.

Trial court did not abuse its discretion in dismissing landlord's argument, on appeal of decision of borough rental registration and property maintenance hearing board, that ordinance requiring payment of residential rental registration fees was not properly advertised as required by the Sunshine Act and thus was void ab initio. Landlord failed to present any evidence in support of argument, record did not contain any allegation that hearing at which ordinance was enacted was closed to the public, and landlord was aware of ordinance but first challenged its validity well in excess of the 30-day limitations period in the Act or the Judicial Code.

Ordinance specifying due date of residential rental registration and rental occupancy license fees for the next calendar year was not retroactive, and thus borough could proceed under new or prior ordinances to collect outstanding fees against landlord. New ordinance merely provided that any owner of a residential rental unit must register unit and pay appropriate fee beginning with the calendar year, new ordinance did not impose retroactive fees on new units or give different effect to landlord's obligations with respect to his units, and prior ordinance imposed identical registration requirements and fee schedules, which remained enforceable through and to its date of repeal.

UTILITIES - WASHINGTON

Singh v. Covington Water Dist.

Court of Appeals of Washington, Division 1 - September 28, 2015 - P.3d - 2015 WL 5681614

Real estate developer brought action against water district, seeking to recover amounts paid in incremental connection charges after developer abandoned project. The Superior Court granted summary judgment to district. Developer appealed.

The Court of Appeals held that:

- District's authority to charge connection fees and require performance security includes the authority to make fees nonrefundable;
- District's inclusion of nonnegotiable terms in system extension agreement (SEA), including nonrefundable incremental connection charges, did not constitute exercise of unlawful monopoly power; and
- Nonrefundable connection charges constituted fee rather than tax.

GASB Proposes Implementation Guidance Designed to Clarify Recent Pronouncements.

Norwalk, CT, September 30, 2015 — The Governmental Accounting Standards Board (GASB) today issued a proposed Implementation Guide containing questions and answers intended to clarify, explain, or elaborate on recent GASB Statements.

The proposed implementation guide focuses on questions that have been raised related to GASB's new standards on pensions, retiree healthcare benefits, and fair value reporting. The proposed guide also addresses a wide array of practice issues on other topics that have been brought to the GASB's attention. The Exposure Draft of Implementation Guide No. 20XX-X, Implementation Guidance Update—20XX, is available on the GASB website, www.gasb.org. Stakeholders are encouraged to review and provide comments by November 30, 2015.

SEC Charges Municipal Underwriters With Making False Statements.

WASHINGTON — The Securities and Exchange Commission charged and fined 22 municipal-bond underwriting firms, including units of UBS Group AG and PNC Financial Services Group Inc., for giving investors inaccurate information. It was the second batch of penalties this year for such firms under the U.S. agency's voluntary self-reporting program.

Regulators said Wednesday that the firms paid a total of about $4.1 million for violating federal securities laws between 2010 and 2014, by selling municipal debt using offering documents that contained "materially false statements or omissions" about the borrowers' compliance with disclosure obligations.

The SEC, in a news release, also said the firms failed to conduct adequate due diligence to identify the problems before selling the bonds on behalf of states and localities.

The agency launched the crackdown—dubbed the "Municipal Continuing Disclosure Cooperation Initiative," or MCDC—last year in a bid to pressure underwriting firms and state and local borrowers to admit voluntarily to lapses in investor disclosures in exchange for favorable settlement terms. The lapses include such issues as failing to disclose missed filings of annual financial reports or credit-rating changes.

Investors and analysts cite the missing disclosures as a factor curtailing the ability to trade securities in the vast, nearly $4 trillion municipal-debt market.

The program stems from a 2013 settlement with a southern Indiana school district and its underwriter for falsely stating to bond investors that the district had been providing investors with annual financial information and required disclosure notices. Without admitting or denying the charges, the West Clark Community Schools agreed not to repeat the violations and the district's underwriter, City Securities Corp., agreed to a $300,000 penalty.

Wednesday's announcement comes after the agency charged and fined 36 large and medium-size banks a total of about $9 million over similar violations in June. The earlier charges involved units of Bank of America Corp. and Citigroup Inc.

In the latest enforcement round, the largest firms will pay civil penalties up to $500,000 and smaller firms will pay up to $100,000, based on the number and size of the offerings. They also agreed to retain an independent consultant to review policies and procedures for underwriting municipal bonds.

The firms settled without admitting or denying the findings, and agreed to cease and desist from such actions in the future, the SEC said.

A spokeswoman for PNC, which paid the maximum $500,000, declined to comment. A spokeswoman for UBS, which paid $480,000, said in a written statement it is pleased to have resolved the matter.

"The MCDC Initiative has revealed that in recent years, a large number of municipal bond underwriters failed to conduct adequate due diligence before selling municipal bonds to their customers," Andrew Ceresney, director of the SEC's enforcement division, said in a statement. "In addition to effectively addressing this past misconduct, we believe the initiative has been effective in improving underwriter due diligence in municipal securities offerings on a going forward basis."

Robert Doty, president and proprietor of AGFS, a litigation consulting firm specializing in municipal-bond cases in Annapolis, Md., said the SEC's program is successfully motivating banks to avoid underwriting municipal bonds unless the issuers have complied with disclosure promises in prior offerings.

"The mind-set in the market has changed," Mr. Doty said.

In future enforcement actions under the MCDC, the SEC also is expected to expand the scope and bring charges against state and local borrowers, according to people familiar with the SEC's thinking.

THE WALL STREET JOURNAL

By ANDREW ACKERMAN

Updated Sept. 30, 2015 1:05 p.m. ET

—Aaron Kuriloff contributed to this article.

UBS Unit to Pay $34 Million in Settlements Over Puerto Rico Bond Funds.

A unit of UBS Group AG agreed to pay roughly $34 million in settlements with U.S. regulators regarding the sale of Puerto Rico bond funds that plunged in value in recent years.

Tuesday's settlements come as Puerto Rico's financial crisis is drawing increased scrutiny from U.S. lawmakers and regulators. A measure to establish more robust federal oversight over Puerto Rico's mutual-fund industry was introduced in Congress last week and a Senate committee held a hearing on Puerto Rico's financial problems on Tuesday.

UBS Financial Services Inc. of Puerto Rico agreed to pay $15 million to settle charges from the Securities and Exchange Commission, which said the unit failed to supervise a former broker who had customers invest borrowed money in the bond funds. The SEC said the money will be placed into a fund for investors who had losses.

The Financial Industry Regulatory Authority, which oversees securities firms, also said the UBS unit would pay a $7.5 million fine for failure to supervise, and $11 million in restitution to 165 customers who had losses on their funds.

The settlements are in line with other recent enforcement action by the SEC, which has focused on supervisory failures, said Elaine Greenberg, partner in the securities litigation, investigations and enforcement practice at Orrick Herrington & Sutcliffe LLP.

The SEC is "continuing to pursue actions against broker-dealer firms with regards to their policies and procedures, and whether or not those policies and procedures are reasonably designed to prevent and detect violations of federal securities law," Ms. Greenberg said. She previously was head of the SEC's specialized unit on municipal securities and public pensions.

A UBS spokeswoman said: "We're pleased to have resolved these matters with the SEC and Finra with respect to separate inquiries initiated in early 2014. We remain dedicated to serving our customers during this difficult economic time for the commonwealth."

Separately, the SEC said it sued the former broker, Jose Ramirez Jr., in federal court. It alleges Mr. Ramirez increased his compensation by at least $2.8 million by having customers improperly borrow money to invest in the Puerto Rico bond funds.

In addition, a former branch manager, Ramiro L. Colon III, agreed to pay a $25,000 penalty and be suspended from supervisory roles for a year. Mr. Colon is currently employed by UBS in Miami, according to his broker records.

An attorney for Mr. Ramirez, who was fired by UBS in early 2014, said he was examining the lawsuit and had no further comment.

Hundreds of investors who owned the bond funds sold by UBS have filed legal claims with Finra seeking to recoup their losses. UBS has settled some of the cases, at times for millions of dollars. In cases that made it to a hearing, Finra arbitrators have awarded damages in six of them and found in favor of UBS in two cases, according to UBS.

The funds were popular among island residents in part due to generous tax advantages. Many investors say they invested in the funds because their UBS brokers told them the funds, which were heavily invested in Puerto Rico municipal securities, were safe.

Puerto Rico has been facing a sluggish economy and high unemployment for years, and officials

under Gov. Alejandro Garcia Padilla are seeking to restructure the island's $72 billion debt load. Mr. Garcia Padilla has called the island's debt unpayable, and many Puerto Rico bonds are trading well below face value.

THE WALL STREET JOURNAL

By MIKE CHERNEY

Updated Sept. 29, 2015 6:45 p.m. ET

—Aaron Kuriloff contributed to this article.

MarketAxess Looks to Crack Muni-Bond Code.

The firm at the front of the pack in electronic corporate bond trading is trying to crack the code on an even more antiquated corner of the fixed-income market: municipal bonds.

MarketAxess Holdings Inc. is laying the groundwork to connect municipal bond dealers and investors electronically early next year, according to people familiar with the matter. The firm's executives have met with clients and municipal bond dealers in recent months to gauge interest in electronic municipal bond trading including so-called "all to all" trading, which means different types of buyers and sellers trade with each other.

If successful, the New York-based firm would join a small group of existing municipal bond trading platforms and could benefit from its heft in investment grade and high-yield bond trading.

It is the latest attempt to speed trading and transparency in the $3.7 trillion market for debt sold by U.S. state and local governments, which the SEC described in a 2012 report as "illiquid and opaque."

The market poses challenges for electronic trading because it has a larger number of securities and a greater number of dealers than the corporate bond market.

MarketAxess's talks come as regulators have increased efforts to disclose prices, transaction costs and dealer markups to the retail investors who own about 70% of municipal bonds, either individually or through mutual funds, and who typically buy the bonds seeking tax-exempt income, often to fund their retirements.

The Municipal Securities Rulemaking Board last week proposed new rules that would require municipal bond dealers to disclose the mark-ups they charge retail investors on trades. Comments on those proposals are due Nov. 20.

For MarketAxess, the work resurrects pre-crisis efforts to build an electronic municipal bond trading system. Success in the municipal bond market would help diversify its product mix and it is aiming to attract institutional dealers and investors, the people said.

Analysts at Keefe, Bruyette & Woods wrote in a note this month that the potential for MarketAxess to expand into municipal bonds or structured products would require minimal investment because the firm could use existing trading technology. The firm currently has a market capitalization of about $3.5 billion.

"This makes sense to us strategically given that these are also illiquid markets – similar to that of corporate bonds where [MarketAxess] has already had success," the KBW analysts wrote of potential expansion.

THE WALL STREET JOURNAL

By SARAH KROUSE and AARON KURILOFF

Sep 29, 2015

Supreme Court Preview for Local Governments – October 2015

The Supreme Court's last term was big for local governments because the Court decided a number of important cases against them, most notably Reed v. Town of Gilbert, Arizona (2015), holding that strict scrutiny applies to content-based sign ordinances. The October 2015 term is one to watch, and not just because the Court has accepted numerous cases on controversial topics affecting local governments. Adding to the intrigue, many of the Court's decisions this term are likely to be discussed by the 2016 presidential candidates as the election heats up. Here is a preview of the most significant cases for local governments that the Court has agreed to decide so far.

Public Sector Collective Bargaining

In Friedrichs v. California Teachers Association the Court will decide whether to overrule a nearly 40-year old precedent requiring public sector employees who don't join the union to pay their "fair share" of collective bargaining costs. More than 20 states have enacted statutes authorizing "fair share."

In Abood v. Detroit Board of Education (1977) the Supreme Court held that the First Amendment does not prevent public employees who do not join the union from being required to pay their "fair share" of union dues for collective bargaining, contract administration, and grievance adjustment. The rationale is that the union may not discriminate between members and nonmembers in performing these functions. So, no free-riders are allowed.

In two recent cases, the Court's more conservative Justices, including Justice Kennedy, have criticized Abood.

If the Court doesn't overrule Abood, it may instead rule that public employees may be allowed to opt-in rather than required to opt-out of paying "nonchargeable" union expenditures, in which case presumably fewer will opt-in.

"Fair share" and opt-out are foundational principles for public sector collective bargaining in the United States. Overturning either of them would mean a major change in the law that would substantially weaken public sector unions.

Redistricting

The U.S. Constitution Equal Protection Clause "one-person one-vote" principle requires that voting districts have roughly the same population so that votes in each district count equally. But what population is relevant — total population or total voting population — and who gets to decide? The Court will answer these questions in Evenwel v. Abbott.

Over the last 25 years the Supreme Court has repeatedly refused to decide (in cases all involving local governments) whether total voter population must be equalized in state and local legislative districts.

Plaintiffs claim that total voter population must be the metric. They argue their votes are worth less than other voters because they live in districts that substantially deviate from the "ideal" in terms of number of voters or potential voters.

The lower court disagreed because the Supreme Court has never held that any particular population metric is unconstitutional. Most state legislatures use total population, not total voting population data.

Asset Forfeiture

The question in Luis v. United States* is whether not allowing a criminal defendant to use assets not traceable to a criminal offense to hire counsel of choice violates the Sixth Amendment right to counsel.

Local law enforcement often receive asset forfeitures related to drug crime.

This case comes on the heels of Kaley v. United States (2014) where the Supreme Court held 6-3 that defendants may not use frozen assets which are the fruits of criminal activities to pay for an attorney.

Luis argues that it is "inconceivable" that she may not use "her own legitimately-earned assets to retain counsel." The federal government responded that per her reasoning criminal defendants "could effectively deprive [their] victims of any opportunity for compensation simply by dissipating [their] ill-gotten gains."

The Eleventh Circuit ruled against Luis, who was indicted on charges related to $45 million in Medicare fraud.

Local Governments Sued Out-of-State

In Franchise Tax Board of California v. Hyatt* the Court will decide whether states must extend the same immunities that apply to them to foreign local governments (and states) sued in their state courts. Hyatt is important to local governments who are often sued out-of-state.

The Franchise Tax Board (FTB) of California concluded that Gilbert Hyatt didn't relocate to Nevada when his tax returns indicated he did and assessed him $10.5 million in taxes and interest. Hyatt sued FTB in Nevada for fraud among other claims.

In Franchise Tax Board of California v. Hyatt (2003) the Supreme Court held that the Constitution's Full Faith and Credit Clause does not require Nevada to offer FTB the full immunity that California law provides.

A Nevada jury ultimately awarded Hyatt nearly $400 million in damages.

The Nevada Supreme Court refused to apply Nevada's statutory cap on damages to Hyatt's fraud claim, reasoning that Nevada has a policy interest in ensuring adequate redress for Nevada citizens that overrides providing FTB the statutory cap because California operates outside the control of Nevada.

Hyatt has also asked the Supreme Court to overrule Nevada v. Hall (1979), holding that a state may be sued in another states' courts without consent. If the Court overrules this case, the question of whether the immunities a state enjoys must be offered to a foreign local government (or state) will be moot.

Affirmative Action

For the second time the Court has agreed to decide whether the University of Texas at Austin's race-conscious admissions policy is unconstitutional in Fisher v. University of Texas at Austin.

Even though this case arises in the higher education context, the Supreme Court decides relatively few affirmative action cases so all are of interest to local governments that use race as a factor in decision-making.

Per Texas's Top Ten Percent Plan, the top ten percent of Texas high school graduates are automatically admitted to UT Austin, which fills about 80 percent of the class. Most other applicants are evaluated through a holistic review where race is one of a number of factors.

Abigail Fisher claims that using race in admissions is unnecessary because, in the year she applied, UT Austin admitted 21.5 percent minority students per the Top Ten Percent Plan.

The Supreme Court has held that the use of race in college admissions is constitutional if race is used to further the compelling government interest of diversity and is narrowly tailored.

In Fisher I the Court held that the Fifth Circuit, which upheld UT Austin's admissions policy, should not have deferred to UT Austin's argument that its use of race is narrowly tailored.

When the Fifth Circuit relooked at the plan again it concluded that it is narrowly tailored.

Only time will tell whether the Court agrees.

Conclusion

The Court's docket is only about half full right now. Interestingly, the Court hasn't accepted a Fourth Amendment or qualified immunity case yet — but no term would be complete without a few such cases. Of interest to the Court may be a case involving whether cell phone location data may be obtained without a warrant.

The National League of Cities

About the Author: Lisa Soronen is the Executive Director of the State and Local Legal Center and a regular contributor to CitiesSpeak.

Munis Cheapest in 5 Weeks to Treasuries as Payrolls Fall Short.

Prices in the $3.6 trillion municipal-bond market are the cheapest in five weeks relative to Treasuries after U.S. payrolls rose less than projected in September, spurring a rally in federal government debt on signs the global slowdown is affecting the world's largest economy.

Benchmark 10-year munis yield 2.09 percent, compared with 1.92 percent on similar-maturity Treasuries, data compiled by Bloomberg show. The ratio is a measure of relative value between the

asset classes. It reached 109 percent Friday, the highest since August, signaling that tax-free bonds are cheap relative to their federal counterparts.

Ten-year Treasury yields plunged 0.11 percentage point after a Labor Department report showed the U.S. added 142,000 jobs, lower than the median forecast of 201,000 from a Bloomberg survey of 96 economists. Weakening foreign markets, a stronger dollar and lower oil prices raise the risk that employers will hold off on adding workers.

Munis rallied to a smaller degree. As prices rose, the yields on both 10-year and 30-year AAA bonds fell 0.02 percentage point to the lowest since April, data compiled by Bloomberg show.

The 10-year muni-Treasury ratio was as low as 94 percent in July. Over the past decade, the figure has averaged 97 percent.

Bloomberg News

by Brian Chappatta

October 2, 2015 — 6:49 AM PDT

Puerto Rico Electric Utility Wins Extension From Bondholders.

Puerto Rico's main electric provider won a two-week extension from bondholders to negotiate how to restructure $8.3 billion of debt.

Investors holding about 35 percent of the utility's debt and its fuel lenders agreed to delay until Oct. 15 the expiration date on an agreement that was set to end Thursday, Lisa Donahue, the power provider's chief restructuring officer, said in a statement. The contract, called a forbearance agreement, keeps discussions out of court. The parties first signed the accord in August 2014. It is the ninth extension.

Puerto Rico Electric Power Authority, known as Prepa, and the bondholder group on Sept. 1 reached a tentative agreement that would require investors to take losses of about 15 percent in a debt exchange. Bond insurers Assured Guarantee Ltd., Syncora Guarantee Inc. and MBIA Inc. have balked at the plan and declined to continue the forbearance.

"We continue to work with the monolines in an effort to reach a consensual agreement on terms that would be beneficial to all parties involved," Donahue said.

Below Proposal

A Prepa restructuring would be the largest-ever in the $3.6 trillion municipal-bond market. Puerto Rico and its agencies, including Prepa, owe about $73 billion after years of borrowing to delay debt payments and fill budget deficits. The utility restructuring is the first step toward Puerto Rico's goal to lower its debt burden.

Prepa bonds maturing July 2040 traded Friday at an average of 59.2 cents on the dollar, according to data compiled by Bloomberg. That's higher than an average 53.5 cents on Aug. 28, the last time the bonds traded before the Sept. 1 agreement. But that's still lower than the 85 cents that bondholders would receive in a proposed debt exchange.

The bonds yielded 9.59 percent.

Bloomberg News

by Michelle Kaske

October 1, 2015 — 3:46 PM PDT Updated on October 2, 2015 — 9:32 AM PDT

Bloomberg Brief Weekly Video - 10/01/15

Taylor Riggs, a contributor to Bloomberg Briefs, talks with reporter Brian Chappatta about this week's municipal market news.

Watch the video.

October 1, 2015

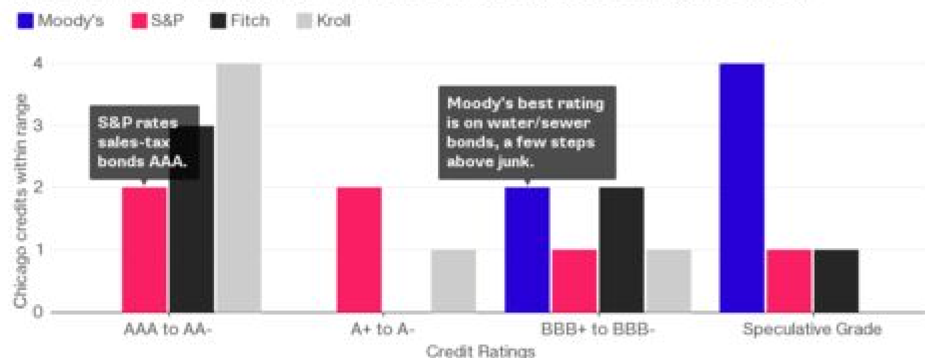
Junk or AAA? Rating Split Plagues Chicago as It Borrows Billions.

What's Chicago's risk to municipal-bond investors? It depends on which credit-rating company you ask.

In the eyes of Moody's Investors Service, most of the $20 billion of bonds tied to Chicago are junk, as speculative as a charter school or regional hospital that could shut down. To Standard & Poor's, the city's park district is as credit-worthy as the U.S. government, and its sales-tax-backed debt is even safer. Only Kroll Bond Rating Agency deems the public schools worthy of an investment grade.

No U.S. city has caused a larger difference of opinion in the municipal-bond market than Chicago, which is being squeezed by soaring bills to its underfunded retirement system. The city's sales-tax, motor-fuel-tax, water, sewer and park bonds all have at least a six-level gap between the lowest and highest ratings, data compiled by Bloomberg show. The discrepancy has led investors to err on the side of caution by demanding higher yields, threatening to saddle Chicago with added costs as it prepares to issue about $3 billion of debt.

"The dispersion in ratings just doesn't make sense," said Mikhail Foux, head of municipal research at Barclays Plc in New York. "Moody's is too conservative and S&P is too relaxed about this. The truth is probably somewhere in the middle."



Chicago illustrates a rift in the approaches that rating companies use to assess municipalities, whose securities are backed by varying revenue sources and legal safeguards. Those can leave some bondholders sheltered if a city faces a budget shortfall or collapses into bankruptcy, as Detroit did two years ago.

The views on Chicago have become more divergent since May, when Moody's lowered its general obligations to Ba1, one step below investment grade. While S&P and Fitch Ratings followed with their own downgrades to those securities, the companies have been at odds over how to gauge the rest of the city's bonds.

Moody's was the only one to downgrade all of Chicago's other major securities: It reduced the park, sales-tax and motor-fuel-tax debt to the same level as the city, while the water and sewer bonds were cut to the lowest investment-grade tier. S&P and Fitch left some of those ratings unchanged, despite their more dour assessment of the city's finances.

Buying Opportunity

The inconsistency has created pockets of value, Foux said. In particular, water and sewer bonds are trading at higher yields than they should, he said. The city plans to sell $439 million of the securities this month, the latest in a wave of offerings from Chicago.

"The market really does trade a lot of times to the worse-case scenario," said Dan Solender, who oversees $17 billion, including Chicago debt, as head of munis at Lord Abbett & Co. in Jersey City, New Jersey. "Most of the market isn't really looking at the higher rating anymore."

Moody's analyst Rachel Cortez said its Chicago ratings are so closely aligned because the securities draw from the same tax base or aren't separated sufficiently from the city's grasp to warrant a higher grade.

S&P said in a Sept. 24 report that a Chicago agency won't be penalized just because of the pressure on the budget, given that some bonds are sheltered from those strains. Jane Ridley, the analyst who wrote the report, said sales-tax bonds have the first claim on that money, which gives them less risk that general obligations.

Karen Daly, a senior managing director at Kroll, said the rating differences can be explained by the separate security pledges backing Chicago's bonds.

The analysis has been complicated by the risk of bankruptcy, a tool that Republican Governor Bruce Rauner has so far unsuccessfully sought to extend to Illinois municipalities. Were Chicago able to write down its debts in court, water and sewer bondholders wouldn't stand to lose as much as

owners of other securities, Fitch analyst Amy Laskey wrote in a Sept. 22 report. Hence the higher rating.

“All the different operating entities have differing bankruptcy risks,” Laskey said in an interview. Though Illinois currently doesn’t allow it, she said, “we always believe that if there were an entity that was in need of filing, that the state would find a way to allow them to.”

Market’s View

Trading in Chicago bonds shows the market is siding with Moody’s, which assigned the lowest ratings, said Justin Land, who oversees $4 billion of munis as director of tax-exempt management at Wasmer Schroeder & Co. in Naples, Florida.

The most-traded Chicago sales-tax bonds changed hands Thursday at an average yield of 4.6 percent, compared with 3 percent for munis with a similar 23-year maturity and the same top grade from S&P, data compiled by Bloomberg show.

Park district debt due in 2024 traded last week at an average 3.86 percent, compared with about 2.1 percent for AAA munis, Bloomberg data show. Sewer bonds due in 2021 changed hands last week at a yield of 3.2 percent, or 1.58 percentage points above the benchmark, while water bonds maturing in 2032 traded at 4.5 percent, a difference of 1.75 percentage points.

“Typically we’ll be on the side of caution and kind of lean our viewpoint toward the weaker credit rating,” said Dan Heckman, senior fixed-income strategist in Kansas City, Missouri, at U.S. Bank Wealth Management, which oversees about $127 billion. “People are very well aware of the issues, and they want to have substantial compensation.”

Bloomberg News

by Brian Chappatta and Elizabeth Campbell

September 30, 2015 — 9:01 PM PDT Updated on October 1, 2015 — 12:08 PM PDT

Muni Junk Bonds Are Outperforming Other High-Yield Options.

Investors are finding an unlikely haven amid the rout in corporate junk bonds: their tax-exempt counterparts sold by municipalities.

The riskiest local-government bonds returned 2.9 percent through Sept. 29, heading for their best month since August 2014, Bank of America Merrill Lynch data show. That’s more than four times the gain in the broader municipal market and stands in contrast to the shift away from debt sold by struggling businesses. High-yield corporate securities have lost 2.7 percent this month.

“People are looking for income streams, and at the same time they want some level of safety,” said Dan Heckman, senior fixed-income strategist in Kansas City, Missouri, at U.S. Bank Wealth Management, which oversees about $127 billion of assets, including high-yield municipal bonds. “They view the high-yield muni as a little safer place out of other risk areas that contain higher yields.”

After the Federal Reserve decided not to raise interest rates at its Sept. 17 meeting, money flooded

into mutual funds focused on high-yield municipals. The funds pulled in $178 million in the week ended Sept. 23, the first in a month, Lipper US Fund Flows data show.

The municipal bonds, which are sold for specific projects or by strained governments such as Puerto Rico and Chicago, have skirted the turmoil in other financial markets over the past two months, when stocks tumbled amid speculation that the world's economy will slow.

Their relative security has been a draw to investors seeking to ride out the volatility, said Heckman. High-yield munis had a default rate of 7.5 percent over the last decade, compared with 32 percent for comparable corporate debt, according to a July 24 report from Moody's Investors Service.

The recent gains stem the losses that came this year as Puerto Rico's fiscal crisis escalated. The commonwealth defaulted on some securities for the first time in August and plans to ask investors to restructure debt that Governor Alejandro Garcia Padilla says the government can no longer afford.

The default didn't trigger an exodus from the municipal-bond market because the long-brewing crisis is seen as limited to the island. After initially pulling money from high-yield funds amid speculation about the potential ripple effects, investors have been adding money back, seeking higher yields as interest rates hold near generational lows.

With "the low-rate environment, there's demand for incremental yield," said Dan Solender, who helps manage $17 billion as head of state and local debt at Lord Abbett & Co. in Jersey City, New Jersey. "The credits have been holding in well. There's not been significant issues so the credits are performing well.'

Chicago bonds, which were cut to junk by Moody's in May, have pared their losses as Mayor Rahm Emanuel proposed a record property-tax increase to help cover the city's rising pension-fund bills. Federally taxable Chicago bonds maturing in 2042 traded Wednesday for an average of $1.02 on the dollar, up from 96.7 cents on Aug. 31.

Puerto Rico securities have also rebounded since June. Garcia Padilla's administration plans to ask investors to voluntarily exchange their securities for new ones with lower interest rates or longer maturities, a process that could shelter some bondholders from losses. Puerto Rico debt maturing in 2035 traded for an average of 74 cents on the dollar Wednesday, up from as little as 64 cents on June 30. That pushed the yield down to 11.2 percent from 13.1 percent.

"The Puerto Rico influence in the high yield indexes could be as much as 20 percent," said Jim Colby, who manages about $1.6 billion of high-yield municipals at Van Eck Global in New York. "So that I think it is a very significant element of why we've had such good performance."

Bloomberg News

by Elizabeth Campbell

September 29, 2015 — 9:00 PM PDT Updated on September 30, 2015 — 9:49 AM PDT

Puerto Rico Debt Crisis Eludes U.S. Fix, Top Republicans Say.

Top Senate Republicans showed no intention of acting soon to rescue Puerto Rico from its escalating financial crisis, saying there's no easy way for the federal government to steady the Caribbean island

pushed to the brink by $73 billion of debt.

Republicans who lead both chambers of Congress have signaled little urgency in aiding Puerto Rico, and the White House has made it clear it won't bail out the commonwealth. The reticence was on display Tuesday at a Senate Finance Committee hearing, the first in Congress since Governor Alejandro Garcia Padilla said the island can't afford to repay what it's borrowed.

While Puerto Rico officials are pushing for more funding for some federal programs, Senator Orrin Hatch of Utah, the chairman of the finance committee, expressed skepticism that additional money would be sufficient. He noted that it's received billions in additional federal funds since 2009.

"Even with those boosts in federal funding and the related increases in commonwealth spending, all we see is added commonwealth debt," he said at a hearing in Washington Tuesday.

Providing more money for health-care programs, for example, "would necessarily mean reduced funding for other priorities, increased taxes, or even more federal debt," he said. "That is the unpleasant budget arithmetic that we face. There are no easy answers."

The commonwealth of 3.5 million people is teetering because of years of borrowing to cover budget shortfalls as the economy stumbled and residents left for the U.S. mainland. Garcia Padilla is seeking to postpone or reduce the government's debt bills, moving the island toward what would be the biggest restructuring ever in the $3.6 trillion municipal-bond market.

Senator Charles Grassley, the Iowa Republican who chairs the judiciary committee, during the hearing stopped short of endorsing legislation Puerto Rico is seeking that would allow its publicly owned corporations, such as the power company, to file for bankruptcy, as U.S. cities can.

Instead, he recommended exempting Puerto Rico from the minimum wage and shipping laws that drive up the cost of goods. He also suggested setting up a federal board to oversee its finances, though he said any Congressional steps would depend on whether Puerto Rico moved to eliminate deficits at the root of the crisis.

"Congressional help without meaningful reform by the Puerto Rican government won't work," Grassley said at the hearing.

The commonwealth is rapidly draining its cash. Unless it can raise money in the capital markets, it could run out of money by the end of the year, just before a large payment is due on its general-obligation bonds, Government Development Bank President Melba Acosta said.

She told the senators that "federal action is essential," including giving it the same access to the Medicaid and Medicare health-care programs that states have and extending municipal bankruptcy access to the island.

"Puerto Rico has passed the tipping point and faces an immediate liquidity crisis," she said. That's "threatening the ability of the government to continue to provide essential services to its residents and to pay its debts when due."

In addition to approximately $73 billion of public debt, Acosta said Puerto Rico has a $45 billion shortfall in its workers' retirement system that's threatening to put more strain on the budget.

Bankruptcy Bill

Puerto Rico, which has already defaulted on some bonds, wants Congress to approve the legislation

giving some entities access to Chapter 9 bankruptcy protection. That could avoid a protracted legal fight by allowing the government to restructure some debt in court, rather than through individual negotiations. That bill has yet to advance for lack of Republican support.

With bonds sold through more than a dozen agencies, Puerto Rico has yet to say which securities could be affected and by how much, which has left investors speculating about the scale of losses they may be asked to take. The administration plans to ask investors to exchange their bonds for new debt with lower interest rates or longer maturities. Such a plan may come in the next few weeks.

Going Alone

During the hearing, Puerto Rico’s representative in Congress, Pedro Pierluisi, said lawmakers should end the disparate treatment that applies to the island with respect to federal programs.

“Any notion that the territory alone got itself into this situation and the territory alone must extricate itself from this situation is totally false,” he said. “The truth is that the federal government bears tremendous responsibility for the crisis in Puerto Rico, and so Congress and the president must be part of any solution.”

Bloomberg News

by Kasia Klimasinska

September 29, 2015 — 7:13 AM PDT Updated on September 29, 2015 — 11:39 AM PDT

Stalemate Over Tax Increases Pushes Pennsylvania Yields Higher.

As Congress races to avert a government shutdown, what may be a more prolonged political fight over the budget is dragging on in the state capital 120 miles (193 kilometers) to the north.

In Harrisburg, Pennsylvania, the state government is almost three months into the fiscal year without an agreement on what it can spend because of a divide between the Republican-led legislature and Governor Tom Wolf, a Democrat. At least two school districts say they may soon have to close. Some debt has been downgraded. And investors have pushed yields on the Keystone State’s bonds close to recent highs over top-rated securities, a measure of the perceived risk.

Pennsylvania is the only state aside from Illinois that’s still locked in a stalemate over the budget, a standoff reminiscent of those that once played out in statehouses around the nation after the recession. While public finances have recovered along with the economy, Pennsylvania lawmakers are contending with a $53 billion pension-fund shortfall that’s threatening to hit the state with rising bills, as well as pressure to steer more money into schools.

As a result, investors are demanding yields on 10-year Pennsylvania bonds of 2.71 percent, 0.56 percentage point more than AAA municipal securities, according to data compiled by Bloomberg. That’s just shy of the 0.61 percentage point reached in June, which was the highest since the data began in 2013. Only Illinois and New Jersey, which have even larger pension shortfalls, pay more, according to data on 20 states.

“Pennsylvania is not in as bad a situation as New Jersey or Illinois,” said Scott McGough, director of

fixed income for Glenmede Trust Co. in Philadelphia, who is reducing his holdings of Pennsylvania debt. “But clearly, the trend is poor at this point.”

The legislature took a step to temporarily ease the crunch last week, when it passed a budget to provide about four months of funding to schools and other agencies. Wolf, who took office in January, rejected it on Tuesday, saying he wants a comprehensive spending plan.

“The citizens of Pennsylvania want more than half measures, and they deserve better than the status quo,” Wolf said in his veto message to the legislature. The temporary budget locks in human services cuts and is “an avoidance maneuver that fails to adequately fund education.”

Pension Politics

Since March, Wolf and Republicans have been at loggerheads over how to shore up the retirement system, which has less than two-thirds of the assets needed to cover the benefits promised to about 700,000 employees. Wolf vetoed a Republican bill that would have put new workers into defined-contribution plans similar to 401(k)s. He wants to sell $3 billion of debt to inject cash into the retirement system to make up for years of shortchanging it.

Republicans have also balked at his proposal to implement a new tax on natural-gas drillers and raise levies on income and retail sales to fund schools.

The effects are starting to be felt beyond the capital. This month, Moody’s Investors Service lowered the credit ratings of schools that sell bonds through a program that diverts state aid to investors if the districts default. The credit rater said the lack of a budget has cast uncertainty over the funding, heightening the risks to bondholders. Standard & Poor’s has put the districts’ ratings on watch, a first step toward a downgrade.

School Closings

School districts in Carbondale, in the northern part of the state, and to the west in Erie, have warned that they may temporarily close without funds if the budget impasse continues. By October, 41 school districts may see “significant cash-flow difficulties,” according to a senate Republican committee memo. Another 120 would be added to the list by December.

By next month, school districts would be running without more than $3 billion in state aid that was anticipated for the year, according to the Pennsylvania Association of School Business Officials. Administrators have been tapping reserves and lines of credit to compensate, the Harrisburg-based group said.

Schools have borrowed at least $347 million so far and may run up an additional $122 million of debt in October to keep classrooms open, State Auditor General Eugene DePasquale said Tuesday.

Some are pushing down the pain to charter schools. About 24 school districts have eliminated or reduced payments to charter schools, said Tim Eller, executive director of the Keystone Alliance for Public Charter Schools.

Pennsylvania is graded two steps below the state average, in part because of the deficit in its retirement system. S&P and Fitch Ratings cut the state last year to AA-, the fourth-highest level. Moody’s grades Pennsylvania Aa3, the same rank.

Glenmede’s McGough said investors may continue to demand higher yield premiums if the Pennsylvania’s leaders don’t repair the government’s finances.

"You have to address the budget as is, given the revenue coming in, and really right-size your budget," he said.

Bloomberg News

by Romy Varghese

September 28, 2015 — 9:01 PM PDT Updated on September 29, 2015 — 9:25 AM PDT

Connecticut Tax Bonds Draw Buyers Losing Faith in State Pledges.

Connecticut bond investors have more faith in the tax man than in the full faith and credit pledge of the state.

Though the extra yield investors demand to own the state's general obligations instead of top-rated debt is almost the highest on record, its $840 million bond sale this week is drawing interest from Conning, Eaton Vance Management and Nuveen Asset Management. That's because the debt, which will pay for transportation projects, is backed by dedicated taxes on motor fuels, oil companies and retail sales — none of which can be touched by lawmakers until bondholders are paid.

"If you're going to make an investment in Connecticut, this is a credit that should be strongly considered," said Paul Mansour, head of municipal research at Conning, which oversees $11 billion of the debt, including some state bonds. "There's no appropriation required. So if there's ever a budget stalemate, there's less risk of a delay in getting paid."

Connecticut reflects a shift in the $3.6 trillion municipal market, where investors have given greater scrutiny to securities backed only by a government's promise since Detroit foisted losses on bondholders following its 2013 bankruptcy. This year, debt funded by legislative appropriations was tarnished when Puerto Rico chose to default and Illinois's budget stalemate caused the credit rating of Chicago's convention center agency to be cut from AAA to near junk.

Malloy's Maneuver

Connecticut Governor Dannel Malloy signed a law that boosted the share of the sales tax for transportation-project bonds this year and walls it off from the money spent by the legislature, an effort to spur spending on public works. As a result, oil company and sales taxes are being sent to a special fund, providing added security to investors.

Connecticut, the wealthiest U.S. state, has an Aa3 credit rating from Moody's Investors Service. Only Illinois and New Jersey are ranked lower. That's because the state's economy has rebounded slowly from the recession, its pension system is the third-most underfunded nationwide and it has the most debt per resident.

The extra yield investors demand to buy 10-year Connecticut general obligations rather than benchmark municipals has climbed to 0.47 percentage point from as little as 0.27 percent in January, data compiled by Bloomberg show. That spread is near the widest since at least January 2013, when the data begin, signaling that the debt is viewed as relatively riskier.

The transportation bonds have retained their value. Debt issued a year ago that's due in September 2026 traded last week at a spread of 0.49 percentage point, unchanged from the average over the

past five months, data compiled by Bloomberg show.

“We do prefer this type of revenue stream versus the state of Connecticut G.O. pledge,” said Michael Hamilton, who runs a $284 million Connecticut open-end mutual fund at Nuveen Asset Management. He owns some of the transportation debt. “I have some room to buy if the deal comes a little wider, given the state has widened out as well.”

Malloy made improving Connecticut’s infrastructure a focus of his budget, which also cut spending and raised taxes on corporations and the highest earners. To fund his initiative, 0.3 percent of the 6.35 percent sales tax will be funneled toward the revenue bonds this year. The share will ramp up to 0.5 percent by the 2018 fiscal year, according to bond documents.

Railway, Roads

Proceeds from the new bonds, which are set to be sold Thursday, will fund improvements to the New Haven Rail Line, the I-84 expressway and the Pearl Harbor Memorial Bridge.

Fitch Ratings last week ranked the bonds AA, the same as Connecticut’s general obligations. The credit rater in July raised the state’s outlook to stable from negative, pulling it back from the brink of a downgrade, citing a budget for the next two fiscal years that appears balanced.

Carl Thompson, an analyst at Eaton Vance, said he agrees with Fitch’s more optimistic assessment. Mansour, the analyst at Conning, said his outlook for the state is still negative: His company’s May ranking of the fiscal health of states put Connecticut sixth-to-last.

Yet both agree the transportation bonds are a potential buying opportunity.

“Despite similar ratings as the state, I think that Connecticut’s special tax bonds are a much stronger credit,” Mansour said. “The state has accelerating debt service and pension obligations. With these bonds, you have much more predictable and stable expenses.”

Bloomberg News

by Brian Chappatta

September 27, 2015 — 9:01 PM PDT Updated on September 28, 2015 — 6:13 AM PDT

Ohio Firefighter and Police Pension Fund to Put Spending Records Online.

The Ohio Police and Fire Pension Fund volunteered to put its spending records online as part of a partnership with State Treasurer Josh Mandel’s online checkbook program.

The announcement comes exactly a week after Mandel criticized the Ohio Public Employees Retirement System for not joining his initiative, which can be accessed at OhioCheckbook.com.

Mandel accused OPERS of trying to hide information from the public, which OPERS officials quickly denied.

“The executive director of OPERS feels that taxpayers do not have a right to see this information and she’s just flat out wrong,” Mandel said today during a press call. “It’s dumfounding that they still refuse to volunteer to put their finances online.”

OPERS officials have continued to say they support transparency, as evidenced by "extensive financial information" provided on their own website.

"It's disappointing to be continually mischaracterized by the treasurer of state," said Julie Graham-Price, a media representative from OPERS. "We intend to evaluate the online checkbook initiative; unfortunately, it's not on the treasurer's timeline."

OPERS and Mandel have a history of disagreement. The two sides have clashed over who should control where the multibillion-dollar pension fund's resources should be invested among other disagreements over reforms.

The police and fire fund is the first pension fund in the United States, according to Mandel, to volunteer to put their financial information online.

"We see no reason why our members as taxpayers should not be able to see what vendors we use, what services we use, what consultants we use, how much we're paying for our paperclips and pencils, things like that," said John Gallagher, executive director of the fund. Gallagher added that confidential information would not be put on the website.

The pension fund joins more than 100 state and local government entities that have volunteered to put their spending habits online.

"Obviously we're a huge fan of the local government stuff … but it really is important for the pension funds to step it up," said Greg Lawson of the Buckeye Institute, a Columbus-based free market think tank. "It's just a great example of good government."

Mandel's initiative helped the state jump from No. 46 to No. 1 on a U.S. Public Interest Research Group list of transparent states providing online access to government spending.

BY TRIBUNE NEWS SERVICE | OCTOBER 2, 2015

By Dina Berliner

(c)2015 The Columbus Dispatch

Government's Continuing Budget-Buster: Paid Sick Leave.

While paid sick leave is critical to economic security and health for employees and their families, its impact is even more far-reaching — even contagious: When ill employees go to work, co-workers, clients and employers can get sick as well. But there is another health factor associated with paid sick leave: employers' fiscal health.

For governments and the private sector alike, overly generous sick-leave policies can lead to unexpected back-end costs and potentially significant unfunded liabilities. In terms of employer costs, paid sick leave ranks only behind medical and retirement benefits. This issue is particularly acute for governments: While in the private sector almost 40 percent of employers do not offer paid sick leave, nearly all full-time public-sector employees receive some form of coverage.

So how are local governments managing their paid-sick-leave programs? And are cities and counties making the types of post-recession reforms that we have seen in other benefit areas such as

pensions and retiree health care?

The answer is that paid sick leave (PSL) appears to still be quite generous, with few local governments seeking to reform longtime practices. In a national survey of human-services professionals for large cities and counties, Michael Thom of the University of Southern California and I found that only 14 percent of local governments had sought to reduce their cost exposure by enacting post-recession PSL reforms.

Most local governments have continued to offer generous sick-leave policies, including allowing employees to accrue more than 120 hours of PSL annually (53 percent) and having no limit on the number of PSL hours that can be rolled over from year to year (77 percent). Further, over 50 percent allowed employees to cash out unused paid sick leave upon leaving their jobs, while 40 percent allowed unused PSL to be used in calculating retiring employees' service credits for pension purposes — one form of "pension spiking."

Allowing paid sick leave for family members was widespread (89 percent), but other practices, such as sharing programs (allowing employees to donate unused sick leave to needier co-workers) and converting unused sick leave to vacation time, were not as prevalent (42 percent and 13 percent, respectively). While the percentage of local governments requiring a doctor's note for prolonged sickness was quite high (over 70 percent), the number that perform sick-leave audits and have incentive programs to avoid unnecessary use of sick leave were quite low (both less than 25 percent).

Collective-bargaining status and employee classification — such as public safety vs. general staff — were both significant factors in determining certain practices. In local governments with collective bargaining, the practice of allowing employees to include unused PSL in pension calculations was more likely. Further, public-safety employees were less likely to be affected by budget-savings reforms after the recession, less likely to be required to have a doctor's note for prolonged absences, and more likely to have sharing programs.

When governments elect to allow PSL to be accrued and rolled over from year to year with no limit, and either be cashed out when employees leave or used in pension calculations, the costs and impact can be substantial. That's because much of the paid sick leave may have been earned during years in which an employee had a lower salary, while payouts at termination and for pension determinations are calculated at the highest salary levels. Also, many local governments treat PSL costs as a pay-a--you-go item, which means these expenses are seldom included as fixed items in their budgets.

As local governments recover from the recent recession and continue to grapple with unfunded pension and retiree health-care costs, their focus undoubtedly will turn to other cost drivers such as paid sick leave. Serious consideration for cost-containment measures should include ending the practice of applying unused PSL hours in pension-benefit calculations; limiting the amount of hours that can be accrued and rolled over from year to year; and limiting unused-PSL payouts to a nominal or fixed amount paid annually instead of allowing it to accumulate until retirement.

With such fundamental change on the horizon, local governments should work with their employees to adopt more sustainable, fair and innovative paid-sick-leave practices that also will provide employees with incentives to avoid unnecessary absenteeism.

GOVERNING.COM

BY THOM REILLY | OCTOBER 1, 2015

Thom.Reilly@asu.edu

Louisiana Election 2015: Should Governments Pay Taxes to Other States?

Louisiana is letting voters decide whether local governments should be allowed to tax property in their borders that's owned by other governments.

For four years, West Carroll Parish in the northwest corner of Louisiana billed the Memphis Light, Gas, and Water Division about $100,000 per year in property taxes for storing some of its natural gas in the parish limits.

But in 2013, Memphis stopped paying its bill. The Tennessee city argued that the natural gas storage site was government-leased property and used for a public purpose and therefore exempt from a property tax. Two years and a few court battles later, West Carroll Parish lost the argument and had to refund Memphis more than $400,000.

The problem? Louisiana's constitution doesn't clarify that the public-use exemption only applies to property owned by a Louisiana government, so outside state and local governments don't have to pay a tax either.

Many state exemptions are silent about this issue. Only 11 expressly allow local governments to tax property that's owned by another government, according to the Lincoln Institute on Land Policy. The bad news for Louisiana is that it is literally surrounded by states that do specify that other state and local governments have to pay property taxes in their state.

The state is trying to remedy the situation with a proposed constitutional amendment that would allow Louisiana to tax property owned by out-of-state governments like the Memphis utility.

"This will basically level the playing field for Louisiana and mirrors the current law in Texas, Arkansas, Mississippi and Tennessee," said State Rep. Charles Chaney, whose district includes West Carroll Parish.

Among the handful of states with laws about this issue, Ohio has a unique approach. Its law says that property in Ohio used for public purposes out-of-state can be tax-exempt only if that state can offer Ohio the same exemption.

Chaney said he won't push for the issue again if the ballot measure fails next month. Still, he's concerned the measure won't survive voter fatigue — Louisiana voters must choose a new governor, state legislators and other local officers. By the time they get to the statewide ballot measures, voters could be more inclined to vote "no" or leave the box blank, rather than decide for the measure on its merits, said Chaney.

"It's a down ballot issue and placement and that is very worrisome to me," he said.

GOVERNING.COM

BY LIZ FARMER | SEPTEMBER 29, 2015

S&P's Public Finance Podcast (Garden City Schools, Michigan, And The Town Of Lawrence, Wisconsin)

In this week's Extra Credit, ratings analysts Anna Uboytseva and Michael Furla discuss what spurred our rating actions on Garden City Schools, Michigan, and the Town of Lawrence, Wisconsin.

Listen to the Podcast.

Oct. 2, 2015

Expert Urges Expanded Use of P3s to Protect Water Resources.

More than 2,000 U.S communities are using public-private partnerships to meet pressing water-related infrastructure needs and many more localities should pursue them, argues the head of a water company trade association.

Municipalities can negotiate P3s to gain access to capital and technical, management and process-improvement expertise. These partnerships also will help them to apply new technologies that they could not take advantage of without such support, wrote Michael Deane, executive director of the National Association of Water Companies, in a Sept. 30 American City and County magazine column.

P3s can step in to offer fund system repairs and upgrades that the budget-strapped federal government cannot, he argues, citing the Environmental Protection Agency's findings that more than 240,000 water main breaks occur each year. To make matters worse, the agency says it lacks the $384 billion needed to maintain drinking water systems through 2020.

On the other hand, the federal government is committed to fostering infrastructure P3s, Deane wrote, offering as examples, President Obama's Build America Investment initiative and the EPA's recently launched Water Infrastructure and Resiliency Finance Center. The center "will help ensure that communities have the information and tools to explore all opportunities for innovation in project finance, delivery and operations," Deane wrote.

He singled out several examples of successful water-related P3s: A 40-year concession agreement through which United Water and investment firm KKR are investing in and operating Bayonne, N.J.'s water and wastewater systems and a similar 30-year deal Rialto, Calif., negotiated with Veolia North America. Meanwhile, CH2M and Spacient Technologies are improving communication between the city's water distribution and wastewater collection personnel to improve operations, services and customer support.

Other success stories include a P3 through which United Water is, for 20 years, operating, managing and maintaining Nassau County's wastewater plants that were damaged by Hurricane Sandy and Prince George's County, Md.'s collaboration with Corvias Solutions to install infrastructure that will capture stormwater runoff and prevent it from polluting the Chesapeake Bay.

The Prince George's stormwater P3 and others will be discussed during the CBP3 Sustainable Stormwater Infrastructure Summit to be held Dec. 7 in Philadelphia. For more information, visit the event website.

NCPPP

By Editor

October 1, 2015

High Coverage and Strong Legal Provisions Contribute to Strong U.S. Lottery Revenue Bond Ratings in 2015, Report Says.

NEW YORK (Standard & Poor's) Sept. 30, 2015–Even in a period of expansion in casino gambling, national lottery sales continue to grow and to remain stable said a report published today by Standard & Poor's Ratings Services.

"We attribute this to the monopolies states enjoy on lottery sales, relatively modest prices, and consumers' ability to purchase a product instantly at diverse retail establishments," said Standard & Poor's credit analyst David Hitchcock. "We also don't see a lottery ticket bought at a retail checkout counter as necessarily representing direct competition to or from a casino visit," Mr. Hitchcock added.

Standard & Poor's maintains ratings on lottery bonds issued by four states– Arizona, Florida, Oregon, and West Virginia–under its lottery revenue bond criteria (see "Lottery Revenue Bonds," published June 13, 2007, on RatingsDirect). In our sector review, entitled "Why The Odds Favor Continued Strong Credit Quality For U.S. Lottery Revenue Bonds," we discuss the reasons why we rate these bonds 'AA' or higher.

Under Standard & Poor's policies, only a Rating Committee can determine a Credit Rating Action (including a Credit Rating change, affirmation or withdrawal, Rating Outlook change, or CreditWatch action). This commentary and its subject matter have not been the subject of Rating Committee action and should not be interpreted as a change to, or affirmation of, a Credit Rating or Rating Outlook.

The report is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. If you are not a RatingsDirect subscriber, you may purchase a copy of the report by calling (1) 212-438-7280 or sending an e-mail to research_request@standardandpoors.com.

Ratings information can also be found on Standard & Poor's public Web site by using the Ratings search box located in the left column at www.standardandpoors.com. Members of the media may request a copy of this report by contacting the media representative provided.

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TAX INCREMENT FINANCING - COLORADO

[1405 Hotel, LLC v. Colorado Economic Development Commission]

Colorado Court of Appeals, Div. I - September 10, 2015 - P.3d - 2015 WL 5259813 - 2015 COA 127

Hotels brought judicial review and declaratory judgment action challenging decision of Colorado Economic Development Commission (CEDC) to award city a tax increment subsidy under the Regional Tourism Act (RTA). The District Court dismissed action. Hotels appealed.

The Court of Appeals held that:

- As a matter of apparent first impression, point of administrative finality of award to city under RTA, as would trigger time period for filing of judicial review action, was time when CEDC adopted resolution memorializing terms of award;
- Hotels' premature filing of judicial review complaint did not render complaint untimely; and
- Hotels' alleged injury was indirect and incidental, and therefore hotels lacked standing to bring action.

Point of administrative finality of grant to city by the Colorado Economic Development Commission (CEDC) under the Regional Tourism Act (RTA), as would trigger time period for filing of action for judicial review, was time when CEDC adopted resolution memorializing terms of grant, not when CEDC gave it preliminary approval. Preliminary approval contained conditions which city had 120 days to fulfill, and to hold that conditional approval constituted final agency action would require parties affected by a conditional approval of a grant under the RTA to commence litigation before knowing whether the recipient of the RTA grant would fulfill those conditions and receive final approval.

Hotels' alleged injury from decision of Colorado Economic Development Commission (CEDC) to make grant to city for hotel and conference center development project, pursuant to the Regional Tourism Act (RTA), was indirect and incidental to city's alleged wrongdoing, and therefore hotels lacked standing to bring judicial review and declaratory judgment action challenging CEDC's and city's alleged failure to comply with RTA, including failure to require city to make new application for grant following change in developer. Even assuming project would cause hotels economic harm by drawing away some of their existing customers, such harm was not directly caused by CEDC's or city's alleged failure to comply with RTA but rather would result from development project's subsequent lawful conduct of competing in the tourism marketplace.

TAX - CALIFORNIA

[Myers v. State Board of Equalization]

Court of Appeal, Second District, Division 3, California - September 25, 2015 - Cal.Rptr.3d - 2015 WL 5656124

A taxpayer brought a mandamus and declaratory judgment action to compel state officials to collect a gross premium tax from two health care service plans on the basis that they were "insurers." The Superior Court sustained state officials' and health care service plans' demurrers without leave to amend. Taxpayer appealed.

The Court of Appeal held that:

- On issue of first impression, health care service plans were "insurers" subject to gross premium

tax if indemnifying against future contingent claims represented a significant financial proportion of their businesses;
- Prior final judgment denying declaratory and injunctive relief on same issue was within public interest exception to res judicata rule; and
- Taxpayer's action did not improperly seek to prevent or enjoin the collection of any tax.

Two taxpayers were "insurers" subject to the state constitution's gross premium tax if indemnifying against future contingent claims represented a significant financial proportion of taxpayers' businesses, even if the taxpayers were designated as "health care service plans" for regulatory purposes under the Knox–Keene Health Care Service Plan Act.

Trial court's prior final judgment denying declaratory and injunctive relief to compel a health care service plan to pay the state constitutional gross premium tax as "insurers" was within the public interest exception to the res judicata rule, in a new mandamus and declaratory judgment action against the same health care service plan and another plan, since the applicability of the gross premium tax presented a pure question of law, the matter affected public finances, and the prior judgment did not result in an appellate opinion.

The constitutional provision stating that no legal or equitable process shall issue to prevent or enjoin the collection of any tax did not bar taxpayers' mandamus and declaratory judgment action to compel state officials to collect a gross premium tax from two health care service plans on the basis that they were "insurers," since the action did not seek to enjoin the state from collecting any other taxes or fees. Whatever effect the "in lieu of" clause of the gross premium tax provision would have on the corporate franchise taxes the state had previously collected from the health care service plans was a matter for the plans to raise in a subsequent tax refund action.

TAX - ILLINOIS

Hertz Corp. v. City of Chicago

Appellate Court of Illinois, First District, Second Division - September 22, 2015 - N.E.3d - 2015 IL App (1st) 123210 - 2015 WL 5578591

Car rental companies brought declaratory judgment actions against city, asserting that ruling by city's department of revenue as to tax on use of vehicles leased by city residents was unconstitutional. The Circuit Court declared ruling facially unconstitutional and entered permanent injunction. City appealed.

The Appellate Court held that:

- Tax which ordinance imposed on any lessee of personal property who entered into any lease transaction in the city, irrespective of where leased property was used, and on lessees who used leased personal property more than 50 percent of the time in the city, irrespective of where lease transaction took place, was a use tax rather than a transaction tax, and therefore tax did not exceed city's home rule authority by taxing non-city vehicle lease transactions, even though ordinance imposing tax was titled "Personal Property Lease Transaction Tax." Taxable event was the privilege of using leased personal property inside the city. and
- Ruling did not exceed scope of ordinance.

Ruling by city's department of revenue requiring car rental companies to maintain records relating to whether vehicles were used within city and whether customers were residents of city, as proof of

claimed exemption for vehicles used outside of city for more than 50% of time, was not unreasonable, in declaratory judgment action brought by companies challenging ruling, which was promulgated pursuant to ordinance which taxed use of vehicles within city even if lease transaction took place outside city but within three miles of city's border, where companies already obtained such records from its customers in form of driver license information and form requiring customer to check box next to question on intended use of vehicle.

MSRB Amends its Continuing Education Requirements to Facilitate Web-based Delivery of Regulatory Element Training.

The Municipal Securities Rulemaking Board (MSRB) filed with the Securities and Exchange Commission amendments to MSRB Rule G-3 to facilitate the Web-based delivery method for the Regulatory Element of the Continuing Education ("CE") requirements. The CE amendments are effective immediately and will become operative on October 1, 2015 to coincide with the launch of the first Web-based modules for the Regulatory Element.

View the regulatory notice.

NABL: SEC Announces Second Round of MCDC Enforcement Actions.

The SEC announced today the second round of MCDC enforcement actions. The enforcement actions are against 22 underwriters with settlement amounts ranging from $20,000 to $500,000.

The SEC's press release announcing the enforcement actions is available here.

The orders are available here.

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22 MCDC Settlements With Firms to be Followed by Another Round.

WASHINGTON – The Securities and Exchange Commission's settlements ordering 22 municipal securities underwriting firms to pay $4.12 million for disclosure violations, is likely to be followed by a third round of settlements with firms under the SEC's Municipalities Continuing Disclosure Cooperation initiative, lawyers said on Wednesday.

"My understanding is that there will be another round of underwriter settlements," said National Bond Lawyers Association president Kenneth Artin, a shareholder at Bryant Miller Olive.

"I do believe that it is very likely that we will in fact see a third round of orders against underwriters," said Elaine Greenberg, a partner with Orrick, Herrington and Sutcliffe and former chief of the SEC enforcement division's municipal securities and public pensions unit.

After the underwriter settlements are completed, the SEC will release settlements with muni issuers.

In this round, PNC Capital Markets, LLC, which declined to comment on its settlement, paid the maximum penalty of $500,000 and Fifth Third Securities Inc. paid the lowest penalty of $20,000.

Each of 22 underwriting firms agreed to hire an independent consultant to review its policies and procedures on due diligence for municipal securities underwriting.

The MCDC initiative allows underwriters and issuers to receive lenient settlement terms from the SEC if they voluntarily self-reported any instances during the past five years in which the issuers falsely claimed in official statements that they were in compliance with their self-imposed continuing disclosure agreements and the underwriters were negligent in failing to discover the misstatements. Underwriters had to voluntarily report the violations by Sept. 10, 2014 and issuers by Dec. 1, 2014

The civil penalties for each firm are assessed according to the number and size of the issuers' fraudulent offerings, up to a cap based on the firm's size. The maximum possible penalty under the MCDC initiative is $500,000.

In this round, only PNC reached the $500,000 ceiling. This is a departure from the first round of underwriter settlements on June 18, in which 10 of 36 underwriters that paid a total of $9.3 million hit the maximum penalty.

In this round, the SEC found that between 2010 and 2014 the 22 firms sold munis using offering documents that contained materially false statements or omissions about the issuers' continuing disclosure compliance and were negligent in failing to conduct adequate due diligence to identify the misstatements and omissions before offering and selling the bonds. Those failures violated Rule 15c2-12 of the Securities and Exchange Act of 1934 on disclosure and showed a willful violation of Section 17(a)(2) of the Securities Act of 1933, according to the commission.

The 22 firms neither admitted nor denied the findings but agreed to cease and desist from such violations in the future.

"The MCDC Initiative has revealed that in recent years, a large number of municipal bond underwriters failed to conduct adequate due diligence before selling municipal bonds to their customers," said Andrew Ceresney, director of the SEC's enforcement division. "In addition to effectively addressing this past misconduct, we believe the initiative has been effective in improving underwriter due diligence in municipal securities offerings on a going forward basis."

The settlements provide more clues as to what it considers material failures to disclose compliance with continuing disclosure agreements.

In its order against Commerce Bank Capital Markets Group, the SEC the firm underwrote bonds in 2013 for an issuer that was timely in filing its annual financial report in its official statement but failed to cross-reference to its official statement on EMMA. The situation was similar to one in the first round of settlements involving Loop Capital Markets, but in that case the issuer failed to file its annual financial disclosure documents on time, as well as failed to cross-reference to its official statement on EMMA. This round shows the SEC's belief that cross-referencing to an official statements on EMMA is materially significant.

The majority of other specific examples the SEC provided in the 22 orders involved instances where issuers and obligors were either late in providing annual financial reports or annual operating data, or failed to disclose them at all. Crews & Associates, which was ordered to pay $250,000, underwrote bonds in 2013 for an issuer that had made no statements on prior disclosure compliance and no filings of financial disclosures on EMMA since 2009. The SEC found that other firms underwrote for issuers that ran the gamut for lateness. The SEC found that Estrada Hinojosa & Co. offered and sold bonds for an issuer that was 33 days late filing its annual financial report, while Joe Jolly & Co. sold bonds for an issuer that waited four years to file an annual financial report after it

was due.

The SEC granted waivers to each of the firms to prevent them from being disqualified from certain exemptions and safe harbors in SEC rules. Without those waivers, the firms charged in the settlements would probably be unable to do certain types of non-muni transactions.

The SEC's orders and penalty amounts for the second round of 22 underwriters are:

- Ameritas Investment Corp. – $200,000
- BB&T Securities, LLC – $200,000
- Comerica Securities, Inc. – $60,000
- Commerce Bank Capital Markets Group – $40,000
- Country Club Bank – $140,000
- Crews & Associates, Inc. – $250,000
- Duncan-Williams, Inc. – $250,000
- Edward D. Jones & Co., L.P. – $100,000
- Estrada Hinojosa & Company, Inc. – $40,000
- Fifth Third Securities, Inc. – $20,000
- The Frazer Lanier Company, Incorporated – $100,000
- J.J.B. Hilliard, W.L. Lyons, LLC – $420,000
- Joe Jolly & Co., Inc. – $100,000
- Mesirow Financial, Inc. – $100,000
- Northland Securities, Inc. – $220,000
- NW Capital Markets Inc. – $100,000
- PNC Capital Markets LLC – $500,000
- Prager & Co., LLC – $100,000
- Ross, Sinclaire & Associates, LLC – $220,000
- UBS Financial Services, Inc. – $480,000
- UMB Bank, N.A. Investment Banking Division – $420,000
- U.S. Bank Municipal Securities Group, a Division of U.S. Bank National Association – $60,000

THE BOND BUYER

BY JACK CASEY

SEP 30, 2015 10:41am ET

Orrick: SEC Eliminates References to Credit Ratings in Money Market Fund Rules.

On September 16, 2015, the Securities and Exchange Commission ("SEC") adopted revisions to Rule 2a-7, the primary rule governing money market funds. The amendments implement provisions of the Dodd-Frank Act that require federal agencies to replace references to credit ratings in regulations with alternative standards of credit-worthiness, and are consistent with the SEC's goal of reducing its reliance on credit ratings.

Rule 2a-7 currently requires that money market funds may only invest in "eligible securities" that receive one of the two highest short-term credit ratings. The current rule also requires funds to invest at least 97% of their holdings in securities that receive the highest short-term credit ratings.

Under the September 16 amendments, money market funds will now be required to invest in eligible securities that are determined to impose a "minimal credit risk" to the respective fund.

What is "minimal credit risk"? Funds will be required to determine "minimal credit risk" by using credit analysis factors related to the ability of the security's issuer/guarantor/demand-feature provider to meet its financial obligations. The relevant factors include, but are not limited to:

- financial condition;
- sources of liquidity;
- ability to react to future market-wide or issuer/guarantor-specific events (including the ability to repay debt in a highly adverse situation); and
- strength of the issuer/guarantor's industry within the economy and the issuer/guarantor's competitive position in the industry.

The SEC also revised Form N-MFP, a form used by money market funds to report portfolio information to the SEC on a monthly basis. Pursuant to the revisions, money market funds will now be required to disclose credit ratings they used in making their minimal credit risk determination, as well as the agency that provided the rating.

Additionally, the SEC adopted revisions to Rule 2a-7's diversification provision, which generally prohibit money market funds from investing more than 5% of their total assets in the securities of a single issuer. The current rule excludes from the diversification requirement securities that are subject to a guarantee by a "non-controlled person" (i.e. a person who does not control, is not controlled by, or under the common control of the security's issuer). Under the September 16 amendments, however, money market funds that invest in any security subject to a guarantee will be required to comply with the rule's issuer diversification requirement, regardless of whether the guarantor is a non-controlled person.

The revised rules become effective thirty days after they are published in the Federal Register and have a compliance date of October 14, 2016.

Last Updated: September 29 2015

Article by Suzette Pringle, Christin Joy Hill and Michael Tu

Orrick

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

NABL: SLGS Window May Re-Open in 5 Weeks.

Few things are certain when it comes to legislating, but news from the Treasury Department yesterday could mean that the SLGS window will reopen in late October or early November. The window has been closed since the Federal government's debt ceiling was reinstated last March. Treasury has been using its "extraordinary measures" to allow the government to continue to pay its bills and avoid default. Yesterday, Treasury Secretary Lew sent a letter to the Congressional leadership that tax receipts have not been as high and expenses have been higher than earlier projections indicated. The net result is that he now projects that on or about Thursday, November 5, the Treasury Department will have exhausted the extraordinary measures and have less than $30

billion in cash on hand. The following day is a payday for Federal employees and the following Tuesday is a payment date for some Social Security recipients. No doubt some Treasury bonds or notes will also mature around that time.

To read the full article, click here.

TEB Resources Allocation for FY 2016.

In a message released by IRS Tax Exempt and Government Entities Division (TE/GE) Commissioner Sunita Lough, half of the resources allocated to Tax-Exempt Bonds will be used for examination casework. Additionally, 30 percent of the resources will be used for the VCAP program to ensure its continued transparency and efficiency.

More information regarding the TE/GE workplan can be seen here on pages 12 and 13.

Key Firms Still Absent From Settlements as NABL Surveys MCDC Aspects.

WASHINGTON – At least two major Wall Street firms have not settled with the Securities and Exchange Commission under its Municipalities Continuing Disclosure Cooperation initiative, noted some lawyers who were involved with a National Association of Bond Lawyers survey on the impact of MCDC.

Carol McCoog, a partner at Hawkins, Delafield & Wood in Portland and the chair of NABL's securities law and disclosure committee, said the absence of large underwriting firms like Barclays Capital and Wells Fargo & Co. from the settlements likely means the SEC has more settlements coming.

"Maybe the SEC is just taking a little longer going through what I would anticipate would be more filings," McCoog said.

Another lawyer familiar with the enforcement process said it is not surprising that the firms have yet to be included.

The two large firms were among the top ten senior managing underwriters in the market in each of 2012 and 2013, the two years before the SEC announced the MCDC initiative. They held about 10% of the market share in each year and were also among the top ten underwriters for negotiated issues, which far outpaced the number of competitive issues that showed up in the first two rounds of MCDC settlements.

One perhaps surprising piece of information from the NABL survey was that 43% of the attorneys who responded said none of the underwriters they represented or advised self-reported under the initiative.

The survey, which included responses from 220 lawyers, was completed in January after the filing deadlines for underwriters and issuers. But it was not publicly disclosed until MCDC discussions at NABL's Bond Attorney's Workshop conference in Chicago last month and not made publicly available until Thursday.

The MCDC encouraged underwriters and issuers to voluntarily report to the SEC any time in the previous five years that they sold or underwrote bonds with offering documents that contained materially false or misleading statements or omissions. The deadline for underwriters to submit under the initiative was Sept. 10 of last year and the deadline for issuers was Dec. 1.

According to the survey, 91% of the respondents said they discussed establishing new disclosure policies and procedures with issuer clients because of MCDC. That response seems to provide evidence to back up the SEC's claims that the MCDC initiative has had a beneficial impact on continuing disclosure in the muni market. NABL added to that discussion by releasing a paper on Aug. 20 to help provide lawyers and their clients with considerations to take into account when crafting strong disclosure policies and procedures.

More issuers than underwriters seemed to self-report MCDC violations, according to the survey. Seventy-three percent of the lawyers that responded said all, most or some of their issuer and borrower clients self-reported, while only 58% said all, most or some of their underwriter clients self-reported. Lawyers said issuer clients sought approval from their governing bodies before reporting, with 44% saying the issuers did so without exception and 31% saying that they did so generally.

Some of the most surprising responses were related to questions regarding materiality. Roughly 93% of the lawyers that responded said their underwriter and issuer clients self-reported some or many misrepresentations about compliance with continuing disclosure obligations that were not material. According to case law, information is material if an investor would want to know it before buying or selling securities.

Further, 75% of respondents said their issuer or borrower clients analyzed the materiality of lapses before self-reporting and 45% said their clients felt they had to self-report lapses if underwriters had reported them, regardless of materiality.

Only 20% of lawyers who responded said they spent more than 50 hours representing or advising underwriters under the MCDC initiative and 59% said they spent less than 10 hours. In contrast, 57% of the lawyers spent more than 50 hours representing or advising issuers and borrowers on MCDC and only 5% spent less than 10 hours.

Most issuers and obligated persons declined to disclose their participation in MCDC in official statements for transactions that were taking place at that time or on EMMA. About 84% of the lawyers said clients did not include the information in an OS and 94% said clients never filed an EMMA notice on their MCDC participation.

THE BOND BUYER

BY JACK CASEY

OCT 5, 2015 4:03pm ET

Shining A Light On Municipal Bond Markups.

Transparency is an overused word that is rarely executed–especially in the bond market. Think about how long it took regulators to require that bond desks post trade prices, and amounts purchased and sold. Years. All the while bond dealers squirmed, kicked and screamed, claiming it would destroy the

debt market. Today, the bond market is alive and well—even with electronic pricing.

The Municipal Securities Rulemaking Board (MSRB) is currently proposing that bond dealers acting as principals fully disclose their markup or markdown to retail customers. That's right. When you purchase or sell a municipal bond your confirmation prints the trade profit your broker took. The industry calls this the spread. Details of this proposal are still evolving.

Here's how The Bond Buyer describes it:

> "Under the markup proposal, a dealer buying or selling bonds for its own inventory would be required to disclose the markup or markdown on a customer's confirmation when: it executes a transaction on the same side of the market as the customer; the transaction is greater than or equal to the size of the customer's; and the dealer transaction occurs within a two-hours window on either side of the customer transaction.
>
> Those markups and markdowns would be equal to the 'difference between the price to the customer and the prevailing market price for the security,' and would have to be disclosed both as a total dollar amount and as a percentage of the principal amount of the customer transaction."

I have one word to express my glee if this rule passes: Whoopie! That is because for years investors never knew what their broker was earning on their municipal bond trades. Certainly they could go to the emma.msrb.org Web site. And for those few who utilize the Web site, it's not clear for actively traded issues whose 25,000 or 50,000 trade actually belonged to whom. If this new rule goes into effect there will be no second-guessing—the telltale information will be right on the investor confirmation.

The SEC has said it wants more transparent markup and markdown disclosure. I couldn't agree more. Finally, investors will know if their broker or the Web site they point and click on is being fair or egregiously piggy.

Count on one thing: the brokerage industry will kick and scream, negotiate and whine, stomp and cry while trying to delay its implementation. In my opinion, the rule will be implemented. Small investors will be the biggest beneficiaries. Brokers and their firms will have no choice but to take less of your hard-earned investment dollars.

FORBES

MARILYN COHEN, CONTRIBUTOR

Marilyn Cohen is president of Envision Capital Management, Inc., a Los Angeles fixed-income money manager.

SEP 30, 2015

Munis Cheapest in 5 Weeks to Treasuries as Payrolls Fall Short.

Prices in the $3.6 trillion municipal-bond market are the cheapest in five weeks relative to Treasuries after U.S. payrolls rose less than projected in September, spurring a rally in federal government debt on signs the global slowdown is affecting the world's largest economy.

Benchmark 10-year munis yield 2.09 percent, compared with 1.92 percent on similar-maturity Treasuries, data compiled by Bloomberg show. The ratio is a measure of relative value between the asset classes. It reached 109 percent Friday, the highest since August, signaling that tax-free bonds are cheap relative to their federal counterparts.

Ten-year Treasury yields plunged 0.11 percentage point after a Labor Department report showed the U.S. added 142,000 jobs, lower than the median forecast of 201,000 from a Bloomberg survey of 96 economists. Weakening foreign markets, a stronger dollar and lower oil prices raise the risk that employers will hold off on adding workers.

Munis rallied to a smaller degree. As prices rose, the yields on both 10-year and 30-year AAA bonds fell 0.02 percentage point to the lowest since April, data compiled by Bloomberg show.
The 10-year muni-Treasury ratio was as low as 94 percent in July. Over the past decade, the figure has averaged 97 percent.

Bloomberg News

by Brian Chappatta

October 2, 2015 — 6:49 AM PDT

Port Authority Leads Rise in Muni Sales; Redemptions Decline.

Municipal bond sales in the U.S. are set to increase in the next month by the most since March, while the amount of redemptions and maturing debt falls.

States and localities plan to issue $15.3 billion of bonds over the next 30 days, according to data compiled by Bloomberg. A week ago, the calendar showed $12.1 billion planned for the coming month. Supply figures exclude derivatives and variable-rate debt. Some municipalities set their deals less than a month before borrowing.

Port Authority of New York and New Jersey plans to sell $2 billion of bonds to refund older securities, Chicago O'Hare International Airport has scheduled $2 billion of mostly refunding debt, Texas Water Development Board will offer $862 million and California will bring $446 million to market.

Municipalities have announced $8.3 billion of redemptions and an additional $8.4 billion of debt matures in the next 30 days, compared with the $25.1 billion total that was scheduled a week ago.

Issuers from New York have the most debt coming due with $2.03 billion, followed by California at $1.16 billion and New Jersey with $602 million. New York City Transitional Finance Authority has the biggest amount of securities maturing, with $916 million.

The $3.6 trillion municipal market shrank by 4 percent in 2014. This year, maturities are poised to drop 38 percent to $176 billion from the 2014 levels.

Investors added $628 million to mutual funds that target municipal securities in the week ended Sept. 23, compared with a reduction of $589 million in the previous period, according to Investment Company Institute data compiled by Bloomberg.

Exchange-traded funds that buy municipal debt increased by $243 million last week, boosting the value of the ETFs 1.4 percent to $17.6 billion.

State and local debt maturing in 10 years now yields 103.873 percent of Treasuries, compared with 103.631 percent in the previous session and the 200-day moving average of 102.526 percent, Bloomberg data show.

Bonds of Tennessee and Michigan had the best performance over the past year compared with the average yield of AAA rated 10-year securities, the data shows. Yields on Tennessee's securities narrowed 16 basis points to 2.00 percent while Michigan's declined 9 basis points to 2.30 percent. Puerto Rico and Illinois handed investors the worst results. The yield gap on Puerto Rico bonds widened 72 to 10.69 percent and Illinois's rose 22 basis points to 3.92 percent.

Bloomberg News

by Kenneth Kohn and Luis Daniel Palacios

October 5, 2015 — 4:36 AM PDT Updated on October 5, 2015 — 8:21 AM PDT

Butler Snow: Fed's Proposed Treatment of Municipal Securities as High-Quality Liquid Assets.

Fed's Proposed Treatment of Municipal Securities as High-Quality Liquid Assets

Financial Crisis and Bank Regulatory Response

In the aftermath of the financial crisis of 2008 and 2009, international banks sought to ensure sufficient liquidity for the largest banks by establishing a quantitative liquidity coverage ratio standard pursuant to the Basel III capital and liquidity reforms. United States bank regulators, including the Board of Governors of the Federal Reserve System (the "Fed"), the Office of the Comptroller of the Currency (the "OCC"), and the Federal Deposit Insurance Corporation (the "FDIC") published a joint Notice of Proposed Rulemaking (the "NPR"), adopted on September 3, 2014 [1], that established a Liquidity Coverage Ratio ("LCR") to be maintained by larger banks and holding companies [2]. The LCR would require covered institutions, during periods of non-stress, to maintain an amount of high-quality liquid assets ("HQLA") that is not less than 100% of its total net cash outflows over a prospective 30 calendar day period.

Significantly for municipal securities issuers and the municipal securities industry, securities issued by "public sector entities" (i.e., state and local government issuers) were not included as HQLAs in the original NPR.

Objections to NPR and Subsequent Fed Proposal

After predictable objections from trade groups representing municipal issuers, banks and the municipal securities industry, based upon potential harm to municipal securities issuance from exclusion of municipal securities as eligible HQLAs under the NPR, on May 28, 2014, the Fed (but without participation by the OCC or the FDIC) issued a proposal (the "Fed Proposal") that would permit covered institutions to include certain U.S. municipal securities as HQLAs under strict criteria described below.

The Fed Proposal

The Fed Proposal limits eligibility of U.S. municipal securities to investment grade general obligations that are not insured. Revenue obligations, irrespective of credit standing, would not qualify as HQLAs. [3] Additionally, the Fed Proposal imposes significant concentration risk limitations on a covered institution's holdings of HQLA-eligible U.S. municipal securities:

- No more than 25% of an individual CUSIP may be included in a bank's stock of HQLA;
- No more of a single issuer's bonds than an amount equal to two times the average daily trading volume of that issuer's bonds over the previous four quarters may be included in a bank's stock of HQLA; and
- No more than 5% of a bank's total stock of HQLA may be comprised of municipal securities.
  Issuer and Industry Comments

During the public comment period on the Fed Proposal, which ended July 24, 2014, the Fed received 13 comment letters from issuers and industry groups [4]. All commenters argued that the HQLA standards for municipal securities in the Fed Proposal were excessively limiting, with the exception of Better Markets, Inc., which argued that municipal securities should not be included in HQLAs at all because of the provision in the Fed Proposal that leaves the determination whether a security is "investment grade" to the covered institution itself.

A primary objection from all trade group commenters – including the Securities Industry Finance and Marketing Association ("SIFMA"), the Bond Dealers Association ("BDA") and a joint comment from 15 issuer groups that included the Government Finance Officers Association, the National Association of Counties, the National League of Cities and the U.S. Conference of Mayors – was the exclusion of investment grade revenue obligations from HQLA eligibility. Specifically, SIFMA noted that the credit quality of many revenue obligations is regarded by the market as preferable to general obligations, particularly in light of adverse treatment of general obligations in recent municipal bankruptcies such as Detroit's. Indeed, the PFM Group noted that the Fed Proposal "reduces the universe of outstanding eligible municipal securities by more than $2 trillion." Likewise, the Bond Dealers Association noted that the exclusion of revenue securities from HQLA effectively limits the municipal securities that would be eligible for inclusion as HQLA to less than 40% of securities issued in 2015.

Commenters, including municipal bond insurer Build America Mutual Assurance Company, also criticized the exclusion of insured general obligations from the HQLA eligibility, arguing that the Fed Proposal misconceived the role of bond insurance of otherwise investment grade obligations, which does not substitute for the underlying credit and actually adds liquidity to such securities.

Regarding the concentration risk limits in the Fed Proposal, commenters argued that they are based on misunderstandings of the municipal market. With regard to the limitation to 25% of a pertinent CUSIP (i.e., maturity), commenters argued that the rule would push banks to hold many smaller portions rather than large-block portions that are more liquid because of their appeal to institutional investors. SIFMA argued that the 25% limit is actually counterproductive to liquidity and that, alternatively, this rule should be dropped "in favor of reliance on the risk management systems banks already have in place."

Regarding the two-times average daily trading volume limitation, SIFMA noted that historic trading volume may not be the best indicator of liquidity in that many bonds are bought as buy-and-hold investments.

Regarding the limitation of U.S. municipal securities to not more than 5% of a bank's total HQLA,

SIFMA noted that no other asset class eligible for inclusion in HQLA, including corporate securities, has an asset-specific limitation. Additionally, the LCR rule separately limits 40% of total HQLA for Levels 2A and 2B combined and has a 15% limit for Level 2B. Thus, SIFMA argued that the existing limitations are sufficient without the addition of the 5% limit.

Potential Impact of the Fed Proposal?

What, then, will be the impact of the Fed Proposal if adopted in its present form? On the one hand, indications are that the HQLA limitations will reduce demand for U.S. municipal securities for covered banks and thus result in increased interest rates for securities bought by covered banks. Also, the absence of a joint regulation that includes the OCC and the FDIC could result in differential standards that could disrupt the market even further. However, since the Fed Proposal, as finally adopted, will directly affect only a dozen or so of the largest U.S. banks, it is unknown whether the ultimate Fed HQLA standards will affect non-covered bank lenders and the bond market generally [5].

1. 79 Fed. Reg. 61440 (October 10, 2014).
2. As of March 31, 2015, the U.S. banks meeting the criteria for "covered companies" under the Basel III standards are as follows: J.P. Morgan Chase & Co., Bank of America, Citigroup, Wells Fargo & Co., Goldman Sachs Group, Morgan Stanley, U.S. Bancorp, Bank of New York Mellon, PNC Financial Services Group, Capital One, HSBC North America Holdings, State Street Corporation, and TD Bank U.S. Holdings.
3. The LCR divides HQLA into three categories of assets: Level 1, Level 2A, and Level 2B liquid assets. Specifically, Level 1 liquid assets are limited to balances held at a Federal Reserve Bank and foreign central bank withdrawable reserves, all securities issued or unconditionally guaranteed as to timely payment of principal and interest by the U.S. government, and certain highly liquid, high credit quality sovereign, international organization and multilateral development bank debt securities. Level 1 liquid assets, which are the highest quality and most liquid assets, may be included in a covered company's HQLA amount without limit and without haircuts. Level 2A and 2B liquid assets have characteristics that are associated with being relatively stable and significant sources of liquidity, but not to the same degree as Level 1 liquid assets. Level 2 liquid assets include obligations issued or guaranteed by a U.S. government-sponsored enterprises (GSE) and certain obligations issued or guaranteed by a sovereign entity or a multilateral development bank that are not eligible to be treated as Level 1 liquid assets. The LCR subjects Level 2A liquid assets to a 15% haircut and limits the aggregate of Level 2A and Level 2B liquid assets to no more than 40% of the total HQLA amount. Level 2B liquid assets, which are liquid assets that generally exhibit more volatility than Level 2A liquid assets, are subject to a 50% haircut and may not exceed 15% of the total HQLA amount. Under the LCR, Level 2B liquid assets include certain corporate debt securities and certain common equity shares of publicly traded companies. Level 2 liquid assets, including all Level 2B liquid assets, must be liquid and readily marketable as defined in the LCR to be included in HQLA. Under the LCR final rule, U.S. municipal securities were not included in the definition of HQLA. However, under the Fed Proposal all U.S. municipal securities that qualify as HQLAs will constitute Level 2B liquid assets.
4. All public comments to the Fed Proposal are available on the Fed website at http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm.
5. Many thanks to Belinda Hannah at First National Banker's Bank in Birmingham, Alabama, and Alan Ganucheau, Greg Brewer, Jason Thomas and Steve Cole at Hancock Bank, for taking the time to discuss the Fed Proposal and its potential impact on the municipal securities market. However, nothing in this post is attributable to them or their employers, and, of course, any errors in this post are my own.

By E. Alston Ray
September 26, 2015

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Ballard Spahr: Proposed Legislation Provides Further Support for P3 Transportation Infrastructure Projects.

Legislation recently introduced in the U.S. House of Representatives calls for the senior procurement executive of the U.S. Department of Transportation (DOT) to enhance the services of the Office of Contract and Procurement by working with agencies, states, and other grant recipients on implementing public private partnership (P3) procurement best practices.

The legislation, H.R. 3465, was sponsored by Representative Sean M. Maloney of New York, who sits on the House Transportation and Infrastructure Committee. He served on a special committee panel that issued a report in September 2014 finding that P3s can be better utilized to enhance the delivery and management of transportation infrastructure projects across the country. The legislation calls for the senior procurement executive at DOT to develop suggested best practices to encourage standardizing state P3 authorities, including consistent, fair and balanced assumptions made in the calculations of unsolicited bids, noncompete clauses and other major P3 agreement elements.

A report by the Congressional Budget Office issued earlier this year found that P3 expenditures for the 36 highway and bridge P3s that have occurred in the United States over the last 25 years have totaled nearly $32 billion, which is less than 1 percent of the approximately $4 trillion spent on similar projects by all levels of government over that same period. While P3s cannot provide the sole solution to the nation’s infrastructure needs, H.R. 3465 intends to further encourage the use of P3s in financing transportation infrastructure needs. The legislation is among a series of recent steps taken to encourage the use of P3s.

A list of recent Ballard Spahr alerts on this topic are below:

Bill Would Create New Category of Tax-Exempt Bonds, Tax Credits for P3 Projects

Obama’s Proposed 2016 Budget Seeks To Address Infrastructure Needs

New P3 Legislation To Take Effect in Washington, D.C.

President Announces New Build America Initiatives; Introduces New Type of Municipal Bond

The full text of H.R. 3465 can be found here.

September 24, 2015

by the P3/Infrastructure Group

Attorneys in Ballard Spahr’s P3/Infrastructure Group routinely monitor and report on new developments in federal and state infrastructure programs related to transportation and other types of projects. For more information, please contact P3/Infrastructure Practice Leader Brian Walsh, William C. Rhodes, Steve T. Park, Christopher R. Sullivan, or the member of the Group with whom

you work.

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How to Pay for Local California Infrastructure Projects? New Website Offers an Answer.

Downtowns are back in demand. After decades of urban sprawl—and the long commutes, high infrastructure and housing costs, and loss of open spaces that accompany it—Californians are ready for something different. It's fair to say that there is a growing consensus among the state's civic leaders that vibrant, walkable communities will be a vital part of sustaining the economy and improving our quality of life.

The question is, how to pay for it?

While market demand for walkable urban places is climbing rapidly—prompting new interest in infill development—this demand has not been supported by reinvestment in the critical infrastructure that denser neighborhoods demand. Nor have communities had access to all the planning and financing tools they need to move ahead quickly with infill projects.

Until now, that is. With the governor's signature last week on a package of legislation that will expand local governments' infrastructure financing powers, civic leaders now have at their fingertips everything they need to begin making investments in projects from transit stations and housing to next-generation water facilities.

On the financing side, the new Enhanced Infrastructure Financing Districts may offer the most exciting possibilities. The California Economic Summit has been working over the last year to strengthen these powers, highlighting how they work and identifying the types of projects that could benefit from them. Mark Pisano, co-lead of the Summit Infrastructure Action Team and professor of the practice of public administration at the USC Sol Price School of Public Policy, recently said the new authority had the "potential to be one of [California's] most significant innovations in public finance over the last decade."

Now, it is time to spread the word—and show every community in California how they could benefit from this new authority. That's why Crowdbrite, a longtime partner of the Summit with a strong track record of expanding civic engagement around public projects, has created a new interactive website for these enhanced districts: www.eifdistricts.com.

Designed for city leaders and residents alike, the site provides details on the new statute, summarizing what types of projects communities can finance with these new authorities and providing short videos with frequently asked questions about the new powers. (No, they're not quite the same as redevelopment).

The site's Infill Score tool also offers a survey that allows users to assess their own community's infrastructure needs, to consider what types of projects could earn community support, and to think about how they might be able to deploy these new financing tools to revitalize their neighborhoods and support infill development. This infill-readiness assessment, which calculates a score based upon a community's record of using 30 unique strategies for incentivizing infill development, builds on the work of the U.S. Environmental Protection Agency and was developed in partnership with the Local

Government Commission and a group of city managers and national advisers.

While several major California cities are making plans to use their new EIFD authority (including Los Angeles, Sacramento, and San Jose), Crowdbrite's new online tool is already beginning to increase awareness of its potential for infill development. Since the website was launched ten days ago, 11 California cities have already completed the survey. Internationally, nearly 1,500 cities have signed up, with 50 cities taking action on this first step to community revitalization.

Now, it's your turn.

Take a moment to calculate your city's Infill Score to gauge your community's readiness for new infill development—and then use the online tool to establish priority projects and identify how to leverage public investment your community's infrastructure projects require.

After that, it may be time to reach out to your city's leaders—and to start reinvesting in your community and building a brighter future.

SEPTEMBER 30, 2015 BY DARIN DINSMORE

Darin Dinsmore is the CEO of Crowdbrite. An urban planner and landscape architect with over 15 years experience in community-based planning and design, Dinsmore is also a member of the Summit Infrastructure Action Team.

Webcast: Understanding Proposed IRS Rules on Issue Price and the Industry Impact

Topic: Understanding Proposed IRS Rules on Issue Price and the Industry Impact

October 20, 2015
@ 1:00 pm Eastern

A new proposal was issued this summer from the IRS affecting how and when the issue price of tax-exempt bonds is calculated. Will this added regulation serve as a disincentive to players in the bond field? Or could it allow for more versatility between public and private sector participants? During this installment of the CDFA // BNY Mellon Development Finance Webcast Series, hear our expert panel discuss the proposal and explain how this could change issuances going forward. Issuers, underwriters, advisors are encouraged to join this important conversation in advance of the IRS public hearing on the topic scheduled for later this month.

Click on the Register button below to confirm your participation and receive login information. Registration is free and open to all interested stakeholders.

REGISTER

The CDFA // BNY Mellon Development Finance Webcast Series is aimed at addressing real-time issues through the perspective of the industry's top leaders, giving the entire development finance industry access to these critical discussions. The Webcast Series will include panels of speakers discussing topics, challenges, opportunities and critical issues within the capital markets, municipal bond, state and local finance, and general economic development communities. Webcasts are also recorded and saved for future review by individuals not able to attend the live presentations.

Truth in Accounting: The Real Taxpayer Burden.

A new report by the financial transparency advocate Truth in Accounting shows what states' financial statements could look like soon with new pension accounting rules in place. The group tallies up state debt, and includes pension unfunded liabilities and retiree healthcare obligations. Starting this year, Government Accounting Standards Board (GASB) rules require states to include their unfunded pension liabilities in their government-wide financial statements to better reflect their debt burden. In a few years, accounting rules will require states to report unfunded retiree healthcare liabilities in the statement as well.

All states except Vermont have a balanced budget requirement, but annual budgets don't reflect long term debt. The total debt across all 50 states in 2014 was about $1.4 trillion, according to the report. Some (11) states had a positive balance sheet and enough in available assets to counteract their debt load and. But most (39) were in the red. The group then divided that balance sheet tally among all the state's taxpayers to come up with each state's taxpayer burden.New Jersey showed the biggest ever year-over-year leap in taxpayer burden for any state in the six years of the report's history. The jump was largely thanks to a big increase in its unfunded pension liability after new GASB accounting rules for all governments kicked in last year. The state's taxpayer burden went from $36,000 in 2013 to $52,300 last year, the highest in the country.

The group's report includes in-depth analyses of all 50 states.

GOVERNING.COM

BY LIZ FARMER | OCTOBER 2, 2015

GFOA Executive Board Approves New Best Practices.

On September 25, 2015, GFOA's Executive Board approved five new best practices and seven revised best practices, providing recommendations to government finance officers in the areas of accounting, budget, retirement benefits administration, capital planning, and debt issuance.

Understanding Your Continuing Disclosure Responsibilities. The Committee on Governmental Debt Management updated this best practice to alert issuers to the increasing attention of federal policy makers and investor advocacy organizations on improving disclosure for government bond issuers. The updated best practice emphasizes specific areas for issuers to make improvements in based on the SEC's 2014 Municipalities Continuing Disclosure Cooperation Initiative (MCDC), as well as separate SEC enforcement cases, such as the 2013 case against the City of Harrisburg, PA and the 2014 Allen Park, MI case. The GFOA is firmly committed to helping issuers understand and meet their federal continuing disclosure obligations, and have updated this best practice to further that effort.

Using Technology for Disclosure. Beyond updating this best practice to increase issuer awareness of federal regulatory efforts to improve issuer disclosure, the Debt Committee also wanted to alert issuers to improved uses of not only issuer websites but new features on the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Market Access (EMMA) system, which enable issuers to improve the flow of disclosure information to investors. Updates were also made to this best practice to advise issuers on concerns about using other digital communication platforms (such

as social media) to transmit disclosure information to investors.

Using Credit Rating Agencies. The Debt Committee developed this new best practice to provide guidance to governments about how to select and manage credit rating agencies. The best practice was organized to help finance officers navigate the ever changing landscape of credit rating methodologies, and alert governments to the key factors they should consider in hiring one or multiple rating agencies, the types of debt issues that may benefit from obtaining a credit rating, what an issuer should be prepared to do to maintain a credit rating, and guidance on terminating a relationship with a rating agency.

Defined Contribution Plan Fiduciary Responsibility. Recognizing many governments offer defined contribution retirement plans as a supplement to a defined benefit plan, or in some cases, as the sole employee retirement plan, this new best practice developed by the Committee on Retirement and Benefits Administration (CORBA) provides thorough guidance on a clear and well-documented governance structure to guide plan administrators, sponsoring entities, and governing bodies as they provide sound fiduciary guidance of the defined contribution retirement plan.

Informing and Educating Employees about Retirement Benefit Adequacy. CORBA built this new best practice to provide guidance to public-sector employers and plan administrators who have a responsibility to inform and educate employees about future retirement income in the context of the many variables that may compromise retirement benefit adequacy.

Adopting Financial Policies. The Committee on Governmental Budgeting and Fiscal Policy (Budget Committee) rewrote this best practice, which was last updated in 2001. The document recommends that governments formally adopt financial policies, and provides steps to consider when making effective financial policies include scope, development, design, presentation and review.

Determining the Appropriate Level of Unrestricted Fund Balance in the General Fund. This best practice is the result of the Budget Committee's efforts to combine the existing Determining the Appropriate Level of Unrestricted Fund Balance in the General Fund and Replenishing General Fund Balance best practices. In the new version of the document the GFOA recommends that governments establish a formal policy on the level of unrestricted fund balance that should be maintained in the general fund for GAAP and budgetary purposes. The Budget Committee recommends that such a guideline should be set by the appropriate policy body and articulate a framework and process for how the government would increase or decrease the level of unrestricted fund balance over a specific time period.

The Impact of Capital Projects on the Operating Budget. The Budget Committee prepared this new best practice following committee discussion about the analysis of operating impacts from capital, and the consensus opinion that such analysis is often deficient in practice. This is an indicator that practitioners are failing to understand the need, not effectively making the argument within their jurisdictions to include it, or lacking the tools and methodologies for calculating or showing the costs. To assist practitioners, this best practice recommends that governments discuss and quantify the operating impact of capital projects in their budget documents, and ensure that the impacts are identified on an individual project basis.

Assessing Risk and Uncertainty in Economic Development Projects. GFOA's Committee on Economic Development and Capital Planning (CEDCP) updated this best practice to better enumerate the steps in the risk assessment. The best practice recommends that governments recognize and evaluate risks related to participation in an economic development project before authorizing participation, and recommends that a project should not be undertaken if risks are determined to not be acceptable, and cannot be mitigated.

Monitoring Economic Development Performance. CEDCP updated this best practice to bring greater emphasis to comparing the results of the project to the goals in order to provide more insight on the quality of the decision to authorize the project and to enable organizational learning from the decision. The best practice recommends that recommends that governments monitor economic development projects and program performance to ensure objectives established in an economic development policy are accomplished, and ensure that the finance officer plays a central, functional role in these efforts.

Establishing a Comprehensive Framework for Internal Control. The Committee on Accounting, Auditing, and Financial Reporting (CAAFR) updated this best practice to reflect changes made to the Committee of Sponsoring Organizations' (COSO) Internal Control—Integrated Framework from 1992. The COSO document, the most widely recognized source of guidance on internal control, was updated and expanded in 2013, and the GFOA recommends that state and local governments adopt the COSO's Internal Control—Integrated Framework (2013) as the conceptual basis for designing, implementing, operating, and evaluating internal control. CAAFR also updated its Framework for Entity-wide Grants Internal Control best practice to be consistent with the expanded COSO publication.

Thursday, October 1, 2015

IRS Tax Exempt & Government Entities Priorities for FY2016.

Read the IRS report.

CUSIP: Muni Volume Hits 11 Month Low in August.

CUSIP Global Services (CGS) today announced the release of its CUSIP Issuance Trends Report for August 2015. The report, which tracks the issuance of new security identifiers as an early indicator of debt and capital markets activity, suggests a possible slow-down in new corporate and municipal bond issuance over the next several weeks.

Read the report.

- **PROGRAM NOTE:** As of this week, we are implementing password-protection for the bondcasebriefs.com website. The initial password is: **muni**. The links contained in the weekly newsletter have the password embedded, so a reader who clicks on a link will be taken directly to the corresponding item hosted on the website without being required to enter a password. The password will be required only in the event that the website is accessed directly. We apologize for any technical glitches that may arise during the implementation process.
- MSRB Requests Comment on Requiring Disclosure of Mark-Ups.
- MSRB: Dealers Would Have to Disclose Markups on Principal Transactions.
- S&P Credit FAQ: Proposed Criteria Changes Will Bring Greater Transparency to U.S. Municipal Water and Sewer Systems.
- Incentive To Pay: How Recent Bankruptcies Inform Analysis Of Distressed Local Government

Credits.
- BDA Submits Issue Price Comment Letter to IRS.
- IRS Chief Counsel Blasted for Favorable Ruling on Total Return Swaps.
- NABL Submits Issue Price Comments.
- SIFMA Submits Comments to the IRS on Re-proposed Issue Price Rules.
- And finally, Unclear on the Concept is brought to you this week by *Sherman v. Town of Randolph*, in which the the court's opinion included the following, "Four of those candidates are relevant here: Sherman, who was ranked highest on the eligibility list, and the three candidates who ultimately bypassed him, *whom we shall call* Walter Burton, Blair Lewis, and Martin Duval." Did the court simply decide to get gratuitously creative with its fictitious naming ("No John Doe for us!") or was it indeed unclear on the concept? Please direct your inquiries to the opinion's author, whom we shall call Justice Fernande R.V. Duffly.

ZONING - ILLINOIS

Gurba v. Community High School Dist. No. 155

Supreme Court of Illinois - September 24, 2015 - N.E.3d - 2015 IL 118332 - 2015 WL 5608249

Residential owners of property adjacent to high school filed suit against school Board of Education and high school district seeking to privately enforce city's zoning restrictions with respect to construction of new bleachers for high school football stadium.

Board filed third-party complaint against city and school superintendent, seeking declaratory judgment that city lacked authority to enforce its zoning and storm water ordinances against Board.

The Circuit Court entered summary judgment for city, based on determination that school property was subject to ordinances. Board appealed. The Appellate Court affirmed. Board and superintendent's petitions for leave to appeal were allowed.

The Supreme Court of Illinois held that:

- City had home rule authority to enforce zoning and storm water management ordinances on school property;
- City's exercise of home rule authority to enforce zoning and storm water management ordinances did not interfere with constitutional authority of General Assembly to regulate public education system;
- City's home rule authority to enforce ordinances on school property was not limited to school property that was not used for school purposes; and
- Nothing in Health/Life Safety Code for Public Schools had any bearing on city's home rule authority to enforce ordinances on school property.

INVERSE CONDEMNATION - ALABAMA

Cooper v. Ziegler

Supreme Court of Alabama - September 18, 2015 - So.3d - 2015 WL 5511322

Property owners brought action against director of Alabama Department of Transportation (ALDOT) in his official capacity, asserting inverse-condemnation claim and seeking declaratory and injunctive

relief to enjoin director from prohibiting property owners from obtaining legal permits to build houses on their property. The Circuit Court granted property owners injunctive relief. Director appealed.

The Supreme Court of Alabama held that director was entitled to sovereign immunity.

Denial by Director of the Alabama Department of Transportation (ALDOT), in his official capacity, of property owners' requests to build houses on their property was strictly in accordance with ALDOT's purchased rights in easement and were not done fraudulently, in bad faith, beyond his authority, or under mistaken interpretation of law, and therefore director was entitled to sovereign immunity in injunctive relief action by property owners seeking to enjoin director from prohibiting them from obtaining permits to construct houses on property subject to easement. Director contended that he denied requests to build homes because construction would have required digging, cutting trees, and removing soil, which could have compromised interstate bridge structure and integrity of peninsula on which property was located in flooding conditions by speeding up erosion and causing possible bridge failure.

REFERENDA - ARIZONA

Respect Promise in Opposition to R-14-02-Neighbors for a Better Glendale v. Hanna

Court of Appeals of Arizona, Division 1 - September 18, 2015 - P.3d - 2015 WL 5474447 - 721 Ariz. Adv. Rep. 33

Citizen filed application for writ of mandamus seeking to compel city and city clerk to accept and file referendum petitions challenging the city council's approval of a resolution and settlement agreement, under which city agreed to drop its opposition to Indian tribe's proposed casino project on land contiguous to city's border. The Superior Court denied the application. Citizen appealed.

The Court of Appeals held that:

- Provisions of resolution unrelated to settlement agreement were not legislative acts subject to referendum;
- Settlement agreement was not referable; and
- City clerk had authority to reject referendum petitions.

Provisions of city council resolution that affirmed or acknowledged prior resolutions of the council, expressed support for Indian tribe's proposed gaming project on land contiguous to city's border, and urged the State and its representatives to withdraw their opposition to the project, reflected the council's changed position and did not amount to "legislation," and thus provisions were not subject to referendum. Resolution merely reflected city council's changed position as to the proposed gaming project.

City council's approval of settlement agreement between city, Indian tribe, and gaming enterprise was not "legislation" subject to referendum, although the agreement was a substantive measure that obligated the city to construct infrastructure for the benefit of the gaming project. Council determined that it was in the city's best interests to stop its challenges to the tribe's proposed gaming facility and to end the disputes between them, city's agreement to initially fund off-site infrastructure was a non-referable administrative act, and allowing city's voters to control litigation would result in chaotic and absurd result if settlement agreement was later rejected by voters.

City clerk had authority to reject referendum petitions challenging city council's approval of a resolution and related settlement agreement in support of construction of a casino on land contiguous to city's borders, taken in trust by the Secretary of the Department of the Interior on behalf of Indian tribe, although statute governing challenges to a legislative measure via referendum couched clerk's duties in response to a petition in terms of what the clerk "shall" do in response. Petitions professed to challenge a non-legislative act of the city council, and statutory scheme and relevant constitutional provisions revealed that clerk had authority to reject petitions challenging non-legislative and non-referable acts.

MUNICIPAL SERVICES - CONNECTICUT

Turn of River Fire Dept., Inc. v. City of Stamford

Appellate Court of Connecticut - September 15, 2015 - A.3d - 159 Conn.App. 708 - 2015 WL 5245274

Volunteer fire department and its chief brought action for declaratory and injunctive relief against city, city fire chief, city fire marshal, and city's director of public safety, health, and welfare, alleging that new organizational structure of the fire department violated their corporate, statutory, and constitutional rights. Following trial, the Superior Court rejected all claims. Volunteer fire department and its chief appealed.

The Appellate Court held that:

- Charter amendments did not compel volunteer fire department to continue to provide firefighting services or usurp volunteer department's rights as a private corporation;
- Statute governing the authority of towns to establish a fire department did not apply to municipal fire department created by charter as opposed to an ordinance;
- Charter amendments did not "supersede" volunteer department in violation of statute;
- Charter amendments did not cause a per se regulatory taking in violation of the Fifth Amendment; and
- Volunteer chief did not have a constitutionally-protected property right to direct the volunteer department's fire protection services free from oversight.

PENSIONS - ILLINOIS

Village of Vernon Hills v. Heelan

Supreme Court of Illinois - September 24, 2015 - N.E.3d - 2015 IL 118170 - 2015 WL 5608128

Municipality brought action against police officer seeking declaratory judgment that municipality was not obligated, under the Public Safety Employee Benefits Act (Act), to pay health insurance premiums for officer and his family after officer was awarded a line-of-duty disability pension by the board of trustees for the municipality's police pension fund.

The Circuit Court, Lake County, Margaret entered judgment in favor of officer but denied his motion for sanctions. Municipality appealed and officer cross-appealed. The Appellate Court affirmed. Municipality petitioned for leave to appeal.

The Supreme Court of Illinois held that:

- Where it is uncontroverted that a line-of-duty disability pension has been awarded to a police officer pursuant to the Pension Code, section of Act providing for health insurance benefits upon a "catastrophic injury" is satisfied as a matter of law, and
- Construction of Act as such did not deny due process to municipality.

Where it is uncontroverted that a line-of-duty disability pension has been awarded to a police officer pursuant to the Pension Code, section of the Public Safety Employee Benefits Act (Act) providing for health insurance benefits upon a "catastrophic injury" is satisfied as a matter of law, and there is no need to engage in discovery or present evidence regarding the officer's injury in order to recover benefits under the Act.

Construction of Public Safety Employee Benefits Act (Act) to provide that where it is uncontroverted that a line-of-duty disability pension has been awarded to a police officer pursuant to the Pension Code, section of Act providing for health insurance benefits upon a "catastrophic injury" is satisfied as a matter of law, did not deny due process to municipality, despite argument that construction of statute denied municipality opportunity to litigate nature of officer's injuries, in municipality's action seeking declaration that it was not obligated to pay health insurance premiums for officer and his family after officer was awarded line-of-duty disability pension. Enactment of Act itself afforded municipality all of the process that it was due.

IMMUNITY - ILLINOIS

O'Toole v. Chicago Zoological Society

Supreme Court of Illinois - September 24, 2015 - N.E.3d - 2015 IL 118254 - 2015 WL 5608152

Visitor who tripped and fell on pathway at zoo located on county forest preserve district land brought negligence action against zoological society, alleging it breached duty to inspect and maintain pathway. The Circuit Court dismissed the action on limitations grounds. Visitor appealed. The Appellate Court reversed and remanded. Zoological society petitioned for leave to appeal, which was granted.

The Supreme Court of Illinois held that zoological society did not conduct "public business," and was thus not a "local public entity" to which one-year limitations period would apply under Local Governmental and Governmental Employees Tort Immunity Act.

No factor is more important, in determining whether a not-for-profit is a "local public entity" under Local Governmental and Governmental Employees Tort Immunity Act, than control, since without evidence of local governmental control, it cannot be said that a not-for-profit corporation conducts "public business." Indicative of such control would be evidence that the entity remains subject to state statutes, such as the Open Meetings Act and the Freedom of Information Act, with which governmental units must comply, or even local ordinances that dictate the means and methods to be used by the not-for-profit corporation in conducting its business.

Zoological society, a not-for-profit corporation located in county forest preserve district, did not conduct "public business," and was thus not a "local public entity" to which one-year limitations period would apply to negligence action arising when visitor tripped and fell at zoo, under Local Governmental and Governmental Employees Tort Immunity Act. Contract between zoo and district gave zoological society entire control and management of zoo, including control over daily operations, maintenance of zoo building and collections, 90% of zoological society's board of

trustees and governing members were neither employees nor elected officials of district, and zoo employees were not entitled to state pension or state workers' compensation.

EMPLOYMENT - MASSACHUSETTS

Sherman v. Town of Randolph

Supreme Judicial Court of Massachusetts, Suffolk - September 24, 2015 - N.E.3d - 2015 WL 5599144

Police officer sought review of Decision of the Civil Service Commission dismissing his appeal from town's decision to bypass him for promotion to sergeant. The Superior Court Department entered judgment for Commission. Officer appealed, and petition for direct appellate review was allowed.

The Supreme Judicial Court of Massachusetts held that town's decision to bypass officer was reasonably justified despite flaws in process.

Town's decision to bypass police officer for promotion to sergeant was reasonably justified, even though town's interview process was flawed. Officer received an overall low score, post-interview letters from member of panel articulated reasons why candidates' interview performances warranted bypass, and officer's supervisors had raised concerns that officer had difficulty in following through on case investigation and needed supervision.

A promotional decision may be reasonably justified on the merits, even where the appointing authority uses flawed procedures for selecting candidates, in the following limited circumstance: where the appointing authority had a reasonable justification on the merits for deciding to bypass a candidate, and the flaws in the selection process are not so severe that it is impossible to evaluate the merits from the record.

ZONING - NEW HAMPSHIRE

Merriam Farm, Inc v. Town of Surry

Supreme Court of New Hampshire - September 22, 2015 - A.3d - 2015 WL 5559892

Property owner that was previously denied a building permit for failure to satisfy the frontage requirement appealed from the denial by town's zoning board of adjustment (ZBA) of its application for a variance from the frontage requirement. The Superior Court dismissed the appeal on the basis of res judicata. Owner appealed.

The Supreme Court of New Hampshire held that owner's application for a variance was not the same cause of action as its application for a building permit.

Property owner's application to town's zoning board of adjustment (ZBA) for a variance from the frontage requirement was not the same cause of action as its earlier application for a building permit, which was denied for failure to satisfy the frontage requirement, and thus res judicata did not bar the variance application. Owner could not have added the variance claim to its appeal from the denial of the building permit application, since the building permit could have been granted without a variance if certain other conditions were met, and it was for the ZBA rather than the trial court to decide in the first instance whether to issue a variance.

EMINENT DOMAIN - NEW YORK

Smithline v. Town of Harrison

Supreme Court, Appellate Division, Second Department, New York - September 23, 2015 - N.Y.S.3d - 2015 WL 5568446 - 2015 N.Y. Slip Op. 06921

Homeowners brought action challenging town's exercise of its power of eminent domain.

The Supreme Court, Appellate Division held that homeowners were afforded full opportunity to raise their objections to town's proposed condemnation, and thus town's error was harmless in omitting information regarding homeowners' right to seek judicial review in both its notice of hearing and its notice of determination, which authorized eminent domain and resolved to condemn permanent easement across homeowners' property to install underground drainage and temporary easement for access and stockpiling of materials, where homeowners appeared and participated at public hearing and timely sought judicial review of town's determination.

IMMUNITY - NEW YORK

Lewis v. City of New York

Supreme Court, Appellate Division, Second Department, New York - September 23, 2015 - N.Y.S.3d - 2015 WL 5568629 - 2015 N.Y. Slip Op. 06896

Police officer brought action against city, alleging that injuries he sustained when he was shot in the torso while apprehending a suspect were caused by city's negligence in failing to provide him with bulletproof vest that covered a larger area of his torso, allegedly provided to most other officers and new recruits. City moved for summary judgment. The Supreme Court, Queens County, granted motion. Police officer appealed.

The Supreme Court, Appellate Division, held that city was entitled to qualified immunity.

City's decision-making process regarding particular type of bullet proof vests it issued to police officers was discretionary governmental function, and city's decision to issue certain vest to officer was not irrational or arbitrary, and thus city was entitled to qualified immunity in police officer's negligence action, alleging that city was negligent in issuing vest to officer that was not large enough to protect officer from injuries to his torso he sustained during shooting while apprehending suspect.

PUBLIC TRUSTS - NEW YORK

Gessin v. Throne-Holst

Supreme Court, Appellate Division, Second Department, New York - September 23, 2015 - N.Y.S.3d - 2015 WL 5569019 - 2015 N.Y. Slip Op. 06885

Town taxpayers residing in incorporated village brought action against town trustees, town board, and town comptroller, alleging waste and unlawful expenditure of public funds by town trustees, and seeking declaratory and injunctive relief. The Supreme Court, Suffolk County, denied trustees' motion to dismiss and granted plaintiffs' motion for preliminary injunction. Trustees appealed.

The Supreme Court, Appellate Division, held that:

- Statute granting town trustees control over their affairs and finances governed duties and powers of the trust, and
- Reference to trusts in town law governing town funds did not require revenue of trust to be turned over to town board.

Statute granting town trustees control over their affairs and finances, which was not codified, governed duties and powers of the town trust, precluding town taxpayer's claim that revenues of trust must be turned over to town board. Statute had never been repealed or amended, statute was enacted after creation of town officers further indicating that trustees' authority was independent of town control, and town laws defining town officers and town's administrative unit did not refer to trustees.

Reference to trusts in town law governing town funds did not require revenue of town trust to be turned over to town board, or amend definition of town officers to include town trustees, by instead merely required town boards to designate where trustees' funds were to be deposited and provided that by depositing their funds in such a manner, the trustees would be relieved of liability in the event that the depositing institution failed.

LIABILITY - NEW YORK

Gonzalez v. City of New York

Supreme Court, Appellate Division, First Department, New York - September 22, 2015 - N.Y.S.3d - 2015 WL 5552724 - 2015 N.Y. Slip Op. 06869

After city police officer fatally shot his girlfriend while off duty and then killed himself, girlfriend's estate brought wrongful death action against city, alleging that city was negligent in supervising and retaining officer. The Supreme Court, Bronx County, granted summary judgment to city. Estate appealed.

The Supreme Court, Appellate Division, held that:

- Estate sufficiently alleged a connection or nexus between girlfriend's injuries and officer's malfeasance;
- Person on whom injury was inflicted was foreseeable; but
- Fact issues existed as to breach of duty and proximate cause.

Estate of girlfriend of city police officer sufficiently alleged a connection or nexus between girlfriend's injuries and officer's malfeasance, in action against city for negligent retention and supervision, brought after officer fatally shot girlfriend while off duty and then killed himself. City was alleged to have played a part in both creating the danger, by training and arming the officer, and in rendering the public more vulnerable to the danger, by allowing the officer to retain his weapon and ammunition after it allegedly learned of his dangerous propensities, so that officer's alleged tort was made possible through use of his pistol, which he carried by authority of city.

The person on whom the injury was inflicted was foreseeable, as required for duty element of claim against city for negligent retention and supervision, brought by estate of girlfriend of city police officer after officer fatally shot girlfriend while off duty and then killed himself. City could reasonably have anticipated that its alleged negligence in failing to discipline an officer who had violent propensities would result in the officer using his gun to injure a member of his own family,

including his girlfriend.

Genuine issues of material fact regarding breach of duty and proximate cause, i.e., whether city had received complaints about city police officer's alleged abusive conduct toward his girlfriend and her infant daughter, and whether the intervening intentional tort of the off-duty officer was itself a foreseeable harm that shaped the duty imposed upon city when it failed to guard against a police officer with violent propensities, precluded summary judgment for city, in action for negligent retention and supervision, brought by girlfriend's estate after officer fatally shot girlfriend while off duty and then killed himself.

LIABILITY - TEXAS

Lawson v. City of Diboll

Supreme Court of Texas - September 18, 2015 - S.W.3d - 2015 WL 5458763

Softball game spectator, who sustained injuries in trip-and-fall accident while exiting baseball complex at city park, brought premises defect action against city. City filed plea to the jurisdiction. The District Court denied plea. City appealed. The Court of Appeals reversed. Spectator petitioned for review.

The Supreme Court of Texas held that spectating at youth softball game at city park was not "recreation" under recreational use statute, and thus statute did not limit city's liability for damages claimed by spectator.

Enrollment Opens for Pilot Series 50 Exam for Municipal Advisors.

Alexandria, VA – The Municipal Securities Rulemaking Board (MSRB) announced today that municipal advisors may now begin enrolling to take the pilot Municipal Advisor Representative Qualification Examination (Series 50). The registration window for the pilot exam begins today, September 21, 2015 and closes on January 14, 2016.

Municipal advisor firms will need to utilize the Financial Industry Regulatory Authority's (FINRA) Form U10 to enroll their municipal advisor professionals for the Series 50 pilot exam and to remit the exam fee of $265. Once the Form U10 is accepted, individuals will be able to select a date to sit for the exam during the pilot period of January 15, 2016 – February 15, 2016.

As part of its expanded mandate under the Dodd-Frank Wall Street Reform and Consumer Protection Act, the MSRB amended its Rule G-3 on professional qualifications to establish the requirement that all municipal advisor professionals take and pass a qualifying exam. A municipal advisor professional who takes and passes the Series 50 pilot exam will be qualified as a municipal advisor representative and will not be required to take the permanent Series 50 exam when it is implemented in 2016. A municipal advisor professional who takes and does not pass the Series 50 pilot exam will have the exam fee waived for the first re-take of the permanent Series 50 exam.

"The MSRB encourages municipal advisor professionals to consider participating in the Series 50 pilot exam," said MSRB Executive Director Lynnette Kelly. "Strong participation in the pilot is a good way for municipal advisors to establish their qualifications and will assist the MSRB in validating the question bank and setting the passing score for the permanent exam."

For more information regarding the Series 50 pilot exam, see the MSRB's Regulatory Notice 2015-15.

Access resources and information about municipal advisor professional qualifications and the Series 50 pilot exam on the MSRB's website.

Date: September 21, 2015

Contact: Jennifer A. Galloway, Chief Communications Officer
(703) 797-6600
jgalloway@msrb.org

MSRB Requests Comment on Requiring Disclosure of Mark-Ups.

Alexandria, VA – The Municipal Securities Rulemaking Board (MSRB) is seeking public comment on a proposal to require municipal securities dealers to disclose on retail customer confirmations the amount of the mark-up in a class of principal transactions. The mark-up disclosure proposal seeks to enhance the transparency of investor transaction costs and dealer compensation in the municipal securities market and is the first proposal of its kind in over 20 years.

"Investors need a way to understand the true costs of their municipal securities transactions," said MSRB Executive Director Lynnette Kelly. "Our new proposed approach would offer greater clarity for investors as to dealer compensation while leveraging the existing processes and systems dealers use to comply with their fair-pricing obligations."

The draft amendments to MSRB Rule G-15, in essence, would require dealers acting as principal to disclose to retail customers their mark-up from the prevailing market price of a municipal security if the dealer makes a corresponding trade within two hours of the customer trade. To assist investors in learning more about the market for their traded security, the draft amendments also would require all retail customer confirmations to include a link to the main page for the security on the MSRB's Electronic Municipal Market Access (EMMA®) website. The EMMA website provides free public access to official disclosures, trade data, credit ratings, educational materials and other information about virtually all municipal securities.

The MSRB's request for comment seeks input on possible alternatives to its preferred approach, including a modified version of the MSRB's earlier proposal to require dealers to provide on retail customer confirmations a reference price for a comparable transaction by the dealer and the difference between those prices.

The MSRB's mark-up disclosure proposal to increase the transparency of dealer compensation and transaction costs aligns with the MSRB's strategic priorities and is based on a recommendation in the SEC's 2012 Report on the Municipal Securities Market. Read the request for comment.

The MSRB will host an educational webinar to review its request for comment on Thursday, October 29, 2015 at 3 p.m. Eastern Time. Register for the webinar.

Comments should be submitted no later than November 20, 2015.

Date: September 24, 2015

Contact: Jennifer A. Galloway, Chief Communications Officer
(703) 797-6600
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CUSIP Request Volume Shows Fourth Consecutive Monthly Decline Among Corporate and Municipal Bond Issuers.

“Everyone in the financial markets – including issuers of new debt – is focused on the prospect of the Fed raising rates in September; we’re seeing that reflected in the CUSIP data,” said Richard Peterson, Senior Director of Global Markets Intelligence, S&P Capital IQ. “The combination of increased market volatility and uncertainty around interest rates has created a perfect storm for a slowdown in new issuance. The question now is: how long will it last?”

Read the Press Release.

September 15, 2015

GASB Invites Governments to Participate in Survey of Financial Report Preparers.

The purpose of this survey is to gather information regarding the activities that governments engage in when preparing and publishing their audited annual financial reports in conformity with generally accepted accounting principles (GAAP), when those activities take place, and the number of technical staff hours involved. To assist you in completing the survey, the GASB staff will be available to answer questions throughout the survey period.

The staff also will be conducting two telephone conferences to provide an overview of the survey and answer your questions—on Wednesday, September 30, at 10:00 am EDT and Thursday, October 8, at 4:00 pm EDT.

Download the survey.

Register for the September 30 teleconference.

Register for the October 8 teleconference.

The completed survey should be emailed to dmmead@gasb.org no later than December 15, 2015.

If you have any questions about this survey, please contact:

Pam Dolan (pdolan@gasb.org)

Amy Shreck (ashreck@gasb.org)

THANK YOU

Cities Bear Rising Cost of Keeping Water Safe to Drink.

TOLEDO, Ohio — Standing at the edge of the Great Lakes, the world's largest surface source of fresh water, this city of 280,000 seems immune from the water-supply problems that bedevil other parts of the country. But even here, the promise of an endless tap can be a mirage.

Algae blooms in Lake Erie, fed by agriculture runoff and overflowing sewers, have become so toxic that they shut down Toledo's water system in 2014 for two days. The city is considering spending millions of dollars to avoid a repeat.

Similar concerns about water quality are playing out elsewhere. Farm fertilizers, discarded pharmaceuticals, industrial chemicals and even saltwater from rising oceans are seeping into many of the aquifers, reservoirs and rivers that supply Americans with drinking water.

Combating these growing threats means cities and towns must tap new water sources, upgrade aging treatment plants and install miles of pipeline, at tremendous cost.

Consider tiny Pretty Prairie, Kansas, less than an hour's drive west of Wichita, where the water tower and cast-iron pipes need to be replaced and state regulators are calling for a new treatment plant to remove nitrates from farm fertilizers. The fixes could cost the town's 310 water customers $15,000 each.

Emily Webb never gave a second thought to the town's water until she became pregnant almost two years ago. That's when she learned through a notice in the mail that the water could cause what's known as "blue baby" syndrome, which interferes with the blood's ability to carry oxygen.

"It just kind of scared me," she said. "Now we don't drink it at all."

Instead, she and her husband stock up on well water from her parents' home and buy bottled water even though health officials say the risk is limited to infants. When it comes time to buy their first home, she said, they will look somewhere else.

Pretty Prairie's leaders hope to find a less expensive solution. They say the cost of a new treatment plant would drive people away and threaten the farm town's survival.

Across the country, small towns and big cities alike are debating how much they can afford to spend to make contaminated water fit for drinking.

Cash-strapped cities worry that an unfair share of the costs are being pushed onto poor residents. Rural water systems say they can't expect the few people they serve to pay for multimillion-dollar projects.

The U.S Conference of Mayors, in a report released this summer, found spending by local governments on all water-supply projects nearly doubled to $19 billion between 2000 and 2012. Despite a slowdown in recent years, it remained at an all-time high, the report said.

"We have a real dilemma on our hands," said Richard Anderson, author of the report. "We know we need to increase spending on water, but many houses can't afford it, and Congress won't increase funding."

In California's Central Valley, low-income farming communities have gone without clean water for

years because they don’t have money to build plants to remove uranium, arsenic and nitrates. Drinking fountains at schools have been put off limits, and families spend a large share of their income on bottled water.

A study released in June by the U.S. Geological Survey found nearly one-fifth of the groundwater used for public drinking systems in California contained excessive levels of potentially toxic contaminants.

Compounding the problem is the drought. Because farmers are using more groundwater for irrigation, contaminants are becoming more concentrated in the aquifers and seeping into new wells.

The drought has pushed Los Angeles to plan for the nation’s largest groundwater cleanup project, a $600 million plan to filter groundwater contaminated with toxic chemicals left over from the aerospace and defense industry. Some of the water will be drawn from polluted wells abandoned 30 years ago.

In the Midwest, where shortages typically have not been a concern, more attention is being paid to farming’s effect on drinking water supplies.

Minnesota’s governor this year ordered farmers to plant vegetation instead of crops along rivers, streams and ditches to filter runoff. The water utility in Des Moines, Iowa’s largest city, is suing three rural counties to force tighter regulations on farm discharges.

And in the wake of Toledo’s water crisis, Ohio has put limits on when and where farmers can spread fertilizer and manure on fields.

“But no one really knows how well that works,” said Chuck Campbell, the city’s water treatment supervisor.

Given that, the city has spent $5 million in the past year to bolster its ability to cleanse water drawn from Lake Erie. It is planning a renovation that could approach $350 million and include a system that uses ozone gas to destroy toxins produced by the algae. A 56 percent water rate increase is footing most of the bill.

In many coastal areas, rising seas mean saltwater can intrude into underground aquifers and in some cases ruin existing municipal wells. It’s especially problematic in the Southeast, from Hilton Head Island in South Carolina to Florida’s seaside towns near Miami.

“Nature’s calling the shots and we’re reacting,” said Keith London, a city commissioner in Hallandale Beach, Florida, where six of eight freshwater wells are no longer usable.

The city is considering relocating wells, upgrading its treatment plant or buying water from a neighboring town.

The water that comes out of the tap in the oceanside town of Edisto Beach, South Carolina, is so salty that it corrodes dishwashers and washing machines within just a few years, resident Tommy Mann said.

While technically safe to drink, it tastes so bad that the town gives away up to five gallons of purified water a day to residents and vacationers.

Voters narrowly rejected a proposal two years ago that would have doubled water rates to pay for an

$8.5 million reverse-osmosis filtering system.

Said Mann: “We’re living in a beautiful little town with Third World water.”

By THE ASSOCIATED PRESS

SEPT. 25, 2015, 10:03 A.M. E.D.T.

Chicago Okays $2.7 Billion in Bond Sales Amid Credit Rating Warnings.

CHICAGO — Chicago is poised to issue more than $2.7 billion of debt amid warnings that its core credit ratings could be downgraded depending on the outcome of the city’s fiscal 2016 budget.

Both Standard & Poor’s and Fitch Ratings said this week they could downgrade Chicago’s BBB-plus general obligation ratings if the city does not adequately address escalating pension payments.

“If the final budget that is adopted by the end of the calendar year fails to cover the larger pension payments with an identifiable and reliable revenue source, it would likely strain the rating, potentially resulting in the rating being lowered by multiple notches,” S&P said in a report.

Fitch Ratings said Chicago risks a downgrade if it fails to put pension payments on a solid funding path or raids budget reserves. Moody’s Investors Service, which dropped Chicago’s rating to junk in May, withheld comment until a final budget is enacted.

Mayor Rahm Emanuel proposed a budget on Tuesday that includes the biggest-ever city property tax hike to cover increased contributions to public safety worker pensions.

To make the $543 million tax hike, phased in through 2018, palatable to city aldermen, Emanuel is seeking an expanded tax exemption in the Illinois Legislature to shield homes valued at $250,000 or less from the increase. His budget also counts on enactment of a bill that spreads out the city’s police and fire pension payments.

Additionally, Chicago is betting the Illinois Supreme Court will uphold the constitutionality of a state law aimed at shoring up the sagging finances of its municipal and laborers’ retirement systems, partly through benefit cuts.

S&P said that given these “uncertainties,” it expects city officials to consider contingency plans for addressing a $20 billion unfunded pension liability.

At a press conference on Thursday, Emanuel said the city is “on strong ground” with its legislative efforts.

Earlier, the city council gave final approval to the sale of up to $500 million of general obligation bonds in a deal that will push out payments on $225 million of outstanding debt and refund the rest for possible savings.

Aldermen also approved up to $2 billion of new and refunding O’Hare Airport revenue bonds and up to $225 million of sewer bonds, including $125 million to end interest-rate swap agreements. The airport and sewer bonds are expected to price in October, with the GO bonds selling in the coming months, a city spokeswoman said.

By REUTERS

SEPT. 24, 2015, 3:33 P.M. E.D.T.

(Reporting By Karen Pierog; Editing by David Gregorio)

Lawmakers to Introduce Bill That Subjects Puerto Rico Funds to Federal Regulations.

Legislation that would subject Puerto Rico mutual funds to the same regulations as mainland funds is expected to be introduced in Congress on Friday, the latest sign that Puerto Rico's financial crisis is drawing greater scrutiny from U.S. lawmakers.

Rep. Nydia Velazquez, a Democrat from New York, said she plans to introduce the bill, the Puerto Rico Investor Protection Act of 2015, in the House of Representatives, where it is expected to be referred to the House Committee on Financial Services for discussion. Rep. Maxine Waters of California, the top Democrat on the financial services committee, signed on as co-sponsor.

The proposed law aims to establish federal oversight for Puerto Rico's mutual-fund industry after investors in Puerto Rico municipal-bond funds sustained heavy losses as the island's fiscal crisis deepened. Puerto Rico has faced a sluggish economy and high unemployment for years, and Gov. Alejandro Garcia Padilla in June called the island's $72 billion debt load unpayable.

"It is outrageous that, when investing their hard-earned money for retirement, Puerto Ricans are not afforded the same transparency requirements and consumer protections that apply in the mainland," Ms. Velazquez said in a statement.

Ms. Velazquez, who represents parts of Manhattan, Brooklyn and Queens, is the first Puerto Rican woman elected to Congress. She's not the only official from New York state, which has the nation's largest Puerto Rican population outside the island, to make Puerto Rico's debt woes a priority. In September, New York Gov. Andrew Cuomo visited the island and said he supported allowing Puerto Rico to seek bankruptcy protection. Puerto Rico and its public agencies currently can't file for bankruptcy.

Puerto Rico is attracting broader attention as well. Presidential contenders Hillary Clinton and Sen. Marco Rubio have also visited the island in recent weeks, and Jeb Bush paid a visit in April. In Washington, the Senate Committee on Finance will hold a hearing on Puerto Rico's financial and economic problems on Tuesday.

Mutual funds in the U.S. mainland are subject to the Investment Company Act of 1940. The law, however, doesn't apply to funds located in U.S. possessions that are sold only to residents of those possessions. At the time, the thinking was that the cost of travel would make it too expensive for regulators in Washington to oversee funds in far-flung, overseas territories.

Puerto Rico passed its own fund-oversight law in 1954, but analysts say it had become less stringent than current federal regulations. In Puerto Rico, UBS Group AG—whose local brokerage unit has a dominant position on the island—was able to underwrite bonds from Puerto Rico municipal entities and then sell those bonds to funds managed by UBS, collecting fees along the way. Some of the UBS funds amassed big positions in certain bond issues that were underwritten by UBS.

That behavior wouldn't have been allowed under federal law, said Mercer Bullard, a securities law professor at University of Mississippi School of Law who has also created an investor advocacy organization called Fund Democracy. Federal regulations would have "prevented the chain of relationships that UBS had at every step of the underwriting and distribution process," Mr. Bullard said.

The losses in UBS' Puerto Rico bond funds have been so severe that investors have filed hundreds of legal claims against the Swiss giant's Puerto Rico brokerage unit. UBS says it is facing more than $1.1 billion in damages tied to its Puerto Rico activities. Many investors who filed claims are retirees who say that UBS brokers told them the funds were safe, when in fact they were heavily invested in just a few Puerto Rico bond issues and had used leverage, a risky strategy, to boost returns.

The legal claims have been filed with the Financial Industry Regulatory Authority, which uses arbitrators to adjudicate the cases. Arbitrators have ruled in favor of investors in some cases and in favor of UBS in others. The bank has also settled some cases, at times for millions of dollars.

UBS declined to comment on whether its Puerto Rico funds should be regulated under federal law. The bank has said previously that investors in the funds had received excellent returns for years, often exceeding the broader bond market.

Puerto Rico passed a new fund-oversight law in 2013, which according to Fitch Ratings aligns more closely to federal law. Still, making Puerto Rico funds subject to federal regulations "may help restore some confidence from investors that have had some difficulties," said Ian Rasmussen, senior director in the fund and asset manager group at Fitch.

THE WALL STREET JOURNAL

By MIKE CHERNEY

Sept. 25, 2015 12:01 a.m. ET

Write to Mike Cherney at mike.cherney@wsj.com

High-Yield Muni Fund Plays the Edges.

As investors fled Chicago's debt this year when its ratings were cut to junk, Nuveen Asset Management LLC fund manager John Miller gathered his team of analysts and asked if it was finally time to buy.

It was a typical move by Mr. Miller, who digs around in the corners of the $3.7 trillion municipal-bond market for big bets that might pay off for his High Yield Municipal Bond Fund.

The approach once counted as fringe behavior in a market typically described as dull and safe. But business is booming as the long stretch of interest rates near zero pushes investors into riskier holdings and redefines what it means to be a buyer of bonds.

Investors poured about $9 billion into high-yield municipal-bond funds last year, according to Lipper. Nuveen's High Yield fund has been a big beneficiary, swelling to about $10.6 billion of assets from a peak of around $6 billion before the financial crisis. It is now the sixth-largest municipal-bond fund in the U.S., according to Morningstar Inc.

“It’s a reflection of the fact that interest rates have been low for so long,” said Howard Cure, director of municipal research at Evercore Wealth Management. “In their search for yield, investors are more willing to buy high-yield paper.”

Mr. Miller’s willingness to look for winners among bonds most prone to distress and default has produced market-leading returns in two of the past three years. But it is also a strategy that can lead to hefty volatility in times of market stress and outsize losses when investors want their money back.

In 2008, when municipal bonds fell about 2.5%, the High Yield fund dropped 40%. Then the market’s risks increased as bond insurance all but vanished, Detroit declared bankruptcy and Puerto Rico began slipping into financial crisis.

“We want to manage risk, but not shy away from risk altogether,” said Mr. Miller, who heads a team that manages more than $100 billion.

The municipal-bond market used to be all about shying away from risk. Investors prized protecting wealth over increasing it and bought the debt seeking tax-free income to fund their retirements. Mr. Miller’s introduction to it came in 1993, when he worked as a credit analyst at a Chicago firm managing highly rated bonds for wealthy individuals.

In 1996, he joined Nuveen as an analyst and soon was running a new $20 million high yield municipal-bond fund.

One of his big bets was on the Pocahontas Parkway, a nine-mile stretch of highway southeast of Richmond, Va. In 2003 and 2004, he said, he bought parkway bonds that were backed by tolls and had a face value of about $100 million for 80 cents on the dollar. The bonds were under stress, because some drivers were choosing free alternative roads and because the road had a reputation for being haunted.

It was the fund’s largest holding when an Australian company bought the parkway and backed the debt with Treasurys. The bonds went to about 110 cents on the dollar.

Mr. Miller has also poured money into charter schools, which can lose state funding if students leave. Today, his funds own about $1.4 billion in charter-school debt, a big chunk of the roughly $10 billion that has ever been sold in the U.S.

In 2008, Lehman Brothers failed, and clients pulled out hundreds of millions of dollars. Selling the bonds needed to meet those redemptions wasn’t easy. About half of the High Yield fund involved bonds with no ratings at all that wouldn’t mature for years. Mr. Miller had tried to hedge his funds against higher interest rates by betting against Treasurys. But interest rates fell and the price of U.S. government debt rose, amplifying the losses.

“I went out on the road, and it was difficult to be out there, because people were upset about the performance of the High Yield fund,” Mr. Miller said.

That year left the High Yield fund with about $2.8 billion in assets. It has since bounced back. Over five years, its total return of 7.71% was almost double the market’s, counting interest payments and price appreciation, according to Morningstar. Even so, an investor would have made more money over the past decade in an investment-grade municipal-bond fund from Vanguard—and would have paid lower fees and had less anxiety, several financial advisers said.

Mr. Miller says he adjusted the portfolio structure to prevent that kind of volatility from hitting the fund again. He also says he doesn’t court risk for risk’s sake. Unlike other operators of high-yield

funds, Mr. Miller was wary early on about junk-rated Puerto Rico, which is in talks to restructure its $72 billion in debt.

But he did take a big swing on American Airlines. In 2012, when the airline went through bankruptcy, he went shopping for the riskiest debt available: $100 million in unsecured bonds issued by cities to build its facilities and paid by fees from the airline. Those bonds, worth pennies on the dollar, surged more than 60% in value two years later when American merged with US Airways. The new company converted the debt to equity, and the fund now holds about $145 million in American Airlines stock, one of its largest holdings.

Chicago, meanwhile, has underfunded its pensions for a generation and sold billions in debt, but Mr. Miller sees no sign of future financial distress. It has a strong business and financial community, many universities and few fiscal problems that couldn't be solved by raising its relatively low taxes, according to Nuveen research.

The week after the downgrade, Chicago sold about $674 million in bonds at yields approaching 6%—more than 2 percentage points higher than comparably rated bonds.

As the sale opened, Mr. Miller sat in the tip of a triangular room full of traders manning their terminals and started buying.

THE WALL STREET JOURNAL

By AARON KURILOFF

Sept. 22, 2015 8:54 p.m. ET

Write to Aaron Kuriloff at AARON.KURILOFF@wsj.com

Chicago Faces Tax Increase, Rise in Fees.

CHICAGO — Mayor Rahm Emanuel is proposing a historic property tax increase, while expanding fees on trash collection and taxi rides under a plan to confront a growing fiscal crisis in the nation's third largest city.

The proposal comes months into the second term of Mr. Emanuel, a former congressman and chief of staff to President Barack Obama, as he runs out of options to address ballooning pension costs that are coming due.

During his first term, the mayor focused on trying to gain concessions from city workers and retirees, but was stymied by the courts and organized labor.

Mr. Emanuel's plan would raise an additional $544 million from property taxes alone phased in over four years under what is being described as the largest tax rise in city history. He also proposes raising additional revenue by taxing e-cigarettes, expanding fees on garbage pickup, and adding fees on taxi and ride-sharing services.

"As we continue to grow our economy, create jobs and attract families and business to Chicago, our fiscal challenges are blocking our path," Mr. Emanuel said in a statement.

Details of the proposal were released by the Emanuel administration Monday ahead of his budget

address to the city council on Tuesday.

Parts of the plan leaked in recent weeks have faced pushback from some aldermen and public rebuke at hearings. Many have voiced concerns about the cost to working families.

“We must ask the very wealthy and big corporations to pay their fair share in taxes so we can finally fix our structural deficit and get on track to fiscal sanity,” said Alderman Leslie Hairston, who is among the council members pushing for tax rebates for working families and changes in how commercial buildings are taxed.

The Emanuel administration said it would seek changes in state law to protect those who own homes valued at $250,000 or less from the brunt of the tax increase.

The proposal comes as Mr. Emanuel looks to keep Chicago from becoming an increasing outlier among U.S. cities. The Midwest hub faces many of the challenges that other aging cities are experiencing, from population declines to crumbling infrastructure.

But sharply rising municipal pension costs and mounting state fiscal problems have helped set Chicago apart. Moody’s Investors Service dropped the city’s credit rating to junk earlier this year.

Mr. Emanuel’s proposal includes cost savings from eliminating vacant positions to redesigning how streets are swept, but largely relies on new revenue to confront its fiscal problems.

The property-tax boost would go to pay for a $550 million increase in pension costs for police officers and firefighters required by the state to ensure their retirement systems remain solvent. The Emanuel administration is lobbying the state to allow the hike to be phased in over time, matching the property-tax-increase schedule.

Administration officials said the mayor has few options.

During his first term, Mr. Emanuel had focused on reaching agreements with city workers to lower pension expenses by reducing cost of living increases and requiring current employee to increase their contributions. But a court ruling in July derailed such efforts, saying the city couldn’t change already promised retirement benefits.

Monday’s proposal is separate from the Chicago school district’s budget, which isn’t funded through the school year and is counting on help from the state.

THE WALL STREET JOURNAL

By MARK PETERS

Updated Sept. 21, 2015 8:07 p.m. ET

Write to Mark Peters at mark.peters@wsj.com

BDA Submits Issue Price Comment Letter to IRS.

BDA letter to IRS on Issue Price highlights potential negative impact to market and smaller issuers

Today, BDA submitted a comment letter to IRS in response to its request for comment on a proposed

rule to re-define ‘issue price’. The proposal partially withdraws the 2013 issue price proposal.

The BDA’s draft letter focuses on:

- Problems for issuers and the marketplace that will be caused by an actual sales approach and the absence of a reasonable expectation standard
- Issues associated with the unworkable proposed alternative to the general rule, including compliance concerns
- The rule’s negative impact on smaller issuers, especially due to the 10% maturity-by-maturity ‘substantial amount’/actual-sales requirement
- The need for a safe harbor or alternative standard for competitive deals

BDA’s previous issue price letters, including the BDA letter to IRS in May 2015 can be read here.

09-22-15

Fitch: U.S. Municipal Ratings Higher than GO Ratings Not Usually Warranted.

Fitch Ratings-New York-22 September 2015: Market participants have expressed concern over a perceived increase in the incidence of widely divergent U.S. municipal ratings. One area in which Fitch Ratings’ opinion differs from some other rating agencies’ is the conditions under which dedicated tax backed (DT) debt may be rated higher than the general credit quality (GO debt) of the issuing municipality.

A notable example is the divergent ratings on the City of Chicago, IL sales tax bonds, which carry ratings ranging from ‘AAA’ to below investment grade. Bondholders should insist on a reasonable legal basis to separate ratings of DT bonds such as the Chicago sales tax bonds from the city’s GO rating. Fitch notes that there is none in this case.

Fitch rates the bonds ‘BBB+’ with a Negative Outlook, on par with the city’s GO debt rating. Certain other agency ratings (Kroll and S&P) are not capped by the city’s general credit quality which Fitch believes may lead bondholders to mistakenly conclude that these DT bonds backed by general sales tax revenues are legally inoculated from the bankruptcy risk of the city. In Fitch’s view, if the legal protections do not insulate revenues supporting the rated DT bonds from the automatic stay provisions of the bankruptcy code in a bankruptcy proceeding, the rating must be capped at the city GO. Although the risk of bankruptcy remains remote at ‘BBB+’, the city’s GO rating is the clearest, most direct expression of both the risk of bankruptcy and the linkage its DT bond has to that risk. Rating above the city GO can only be supported by one of three legal structures, none of which apply to Chicago’s DT bonds backed by general sales tax revenues.

SPECIAL REVENUE DESIGNATION ONE OF THREE LEGAL FRAMEWORKS SUPPORTING RATINGS DISTINCT FROM GENERAL CREDIT

One legal framework that permits Fitch to rate debt based on specific revenues free of the risk that a related municipality’s bankruptcy proceeding would interrupt payments is created under the federal bankruptcy code in the provisions that define ‘special revenues”. Fitch could rate debt backed by a strong revenue source multiple categories above the general credit of the municipality if Fitch believes the case for special revenue status is very clear.

The concept of “special revenues” is unique to Chapter 9 and the municipal bankruptcy process.

Special revenue bonds are insulated from the municipality's bankruptcy in two powerful ways. First, the lien interest in the special revenues continues even if it is a mere consensual lien. If the revenues are not special revenues, then the lien is lost as applied to revenues collected post-bankruptcy. Second, the application of special revenues and actions to apply them to debt payment is exempt from the automatic stay provision of the bankruptcy code. This exemption means that the trustee can continue to apply the pledged special revenues to pay debt service on qualified DT bonds. The power of these protections was evident in both the Stockton bankruptcy and the Detroit bankruptcy where water system bondholders were continuously paid debt service. Additionally, Fitch rates the Chicago water and sewer senior and junior debt as special revenue obligations at 'AA+' and 'AA, respectively, notably higher than the city's GO.

In Fitch's opinion, there is no plausible basis to claim that the pledged sales taxes are "special revenues". The Chicago sales taxes supporting the DT bonds are unmistakably general revenue for general governmental purposes and as such, are excluded from the definition of 'special revenues' in section 902 of the U.S. Bankruptcy Code. Fitch expects the sales tax revenues would be subject to the automatic stay and default of the DT bonds would be likely in the case of a city bankruptcy. Therefore, an accurate and fair signal of the likelihood of in-full and on-time payment of the sales tax bonds must incorporate the city's GO credit quality and ratings which ignore it understate bondholder risks.

SECURITIZATION AND SEPARATE REVENUE OWNERSHIP ALSO SUPPORT DISTINCT RATINGS

A second legal framework is a securitization authorized by state law where a municipality is empowered to "sell" its future revenues and these revenues are in turn used to support an asset backed security. This legal framework is the technique used by the New York City Transitional Finance Authority whose debt Fitch rates 'AAA'. A third legal framework supporting higher ratings is a state intercept program where the state creates a flow of revenues and establishes a legal framework that directs those flows into a trust account solely for benefit of bondholders in which the municipality has no property rights except to flows released from the trust. In both of these frameworks, the basic idea is that the flows into the account are not property of the municipality. The municipality's interest is only in residuals as they emerge, so the flows available to the debt are not interrupted when a municipality files a bankruptcy proceeding. The Chicago sales tax bonds fall into neither of these two categories.

RECOVERY PROSPECTS AND RECOVERY NOTCHING

Fitch's ratings of municipal debt obligations are default risk ratings and are not "notched up" from default risk to incorporate an assessment of recovery. However, even if some form of notching methodology was applied, it is unlikely to benefit the rating of the Chicago sales tax bonds and certainly not by full rating categories. As the sales tax bonds are clearly not special revenue obligations, the consensual lien on revenues granted by the city would not continue following a bankruptcy filing. Bondholders would be competing with pension claims and GO debt holders for recovery. Of course a statutory lien could improve prospects for bondholders compared to general obligation debt and pension claims as a statutory lien continues post-bankruptcy. But there is no statutory lien benefiting the Chicago sales tax bonds. Even if there were one it would not in Fitch's view support a multiple category separation.

LACK OF CHAPTER 9 OPTION IN ILLINOIS NOT A CREDIT FACTOR

Fitch does not make rating distinctions between municipalities in states where bankruptcy is an option and those where it is not. If bankruptcy is not currently authorized, Fitch believes it likely that the state could authorize it if necessary, or absent that, the municipality in severe fiscal distress

would default on its obligations and take its chances in state court lien enforcement proceedings. Recent proposals and discussion in Illinois to allow municipal bankruptcy as an option for financially stressed issuers illustrates the basis for this approach.

Kroll acknowledges the risk when it writes in its Local Special Revenue Report on Chicago sales tax debt that a key rating concern on its AA+ rating of the sales tax debt is “the uncertainty of the lien on pledged revenues that would result if the city were granted the ability to seek relief under Chapter 9 of the Bankruptcy code and in addition if such relief was sought.” Fitch’s view is that this risk needs to be reflected in the rating up front. Failing to signal this connection in the ratings sets up a scenario in which bond pricing and yield can change radically when DT bond ratings inevitably begin aligning to the GO rating if distress increases and the GO rating declines.

For more information see ‘Statutory Liens Do Not Boost Debt Ratings’, dated July 21 of this year and available at ‘www.fitchratings.com’ or by clicking on the link at the end of the press release.

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Additional information is available at ‘www.fitchratings.com’.

Puerto Rico Sends Reassurance as Debt Talks Poised to Begin.

Puerto Rico’s pledge to take the constitutional priority of its general-obligation bonds in consideration is seen as a message that the commonwealth is willing to work with investors as debt restructuring talks begin.

“It’s an important step for them just to reinforce that there are rules and that they know that there are rules and that they’re going to be trying to work around them with bondholders,” said Matt Fabian, a partner at Concord, Massachusetts-based Municipal Market Analytics. “Maybe that works, maybe it doesn’t.”

Administration officials tasked with reducing the island’s debt load or suspending debt-service payments met Thursday with Governor Alejandro Garcia Padilla and lawmakers to develop guidelines for a potential voluntary exchange of existing debt for new bonds with possible security improvements, according to a document released late Thursday. Those principles include seeking to

take into account the priorities of the debt that creditors hold.

Puerto Rico has $13 billion of general-obligation debt outstanding, which the island's constitution stipulates must be repaid first. Other securities are backed by specific revenues and lack that protection. Acknowledging that it would seek to respect the constitutional priority of its general obligations may help Puerto Rico in the future when it looks to borrow through the capital markets, said Fabian.

Puerto Rico's government and its advisers said on Sept. 9 that a proposal to pare the commonwealth's debt would be released in a few weeks. The government plans to start meeting with investors by mid-October to begin negotiations.

Puerto Rico has already initiated talks with advisers to bondholders of Government Development Bank debt, seeking to potentially exchange those obligations for new securities. About $336 million of GDB debt matures Dec. 1.

Here's a list of the island's biggest bond issuers, how much long-term debt they have, and when major monthly payments are due, according to data compiled by Bloomberg.

General-obligations: $13 billion. The debt backed by the commonwealth's full faith and credit. The island's constitution says general obligations must be repaid before other expenses. Puerto Rico owes $357 million of interest in January and an additional $805 million of principal and interest is due July 1.

Puerto Rico Sales Tax Financing Corp.: $15.2 billion. The bonds, known by the Spanish acronym Cofinas, are repaid from dedicated sales-tax revenue. A $6.2 billion portion of the debt, called senior-lien, is repaid first. The remaining $9 billion, called subordinate-lien, get second dibs. After paying $12.5 million of principal and interest in August, $1.2 million of interest is due in November, February and again in May.

Puerto Rico Electric Power Authority: $8.3 billion. Prepa, as it's called, is the island's main supplier of electricity and repays the debt from what it charges customers. The utility owes $196 million of interest in January and $420 million of principal and interest July 1.

Puerto Rico Government Development Bank: $5.1 billion. The GDB lends to the commonwealth and its localities. When those loans are repaid, the bank can pay off its debt. The GDB is seeking to restructure its obligations through a debt exchange. The bank owes $354 million in December and $422 million in May.

Puerto Rico Highways & Transportation Authority: $4.7 billion. The highway agency repays its debt with gas-tax revenue. It owes $106 million of interest in January and $220.7 million of principal and interest in July.

Puerto Rico Public Buildings Authority: $4.1 billion. The PBA bonds are repaid with lease revenue from public agencies and departments of the commonwealth. The agency owes $102.4 million of interest in January and $207.6 million of principal and interest in July.

Puerto Rico Aqueduct & Sewer Authority: $4 billion. The utility, called Prasa, supplies most of the island's water. The debt is repaid from water rates charged to customers. The water agency owes $86.5 million of interest in January and $135.1 million of principal and interest in July.

Puerto Rico Pension-Obligation Bonds: $2.9 billion. The taxable debt was sold to bolster the island's main pension fund. The bonds are repaid from contributions that the commonwealth and

municipalities make to the retirement system. The next maturity is July 2023 and the system pays $13.9 million of interest every month in this budget year.

Puerto Rico Infrastructure Financing Authority: $1.9 billion. Called Prifa, the agency has sold the island's rum-tax bonds. These are securities repaid from federal excise taxes on rum made in Puerto Rico. Prifa owes $37.2 million of interest in January and $77.8 million of principal and interest in July.

Puerto Rico Public Finance Corp.: $1.09 billion. The PFC bonds are repaid with money appropriated by the legislature. The agency defaulted on its Aug. 3 and Sept. 1 debt-service payments because the legislature failed to allocate the funds. It owes interest every month, the largest being a $24 million payment in February.

Bloomberg News

by Michelle Kaske

September 25, 2015 — 12:59 PM PDT

Muni Distressed Debt Firm Rosemawr Sues Over Revel Energy Bonds.

An investment firm focusing on high-yield and distressed municipal bonds sued the developer of a power plant that serves Atlantic City's shuttered Revel Casino for securities fraud.

Rosemawr Management LLC, a $1 billion fund started by Lehman Brothers Holdings Inc.'s former head of municipal-derivatives trading, alleged that ACR Energy Partners LLC concealed defaults and used almost all its assets to make improper dividend payments to its parent company. In March 2014, New York-based Rosemawr bought $35 million of bonds that financed the power plant at 92.25 cents on the dollar. The securities have since lost 70 percent of their value.

"Although it was public knowledge that the Revel facility was not performing as well as Revel had intended, there was no reason to believe that Revel was defaulting on its payment to ACR," Rosemawr said in the Sept. 16 suit, filed in federal court in Camden, New Jersey. "As a direct result of the fraudulent concealment of material information, plaintiffs purchased the bonds at artificially inflated prices."

Distressed Municipalities

Rosemawr was formed in 2008 by Greg Shlionsky, a former Lehman Brothers managing director. The firm, which bought bonds backed by revenue from Harrisburg, Pennsylvania's parking garages and has lent money to an assisted living facility in Georgia and a storm drain project in the Detroit area, also includes former Lehman municipal derivatives trader James Lister.

Greg Usry, Citigroup Inc.'s former co-head of municipal credit and financial products and Julie Morrone, who formerly managed Morgan Stanley's high yield muni funds, also work at Rosemawr, according to the firm's website.

Revel, which opened at a cost of $2.4 billion in 2012, was an attempt to bring a bit of Las Vegas to the east coast by offering more shows, restaurants and shopping. The property suffered from poor design and competition from new casinos in other states. It went bankrupt twice before closing in

September 2014.
New Jersey’s Economic Development Authority issued about $119 million of unrated tax-exempt and taxable municipal bonds in 2011 on behalf of ACR, which used the money to build a heating, cooling and electric plant for the Revel resort and casino.

Bond Covenants

Revel had a 20-year contract to buy power and other utility services from ACR, a joint venture between South Jersey Industries Inc. and DCO Energy LLC. Dan Lockwood, a spokesman for South Jersey Industries, didn’t immediately return a call seeking comment. Frank DiCola, chairman of Mays Landing, New Jersey-based DCO also didn’t return a message.

Two Rosemawr funds bought $35 million of the power plant bonds at 92.25 cents per $100 face amount in March 2014. ACR and its owners “flatly lied” about defaults under the bond covenants which, if disclosed, would have lowered the price of the securities, Rosemawr said.

ACR hid Revel’s failure to make required monthly payments under the energy service agreement and entered into a “special arrangement” with the casino to extend payment terms without bondholder permission, Rosemawr said. ACR also didn’t notify bondholders it failed to fully fund a required reserve account.

The account “provided crucial protection of bondholders’ interests, because it provided a source of payments to bondholders until Revel became consistently profitable.”

Dividend Payments

Finally, ACR made $11 million in improper and fraudulent divided payments to its sole controlling member, an entity set up by South Jersey Industries and DCO, according to the suit. Under the bond documents, dividends were restricted if there was an event of default, Rosemawr said.

The $11 million payments “represented substantially” all of ACR’s liquid assets. ACR missed its June 15, 2014, debt service payment.

The offering statement for ACR’s bonds warned investors that the shuttering of the Revel resort or an ownership transfer meant bondholders couldn’t be assured energy produced by the plant was necessary or that new owners might get energy elsewhere.

Rosemawr said it believed financing wouldn’t be jeopardized because Revel would need power, regardless of who purchased the building or its long-term use.

“Had the plaintiffs known the information that was fraudulently concealed by the defendants prior to the purchase of the bonds, the plaintiffs would either have not purchased the bonds altogether, avoiding any losses, or would have purchased the bonds only at a dramatically lower price, thereby significantly reducing their losses,” Rosemawr’s complaint said.

Bloomberg News

by Martin Z Braun

September 21, 2015 — 11:22 AM PDT

Moody's: Entrance of U.S. Not-for-Profit Hospitals into Health Insurance Will Continue to Rise.

New York, September 25, 2015 — More US not-for-profit hospitals are likely to venture into the commercial health insurance business in the next few years either to gain market share or reduce costs through improved healthcare management, Moody's Investors Service says. However, starting a new plan or acquiring an existing business carries significant credit risks as managerial skills shift, competition intensifies, and start-up costs rise.

"Different management expertise is needed to operate a commercial health insurance business versus an acute care hospital. Health plans require actuarial skills for pricing models and specific marketing and service acumen, for example," says Moody's Vice President — Senior Analyst Mark Pascaris.

Despite substantial risks to cash flow margins, the trend is expected to persist, especially among larger systems which can absorb the costs. Drivers include the Affordable Care Act (ACA), which encourages care coordination and population health management; continued focus on cost reductions, synergies through greater economies of scale, and creating new revenue streams, Moody's says in "Hospitals Entering Insurance Business Gamble on Long-Term Payoff."

"Not-for-profit hospitals with a health insurance business (often known as an integrated delivery system, or IDS) tend to operate at noticeably lower operating cash flow margins than similar health systems without insurance," Pascaris says. "Entering the insurance business inevitably suppresses hospital system margins from the beginning."

Moody's says this is due to the inevitable mismatch between expense ramp-up and premium reserves essential to meet cash reserve requirements to execute the plan. The effect on credit will largely be driven by the pace and magnitude of the strategy and management's ability for rapid adjustment, if needed.

Aside from new managerial skills, competition from other national and regional health plans is intense. Moreover, this is compounded by recent merger and acquisition activity among Anthem Inc. (Baa2, under review possible downgrade) reached an agreement to acquire Cigna Corp . (Baa1, possible downgrade), following Aetna Inc.'s (Baa1, possible downgrade) deal to buy Humana Inc. (Baa3, possible upgrade) which has skewed negotiating leverage between commercial payors and hospitals decidedly toward the insurance companies.

There are some hospitals with long-standing health insurance plans that have developed an expertise in managing both the underwriting and delivery sides of the business. These health systems have ample cash reserves to weather insurance cycles and regulatory changes that come with the line of business.

The report is available to Moody's subscribers here.

Bloomberg Brief Weekly Video - 09/24/15

Taylor Riggs, an editor at Bloomberg Brief, talks with reporter Kate Smith about this week's municipal market news.

Watch the video.

September 24, 2015

Puerto Rico's Bonds Overshadow Pension Fund Poised to Go Broke.

Puerto Rico's $72 billion debt burden overshadows another financial threat to the Caribbean island: a government workers pension fund that's set to go broke in five years.

As Governor Alejandro Garcia Padilla prepares to push for bondholders to renegotiate debts he says the commonwealth can't afford, he's also contending with an estimated $30 billion shortfall in the Employees Retirement System. The pension, which covers 119,975 employees, as of June 2014 had just 0.7 percent of the assets needed to pay all the benefits that had been promised, a level unheard of among U.S. states.

If not fixed, the depleted fund could jeopardize a fiscal recovery by foisting soaring bills onto the cash-strapped government even if investors agree to reduce the island's debt. The system is poised to run out of money by 2020, which would leave the government on the hook for more than $2 billion in benefit payments the next year alone, according to Moody's Investor's Service. That's equal to about one-fourth of this year's general-fund revenue.

"As Puerto Rico shoulders that burden of paying for pension benefits outright, that's obviously going to cripple their budget," said Ted Hampton, a Moody's analyst in New York.

Crisis Builds

The debt crisis gripping the island, with a population of 3.5 million, is the outcome of years of borrowing to pay bills while the economy stumbled and residents left for the U.S. mainland. In August, Puerto Rico defaulted on some bonds for the first time, and Garcia Padilla has said that reducing its debt is crucial to the island's economic recovery.

His administration and outside advisers on Sept. 9 released a plan to repair the island's finances, which included closing schools and reducing benefits to the poor. It also envisions making increased pension payments that have been delayed because the government hasn't had the money.

"We believe this plan addresses the system's needs and assures pensioners and participants that their benefits will be paid," Pedro Ortiz Cortes, administrator for the retirement system, said in an e-mail Thursday.

Workers' Doubts

Puerto Rico's failure so far to address its long-building pension shortfall has fostered anxiety among workers, who are concerned that their benefits will be reduced amid competing demands from creditors. "A reduction in benefits would be horrible," said Eduard Rodriguez Santiago, a 38-year old firefighter. "Things are getting more expensive."

Garcia Padilla, in a speech after the release of the fiscal plan, said that workers have already sacrificed enough. In 2013, the government raised the retirement age, increased employee contributions and reduced or eliminated retiree bonuses.

"Solving the pension problem is almost tougher than debt because people will take to the streets if you start seeing pension checks quit going out," said Tom Schuette, co-head of credit research at Solana Beach, California-based Gurtin Fixed Income Management LLC, which manages $9.6 billion of municipal securities. "It's almost much easier to anger investors on the mainland as opposed to residents who can vote you out of office."

Current and prior administrations have implemented changes to improve the pension system, including by closing it to new employees and offering them annuities instead. To give it cash to invest, it sold $2.9 billion of bonds in 2008, just before the credit crisis caused stock prices to plunge. The system is now obligated to repay the securities, which have tumbled in value amid doubts about its ability to do so.

As Puerto Rico has cut the number of workers on its payrolls, there are fewer paying into the retirement system. The island had 116,000 central-government employees in May 2015, down 27 percent from seven years earlier, according to the report by the government and its advisers.

While new employees haven't been eligible for traditional fixed-benefit pensions since 2000, the step didn't stop Puerto Rico's growing liabilities. The new employees, called System 2000 participants, will receive an annuity instead. Their contributions are being used by the pension system to meet its obligations.

New Liabilities

"They're using these payments to shore up their existing defined-benefit plan," said Hampton, the Moody's analyst. "Their defined-contribution plan isn't really taking hold. It's just creating new liabilities for the central government."

Puerto Rico is facing more immediate concerns because it may be short of cash as soon as November. That may leave it forced to choose between paying workers and retirees or bondholders, with $357 million of interest on its general obligations due Jan. 1.

"If the government has to decide between making a big general-obligation payment in January or making sure they have enough for payroll or for pensioners in December, I think they're going to go with the pensioners or payroll," Sergio Marxuach, public-policy director at the Center for a New Economy, a research group in San Juan. "You're not going to send government workers home without money during Christmastime."

Bloomberg News

by Michelle Kaske

September 24, 2015 — 9:01 PM PDT Updated on September 25, 2015 — 5:33 AM PDT

Puerto Rico Agency Reaches Tentative Pact With Fuel Lenders.

Puerto Rico's main power utility reached a tentative agreement with lenders on fuel purchases that would reduce interest rates on $700 million of debt that has already matured and extend repayment for at least six years.

The Puerto Rico Electric Power Authority and lenders including a unit of Bank of Nova Scotia and

Solus Alternative Asset Management agreed to convert the debt, which matured in 2014, into six-year term loans with a 5.75 percent interest rate or exchange all or part of the principal due under existing credit agreements for new bonds. The securitized debt would include a 15 percent principal reduction and a five-year moratorium on payments.

The principal reduction is equal to the amount accepted by holders of about 35 percent of its $8.3 billion in bonds earlier this month. The utility, known as Prepa, is still in talks with tax-exempt bond insurers in what would be the largest-ever restructuring in the $3.6 trillion municipal-bond market.

The utility restructuring is the first step toward Puerto Rico's goal to lower its debt burden.

"The terms for those lenders are very attractive in this agreement, but the total amount is small and Prepa needs access to fresh fuel financing," said Matt Fabian, a partner at Concord, Massachusetts-based Municipal Market Analytics.

The tentative pact comes a year after the fuel lenders entered a forbearance agreement, where they pledged to not file suit against Prepa while the debt talks were ongoing. That accord was set to expire Sept. 25.

Bond Insurers

"The best path forward for Prepa, as well as the creditors, involves sharing the burden among all stakeholders. We continue to negotiate with our monoline bond insurers in an effort to reach agreement that will allow Prepa to continue to implement its transformation," said Lisa Donahue, Prepa's chief restructuring officer, said in a statement Tuesday.

Prepa owed Scotiabank de Puerto Rico about $550 million as of August 2014, according to the forbearance agreement. The utility owed another $146 million to Citigroup Inc. as of that period. Solus bought that loan from Citigroup earlier this year. The agreement would lower interest rates to 5.75 percent from 7.25 percent, according to Prepa's statement.

"We are pleased that the syndicate of fuel-line lenders and Prepa have reached a mutually beneficial agreement in principle to support Prepa's ongoing operational transformation," Marcelo Gomez-Wiuckstern, a spokesman for Scotiabank, said in an e-mail.

Solus declined to comment through Julia Kosygina, a representative at Abernathy MacGregor Group Inc.
Bond insurers including Assured Guarantee Ltd. and Syncora Guarantee Inc. declined to extend their forbearance contract beyond Sept. 18. MBIA Inc. dropped out of the forbearance earlier this month. An accord with bondholders will expire Oct. 1 unless the parties extend it.

Bloomberg News

by Michelle Kaske

September 22, 2015 — 1:27 PM PDT Updated on September 22, 2015 — 2:43 PM PDT

BlackRock Sees Higher Puerto Rico Gap Than Morgan Stanley.

Puerto Rico's five-year budget deficit leans closer to the commonwealth's $14 billion forecast rather

than a Morgan Stanley estimate that cuts that figure by more than half, according to BlackRock Inc.'s Peter Hayes.

Commonwealth officials and their advisers, called the Working Group, unveiled on Sept. 9 a five-year fiscal and economic growth plan that projects the island's budget will be short $14 billion because of increasing health-care expenses and retirement costs. The report's base-case scenario estimates the island's gross national product will decline by one percent and may increase by as much as 2 percent in a high-growth scenario, according to the plan.

One Morgan Stanley scenario takes a different view. Puerto Rico has overestimated its funding gap, according to a presentation distributed Sept. 11 by Ryan Brady, an analyst on Morgan Stanley's municipal-debt trading desk in New York. The bank estimates a $5.57 billion deficit through fiscal 2020, according to the report. Yet that forecast may be too low, Hayes said Tuesday on Bloomberg Television.

"We're on the higher side," said Hayes, who helps oversee $116 billion as head of municipal debt, including Puerto Rico securities, at New York-based BlackRock. "We think some of the economic assumptions are well founded," Hayes said about the Working Group's estimates.

How to best gauge Puerto Rico's estimates are even in dispute within Morgan Stanley. Research analysts led by Michael Zezas, who work separately from the trading desk, put out a note the day before Brady's presentation stating that "we could not patch together a budget baseline with a strong enough degree of confidence."

Puerto Rico and its agencies owe $72 billion. Officials plan to offer investors a debt-restructuring proposal in the next few weeks after saying the commonwealth will only have $5 billion in the next five years to repay $18 billion of principal and interest coming due. Governor Alejandro Garcia Padilla in June said Puerto Rico and its localities were unable to repay all of its obligations on time and in full.

The Working Group's five-year plan follows a report compiled by former International Monetary Fund economists led by Anne Krueger and commissioned by Puerto Rico. The Krueger report calculates a five-year deficit of $9.6 billion.

"When you look at the economy of Puerto Rico, there's a lot of reforms that need to take place," Hayes said. "And if they don't, it's likely that deficit is going to be higher rather than smaller."

Bloomberg News

by Michelle Kaske

September 22, 2015 — 11:48 AM PDT Updated on September 22, 2015 — 12:32 PM PDT

Goldman Sachs to Extend Maturity Date of Headquarter Bonds.

Goldman Sachs Group Inc. is extending the life of some debt that financed its downtown Manhattan headquarters.

The New York Liberty Development Corp. plans to issue $22 million of tax-free debt on behalf of a Goldman Sachs subsidiary that funded construction of the firm's 1.9 million-square-foot building at

200 West Street. The 20-year bonds will be tacked onto its outstanding $1.24 billion of securities due in 2035 that were sold 10 years ago. Proceeds will pay off owners of obligations that mature Oct. 1, according to offering documents.

The New York agency, which was created to spur development after the terrorist attacks on Sept. 11, 2001, is an example of conduit agencies across the U.S. that give companies access to the tax-exempt securities market to reduce interest costs. Goldman Sachs initially borrowed about $1.3 billion in 2005 through the Liberty Bond program, which was projected to save it at least $100 million over the life of the debt.

Trade Center

"This is a relatively small chunk of the deal that's coming due and to try to re-market that separately can be difficult," Jonathan Beyer, senior legal counsel at Empire State Development, said at a Sept. 1 meeting. The Liberty Development Corporation is a subsidiary of the firm. "The idea is to extend the maturity and consolidate it in a larger package for sale."

Others who have tapped the public corporation for financing include developer Larry Silverstein, who sold $1.6 billion of tax-exempt bonds last year to finance the construction of 3 World Trade Center, and Bank of America Corp., which borrowed for its tower across from Bryant Park in midtown Manhattan.

The new bonds for Goldman Sachs are considered a second tranche of the 2005 borrowing and will carry the same 5.25 percent interest rate as the 2035 debt. The securities could still be priced at a lower yield. Municipal debt due in two decades yield 0.6 percentage point less than 10 years ago, Bond Buyer data show.

While a security reopening is common in the U.S. Treasury market, it's rare in the $3.6 trillion municipal market. In such a transaction, a borrower sells an extra portion of previously issued debt with the same maturity and interest rate, even though it comes to market later at a different price.

The bonds have the same ratings as Goldman Sachs, which guarantees the debt service payments of its subsidiary. Moody's Investors Service has the debt at A3, four steps above speculative grade and equivalent to the A- rank from Standard and Poor's.

Tiffany Galvin, a spokeswoman in New York for Goldman Sachs, declined to comment on the deal beyond the offering statement.

Bloomberg News

by Brian Chappatta

September 22, 2015 — 9:07 AM PDT Updated on September 22, 2015 — 1:38 PM PDT

Bloomberg Video: What's Behind the Municipal Bond Mess?

BlackRock Municipal Bond Head Peter Hayes discusses municipal bonds and Puerto Rico's debt. Bloomberg's Kate Smith also reports on "Bloomberg Markets."

Watch the video.

September 22, 2015

How UBS Spread the Pain of Puerto Rico's Debt Crisis to Clients.

The Swiss bank packed pension bonds it underwrote into mutual funds it marketed on the island with a hard sell.

UBS had a good thing going in Puerto Rico. The Swiss bank served as an adviser to the commonwealth's Employees Retirement System, led the underwriting of a $2.9 billion bond issue for the pension agency in 2008, and then stuffed half of those bonds into a family of closed-end mutual funds it sold exclusively to customers on the island. It collected fees at every step.

Now, with the U.S. territory in the downward spiral of a government debt crisis, it's all coming apart for UBS, long the biggest retail brokerage on the island. After UBS helped the government dig itself into a deeper hole and put island customers on the hook for the losses that followed, its Puerto Rico saga has become a cautionary tale of how risks can multiply.

Angry customers have filed hundreds of arbitration claims with the Financial Industry Regulatory Authority. They're seeking more than $1.1 billion in damages from UBS after huge losses in the tax-free bond funds, sold as high-income investments that would preserve their capital, and in the bonds themselves. Three of UBS Puerto Rico's five offices have closed since 2010, and nearly 60 of the unit's 140 financial advisers have departed. The bank's retail brokerage market share on the island has dropped to 33 percent from 48 percent over that period.

Retiree Juan Burgos Rosado was 66 in December 2011, when he opened an account with UBS. A month earlier, he had taken a fall from a tall ladder, ending his career rehabbing real estate. Rosado was "the quintessential conservative investor," according to the arbitration panel that heard his case. UBS advised him to move $325,000 from a maturing certificate of deposit into its high-income funds. Rosado invested a further $200,000 in 2012, when he sold a house, and $600,000 more in January 2013, when another CD matured. He tried to sell the funds later that year as they plunged in value. His statements showed they were still worth $450,000, but UBS offered him just $90,000. While most closed-end funds are listed on an exchange, these were not, so clients depended on bids and offers from UBS Puerto Rico to get in or out.

Rosado didn't sell; he went to arbitration and won. In May, the arbitrators wrote in their decision that Rosado was "grossly over-concentrated" in the bond funds, which were unsuitable for a senior with no investing experience. UBS was ordered to pay Rosado $1 million, including $602,000 in damages. With six other arbitration cases decided on the merits so far this year, one of which went in favor of the bank, UBS has been ordered to pay out a total of more than $7 million.

The bank was disappointed in the outcome of Rosado's case, says UBS spokesman Gregg Rosenberg. The claims arbitrated so far are not indicative of how other claims might be decided, says Rosenberg, who's based in New York. "For more than 20 years, investors in UBS's Puerto Rico municipal bonds and closed-end funds received excellent returns." Losses beginning in mid-2013 occurred amid general weakness in municipal bond markets and Puerto Rican debt, the bank says. The funds, which have declined as much as 75 percent from their initial prices, have continued to pay dividends.

The UBS Puerto Rico funds were lucrative for the bank, bringing in hundreds of millions of dollars in fees and commissions. The fund family, which had as much as $8.9 billion in assets in 2009, was

designed to be heavily invested in the island's municipal bonds, using borrowed money. By mid-2013, the bonds UBS had underwritten for the pension agency represented more than half of the net assets in five of the funds. The pension agency bonds lost more than 80 percent of their value from when they were issued in 2008 through August of this year. On Sept. 10, Standard & Poor's predicted with "virtual certainty" that the bonds will default.

Putting bonds UBS had underwritten into funds UBS managed would have been forbidden by the Investment Company Act of 1940—if the funds were sold on the mainland. But Congress exempted Puerto Rico when the law was enacted. Bloomberg Markets first reported on UBS's activities on the island in 2009.

"UBS made itself a ton of money at the expense of its clients, with these huge conflicts of interest," says Craig McCann, a former senior economist at the U.S. Securities and Exchange Commission who has been hired by investors' lawyers to review more than 200 of the arbitration claims.

McCann, a principal at Securities Litigation & Consulting Group in Fairfax, Virginia, says UBS Puerto Rico sold its fixed-income mutual funds and the pension debt to customers with no regard for diversification or the appropriateness of the risk. "Whether it was a $50,000 account or a $50 million account, systematically UBS put clients into the same securities," he says. "I've never seen anything like it."

The bond funds have landed UBS Puerto Rico in trouble before. In May 2012, UBS paid $26.6 million in fines and restitution and was censured by the SEC, which said the bank had manipulated the prices of the funds in 2008 and 2009. UBS didn't admit or deny wrongdoing.

While UBS settled with the regulators, Miguel Ferrer, then-chairman of UBS Puerto Rico, fought a parallel proceeding that the SEC brought against him—and got his case dismissed. In October 2013, an administrative law judge ruled the regulator had failed to prove its case. She found that the prospectuses and literature describing the funds were accurate. Ferrer, who built what eventually became UBS Puerto Rico, starting with a two-man office 50 years ago, retired in 2014.

Ferrer had championed the bond funds. "What is the problem?" he asked his brokers during a June 2011 sales meeting in San Juan that was recorded. "We have in your accounts almost $1 billion in cash that does not generate commissions," he said. He touted the high income the funds offered and argued that they were diversified. "You have current yield, and you have a history of good performance. What the f-ck do you want?" The audio recording, first reported by Reuters earlier this year, wasn't used in the SEC case; it's in the hands of lawyers handling the arbitration claims. Ferrer didn't respond to a request for comment made through his lawyers.

Retail investors aren't the only UBS clients who've suffered. So has the pension agency whose bonds the bank underwrote. The debt issue was intended to help rescue a troubled system that was, at that time, underfunded by $10 billion. It actually made things worse, according to a 2010 study prepared for the pension fund by consulting firm Conway MacKenzie. "The $3 billion transaction was inherently flawed, misconceived and speculative as a mechanism to improve the system's funded ratio," it found.

In May, Puerto Rico estimated the fund's deficit versus future obligations had tripled to $30 billion.

José J. Villamil, an economist in San Juan, said in a 2009 interview with Bloomberg Markets that the bond deal relied on unreasonable projections of future funding of the pension system to service the debt. "I don't know what they were smoking when they put this together," he said, referring to revenue forecasts in a report by Global Insight, a mainland U.S. consulting firm since acquired by

IHS. Jim Diffley, lead author of the report, defends his work. “There were all sorts of disclaimers that these are forecasts and subject to error,” he says.

A year after settling with the SEC, UBS hired Villamil to serve as an independent director of 18 of its Puerto Rico mutual funds. So he’s now on the payroll of an affiliate of the underwriter, but Villamil still says that it was a terrible idea to issue the pension bonds in the first place. “I think it was a huge mistake.”

Bloomberg Markets Magazine

by David Evans

September 21, 2015 — 9:01 PM PDT

[Chicago Faces Record Tax Hike as Pensions Compound Deficit.]()

Chicagoans are bracing for the biggest property tax increase in the city’s history as Mayor Rahm Emanuel contends with a budget shortfall and soaring retirement bills that have sent its credit rating tumbling.

Emanuel, a Democrat, on Tuesday proposed raising property taxes by $588 million over the next four years. That would inject cash into the city as it faces a $426 million deficit and a pension-plan debt that’s grown to $20 billion, more than $7,000 for each resident.

The tax increase would mark one of the biggest steps yet by Emanuel to shore up the finances of the third-largest U.S. city, which is under pressure from Wall Street as investors demand higher yields to buy its securities. Moody’s Investors Service, Standard & Poor’s and Fitch Ratings have all downgraded Chicago this year, giving it the lowest rating of any big U.S. city except for once-bankrupt Detroit.

“Our greatest financial challenge today is the exploding cost of unpaid pensions,” Emanuel said during his budget speech, which ended with a standing ovation from the packed city council chamber. “It’s a dark cloud that hangs over the rest of our city’s finances.”

“The bill is due today,” Emanuel said. Without the new revenue, the city would need to lay off 2,500 police officers, close 48 fire stations and cut 2,000 firefighting jobs to cover pensions costs, he said.

Welcomed Move

The prospect of higher taxes has been welcomed by investors. Federally tax-exempt Chicago bonds maturing in 2035 traded Tuesday for an average of 94.6 cents on the dollar, up from 88.7 cents on Aug. 27. That lowered the yield to 5.5 percent, about 2.5 percentage points more than top-rated debt, according to data compiled by Bloomberg.

“This is not kicking the can down the road,” said Paul Mansour, head of municipal research in Hartford, Connecticut, at Conning, which holds Chicago debt among its $11 billion of municipal securities. “We’re actually going to do something here that is going to sting. We’re moving from gamesmanship to action steps.”

The financial squeeze on Chicago emerged after officials shortchanged the pension funds by more

than $7 billion over the past decade, freeing up cash for other uses. That's caused the projected retirement bill to swell to about $1 billion next year, more than doubling since 2014, as it makes up for years of failing to set aside enough to cover pension checks for police officers, firefighters and other city employees.

The move to raise taxes, which needs the approval of the city council, is a shift for Emanuel, who won re-election in April after touting his record of not lifting property, gas or sales taxes. In May, Moody's cut Chicago's bonds to junk, saddling the city with higher interest bills as it refinanced debt.

"I think that public service requires people to display courage and to take tough votes," Alderman Edward Burke, chairman of the finance committee told reporters after Emanuel's address. "This is going to be a tough vote."

The property tax hike, which will be used for pensions, will start with a $318 million increase in 2015 followed by an additional $109 million in 2016, $53 million in 2017 and $63 million in 2018. A $45 million special real-estate levy that state lawmakers approved in 2003 would also be enacted to ease overcrowding at schools.

"It's a good faith example of what Chicago needs to kind of right their ship and improve their finances," said Alan Schankel, a managing director at Janney Montgomery Scott LLC in Philadelphia. "It's not going to solve all the problems of the world, but they're taking the right steps and that's important."

Chicago's next annual pension payment will jump 10 percent $976 million, according to an annual financial analysis released July 31. That's on top of the $549 million it still owes to police and firefighter retirement funds for this year. While state lawmakers approved lowering this year's payment to $328 million, Republican Governor Bruce Rauner has yet to sign it.

The city is also fighting a court challenge to its effort to cut some employee benefits and require them to pay more into the retirement system. A state judge in July ruled that the steps are illegal, siding with the workers.

Business Opposition

The tax-increase plan has already drawn some opposition from businesses. The burden may fall largely on commercial property owners, said Ron Tabaczynski, director of government affairs for the Building Owners and Managers Association of Chicago. Emanuel wants to exempt owners of homes valued at $250,000 or less from the hike.

"Businesses start rapidly approaching that tipping point where it's just not worth doing business here," Tabaczynski said.

The fiscal pain is being shared in other ways. Residents who don't already pay for garbage pick-up will have to pay $9.50 a month for refuse collection, generating about $62.7 million, according to Emanuel's proposal. He's also pitching higher fees on taxis and ride-hailing services like Uber Technolgies Inc. to produce about $48.6 million.

This tax increase is welcome step toward dealing with Chicago's financial strains, said Dan Heckman, senior fixed-income strategist in Kansas City, Missouri, at U.S. Bank Wealth Management, which oversees about $127 billion of bonds.

"Doing nothing is not going to solve it, and doing only a little will only prolong this," said Heckman,

whose firm doesn't hold Chicago debt. "That's a concern on a lot of investors' minds."

Bloomberg News

by Elizabeth Campbell

September 21, 2015 — 3:46 PM PDT Updated on September 22, 2015 — 10:36 AM PDT

Hospitals Issue Debt at the Fastest Pace Since 2012.

Nonprofit hospital bonds are being issued at the fastest pace since at least 2012 as earlier concerns over the Affordable Care Act's implementation have largely abated.

As of Sept. 16, nonprofit hospitals in the U.S. have issued $18 billion of municipal bonds this year, already surpassing 2013's and 2014's annual totals, according to Bloomberg data.

This year's pick-up in issuance reverses two years of pullback. As the Affordable Care Act — often dubbed Obamacare — began official implantation in 2013, wary hospitals put the brakes on capital investment until the future was more clear, said Mike Quinn, a managing director at Chicago-based B.C. Ziegler & Co.

"With factors like Obamacare decreasing utilization, reimbursement risk at the federal and state level and spirited negotiations with private health insurers, it's hard to understand what your future earnings stream is going to look like with those headwinds," said Quinn, who specializes in health-care investment banking. "So they borrowed less money for new money purposes."

As a result, issuance in this sector fell 40 percent to $16 billion in 2013 from $27 billion in 2012, data from Bloomberg show. The following year, it fell even further, to $15 billion.

Trinity Health

The largest of this year's deals was a $897 million borrowing from the Indiana- and Michigan-based Trinity Health Corporation Obligated Group priced in February, followed by a $504 million issuance from the North Shore-Long Island Jewish Obligated Group sold in June, data from Bloomberg show.

Issuers aren't the only ones turning more bullish on the sector. The two biggest credit graders — Standard &Poor's and Moody's Investors Service — lifted their negative outlooks for nonprofit health-care bonds in the past few weeks, citing positive impacts from health-care reform. Moody's had previously had the sector on negative watch since 2008, when the Affordable Care Act was first announced. S&P lifted its negative outlook on Sept. 9, noting that sector still had challenges ahead but was "stable."

Refinancing Transactions

Much of the boost in issuance this year has been the result of refunding, as health-care providers have been eager to take out older more expensive debt with less expensive newer bonds.

"We've had pretty robust issuance in 2015," Quinn said, noting that refinancing transactions have made up a bulk of the issuance. "Borrowers have taken advantage of the decrease in interest rates."

A push to refund debt has been a broader theme in the municipal market this year. State and local

governments have issued just under $300 billion in bonds this year, about two thirds of which has been refinancing older obligations, according to data provided by Bank of America Merrill Lynch.

Bloomberg News

by Kate Smith

September 21, 2015 — 7:03 AM PDT

As Casinos Falter, Mississippi Sells Debt Backed by Gambling Tax.

Mississippi, the poorest U.S. state, is selling its first bonds backed by gambling taxes after its share of the winnings fell to the lowest since 1997, two casinos closed and its neighbors began looking at expanding into the business. Investors may still like the odds.

The $200 million of bonds carry Standard & Poor's fifth-highest credit rating because the state's gaming revenue covers the debt service 10 times over, even though it's fallen almost 30 percent from the 2008 peak.

Potential competition from neighboring states, along with closures of a Harrah's casino in Tunica and another on the Gulf Coast, may lead the the state to dangle higher-than-average yields to draw buyers to the offering on Wednesday, said Burt Mulford at Eagle Asset Management.

"There has been a trend of decline in this sector in terms of state gaming revenue," said Mulford, a manager of tax-exempt funds for the St. Petersburg, Florida-based firm, which holds $2.4 billion of municipal bonds. "It'll come at a very wide spread, at least initially, and because it's a name a lot of managers don't own, they're going to want to add it."

Mississippi joins states across the U.S. that have seen their share of gambling money dwindle as others expanded the industry to bring in cash after the recession. Last year, casino revenue dropped in 10 of the 12 biggest gambling states, including Mississippi, according to data compiled by the University of Nevada, Las Vegas.

With more than $2 billion in revenue from 28 casinos, Mississippi's industry ranks sixth nationwide. That's drawn the attention of its neighbors: Alabama and Georgia pushed to legalize gambling in the last legislative session, said Jon Griffin, who tracks the issue for the National Conference of State Legislatures in Denver.

Alabama sought to establish a lottery and authorize casino gambling. Georgia lawmakers proposed a constitutional amendment to overturn its casino ban. Neither effort succeeded.

"Legalized gaming in Alabama could severely affect gaming revenue" because Mississippi's Gulf Coast casinos drew 2.5 million visitors from its neighbor in 2014, according to the offering statement. Gambling on the Mississippi River, a center of the state's casino industry, has already suffered from expanded options in Arkansas, with visitors from the state and Tennessee declining more than 50 percent in the past four years, the statement says.

Declining Revenue

In addition to the two casinos that closed last year, the Isle of Capri Casino in Natchez will shutter

next month, according to bond documents. Offsetting that, a new one is set to be built by the end of 2015 along the Gulf Coast with more than twice as many slot machines and seven times as many table games.

Mississippi's tax revenue from gambling fell in the 2014 budget year to about $164 million, a 17-year low, from as much as $230 million in 2008, according to offering documents. For the 12 months ended June 30, the collections totaled $167 million.

The state's view on the gaming industry "is it's going to be stable for quite some time," Mark Valentine, director of the bond advisory division in Mississippi, said in an interview. "It's not like there's just one or two casinos."

Almost two-thirds of the 23 million visitors to Mississippi casinos in 2014 came from another state, according to bond documents. While that keeps cash in the pockets of its citizens, it also makes Mississippi more vulnerable to competition, said Howard Cure at Evercore Wealth Management.

Hurricane Katrina

"If you attract people from all over the country, you're taxing tourists, which is always preferred from a political point of view," said Cure, head of municipal research in New York at Evercore, which oversees about $6 billion. "But there's definitely a saturation point to this. I usually stay away from these type of pure gaming-secured-type debt instruments because of those risks."

Mississippi's gambling revenue is also vulnerable to bad weather. After Hurricane Katrina struck in 2005, the Hard Rock Casino didn't open until almost two years later, according to offering documents.

Proceeds will be used to repair and replace bridges. In particular, as much as $18 million will go toward the Vicksburg Bridge, which spans the Mississippi River into Louisiana. It's the most-heavily traveled bridge in the state to be considered "structurally deficient," according to Mississippi's transportation department.

The state's 23-year history in the casino business has given it a leg up on states trying to capture its market share, said Mulford, the investor at Eagle Asset Management. He said that provides some cushion for the bonds, which mature from 2016 to 2035.

Twenty-year tax-exempt revenue bonds with a similar rating yield about 3.7 percent, compared with about 3 percent for top-rated debt, according to data compiled by Bloomberg.

"The trend is down," Mulford said. "But they have such excess coverage in their ability to cover debt service that they're in a good position to cover declining revenues."

Bloomberg News

by Brian Chappatta

September 20, 2015 — 9:01 PM PDT Updated on September 21, 2015 — 6:28 AM PDT

Municipal Bondholders Beware.

The recent bankruptcy rulings in California and Michigan protected retirees' pensions. But at what

expense?

Four cities emerged from bankruptcy court this past year, and in each case, their road to fiscal stability was paved not with cuts to the pensions of firefighters, teachers and other local government employees, but to the wallets of bondholders who had invested in those cities. In California's San Bernardino, Stockton and Vallejo, and in Detroit, bondholders faced losses of up to 99 percent of their holdings, according to Moody's Investor Services. In the bankruptcy resolutions in all three California cities, the courts preserved full pensions for retirees, while in Detroit pensions were cut only by about 18 percent.

This has neither ensured nor clarified the future fiscal sustainability of those cities or for others with structural debt problems. It has merely perpetuated concerns that cities have found a get-out-of-j-il-free card. In May, Moody's sharply downgraded Chicago's credit rating, attributing the decision almost entirely to the city's pension liabilities for its teachers and its inability to pay for schools. Should the Illinois Legislature grant Chicago and other municipalities access to bankruptcy, many fear that municipalities' political inabilities to rein in pension liabilities could trigger future bankruptcy court decisions that, as in California and Michigan, would have repercussions for municipal bondholders throughout the nation.

Naturally this is pitting bondholders against retirees. The former are critical to a municipality's future and its ability to raise money to build and modernize infrastructure and services. The latter are a fiscal burden, but their pensions are stabilizing factors in two ways: They help attract the most competitive applicants to provide city services, and they help ensure that retirees themselves do not become burdens. This was an imperative factor in the resolution of Detroit's plan to exit bankruptcy.

The importance of stable retiree income is echoed in federal law. The Pension Benefit Guaranty Corp. explicitly provides for continuity in pension benefits — but only for nonmunicipal corporate bankruptcies. The exclusion of cities and counties in this critical matter discriminates against the fiscal capacity of a city or county to invest in its own future. Some states, such as Michigan and Rhode Island, have reacted by making unique and needed commitments to the fiscal sustainability of their municipalities. Others such as Alabama and California leave cities to twist in the fiscal wind.

Almost every state that authorizes cities or counties to file for municipal bankruptcy imposes requirements or mandates. In Michigan, for example, that included the suspension or preemption of the authority of elected leaders. The post-bankruptcy process in Detroit of reverting to municipal authority came with strings attached, one of which is a decade of oversight by the state Financial Review Commission. The commission is charged with reviewing and approving Detroit's four-year financial plan and establishing programs and requirements for prudent fiscal management. To emerge from oversight in 2018, Detroit must maintain a balanced budget for three consecutive years.

This state oversight is important to Detroit's fiscal future in two ways. First, it means the state has a stake in Detroit's long-term fiscal sustainability. Second, it means that municipal bond investors have greater assurance and incentives to purchase and hold the Motor City's bonds, providing critical capital investment for Detroit's future. The bankruptcy events of the past two years — in California and Michigan specifically — suggest the need to establish firm and credible fiscal actions to guarantee citizens' essential services and pensioners' sufficient income. Fiscal boards, which are outside of political considerations, would bear the responsibility to guarantee the continuity and honor of the fiscal commitments agreed upon by states and their localities — especially in the wake of a restructuring process.

The road back from fiscal distress or bankruptcy for state and local governments is far more

challenging under current federal laws than for nonmunicipal corporations, so innovations that encourage capital investments in these cities' futures are invaluable. Bondholders are watching.

GOVERNING.COM

BY FRANK SHAFROTH | SEPTEMBER 2015

S&P Credit FAQ: Proposed Criteria Changes Will Bring Greater Transparency to U.S. Municipal Water and Sewer Systems.

Standard & Poor's Ratings Services is currently seeking comments on proposed changes in the criteria it uses to rate debt from publicly owned waterworks, sanitary sewer, and drainage utility systems. Our initial testing of the effects of these proposed changes—which will apply only to revenue-backed debt—indicate that roughly 75% of our more-than 1,500 ratings in this sector will remain the same if we adopt the criteria revisions. Of the remaining 25% of ratings, we are likely to see an even split between upgrades and downgrades, and nearly all will be no more than one notch. We don't expect any rating to shift to speculative-grade status from investment-grade status, or vice versa. We view this sector as relatively safe and stable, and most of our ratings are in the 'A+' and 'AA-' categories. Moreover, because several very large issuers dominate issuance in this sector, we expect the criteria changes to affect ratings on less than 25% of the par value of public water and sewer debt now in the market.

Standard & Poor's last revised the criteria for public water and sewer facilities in 2008, and before, that in, 2002. The changes we're considering now will increase the transparency and replicability of our criteria across the sector and more accurately reflect current and potential future risks associated with these debt issues, which are issued by cities, counties, or other public entities of widely divergent size and in all regions of the country. These new criteria will include some significant changes in how we assess water and sewer debt issues. (See "Request For Comment: U.S. Public Finance Waterworks, Sanitary Sewer, And Drainage Utility Systems: Methodology And Assumptions", published Dec. 10, 2014.) We ask interested parties to send their comments on the proposed criteria revision HERE or HERE by Feb. 28, 2015, and we will take them into consideration before issuing a definitive update to our criteria.

Here are answers to some frequently asked questions about the most significant changes we're proposing to our criteria for these ratings.

Frequently Asked Questions

Can you explain the new "operational management" assessment in the proposed criteria?

As proposed, this assessment will account for 10% of an issuer's total enterprise risk assessment and will take into account several factors pertaining to an entity's day-to-day operations that can have an impact on credit quality. One of these factors, for instance, would be a water utility's drought management plan—a factor that has taken on more importance in some states, such as California. Some questions to consider include "Does the issuer have a clear plan to address a prolonged decline in water availability?" and "Does the utility have the management expertise to fulfill its drought planning and to communicate effectively to its stakeholders?"

Another factor that we'll now explicitly and separately consider as part of the operational management assessment is the utility's rate-setting practices. Although municipal water and sewer

systems tend to have wide latitude in their rate-setting ability, they must still comply with state and federal environmental regulations to ensure public health and safety, and doing so may sometimes require rate adjustments.

The operational management assessment is designed to not only assess the adequacy of the water supply or treatment capacity, but will also take a hard look at the physical integrity and capacity of a system's assets, its ability to meet peak demand in its service area, along with its compliance with all environmental regulations.

How will the proposed "financial management" assessment section of the criteria work?

The financial management assessment will account for 10% of an issuer's total financial risk assessment. This assessment will consider the robustness of a utility's financial policies and internal controls and evaluate whether its long-term planning is well-constructed and realistic, and will also look at the assumptions that go behind that planning. We will also, as part of this assessment, consider the quality, transparency, and timeliness of the utility's financial reports. The financial management assessment would be in line with a similar assessment that Standard & Poor's currently performs for local government general obligation (GO) ratings.

The financial management assessment analyzes how a utility makes financial decisions, including how it identifies and addresses both ordinary and extraordinary costs, its ability to fund them, and whether it transparently reviews and publicly reports those risks. We assume that financial results manifest themselves in other visible ways and address them elsewhere in the criteria, specifically in coverage and liquidity assessments.

What is the "market position" assessment in the proposed criteria?

The market position assessment will essentially look at the rate affordability within a utility's service area. It will account for 25% of the total enterprise risk assessment. Affordability has been an increasingly important factor in some localities, despite the long-held contention that because people can't live without water, they'll always find a way to pay for it. We've recently seen instances where a significant percentage of water bills are going unpaid and management is struggling with collections in light of public health concerns. Affordability has also been an issue for other systems facing consent decrees and rising capital costs. The affordability of water has also come under discussion by the U.S. Conference of Mayors and the Environmental Protection Agency.

This assessment will look at typical water usage in a utility's service area and its cost to consumers, both on an absolute basis and as a share of median household income in that area. And recognizing that there will be households living well below an area's median income, the proposed criteria change will also take into consideration the poverty rate in the utility's service area. These measures will allow us to assess affordability across an area's income spectrum to give a more complete picture of overall affordability.

Will evaluating affordability be separate from looking at an area's local economy?

Although household income is clearly related to an area's economy, we will continue to use a separate assessment of economic fundamentals as the largest part of an issuer's total enterprise risk assessment score, at 45%. The economic fundamentals will continue to include assessments of a utility's customer base, the demographics of its service area, the major employers located there, and trends in the local economy.

Can you explain the changes to coverage metrics in the proposed criteria?

We will now evaluate the total financial capacity of water and sewer bonds using a single metric of "all-in" coverage, regardless of the specific nature of the debt or its lien position. That means we will include any debt or debt-like instruments that are ultimately supported by ongoing utility revenues, whether on- or off-balance-sheet, in our calculation of all-in debt service coverage. We propose to include any debt that receives regular support from surplus net operating revenues, whether specifically pledged or not. We would also include any net revenue transfers from the utility to other jurisdictions (which we now treat as an operating expense) as part of this calculation.

We thus define all-in coverage as: (Revenues-Expenses-Net Transfers + Fixed Costs)/ (All Revenue Bond Debt Service + Fixed Costs + Self-Supporting Debt).

The effect of this change could, in many cases, reduce the debt service coverage we calculate for a utility. For instance, the coverage of its senior debt might be 2x, but when all-in coverage is the measurement, the ratio might fall to 1.5x. The use of a single metric for all-in debt coverage is, under the proposed criteria, similar to Standard & Poor's treatment of coverage for U.S. public power utilities.

Will other major rating factors in your criteria remain the same?

Yes. We will continue to heavily weight economic fundamentals when rating these issues, and a utility's liquidity and reserves—both the number of days of cash on hand and actual cash in dollar terms—will remain significant rating factors. A utility's total debt will also continue to be a major rating factor, including not just the dollar figure, but also the allocation of debt by lien and how quickly or slowly that debt matures. And we will still evaluate how aggressive management has been in the type of debt it has selected, and whether its choices have introduced any contingent risks for the utility.

Will ratings that come out of the proposed criteria be subject to the same caps as before?

We are introducing several specific ratings caps into the rating process. These generally relate to very weak management or exceptionally poor financial performance that threatens timely bond repayment. We will base these caps on the presence or absence of particular characteristics or events that pose extreme risks, which likely have already indicated extraordinary credit weakness.

24-Feb-2015

Community Solar - A New Dimension in Solar Markets.

A Ballard Spahr webinar on October 1, 2015
12:00 PM – 1:00 PM ET

More than 15 states have passed legislation encouraging the development of community solar projects, and more states are considering such legislation. Community solar projects expand access to renewable energy by allowing multiple residential, commercial or industrial electric customers to invest in or subscribe to one central solar energy project and offset their electric usage or charges–through virtual net metering–based on their share of the solar energy generated by the project.

While the "traditional" solar model generally requires direct home or business premise ownership, access, or control, community solar removes this obstacle. Community solar projects can be located

in a variety of places, whether ground-mounted on open land, or installed on the roof of a commercial or government building or a community center.

An immense amount of development, finance, and M&A activity is underway in the community solar space. Please join us for a webinar where you will hear from key industry players who are directly involved in creating and financing community solar programs and projects and managing the associated regulatory and legal issues.

Speakers for the webinar include:

- John Mi, director, Structured Finance, NRG Energy Inc. John has more than six years of experience in solar and wind project financing and energy market analysis, with $180 million of investments closed to date. He leads the origination and structuring of financing for NRG's community solar deals.
- Marie Steele, manager, Electric Vehicles & Renewable Energy, NV Energy Inc. (a Berkshire Hathaway Energy Company). Marie is in charge of the utility's electric vehicle program and the "subscription solar" pilot program recently filed with the Public Utilities Commission of Nevada.
- Rick Umoff, Counsel and Regulatory Affairs Manager of State Affairs, Solar Energy Industries Association. Rick provides legal and regulatory support for SEIA on matters throughout the United States.
- Martin Mobley, CEO, United States Solar Corporation (US Solar). Marty manages the origination, development, and financing of US Solar's offsite solar assets and is the former head of the Solar Desk within Morgan Stanley's Commodities division.
- R. Thomas Hoffmann, (moderator) Practice Group Leader, Ballard Spahr's Energy and Project Finance Group.

As part of this webinar we will also take your questions in advance. Our panel will address your questions on community solar proposals, projects and the associated regulatory and legal issues. Please let us know what questions you would like our panel to answer by typing them into the boxes at the bottom of the registration form. We encourage you to submit up to three questions.

DATE AND TIME

Thursday, October 1, 2015
12:00 PM – 1:00 PM ET

REGISTER

MODERATOR

R. Thomas Hoffmann, Practice Group Leader
Energy and Project Finance Group

SPEAKERS

Marie Steele, Manager of Electric Vehicles & Renewable Energy
NV Energy Inc.

John Mi, Director of Structured Finance
NRG Energy Inc.

Rick Umoff, Counsel and Regulatory Affairs Manager of State Affairs
Solar Energy Industries Association

Martin Mobley, CEO
United States Solar Corporation (US Solar)

This program is open to Ballard Spahr clients and members of the energy industry. There is no cost to attend. This program is not eligible for continuing education credits.

Please register at least two days before the webinar. Login details will be sent to all approved registrants. For more information, contact Lisa M. Cheresnowsky at cheresnowskyl@ballardspahr.com.

Redevelopment Inches Back in California.

LOS ANGELES — California Gov. Jerry Brown has signed legislation that brings back redevelopment, in a limited way.

Brown fought for the laws that dissolved California's more than 400 redevelopment agencies in 2011 and has vehemently opposed efforts to bring them back in any form – until now.

"These important new measures enacted today will help boost economic development in some of our most disadvantaged and deserving communities," Brown said in a statement Tuesday.

Brown signed a trio of bills.

One bill authorizes creation of new community revitalization investment authorities that can use tax-increment financing, the cornerstone of redevelopment.

Such financing involves the issuance of tax allocation bonds that use the incremental growth of property tax revenue in a designated district to back the debt.

Another bill tweaks 2014 legislation that created of new enhanced infrastructure financing districts, also with the power to issue tax-increment debt. The third bill, which received mixed reviews from local government officials and advocates, is designed to streamline the process of dissolving the previous redevelopment agencies.

"We have the trifecta," said Larry Kosmont, president and chief executive officer of Kosmont Companies, a Los Angeles-based government and development consulting firm. "It is going to be a wild and exciting time in California for public-private financing."

Assembly Bill 313 modifies the 2014 enhanced infrastructure financing district law to make it easier to create public-private partnerships while protecting the rights of residents displaced by projects financed through the districts.

Assembly Bill 2 establishes the new revitalization districts, a limited version of redevelopment targeting only the state's most impoverished areas and boosting the set aside for affordable housing to 25%. Under the definition of blight in the new law, districts can only be created in places where residents make less than 80% of the state's annual median income, the area has an unemployment rate 3% higher than the state average, a 5% higher crime rate than the state average, and a severely dilapidated infrastructure.

Neither measure allows the areas to benefit from school districts' share of incremental property tax

growth. Cities, counties and special districts, who would be contributing tax increment, have to agree to contribute their share to the joint partnership authority under AB2.

The exclusion of the school share, as well as the opt-in nature of the bill for other agencies with tax increment, made the concept more palatable to the governor, according to Assembly Speaker Toni Atkins office. Brown credited Atkins' "tireless efforts" for the bills' passage.

"The dissolution of redevelopment removed a valuable tool for creating affordable housing," Atkins said. "Taken together, this trio of measures is a huge step toward filling that gap and helping our most disadvantaged citizens."

The former redevelopment agencies have been going through a complex dissolution process since laws eradicating them took effect in early 2012.

Senate Bill 107 – a bill aimed at streamlining dissolution – went through major modifications in the final hours of the Legislature's session.

Outstanding loans between cities and counties and their former redevelopment agencies have been a bone of contention between the state Department of Finance and the cities. Prior to the bill, the state tended to reimburse for cash loans, but was less likely to approve repayment when the city paid construction costs under an agreement that the redevelopment agency would bond for a project and reimburse the city later.

SB107 expands the definition of loans to include such agreements, but set a ceiling of $5 million on repayments.SB 107 would provide relief to 35 or 40 redevelopment successor agencies that have been prohibited from spending the proceeds of bonds issued between Jan. 1, 2011 and June 28, 2011. The bill sets a sliding scale for how much of the bond proceeds can be spent, ranging from 45% for bonds issued in January 2011 to 20% for those issued in June 2011.

The law that dissolved the state's redevelopment agencies prohibited the use of bonds issued between Jan 1, 2011, the date the RDA dissolution law was introduced, and the June 28, 2011, the state it passed, because some lawmakers felt that agencies were racing to issue bonds before the law dissolving RDAs was passed.

The new law also permits 100% of the proceeds of redevelopment bonds issued for affordable housing in 2011 to be spent.

Kosmont called SB107 redevelopment's last act, further describing it as "How do we bury redevelopment, sooner, rather than later?"

The regulatory processes are designed to insure that redevelopment winds down by 2018, he said.

THE BOND BUYER

BY KEELEY WEBSTER

SEP 23, 2015 4:22pm ET

PortMiami Hoping to Continue P3 Success.

A new public private partnership ("P3″ or "PPP") is coming to PortMiami. Royal Caribbean Cruises,

LTD ("RCCL") seeks to design, build, finance, operate, and maintain a new cruise terminal in the northeast section of the Port. RCCL's plans have been preliminarily memorialized in a non-binding Memorandum of Understanding that was approved at this Wednesday's Miami-Dade County Commission meeting. Subsequent Commission approvals will be needed for the binding deal documents and agreements.

Typical of a P3, RCCL will do more than simply enter into a ground lease for space in a terminal. It will share the risk of designing, constructing, operating, and most importantly to the Port, financing the terminal. The maintenance responsibilities will be split between maintenance of the leasehold improvements by RCCL and maintenance of the common areas outside the leased premises by the County, satisfying the remaining "M" element in the DBFOM (design, build, finance, operate, maintain) acronym that is used to characterize a P3.

The P3 with RCCL comes after the successful completion of the Port Tunnel P3 that has garnered a visit and praise from President Obama who extolled it as an example of the kind of P3 that should be used around the country to modernize aging transportation infrastructure. The $1 billion P3 was built because it was expected to divert vehicles from and reduce congestion in Downtown Miami and reduce travel time to and from the Port. In less than a year, the Port Tunnel met and even exceeded many expectations.

The Port Tunnel P3 was structured as an availability payment-based concession agreement. With this financing structure, the private-sector partner constructs, operates, and maintains the facility with its own funds, and the public agency (in the case of the Port Tunnel, Florida Department of Transportation) makes payments to its partner based on the project's availability for use by the public. The public agency bears risks pertaining to the demand for the facility because the amount it pays to the private sector party does not change even if the project is not used to the extent anticipated, though the availability fee may be offset with user fees received from public use of the project or facility. The risk for the private party includes the fact that this fee structure relies on the public budget, which may be subject to budgetary conditions and constraints and political pressure. There are also risks pertaining to delays, repairs, and increased costs that could lead to the private-sector partner missing key deadlines or taking the project out of service, which would lead to penalties for unavailability.

PortMiami is likely to also have new commercial development on its southwest corner given the interest that has been expressed by several groups, including one whose request for waiver of a competitive process was rejected. As Miami-Dade County continues to make strides in financing projects and providing solutions to infrastructure problems with P3s, it can look to the success at the Port as assurance that P3s can do well in Miami-Dade County.

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posted on: Monday, September 21, 2015

The National Law Review

Stifel's 'Transformational Acquisitions' Fuel Muni Growth.

Stifel Financial Corp. is approaching yet another milestone in its transformation from a regional player into a national wealth management and investment banking firm.

With the acquisition of Sterne Agee Group Inc. just completed, the St. Louis-based firm is focused on finishing its deal to acquire Barclays Wealth and Investment Management Americas by year-end, as it pursues a strategy that has helped build its global wealth management platform to $1.3 billion, according to a September financial report.

"The Stifel story has changed dramatically in the last five to six years," said Ken Williams, executive vice president of the broker dealer division, Stifel, Nicolaus & Co., and director of its municipal finance group.

"The Stifel today is different than it was seven or eight years ago … we have a lot more capital and capabilities," Williams said, as the firm completes a 15th year of aggressive growth, fueled by mergers and acquisitions.

The acquisition of the Barclays unit will further expand Stifel's public finance role and build its presence as a national underwriter seeking senior-managed roles on larger deals.

Williams said Stifel has already broadened its reach into different segments of public finance by increasing its total public finance staff to 170, with most of the growth attributable to key mergers and acquisitions over the last two years.

The most recent growth spurt included the expansion of its wealth management and fixed income capabilities through the June acquisition of Sterne Agee, a Birmingham, Ala.-based financial services firm.

Stifel, Nicolaus this year has advanced to seventh place among all senior book runners, from 10th in 2014, with 485 issues totaling $10.65 billion in the first half of 2015, as of July 6 data provided by Thomson Reuters.

It had secured a top-10 ranking in three categories in 2014. In addition to its 10th place ranking among all senior managers, it was in the top group for negotiated deals and small deals.

The acquisition of Sterne Agee was a seamless transition that added nine municipal professionals — five public finance bankers and four traders – to Stifel, Nicolaus, Williams said.

It also helped boost its public finance banking presence in the South, with the addition of two public finance bankers in Texas, and expanded its coverage of the housing sector.

The Sterne Agee merger is the latest move toward the 124-year-old firm's "strategic vision," which is "to build the premier wealth management and investment banking firm," according to its September financial report.

Sterne Agee's fixed income platform was complementary to Stifel's existing products and services, and the acquisition would allow the firm to "catapult" to a new level, Ronald J. Kruszewski, chairman and chief executive officer of Stifel, said in a Feb. 2015 press release announcing the merger.

The deal will accelerate the growth in the firm's fixed income platform and be a strong contributor to the expansion of the institutional group, Kruszewski said in a June 5 release, when the merger was completed.

"This acquisition furthers our goal of creating a balanced, well-diversified business mix with wealth management and institutional exposure," he said.

Eric Needleman, chairman of Sterne Agee Group Inc., said the merger gives Sterne Agee's

shareholders, clients, and employees an opportunity to “prosper in the ever-challenging financial services arena” after a century of its own growth and success.

“Our goal of being a preeminent financial services company has not changed, but we are accelerating this plan by joining together with a like-minded company with a similar legacy,” Needleman said in the February release.

Stifel has similar expectations for the merger with Barclays, which is expected to come mid-fourth quarter, according to a Stifel spokesperson.

The deal will marry Stifel’s broad investment advisors platform, and asset management and investment capabilities with Barclays’ capital markets division and investment advisory and managed money divisions, among others.

Stifel attributes much of its recent growth and expansion since 2000 to its “transformational acquisitions” strategy.

Stifel’s build-up dates back to at least 2000, when it merged with Hanifen Imhoff. In 2005, it acquired Legg Mason Capital Markets. In 2006, it bought Miller Johnson Steichen Kinnard’s private client group.

In 2007, Stifel acquired Ryan Beck and separately purchased First Service Bank. In 2008, it formed Choice Financial Partners and separately acquired 17 offices from Butler Wick. In 2009, Stifel purchased 56 branches from UBS. In 2010, it acquired Thomas Weisel Partners Group. In 2011, it took Stone & Youngberg, where Williams was the former head of the municipal bond department. In 2012, it purchased Miller Buckfire. In 2013, it merged with Keefe, Bruyette & Woods.

Last year, Stifel acquired the Los Angeles-based public finance investment banking boutique De La Rosa & Co., and also picked up a bond-trading business in 2013 from Knight Capital Group Inc.

“Before Stone & Youngberg, the public finance footprint was primarily in the Midwest and a small footprint in Denver,” Williams said. Prior to Oct. 2011 the firm was mostly active in Missouri, Michigan, Ohio, and had bankers in Illinois and Colorado, he said.

The recent acquisitions have expanded that reach, specifically the municipal operations, he said. “The goal of the municipal division is really reflective of the CEO” and his vision of building a national, rather than a regional, presence.

“The CEO is a big believer of the municipal marketplace,” Williams said. “The growth of the municipal group is part of the overall plan to build a bigger firm and build out a part of the institutional side, which wasn’t what he wanted it to be.”

One of the largest long-term deals that Stifel has managed to date was a six-pronged sale totaling $537.48 million from the Industry, Calif., Public Facilities Authority in June.

Stifel was also senior manager in June of Los Angeles, Calif.’s $1.4 billion tax and revenue anticipation note sale in the short-term market.

“We do business in almost every region in the country,” and maintain public finance offices in 21 different locations, Williams said.

Currently its structure includes, but it not limited to, its global wealth management platform, which includes a private client division that grew by 35% as a result of the merger with Sterne Agee to

2,800 financial advisors in 349 branches with over $200 billion in client assets, according to the firm.

Its asset management platform has over $22 billion in total assets, including fixed income and municipals, according to the report.

The firm offers equity and fixed income sales and trading, and maintains investment banking and research platforms as part of its overall business structure.

“We had a very busy first half and we were busy in July,” Williams said, though the banking activity slowed down because of seasonal cycles like income tax season and summer vacations. “We are expecting the rest of the year to remain busy,” and expect municipal supply to be unencumbered by any potential movement by the Federal Reserve Board before year end, Williams said.

“I don’t know that a modest rate increase by the Fed will have any effects on refunding, and I don’t see a rate hike affecting the volume for new money.”

Williams said the firm hopes to continue the growth and expansion of its municipal operations. The firm aims to maintain its high distribution of municipal bonds and its status as a lead underwriter of K-12 financings and tax increment financings across the country, he said. It also strives to win larger issuer transactions as senior book-running manager and boost its retail presence from its institutionally-driven underwriting and trading focus.

“Our challenge and what we are trying to do,” he said, “is build a more dynamic and successful municipal practice.”

THE BOND BUYER

by Christine Albano

SEP 23, 2015 2:04pm ET

S&P's Public Finance Podcast: (The Rating Action On New Mexico State University).

In this week’s Extra Credit segment, Director Bianca Gaytan-Burrell discusses what prompted our recent rating action on New Mexico State University.

Listen to the podcast.

Sep. 25, 2015

Moody's Predicts Long-Term Increase in Cross-Sector U.S., International P3s.

An increasing number of U.S. state and local governments are likely to use public-private partnerships, to build both transportation infrastructure projects and courthouse, education, water, waste water and other social infrastructure projects, a major credit rating agency predicted, while noting that this list is not likely to include hospitals.

Unlike the United Kingdom and Canada, whose governments are heavily involved in providing national health care, "[t]he U.S. has a diverse mix of public, private and not-for-profit hospitals that each derive revenue from numerous sources, including a mix of private and public insurance. As such, hospitals will likely remain a small component of the U.S. P3 market," Moody's Investment Services said in a FAQ on P3s it issued Sept. 21.

Some states are using P3s to develop other types of social infrastructure projects, ranging from Kentucky's state-wide broadband installation project and university and college student housing projects across the country to a senior housing development in Joplin, Mo.

P3s are being conducted to an increasing extent throughout the world but how they are financed and structured and the political and economic conditions that shape them vary widely from one country to the next, Moody's pointed out.

The United States has long relied on P3s to help finance transportation projects. However, Canada also differs from its North American cousin in that it provides substantial funding for the many types of P3s during the construction phase.

In France and the UK, Europe's largest P3 markets, the number of partnerships increased significantly in 2014; many were not new projects, however, but consisted of legacy or refinancing deals. This lack of growth in new P3 reflects each of these countries' budget constraints, the public's value-for-money concerns and "Eurostat's developing interpretation of accounting rules that will make it more difficult to treat the associated debt as 'off balance sheet,'" Moody's wrote.

In Latin America, Columbia and Peru are on the forefront of countries that are pursuing these partnerships. Brazil and Mexico, on the other hand, have various projects in the pipeline but many are slow to reach financial close or are delayed or canceled. This trend may reflect lack of expertise in negotiating these agreements or changes in political policies or government priorities, Moody's suggested. These countries are likely to continue to pursue these partnerships to address a lack of public infrastructure funding, however.

Australia is expected to increase the number of P3s it conducts to meet infrastructure gaps and the needs of its growing population, even though availability-based P3s remain on governments' balance sheets and incur more debt than publicly funded projects, the credit rating agency reported.

China, a relative newcomer to this procurement approach, hopes to replace regional and local governments' infrastructure financing vehicles with P3s and by issuing bonds. Partnerships would be used to build many different types of projects, "including transportation, municipal utilities and social infrastructure," Moody's wrote.

The central government hopes this procurement model will improve project and local government management practices, spur local public finance reform and reduce local government debt. China's finance ministry has announced 30 P3s and the government has set up a database containing 1,043 projects that would require investment of almost 2 trillion renminbi ($300 billion).

Moody's believes that the United States could become the largest P3 market in the world, Governing magazine reported.

NCPPP

By Editor

September 24, 2015

New Guidance Aims to Speed Up Approval of Federally Funded Infrastructure Projects.

New and updated guidance has been published to help federal agencies expedite the permitting and environmental review of federally funded infrastructure projects.

The new guidance consists of an enhanced permitting dashboard system, along with the establishment of metrics for agencies to follow in conducting permitting and environmental review, and the first update in nearly three decades of the environmental review handbook, the "Red Book."

The Federal Infrastructure Permitting Dashboard was launched in 2011 to track 52 high-priority projects' permitting and environmental review progress with the goal of improving multi-agency coordination. Agencies will now be required to use this tool to set specific reportable permitting and review schedules and milestones for projects that meet specific criteria.

In October, the 11 federal agencies involved in permitting, reviewing, funding and developing infrastructure projects will start identifying new ones that are expected to undergo lengthy and complex permitting and review processes, for which milestones and coordinated schedules will be posted within 90 days. These types of projects include major transit and airport projects, capital improvements and major utility, energy or water projects.

The newly revised Synchronizing Environmental Review for Transportation and Other Infrastructure Projects handbook (Red Book) contains practical, authentic techniques, models and assistance agencies can use to coordinate and synchronize environmental reviews, permits and decisions that affect the siting and building infrastructure projects, the U.S. Department of Transportation (USDOT) said in a press release. These sets of guidance are designed to help agencies turn best practices "into common practices" that have already been followed to accelerate the environmental review and permitting of more than 50 infrastructure projects Examples of such practices include "running different reviews concurrently rather than sequentially and using the Administration's online dashboard to promote accountability for a shared schedule."

Following such "common sense" practices has led to the expedited permitting of more than half of those projects, including New York's Tappan Zee bridge replacement, which took just a year and a half, USDOT said.

NCPPP

By Editor

September 24, 2015

Fitch: Fewer Uninsured Brighten U.S. Nonprofit Hospitals.

Fitch Ratings-New York/Chicago-23 September 2015: The reduction in the number of uninsured patients served by nonprofit hospitals is positive for the sector overall, Fitch Ratings says. The increased numbers of patients with coverage have helped hospitals sustain operating margins even as inpatient volumes have remained largely flat and top-line revenue growth continues to be pressured. Fitch expects the positive impact on performance to continue over the near term,

especially as the healthcare exchanges mature and additional states consider expanding Medicaid.

The U.S. Census Bureau reported that the number of Americans without health insurance fell to 33 million in 2014 from 41.8 million in 2013. Moreover, the number of uninsured declined in every state, even those that did not expand Medicaid. In our view, this is positive for the sector as hospitals are now receiving reimbursement for patients that previously would have been written off as charity care or bad debt. Fitch believes the sharp drop in the number of uninsured Americans also reflects a greater awareness of the eligibility under state Medicaid programs, as Medicaid enrollments have risen in a number of states that did not expand Medicaid.

Fitch's rating actions over the last 18 months support this, as affirmations, upgrades and downgrades have shown little difference between those states that have expanded Medicaid and those that have not. The effect on individual hospital performance varies depending on a number of factors, even among states that have expanded Medicaid. In New York, for example, which already had a robust Medicaid program in place, the subsidized healthcare exchanges have proven more beneficial to hospitals, as the underinsured have fuller coverage, helping increase utilization in a state where medical costs to patients can be high.

The benefit of wider insurance coverage has helped mitigate the impact of tighter reimbursement increases from managed care and Medicare payors. Over the medium, Fitch expects Medicare's value-based reimbursement programs and managed care "risk-based contracts," combined with increasing consumerism among patients, could pressure sector profitability. Furthermore, the expected reduction and redistribution of federal disproportionate share funds could mute what has been solid performance for the healthcare sector.

Introducing the Fitch Revenue Sensitivity Tool for Public Finance.

Read the report.

Rhode Island Averts Pension Disaster Without Raising Taxes.

Chicago is facing its biggest tax increase in memory, to raise money for pension payments. Illinois is stymied by a $110 billion pension shortfall. In New Jersey, public workers are in court over a failed pension deal. From Pennsylvania to California, pensions costs are crowding out aid for public education.

But even as pensions keep squeezing budgets and setting off court battles around the country, Rhode Island, America's smallest state, appears to have found its way out of the quagmire. Its governor, Gina M. Raimondo, has finished a four-year pension overhaul without raising taxes or issuing risky pension-obligation bonds. Union leaders who fought her at first ultimately negotiated the terms, deciding that a court fight over her plan might do more harm than good.

"Raimondo had the highest hill to climb," said Daniel DiSalvo, a senior fellow at the Manhattan Institute who has been comparing different states' efforts to rein in pension costs. Her initiative was among the most ambitious, he said, and she started "from what was, in many respects, the weakest institutional position."

Her experience, Mr. DiSalvo and others say, could be a case study for other states and municipalities struggling with pensions and other long-term obligations that cost much more than expected. And the timing could hardly be more critical, given predictions that the fiscal health of state and local governments is likely to remain under stress for years as the population ages.

“We may be entering a new fiscal ice age,” a long period when demographic forces will make financing cities and states even harder than it is now, Mr. DiSalvo said.

That is not to say everyone is happy with the result. To the contrary, bitterness remains in Rhode Island, where public retirees’ annual increases have been suspended, and public workers have had to trade in part of their defined-benefit pension plan for a 401(k)-style benefit, where they must bear investment risk.

“No other entity would get away with what the State of Rhode Island is doing to their retirees,” said Louise Bright, a retired state financial manager, who had wanted a trial to resolve key legal issues. “A contract is a contract, even when that contract involves senior citizens.”

Ms. Raimondo, who started her battle as state treasurer, faced obstacles not unlike those confronting Mayor Rahm Emanuel of Chicago: entrenched political machinery, powerful unions, a decades-old practice of promising rich pensions without setting aside enough money to pay them, truculent taxpayers, record numbers of retirees and an all-enveloping fog of discredited numbers. Both are Democrats in blue states. Both had to deal with “mature” pension systems that were paying out more in benefits than they were receiving in contributions, a situation that can quickly become unmanageable.

But Ms. Raimondo was able to revamp her state’s pension system, keeping some of the traditional structure while lowering the cost, and surviving lawsuits by workers and retirees who called her moves unconstitutional.

Mr. Emanuel’s attempts to rein in pension costs, in contrast, have been thrown out by a judge, leading to his appeal this week for a big tax increase.

“Our greatest financial challenge today is the exploding cost of our unpaid pensions,” he told the Chicago City Council on Tuesday. “It is a big dark cloud that hangs over the rest of our city’s finances.” Without raising taxes, he warned, Chicago will have to finance its pension promises by laying off thousands of police officers and firefighters, ending rat-control programs and letting street repairs lapse, among other cost-cutting measures.

“Our city would become unlivable,” he said.

That is the bullet Ms. Raimondo has dodged. A former venture capitalist and Rhodes Scholar with an economics degree from Harvard, she could see early on that her state’s cheery pension disclosures were papering over a crisis.

Ms. Raimondo was also willing to rest her case for a pension makeover on a contrarian interpretation of the law and hold firm when the unions sued.

“We thought we had a good case,” she said, “but most important, I knew I couldn’t be afraid of a potential lawsuit.”

Ms. Raimondo also had a quirk of the law on her side. In most states, lawmakers or the courts have taken steps to make public pension systems creatures of contract law, as opposed to mere creatures of statute. This may sound obscure, but the difference is critical. Statutes are relatively easy to

change — lawmakers just amend the law. But states that want to tear up pension contracts face an uphill fight, because of a clause in the United States Constitution that bars them from enacting any law that retroactively impairs contract rights.

The clause dates to post-Revolutionary America, when the framers wanted to stop the states from giving themselves debt relief. Since then, similar clauses have been added to state constitutions as well. And over the last century, many states have extended the contract clause to cover their pension systems.

But in Rhode Island, Ms. Raimondo said, lawmakers never got around to making the state pension system contractual. “In every state it’s different, but in Rhode Island, the whole pension system is set out in statute.”

Unions disputed that, but Ms. Raimondo forged ahead based on her conviction. That gave her a big tactical advantage: All she had to do was persuade the state legislature to amend the pension law, something it had already done many times.

Compare that with Mr. Emanuel’s predicament.

Unlike Rhode Island, Illinois did make public pensions contractual. Its constitution bars cities like Chicago from imposing pension cuts on their workers.

So while Ms. Raimondo was able to move toward her statutory goal in Rhode Island, Mr. Emanuel has been left haggling with 33 unions in Chicago, trying to find common ground for a makeover that would shrink pensions but fund them properly.

Eventually, he did get buy-in from all but three unions and from state lawmakers in Springfield. The city even programmed pension changes into its computers. But then the deal fell apart, when a small number of holdouts won an injunction. Chicago was ordered to wait for the State Supreme Court to decide the constitutionality of a separate pension overhaul by the state. The court found it unconstitutional and not long after that, a Cook County judge said the ruling was binding on Chicago, too.

And that is why Mr. Emanuel is calling for a big tax increase.

For Ms. Raimondo, persuading the state legislature to do radical pension surgery was a matter of explaining the depths of the problems. She began a series of town hall meetings, where she said that the state had promised its workers far more than it could deliver. The mismatch was so big that if the pension system collapsed, it could take the state down with it, she warned.

And then, in the middle of her road show, the small city of Central Falls went bankrupt. It had never joined the state pension system, preferring to run its own plan, and now its pension fund for police officers and firefighters had run completely out of money. The pensions of retirees, some elderly and infirm, were cut sharply.

“You’d see them interviewed on the nightly news,” Ms. Raimondo recalled. “These were guys who did everything right. They followed all the rules, and then their city went bankrupt and their pensions were cut in half.”

That was a persuasive moment for lawmakers. In November 2011, Gov. Lincoln Chafee called the legislature into special session. Amendments to the pension law passed overwhelmingly, allowing cuts to be made.

Unions and retiree groups sued, and the judge hearing the dispute, Sarah Taft-Carter, said early on that unlike Ms. Raimondo, she saw an “implicit contract” protecting public pensions in Rhode Island. But that was not the end of it. Contract jurisprudence still gives a state some wiggle room to unilaterally impair contracts, under narrow circumstances and with close judicial supervision.

Judge Taft-Carter ordered the state and the unions to try to resolve their disputes in mediation, warning that if they failed, there would be a jury trial.

Confidential talks began, but in the meantime, the state was permitted to carry out the changes.

A settlement finally emerged this year, which, among other things, gave one-time payments to current retirees, to soften the blow of losing their cost-of-living adjustments. Judge Taft-Carter held a “fairness hearing,” giving those affected a chance to sound off. Many expressed anger. But one union leader, Robert Walsh of the National Education Association of Rhode Island, said that after much soul-searching he had decided to support the settlement as the best deal for his 7,500 members.

A settlement, he said, “can be fair and heartbreaking at the same time.”

THE NEW YORK TIMES

By MARY WILLIAMS WALSH

SEPT. 25, 2015

TAX INCREMENT FINANCING - ILLINOIS

Devyn Corp. v. City of Bloomington

Appellate Court of Illinois, Fourth District - September 15, 2015 - N.E.3d - 2015 IL App (4th) 140819 - 2015 WL 5430992

Property owner brought action against city, seeking equitable accounting and declaratory judgment for city’s alleged failure to comply with various provisions of Tax Increment Allocation Redevelopment Act. The Circuit Court granted summary judgment to city and denied owner’s motion for leave to amend its complaint. Owner appealed.

The Appellate Court held that:

- City could take activities in furtherance of tax increment redevelopment plan after plan’s estimated date of completion;
- Property owner was not entitled to reconsideration on ground of newly discovered evidence;
- Owner was not entitled to equitable accounting; and
- Owner was not entitled to leave to amend its complaint.

TAX SALE - ALASKA

Tagaban v. City of Pelican

Supreme Court of Alaska - September 18, 2015 - P.3d - 2015 WL 5474352

Lienholder filed suit to challenge city’s tax foreclosure sale on property in which he claimed an

interest. Lienholder moved for summary judgment and city cross-moved. The Superior Court denied lienholder's motion and granted city's motion. Lienholder appealed.

The Supreme Court of Alaska held that:

- Statute governing municipalities' enforcement of tax liens did not violate lienholder's due process interests by limiting its foreclosure notice requirement to property owners;
- Because lienholder had actual knowledge of tax foreclosure during redemption period, and did not seek to redeem the property, he was precluded from raising a due process challenge to the redemption notice statute; and
- Prevailing party fees should not have been awarded for time city spent litigating lienholder's standing to sue as a class representative.

Even if judicial lienholder's interest was reasonably ascertainable, statute governing municipalities' enforcement of tax liens did not violate his due process interests by limiting its foreclosure notice requirement to property owners, where another statute that allowed mortgagees and lienholders to request foreclosure notice, provided a reasonable mechanism by which interest-holders such as the lienholder could protect their property rights.

Alaska's municipal foreclosure notice scheme, requiring lienholders to affirmatively request notice of pending tax sale, is reasonably calculated, under all circumstances, to apprise lienholders of the pendency of the action and afford them an opportunity to present their objections, as required by due process guarantees. Statutory structure reasonably balances lienholder's interest in preserving the ability to enforce a property interest against a governmental entity's interest in efficiently collecting taxes.

TAX - CALIFORNIA

Seibold v. County of Los Angeles

Court of Appeal, Second District, Division 3, California - September 22, 2015 - Cal.Rptr.3d - 2015 WL 5561222

After county assessment appeals board denied taxpayer's application for a refund of property taxes paid to county relating to ground lease and hangar at municipal airport, taxpayer filed complaint against county for declaratory relief and a refund of taxes paid for hangar and ground lease.

The Superior Court granted taxpayer summary judgment with respect to hangar, and following bench trial, found that ground lease constituted taxable possessory interest, but only entered judgment in favor of taxpayer for refund of taxes paid attributable to hangar. After taxpayer's motion to vacate was denied, county and taxpayer appealed. The Court of Appeal dismissed appeals and remanded with instructions, concluding that appeals were not taken from final appealable judgment. On remand, the trial court ruled in favor of taxpayer with respect to ground lease and entered orders enjoining collection of possessory interest taxes and ordering county to refund all possessory interest taxes paid on hangar and ground lease. County appealed.

The Court of Appeal held that:

- Taxpayer's right of possession under ground lease was sufficiently independent to establish taxable possessory interest in lease, and
- Fact issue as to whether hangar was taxable improvement on tax-exempt land precluded summary judgment with respect to hangar.

Taxpayer's right of possession under ground lease at municipal airport was sufficiently independent to establish a taxable possessory interest in lease. Ground lease conferred private benefit on taxpayer to use leased premises for storage of taxpayer's aircraft and aircraft-related equipment, use restrictions did not limit measure of control granted to taxpayer with respect to his authorized private use, but rather restrictions were fully consistent with airport's responsibility to safeguard use of public property and in no way required taxpayer to act as governmental agent when he enjoyed private benefit of storing his aircraft on leased premises.

Genuine issue of material fact existed as to whether taxpayer's airplane hangar located on leased premises at municipal airport was a privately-owned improvement on exempt public land taxable as a possessory interest, precluding summary judgment in favor of taxpayer in action against county for refund of property taxes paid for hangar.

Bill Proposed to Give Regulatory Protection to Puerto Rico Mutual Fund Investors.

Seventy-five years ago, when the federal government set out to regulate mutual funds, investment firms in Puerto Rico were deemed too far off the beaten track to merit scrutiny. So mutual funds on the island, and other United States territories, were excluded from regulation under the Investment Company Act of 1940.

Now, Puerto Rico's economy is teetering, investors in its bonds have suffered big losses and at least one member of Congress says the 75-year-old exclusion has outlasted its shelf life. On Friday, Nydia M. Velázquez, Democrat of New York, introduced an amendment to the 1940 act that would give mutual fund investors in Puerto Rico the same regulatory protection that their counterparts have on the United States mainland.

The bill, if it becomes law, will not replace the money the investors have lost, but it will bar some of the activities that led to their losses — activities that are already illegal on the mainland.

Mutual funds cater to individual investors who want professionally managed investments. The 1940 act protects them by barring those professional investors from engaging in certain kinds of transactions that suggest self-dealing, among other things. But because of the exclusion, such transactions are still legal in Puerto Rico.

A transaction from 2008 shows the repercussions. UBS, a major provider of financial services on the island, advised Puerto Rico's pension fund for government employees and was hired to take an unusual $2.9 billion bond deal to market. The pension fund had a big shortfall, and officials hoped to borrow the money and invest on behalf of the retirees. The deal was expected to be successful as long as the investment rate of return was higher than Puerto Rico's borrowing rate. That did not happen and now the pension fund shortfall is even bigger.

UBS had difficulty selling the bonds in the tough market conditions of 2008. It ended up packaging about half of the issue in its own family of closed-end mutual funds, which were marketed to wealthy Puerto Ricans as a good, tax-sheltered source of retirement income.

The interest on pension obligation bonds is not exempt from federal income taxes, because the Internal Revenue Service considers these securities speculative. But residents of Puerto Rico do not pay federal income taxes, and the Puerto Rican government exempted the bonds from its own estate

and gift taxes.

On the mainland, a bank underwriting a municipal bond issue would run afoul of the 1940 act if it packaged the bonds in mutual funds and sold them. But affiliated transactions are allowed in Puerto Rico.

“This practice constitutes a flagrant conflict of interest, and it must stop,” Ms. Velázquez said. Her bill is co-sponsored by Representative Maxine Waters, Democrat of California, who is the ranking member of the House Financial Services Committee. Chances of passage are unclear because of widely divergent views on what should be done to address Puerto Rico’s debt crisis. The Senate Committee on Finance has scheduled a hearing for Tuesday on some of the issues.

Puerto Ricans who invested in the affected mutual funds have filed more than 800 arbitration claims against UBS with the Financial Industry Regulatory Authority, known as Finra, a self-regulatory body. They are seeking more than $1.1 billion, basing their claims on regulations that are not part of the 1940 act’s exclusion for territories.

The Securities and Exchange Commission has also penalized UBS under other laws and collected a $26.6 million settlement for distribution to the harmed investors.

But Ms. Velázquez said that without an amendment, such things could happen again.

“This archaic exemption is long overdue for repeal,” she said.

THE NEW YORK TIMES

By MARY WILLIAMS WALSH

SEPT. 25, 2015

Muni Investors Face Pension Woes.

The longer the Fed keeps rates low, the worse some city and state pension problems may be. The signals from Detroit and Atlantic City.

There are many reasons to like municipal bonds. They’ve held up well amid recent market volatility, and at longer maturities they yield more than similarly rated Treasuries—much more on an after-tax basis. Tax-equivalent yields for A-rated 10-year munis are around 4%, compared with just 2.2% for the benchmark Treasury.

Yellen & Co. keep promising to raise rates, but investors who hold munis to maturity don’t have to worry about falling prices due to interest-rate risk. They do, however, have to worry about credit risk.

Underfunded state and city pension plans are turning into a bigger headache for muni investors. Pension accounting standards are getting tougher, and rating agencies seem more aggressive about downgrades. Lower investment returns this year for pensions will make funding woes look worse. States are trying to bring funding in line with obligations, but changing benefits to current and former employees have been met with stiff legal challenges.

“Investors should be concerned,” says Vikram Rai, Citigroup’s municipal strategist. “It’s a chronic

problem for many cities and states, and it's going to take a long time to fix. But rating agencies seem to want a quick fix, which is just not possible."

IF THE FED LEAVES RATES lower for longer, pension-fund growth projections will be harder to meet. Veteran bond investor Bill Gross of Janus Capital urged the Fed to raise rates in his October outlook, writing, "Do central bankers not observe that Detroit, Puerto Rico, and soon Chicago, Illinois cannot meet their promised liabilities?"

Ironically, the pension-funding picture is actually improving for most states, a new report from Loop Capital finds. But the troubled states have grown worse. Loop found the aggregate nationwide funded level dipped slightly from 73.1% to 72.6% in the past year. States including Illinois, Alaska, Kentucky, and Connecticut are funded near 50%. New Jersey is at 39%, finds Loop. "There's been a divergence," says Chris Mier, managing director at Loop Capital. "The gap between the best and worst states is widening."

In the past week, New Jersey's foundering gambling capital, Atlantic City, deferred pension payments to balance its budget. Chicago is proposing tax hikes to get out of a pension-funding nightmare that started last spring when the Illinois Supreme Court disallowed earlier pension reforms and Moody's downgraded its debt to junk.

Chicago shows the danger of a downgrade is real. Not only do bonds fall in value, but a downgrade can trigger escalating financial woes. Short-term debt may come immediately due, and institutional holders may be obligated to sell.

In the worst case, downgrades can lead to bankruptcy, still quite rare for municipalities. But in Detroit, bondholders were required by the court to share the pain, taking haircuts on their debt in restructuring—even in general-obligation bonds, which were once considered inviolable. "Detroit set a dangerous precedent," says Hugh McGuirk, who heads T. Rowe Price's muni-bond team. One lesson: "You don't want to be in lower-quality GOs if this comes to a head," he says. He prefers revenue bonds that fund airports and hospitals. Generally, their employees have fully funded 401(k) plans instead of pensions.

Choosing a professionally managed mutual fund is one way to handle pension-related risks. At Columbia Threadneedle, analyst Matthew Stephan monitors accounting changes being implemented by the Governmental Accounting Standards Board this year. New guidelines will probably make states underfunding their pensions look worse, but it varies a lot, he says.

For those individuals who want to do their own digging into state finances, the Electronic Municipal Market Access Website (www.emma.msrb.org) is a good place to start.

BARRON'S

By AMEY STONE

Updated Sept. 26, 2015 2:15 a.m. ET

U.S. Municipal Debt Sales to Hit $6.9 Billion Next Week.

Next week's sale of $6.9 billion of bonds and notes in the U.S. municipal market will feature hefty debt offerings from two states, according to Thomson Reuters estimates on Friday.

Washington state tops the week’s calendar at $944 million.

This includes $497.8 million of general obligation bonds it is offering via competitive bid in part on Wednesday and through Bank of America Merrill Lynch in part on Monday. Those bonds carry serial maturities from 2016 through 2040, according to the preliminary official statement.

The state will also competitively sell nearly $192 million of motor fuel tax GO bonds due from 2016 through 2040, $60.7 million of taxable GO bonds maturing from 2016 through 2021, and $193.7 million of GO refunding bonds maturing from 2016 through 2024.

The bonds are rated AA-plus by Standard & Poor’s and Fitch Ratings, and Aa1 by Moody’s Investors Service.

Connecticut will sell $840 million of new and refunding special tax obligation bonds for transportation infrastructure through lead underwriter RBC Capital Markets. The deal is structured with $700 million of new bonds with serial maturities from 2016 through 2035 and $140 million of refunding bonds maturing from 2018 through 2027, according to the preliminary official statement.

Moody’s rated the bonds Aa3, and Fitch rated them AA.

Meanwhile, flows into U.S. municipal bond funds turned positive in the latest week after four straight weeks of outflows, according to Lipper.

Net inflows totaled $231 million in the week ended on Sept. 23, the most since the week ended on April 29.

REUTERS

Sep 25, 2015

(Reporting by Karen Pierog; Editing by Lisa Von Ahn)

USC Marshall School of Business Study Makes Case for Greater Transparency, New Model for U.S. Bond Markets.

Greater transparency and the adoption of trading procedures similar to those of the nation’s equity markets could save U.S. corporate and municipal bond customers billions a year in transaction fees, according to a new study of bond market practices and transaction costs.

Lawrence Harris, who is Fred V. Keenan Chair of Finance and Business Economics at the USC Marshall School of Business, tabulated millions of bond transactions completed between Dec. 15, 2014 and March 31, 2015 for a study titled Transaction Costs, Trade Throughs, and Riskless Principal Trading in Corporate Bond Markets. What he discovered was that the benefits of electronic bond trading largely accrue to bond dealers who often take little or no risk in exchange for the mark-ups and commissions they charge their customers. Public investors, meanwhile, generally do not have the information they need to trade at the best-available prices. And unlike commissions, they do not even know the mark-ups they pay to dealers to trade.

According to the data, customers incur an average transaction cost of 85 basis points for retail-size trades (under $100,000 in par value) and 52 basis points for larger trades. “These costs are many

times larger than costs for similar-sized trades in equity markets," writes Harris. "Electronic trading has substantially lowered investor transaction costs in equities, but it has provided little benefit to most bond investors."

U.S. bond investors, Harris says, "would benefit if the 850 most actively traded bonds for which dealers provide near continuous electronic quotes were traded in market structures more similar to those in the equity markets. If the public could see national best bids and offers before trading, as they can for equities, dealers would have a strong incentive to offer better pricing. A rule that simply requires brokers to disclose their mark-up rates before a trade also would improve the markets."

The study shows that public investors in U.S. bonds presently pay $26B per year to trade. Greater pre-trade price transparency could save them 20% or more, or about $5B per year according to Harris.

The results of the study and Harris' recommendations are a wake-up call for regulators and may influence how bond markets are structured in the future, says James G. Ellis, dean, USC Marshall School of Business.

"This study's findings and recommendations will inform the growing debate on the future of bond markets in the United States," Ellis said. "Clearly, greater transparency must also be the standard in our bond markets, just as it is now in our equity markets."

The full study is available for download here.

About the USC Marshall School of Business

Consistently ranked among the nation's premier schools, USC Marshall is internationally recognized for its emphasis on entrepreneurship and innovation, social responsibility and path-breaking research. Located in the heart of Los Angeles, one of the world's leading business centers and the U.S. gateway to the Pacific Rim, Marshall offers its 5,700-plus undergraduate and graduate students a unique world view and impressive global experiential opportunities. With an alumni community spanning 123 countries, USC Marshall students join a worldwide community of thought leaders who are redefining the way business works.

September 25, 2015 3:13pm

IRS Chief Counsel Blasted for Favorable Ruling on Total Return Swaps.

WASHINGTON — Former Internal Revenue Service official Mark Scott is urging the IRS to revoke a private-letter ruling that was favorable for a total return swap, or TRS, arguing that they are "arbitrage schemes" that have "resulted in hundreds of millions of dollars of illegal tax benefits being stolen."

Scott, who spent 18 years at the IRS, was director of the tax-exempt bond office, or TEB, for several years before he left for private practice. He was also an ex-special assistant U.S. attorney for the Justice Department, who made the request in a blisteringly critical letter sent to William J. Wilkins, chief counsel in the IRS Office of Chief Counsel on Sept. 8. In an interview, Scott would not comment on whether he has launched a whistleblower case on TRS', but said this is irrelevant to his concerns about these transactions.

The website for his law practice says that he has been “specializing in representing whistleblowers on issues relating to tax-exempt bonds and taxes owed by state and local government,” as well as arbitrage rebate payments.

Scott’s letter to Wilkins refers to the favorable but limited PLR 201502008 that was dated May 21, 2014, but not publicly released by the IRS until Jan. 9 of this year. The ruling did not identify the parties involved but concluded that an extension of a TRS entered into between a borrower and a bank at the same time the underlying tax-exempt bonds were sold “will not be an abusive arbitrage device.”

These transactions, possibly hundreds of which have been done, involve long-term bonds and a short-term TRS. In such deals, a hospital or other borrower through an issuer privately places long-term bonds with a bank, which then enters into a much shorter term TRS with the borrower. The bank becomes the holder of the bonds as well as the swap counterparty.

The borrower typically swaps fixed for variable rates to lower its cost of borrowing. It also takes risk and provides price protection for the bank/bondholder/swap counterparty. When the TRS terminates, or is terminated, the bonds are valued.

If the bonds’ value is below par, the hospital pays the bank. If the value is above par, the bank pays the hospital. However, many TRS’ are rolled over or replaced with new negotiated terms for the life of the bonds. The borrower could be forced to pay if interest rates rise.

The bank/bondholder/swap counter party can make money from the higher tax-exempt bond rate and also from a deduction of its loss from the swap payments. In the case underlying the PLR, the bond proceeds had all been used to current refund some previous bonds, as well as to pay issuance costs. As a result there were no bond proceeds remaining and there was no debt-service reserve fund, from which arbitrage might have generated. If there had been bond proceeds or a reserve fund outstanding, the IRS could have questioned whether calculations should have been based on the bond yield or on the integrated bond and swap. But the facts of this case rendered this issue moot.

The borrower/bondholder/swap counterparty wanted to extend the TRS for another five years. The PLR essentially had to examine the bond and TRS transaction done several years ago to respond to the issuer about whether the extension would violate tax requirements.

In his letter, Scott took issue with the fact that, in this transaction and in any typical TRS, “one party wears two hats as both the swap counterparty and the holder of the tax-exempt debt.” As a result, he said, “the swap counterparty/bondholder, through pricing terms applicable to the ‘total return’ portion of the TRS, can lower its taxable income in exchange for greater tax-exempt income.”

“The ruling, therefore, describes an arbitrage scheme that is quite easy to abuse,” Scott said. “The scheme has been abused using billions of dollars of bonds, and has resulted in millions of dollars of illegal tax benefits being stolen,” he said. In an interview, he said: “The net effect is the bank is reducing its taxable income and increasing its tax-exempt income in a way that looks to be a tax shelter. It’s a way to convert taxable income to tax-exempt income through the use of a tax-exempt bond issue and a TRS. It raises tax issues for the outstanding bonds and the bank.”

TEB GETS UNDERCUT

Scott criticized the chief counsel’s office for issuing the private-letter ruling, while the enforcement side of IRS’ tax-exempt bond office is auditing these deals and finding the bonds taxable. He suggested the chief counsel’s office be completely undercut, or steamrolled over, TEB. It “is well

aware of this abuse" and "has investigated a number of high-coupon, tax-exempt bond issues where the bondholder/swap counterparty deployed TRS structures with phony terms to illegally generate greater tax-exempt income for a longer period of time in exchange for lower taxable income," Scott told Wilkins.

"These audits have been ongoing for some time and the office of tax-exempt bonds has, rightfully, issued adverse findings. Your office knew about these audits and the TRS scheme," Scott said.

Very few IRS audits of TRS' have been disclosed on the Municipal Securities Rulemaking Board's EMMA system: the Electronic Municipal Market Access website. In one that was, the IRS in 2013 found that revenue bonds issued by the New Jersey Health Care Facilities Authority for the Deborah Heart and Lung Center were taxable because the borrower entered into a total return swap. The $37.4 million of revenue bonds had been issued in 1993 and about $17.6 million remained outstanding. Neither the IRS nor the parties involved publicly disclosed the amount paid in settling the tax dispute.

Scott called this latest PLR "a mistake" and said that, "although innocent looking factual representations were presented, the favorable ruling, even with this ostensibly limited application, has emboldened the use of the TRS scheme." Some lawyers said that while PLRs are only supposed to apply to those taxpayers that requested them, this one has been taken as an encouragement that TRS' can be done without violating tax requirements.

Scott also claimed that the PLR was wrong by being limited and failing to address several tax issues. For example, the PLR declined to take a position on whether the TRS caused a reissuance, which would cause the bonds to be reissued and subject to the latest tax requirements. Lawyers had said a reissuance would not have been a problem because there have been no recent tax law changes that would have applied. The chief counsel's office also did not express any opinion on whether the interest paid on the bonds may be excluded from gross income.

Scott said: "The ruling was wrongly reasoned and overlooked the proper application of several long-standing regulations. The ruling should have pointed out that the payment to the issuer for 'price protection' results in additional gross proceeds, the TRS is investment property, and significant modifications made to outstanding tax-exempt debt by a person other than the governmental issuer results in the reissuance of taxable debt."

"By agreeing to entertain this ruling request and to restrict the scope of its legal analysis, your office was used to promote an abusive arbitrage scheme," he told Wilkins. Scott also claimed the chief counsel's office violated IRS procedures, which state that PLRs will not be issued for outstanding transactions. He accused the office of "erasing the distinction between private-letter rules and technical advice memorandums" and helping transaction participants "game the audit process."

"By expressing legal conclusions on outstanding bonds the ruling violates the clear standards set forth in [Revenue Procedure] 96-16, Section 5.04(1)" on rulings and determination letters, according to Scott. That section of the revenue procedure states: "The Service will not issue a nonreviewable ruling on whether an issued and outstanding obligation that is part of an issue of obligations meets one or more conditions for the exclusion of interest on the obligation from gross income under § 103 unless the request is received by the Service before interest on any obligation in that issue is required to be reported by a holder."

"It would be inexcusable to leave this mixed ruling (part technical advice memorandum/part private-letter ruling) on the books to serve as an example of how to game the audit process," Scott told Wilkins.

THE OTHER SIDE

Some lawyers disagreed with Scott.

"I think the ruling was sound and it was consistent with tax policy," said Hobby Presley, Jr. a partner at Balch & Bingham in Birmingham, Ala. "I can't tell from Mark's letter what his concern is. If people are using a total return swap structure in the existing environment, it's highly unlikely they are motivated by arbitrage. Because of the prevailing [low] investment rates, there's no arbitrage to be earned."

Other lawyers agreed, saying that in the TRS in the PLR, there was no real opportunity for arbitrage earnings because no bond proceeds remained outstanding and there was no debt service reserve fund. Milton Wakschlag, a partner at Katten Muchin Rosenman in Chicago, said that while Scott wants the ruling rescinded, "the IRS feels strongly about the quality of the guidance it issues in the first place and the process it goes through."

"In my anecdotal experience, they are not keen on interventions," he said. Wakschlag said the late, former House Ways and Means Committee chair Dan Rostenkowski, D-Ill., once tried to get one of his PLRs overturned, but did not succeed. "I suspect nothing will happen with this," Wakschlag said. The PLR "seems to have taken longer to be released than the norm," likely meaning it was reviewed by many IRS officials, he said. Some lawyers have said that there are questions in TRS' about whether a bank, which often serves as both the swap counterparty and issuer, should be allowed to take tax deductions for loss carry forwards. However, this is an issue for a different IRS division or bank regulators, not TEB, they said.

THE BOND BUYER

BY LYNN HUME

SEP 21, 2015 1:10pm ET

SIFMA, NAMA: Pending MSRB Fee Changes Will Be Unfair, Burdensome.

WASHINGTON — The Municipal Securities Rulemaking Board's pending fee changes will be unfair and excessively burdensome, dealer and advisor groups told the Securities and Exchange Commission.

They complained about the pending fees, some of which are scheduled to take effect beginning Oct. 1, in comment letters sent to the SEC.

The proposed changes show "the MSRB has failed to address" the "disparity between dealer and non-dealer MA fees," even after the self-regulator had said over 90 percent of the MSRB's revenue comes from dealers, said Michael Decker, managing director and co-head of municipal securities at the Securities Industry and Financial Markets Association. SIFMA is asking the SEC to temporarily suspend the rule changes and institute proceedings to disapprove them.

Terri Heaton, president of the National Association of Municipal Advisors, asked the MSRB and SEC to reevaluate the MSRB's true needs and currently available funds, because the changes "will impact small advisors on a larger scale." Small MAs will have to absorb the fee increases "on a greater proportional basis" and face an "undue burden," which would be a violation of the Dodd-

Frank Act, she said.

The MSRB proposed changing its Rule A-12 on initial and annual registration fees to raise its initial fee to $1,000 from $100 and the annual fee to $1,000 from $500, starting on Oct. 1. Heaton suggested the MSRB phase in both fee increases over the next two fiscal years.

Beginning on Jan. 1, the self-regulator plans to change its Rule A-13 on underwriting and transactions fees by reducing the underwriting fee to $0.0275 per $1,000 of the par value of primary offerings from the current $0.03 per $1,000, starting on Jan. 1. It also will make a previously temporary technology fee of $1.00 per transaction for each interdealer and customer sale report to the board permanent and available for use with operating expenses.

Decker, who said muni dealers "have shouldered the cost of the MSRB for 40 years," suggested the MSRB implement activity-based fees on MAs that would mimic the current underwriting transaction fee for dealers. MA regulation is a "significant reason" for increased demands on MSRB resources and "it is time for the MSRB's cost to be fairly shared," he said.

NAMA proposed the MSRB provide information about how its MA rulemaking is affecting the board's cost of operations. Without that "important piece of the puzzle," it is harder to understand the MSRB's need for fee increases, Heaton said. She also said it seems the MSRB's operating reserves "are quite healthy and appear to be in excess of what would be prudent or necessary for an entity that can impose fee increases on an immediately effective basis."

Decker raised a similar concern about the MSRB's decision to make its technology fee permanent. He said that when the fee first went into effect in 2010, the MSRB clearly said it would only be temporary and specifically used for technology-related capital expenses. But now that the MSRB is expanding its use and making it permanent, the board is damaging its credibility and the market's respect of the MSRB, he said.

The SIFMA comment letter also used the technology fee to challenge the MSRB's claim that the fee changes would be "effectively revenue neutral." Decker said that would only be the case if it was assumed the technology fee would be permanent, which is not what the market believed. The MSRB would draw an additional $8 million a year by keeping the fee, he said, adding that the MSRB is in a good financial position as proven by a $3.6 million transaction fee rebate to dealers in 2014.

The MSRB said it proposed the changes in fees after "continuous and ongoing efforts" to "reasonably distribute" them among all market participants based on level of involvement. It said the annual fee has not changed since 2009 and covers fewer total expenses recently. The initial fee has not been changed since it was first adopted in 1975 and the drop in the underwriter transaction fee was meant to more evenly distribute costs because the MSRB saw less than a dozen dealers accounting for about 52% of the payments.

THE BOND BUYER

BY JACK CASEY

SEP 21, 2015 2:46pm ET

SIFMA Submits Comments to the SEC on Increased MSRB Technology Fee.

SIFMA provides comments to the U.S. Securities and Exchange Commission (SEC) on the Municipal Securities Rulemaking Board's (MSRB) adjustment of their fees, increasing them, to align revenues with operational and capital expenses. The MSRB collects technology fees from municipal securities dealers and municipal advisors. SIFMA strongly opposes the rule changes contained in Notice 2015-13 and urge the Commission to exercise its authority to temporarily suspend the Rule Changes and to institute proceedings to disapprove the MSRB's changes announced in the Notice.

Read SIFMA's letter.

SIFMA Submits Comments to the IRS on Re-proposed Issue Price Rules.

SIFMA provided comments to the Internal Revenue Service (IRS) and their recently re-proposed rules related to establishing the issue price on tax-exempt bond issuance transactions. In its release, the IRS withdrew the 2013 issue price proposal, which SIFMA opposed, and offered an alternative approach. The new proposal maintains the requirement that issue price is established when underwriters have firm orders for a threshold amount of each maturity in an offering. However, the new proposal offers an alternative means of establishing issue price when there are insufficient firm orders to meet the threshold test.

View SIFMA's letter.

NABL Submits Issue Price Comments.

NABL has filed its comments on the arbitrage regulations proposed on June 24, 2015. NABL requested several items, including:

- (1) confirmation that an issuer need not choose between the general method and the alternative method prior to the issue date;
- (2) confirmation that, under the alternative method, the issuer's obligation is limited to obtaining a covenant from the sole or lead underwriter;
- (3) clarification that the issuer's due diligence obligation with respect to issue price is that of a prudent person;
- (4) elimination of the uncertainty in the definition of "underwriter;"
- (5) additional alternative methods for determining issue price for bonds sold pursuant to a competitive bid;(6) confirmation that bonds purchased directly from an issuer by a bank or another party for its own investment would fall under the general private placement and buyer rules of Section 1273 of the Code; and
- (7) addition of a cross-reference to the definition of "issue price" for other similar concepts in the tax code.

NABL also requested to testify at the hearing on the proposed regulations to be held on October 28, 2015.

Click here to read NABL's comments.

Senate Finance Panel Hearing Set On Puerto Rico's Fiscal Health.

WASHINGTON – The Senate Finance Committee will hold a hearing on Sept. 29 to discuss the "dire financial situation" in Puerto Rico, committee chair Sen. Orrin Hatch, R-Utah, said Tuesday.

The situation "facing Puerto Rico's economy and its citizens underscores the alarming consequences of crippling debt," Hatch said. "With outstanding debt greater than its economic output, the territory faces default unless a responsible long-term fiscal path forward is found."

The committee has not announced witnesses for the hearing, but Resident Commissioner Pedro Pierluisi, D-PR announced that he has been invited to testify. Gov. Alejandro Garcia Padilla, a Democrat, has also been invited to testify, according to Pierluisi, who said he expects the governor to send a representative.

Hatch said members of the Finance Committee will "have the opportunity to explore how the territory manages its finances and government-backed borrowing entities as well as the interplay between federal entitlement and tax programs and Puerto Rico."

In addition to chairing the Finance Committee, Hatch also sits on the Senate Judiciary Committee, where a bill to extend Chapter 9 bankruptcy protection to Puerto Rico authorities and municipalities has not moved since it was introduced July 15.That bill was introduced by Sens. Richard Blumenthal, D-Conn., and Chuck Schumer, D-N.Y.

A companion bill introduced in February by Pierluisi, has similarly remained stagnant in the House Judiciary Committee.

Sen. Chuck Grassley, R-Iowa, and Rep. Bob Goodlatte, R-Va., who chair the two committees, have said they do not intend to advance the bills unless other avenues are considered.

While the Obama administration and others, are pushing for Congress to extend bankruptcy protections to the territory, groups such as 60 Plus Association, a seniors' advocacy organization, want to see the creation of a federal financial control board.

Puerto Rico continues to struggle with $71 billion in public debt. Gov. Alejandro Garcia Padilla has repeatedly said the debt is not payable without restructuring. Officials on the island recently made numerous suggestions for remedying the situation in the form of an economic growth plan a government working group released Sept. 9. The plan incorporates stimulus measures, spending cuts, fiscal reforms and the creation of a local financial control board.

THE BOND BUYER

BY JACK CASEY

SEP 22, 2015 6:06pm ET

MSRB: Dealers Would Have to Disclose Markups on Principal Transactions.

WASHINGTON — Dealers acting as principals would have to disclose markups and markdowns in transactions with retail customers under rule changes proposed by the Municipal Securities

Rulemaking Board.

The proposed change to MSRB Rule G-15 on confirmations is the first of its kind in more than 20 years and follows what has been a nearly 40-year discussion about the need for markup disclosure in the market. The MSRB is seeking comment on the components of its markup disclosure proposal as well as on alternatives. It is asking that those comments be filed by Nov. 20.

Bond Dealers of America and Securities Industry and Financial Markets Association both said they are reviewing the changes with their members before submitting comment letters by the November deadline. Jessica Giroux, BDA's general counsel and managing director of federal regulatory policy, said BDA is "encouraged" by the MSRB's use of previous comments in drafting its new proposal, such as the exclusions of primary offerings and institutional customers.

Under the markup proposal, a dealer buying or selling bonds for its own account would be required to disclose the markup or markdown on a customer's confirmation when: it executes a transaction on the same side of the market as the customer; the transaction is greater than or equal to the size of the customer's; and the dealer transaction occurs within a two-hour window on either side of the customer transaction.

Those markups and markdowns would be equal to the "difference between the price to the customer and the prevailing market price for the security," and would have to be disclosed both as a total dollar amount and as a percentage of the principal amount of the customer transaction, according to the MSRB. Even if the markup did not have to be disclosed, a dealer would have to provide the investor a hyperlink and URL address to the Security Details page for the security on EMMA as well as a time of execution for the customer's trade.

The MSRB would also try to limit this proposed rule to the secondary market by excluding transactions in new issue securities effected at the list offering price by members of the underwriting group.

There are also two organizational caveats to the rule. If a dealer is executing a transaction from an affiliate's inventory of munis, the rule would require the dealer to "look through" to the affiliate's transactions with the "street" and other customers to see if the affiliate had a same-side of the market transaction within the two-hour window. Dealers that have independently operating trading desks would be exempt from disclosing markups if they could prove that the customer transaction occurred separately from the principal trading desk that executed the dealer's same-side market transaction and that the desk was not aware of the retail customer transaction.

Lynnette Kelly, the MSRB's executive director, said the disclosure requirements would provide investors "a way to understand the true costs of their municipal securities transactions."

"Our new proposed approach would offer greater clarity for investors as to dealer compensation while leveraging the existing processes and systems dealers use to comply with their fair-pricing obligations," she said.

The MSRB previously proposed changing its Rule G-15 in November 2014 to require dealers to disclose on their confirmations a "reference price" of the same security traded on the same day. FINRA proposed a similar rule for corporate bonds. But muni dealers said the reference price rule was too complex and would confuse investors. They asked the MSRB to withdraw it. FINRA has said it also will modify its proposal because of criticism and solicit a second round of comments. But the authority only plans to propose a revised version of the reference price rule it floated earlier.

The MSRB also included modifications to the “reference price” rule in its regulatory notice, although the board noted it would prefer markup disclosure. The board asked commenters to weigh in on whether disclosing a reference price is a better alternative to markup disclosure.

The reference price rule modifications largely mirror the requirements laid out in the markup disclosure proposal. The MSRB is asking whether the reference price rule should: include all retail investors regardless of the trade size cap that was used in the initial proposal; apply exclusively to the secondary market; disclose a total dollar amount as well as a percentage; require a security specific link as well as the time of execution; and offer similar exceptions for inventory-affiliate dealers and independent trading desks.

Securities and Exchange Commission members have been pushing for markup disclosure, and more aggressively since the commission’s enforcement action against Edward Jones in August for overcharging retail customers for sales of new bonds and failing to adequately supervise mark-ups on secondary market trades.

Just after the SEC announced that settlement, four of the five SEC commissioners urged that broker-dealers be required to disclose markups and markdowns on munis, warning that they were ready to make the proposals themselves if self-regulators did not pursue them. SEC chair Mary Jo White did not join the other commissioners in the statement, but previously said she would work with self-regulators to develop rules requiring markup disclosure in riskless principal transactions.

THE BOND BUYER

BY JACK CASEY
SEP 25, 2015 2:09pm ET

S&P: Report Explains Ratings Approach On Distressed Local Government Credits.

CHARLOTTESVILLE (Standard & Poor’s) Sept. 24, 2015—Although rating trends in the U.S. local government sector are positive overall, there have been several recent situations where borrowers wound up in fiscal stress. From Standard & Poor’s Ratings Services’ perspective, municipal bankruptcies and previous distress scenarios are opportunities to help inform our current analysis of distressed issuers with respect to the incentives to pay certain obligations, according to a report published today.

“Our view is that the small number of bankruptcies and credits in distress we have seen do not enable us to predict conclusively which obligations will or will not be impaired in bankruptcy,” said credit analyst Lisa Schroeer. “There are, however, several factors we believe can inform our view and ratings regarding the likelihood of payment on specific obligations for distressed credits. Our local government ratings do not reflect our assessment of expected recovery post-bankruptcy. Our ratings instead reflect our assessment of whether the issuer will pay the bonds in full and on time.””

In particular, in distressed situations, Standard & Poor’s draws on several analytical factors, including the legal structure of the borrower’s debt; the “comparables” (i.e., similar situations that we have seen); and the revenue pledge.

“As we evaluate these distressed credits, examples inform our analysis when assessing the incentives to pay for distressed issuers. Legal structure, political incentives, additional pledge

revenues, and comparable situations all factor into our analysis," said Ms. Schroeer. "When looking at our distressed issuers, our analysis incorporates historic actions while taking into account the unique credit profile of each issuer."

The report is titled, "Incentive to Pay: How Recent Bankruptcies Inform Analysis Of Distressed Local Government Credits," published today."

Under Standard & Poor's policies, only a Rating Committee can determine a Credit Rating Action (including a Credit Rating change, affirmation or withdrawal, Rating Outlook change, or CreditWatch action). This commentary and its subject matter have not been the subject of Rating Committee action and should not be interpreted as a change to, or affirmation of, a Credit Rating or Rating Outlook.

The report is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. If you are not a RatingsDirect subscriber, you may purchase a copy of the report by calling (1) 212-438-7280 or sending an e-mail to research_request@standardandpoors.com.

Ratings information can also be found on Standard & Poor's public Web site by using the Ratings search box located in the left column at www.standardandpoors.com. Members of the media may request a copy of this
report by contacting the media representative provided.

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Incentive To Pay: How Recent Bankruptcies Inform Analysis Of Distressed Local Government Credits.

Though rating trends are overwhelmingly upward across all municipal sectors (see "U.S. Public Finance Positive Ratings Streak Reaches 14-Year High," Sept. 2, 2015) Standard & Poor's Ratings Services has also seen borrowers like Atlantic City, N.J.; Wayne County, Mich.; and, most recently, Hillview, Ky., trying to work through fiscal stress. Though comprising only a very small percent of overall local government ratings, distressed credits bring into play analytical considerations that aren't usually a factor in this overall strong sector.

Often the hallmark of extremely distressed credits is concern regarding sufficient liquidity, whereby issuers may face a decision on who to pay: Peter or Paul (or Jane or Jenny, for that matter). While the framework of our local government criteria applies to all of our local government ratings, for distressed credits, where rating caps are often invoked, we address the questions regarding management's incentives to pay under strain. This report will focus on the somewhat unique

analytical considerations we believe play into this subset of issuers.

Overview

- Pockets of stress continue to arise in the local government sector, though we still anticipate municipal bankruptcies and defaults will remain extremely low.
- Prioritization of payments during distress and while in bankruptcy may not be precedent-setting, but inform our analysis of how governments may act under stress.
- We continue to apply our criteria and insights gained to our analysis and the often unique set of incentives issuers have to prioritize payments. Standard & Poor's U.S. public finance credit ratings reflect the likelihood of default and do not incorporate recovery.

Continue reading.

24-Sep-2015

Rating Correlations For U.S. Local Governments: Proximity Doesn't Always Matter.

When Standard & Poor's Ratings Services evaluates a U.S. local government's general obligation (GO) credit quality, it does so from a holistic point of view, looking at all the features it thinks could influence credit quality. They include financial performance, management, and debt burden and other long-term obligations, as well as the area's economy. Likewise, when a local government requests a rating on a series of revenue bonds (such as a water or sewer system), we review the system, its strengths, and challenges.

For both GO and revenue ratings, the local economy is an important factor in our analysis. This frequently includes the relative health of other municipalities that surround or overlap the issuer, and who often share similar demographic trends. The financial and economic health of these other governments helps inform our understanding of the local economy, be the influence good or bad. In some instances where a direct impact exists–such as a weak state that delays payments of necessary operating dollars to local governments because of its own financial pressures or different municipal entities with shared financial resources such as pooled cash–it can have credit implications.

However, in instances where–save geographic location–no direct link exists between different issuers and/or separate security pledges within one issuer, we don't automatically cap ratings due to the proximity of a struggling municipality or strained internal operations, particularly if the issuers are legally unrelated.

Overview

- Standard & Poor's does not tie the rating on one U.S. local government issuer to another based on geography alone.
- We evaluate U.S. municipal issuers independently, and if a credit quality relationship exists, we factor it into the rating.
- Internal pressures on related issuers are more likely to have a correlating rating impact, and we assess each situation independently.

Continue reading.

24-Sep-2015

[Regulator Revises Proposed Rule on Muni Bond Pricing Disclosure.]

(Reuters) – A U.S. regulator on Thursday modified a proposed rule in hopes of making it easier and less expensive for bond dealers to tell retail customers how much above wholesale they are paying to buy or sell municipal bonds.

The Municipal Securities Rulemaking Board asked for comment on a proposal that would require bond dealers to disclose on customer trade confirmations the dealer "mark-up" – how much more than market price a customer pays to buy muni bonds or how much less to sell them.

The proposal revises one made in November 2014 that would have required dealers to disclose a reference price they paid for bonds taken into inventory on the same day as the trade made with a customer. Dozens of bond dealers told the MSRB in comment letters that the difficulties of determining reference prices and of building systems to identify them made the initial plan unworkable and could lead some of them to stop sales to retail investors.

The contraction from a full day to the two-hour limit aims to ensure that dealers are not taking unnecessary risk in warehousing bonds for which they deserve to be paid. The MSRB proposal notes that since dealers are already required to ensure that their mark-ups on trades from their inventory are fair and reasonable, they should already have systems for mark-up monitoring.

Unlike the original proposal, which would have required disclosure only on bond trades valued at $100,000 par amount or less, the revised one would apply to trades for all retail accounts.

In addition to substituting a mark-up for a reference price, the revised rule would require dealers to print the time of trade execution to the nearest minute so that customers could check the prevailing market price on systems such as the MSRB's EMMA database. Dealers also would have to print a hyperlink and URL address to the Security Details page for the customer's security on EMMA.

The mark-up would be the difference between the price to the customer and the market price, and would be required to be given as a total dollar amount and as a percentage of the principal amount of the customer trade.

While the MSRB noted that it prefers its revised rule to the original one, it will continue to take comments on the original proposal. All comments are due by Nov. 20, 2015.

Sep 25, 2015

(Reporting By Jed Horowitz; Editing by David Gregorio)

[NABL Submits Comments to SEC on MCDC Initiative.]

On September 21, 2015, NABL sent a letter to the SEC Chair and Commissioners concerning the Municipalities Continuing Disclosure Cooperation Initiative. NABL recommended that before the SEC engaged in any similar future initiative that it devise a better way to reach issuers and that any similar future initiative be subject to a cost-benefit analysis. NABL also set out a number of steps

that could be taken to further improve continuing disclosure. Many of those steps could be taken by working groups, but NABL also said that the SEC should provide guidance that issuers no longer need to file notices of ratings changes since those changes are now available on EMMA directly from the ratings agencies.

To read NABL's letter, please click here.

MSRB Reminds Regulated Entities of October 1, 2015 Implementation Date of Amendments to MSRB Rule A-12 on Registration Fees.

The Municipal Securities Rulemaking Board (MSRB) reminds brokers, dealers, municipal securities dealers and municipal advisors that amendments to MSRB Rule A-12 on initial and annual registration fees becomes operative October 1, 2015. Each regulated entity registering with the MSRB on or after October 1, 2015 shall pay to the Board an initial one-time fee of $1,000. Beginning October 1, 2015, each regulated entity shall pay $1,000 annually, based on the fiscal year of the Board, within 30 days of the invoice date.

Read the regulatory notice.

Muni Distressed Debt Firm Rosemawr Sues Over Revel Energy Bonds.

An investment firm focusing on high-yield and distressed municipal bonds sued the developer of a power plant that serves Atlantic City's shuttered Revel Casino for securities fraud.

Rosemawr Management LLC, a $1 billion fund started by Lehman Brothers Holdings Inc.'s former head of municipal-derivatives trading, alleged that ACR Energy Partners LLC concealed defaults and used almost all its assets to make improper dividend payments to its parent company. In March 2014, New York-based Rosemawr bought $35 million of bonds that financed the power plant at 92.25 cents on the dollar. The securities have since lost 70 percent of their value.

"Although it was public knowledge that the Revel facility was not performing as well as Revel had intended, there was no reason to believe that Revel was defaulting on its payment to ACR," Rosemawr said in the Sept. 16 suit, filed in federal court in Camden, New Jersey. "As a direct result of the fraudulent concealment of material information, plaintiffs purchased the bonds at artificially inflated prices."

Distressed Municipalities

Rosemawr was formed in 2008 by Greg Shlionsky, a former Lehman Brothers managing director. The firm, which bought bonds backed by revenue from Harrisburg, Pennsylvania's parking garages and has lent money to an assisted living facility in Georgia and a storm drain project in the Detroit area, also includes former Lehman municipal derivatives trader James Lister.

Greg Usry, Citigroup Inc.'s former co-head of municipal credit and financial products and Julie Morrone, who formerly managed Morgan Stanley's high yield muni funds, also work at Rosemawr, according to the firm's website.

Revel, which opened at a cost of $2.4 billion in 2012, was an attempt to bring a bit of Las Vegas to the east coast by offering more shows, restaurants and shopping. The property suffered from poor design and competition from new casinos in other states. It went bankrupt twice before closing in September 2014.

New Jersey's Economic Development Authority issued about $119 million of unrated tax-exempt and taxable municipal bonds in 2011 on behalf of ACR, which used the money to build a heating, cooling and electric plant for the Revel resort and casino.

Bond Covenants

Revel had a 20-year contract to buy power and other utility services from ACR, a joint venture between South Jersey Industries Inc. and DCO Energy LLC. Dan Lockwood, a spokesman for South Jersey Industries, didn't immediately return a call seeking comment. Frank DiCola, chairman of Mays Landing, New Jersey-based DCO also didn't return a message.

Two Rosemawr funds bought $35 million of the power plant bonds at 92.25 cents per $100 face amount in March 2014. ACR and its owners "flatly lied" about defaults under the bond covenants which, if disclosed, would have lowered the price of the securities, Rosemawr said.

ACR hid Revel's failure to make required monthly payments under the energy service agreement and entered into a "special arrangement" with the casino to extend payment terms without bondholder permission, Rosemawr said. ACR also didn't notify bondholders it failed to fully fund a required reserve account.

The account "provided crucial protection of bondholders' interests, because it provided a source of payments to bondholders until Revel became consistently profitable."

Dividend Payments

Finally, ACR made $11 million in improper and fraudulent divided payments to its sole controlling member, an entity set up by South Jersey Industries and DCO, according to the suit. Under the bond documents, dividends were restricted if there was an event of default, Rosemawr said.

The $11 million payments "represented substantially" all of ACR's liquid assets. ACR missed its June 15, 2014, debt service payment.

The offering statement for ACR's bonds warned investors that the shuttering of the Revel resort or an ownership transfer meant bondholders couldn't be assured energy produced by the plant was necessary or that new owners might get energy elsewhere.

Rosemawr said it believed financing wouldn't be jeopardized because Revel would need power, regardless of who purchased the building or its long-term use.

"Had the plaintiffs known the information that was fraudulently concealed by the defendants prior to the purchase of the bonds, the plaintiffs would either have not purchased the bonds altogether, avoiding any losses, or would have purchased the bonds only at a dramatically lower price, thereby significantly reducing their losses," Rosemawr's complaint said.

Bloomberg News

by Martin Z Braun

September 21, 2015 — 11:22 AM PDT

- NFMA Introduction to Municipal Bond Credit Analysis.
- SEC Urged to Disapprove Rule on MA Core Conduct.
- Neighborly Raises $5.5M from Joe Lonsdale's Formation 8, Ashton Kutcher to Transform the Municipal Debt Market.
- How Standard & Poor's Treats Public-Private Partnerships in U.S. State and Local Government Debt Analysis.
- SIFMA: Alternative Issue Price Method 'Not Workable' As Proposed.
- IRS Rules that No Abusive Arbitrage Device Was Used in Connection With Bond Issue: Tax Analysts
- NABL: TEB Announces VCAP Changes.
- *City of Seattle v. Department of Revenue* – Supreme Court of Oregon holds that cities' interest in electrical transmission capacity, purchased from electrical cooperative and used to transmit electricity over region's federally administered power grid, could be taxed by Department of Revenue as a property interest "held" by the cities.
- And finally, Yet Another Reminder of Why People Hate Lawyers is brought to us this week by *Parker v. Town of Erwin*, in which the court began its opinion thusly, "The evidence in the record tends to show that a Christmas parade was held in Erwin, North Carolina, on 5 December 2011." *"Tends to show?"* Were there cars driving down Main Street? Did one of those cars contain a fat man in a red suit? If yes, I tend to think that we can definitively conclude that a bleepin' Christmas parade was held. Please open your hymnals to page 25 and join us in singing, "We Tend to Wish You a Merry Christmas."

EMINENT DOMAIN - COLORADO

Regional Transportation District v. 750 West 48th Ave., LLC

Supreme Court of Colorado - September 14, 2015 - P.3d - 2015 WL 5315555 - 2015 CO 57

Regional Transportation District filed a petition in condemnation and acquired from landowner property for a light rail project. The District Court appointed a commission of freeholders to determine property's reasonable value. Property owner appealed pretrial and instructional rulings by trial court and certain evidentiary rulings of commission, and the Court of Appeals affirmed. Property owner petitioned for certiorari review, which was granted.

The Supreme Court of Colorado held that:

- Supervising judge's explicit denial of motion to exclude expert witness testimony on relevance grounds precluded commission from sustaining relevance objection at hearing and deeming the evidence inadmissible, and
- Supervising judge had power to instruct commission at end of hearing to disregard certain evidence which the commission had deemed relevant and admissible during the hearing.

Although a condemnation compensation commission may rule on evidence if the judge has not already done so, when a judge issues a definitive ruling on the admissibility of evidence, either on a motion or through instructions, the commission is bound to follow the judge's ruling.

Supervising judge's explicit denial, on relevance grounds, of property owner's motion in condemnation compensation proceeding to exclude expert witness testimony regarding the alternate average-value and income-based approaches to industrial property valuation precluded commission of freeholders from sustaining property owner's relevance objection at hearing and deeming the evidence inadmissible absent any request that the judge revisit her previous in limine ruling.

INVERSE CONDEMNATION - FLORIDA

Caribbean Condominium v. City of Flagler Beach

District Court of Appeal of Florida, Fifth District. - September 18, 2015 - So.3d - 2015 WL 5456819

In February 2010, Appellants filed suit against the City seeking relief under the Bert Harris Act. Appellants subsequently amended their complaint to include claims for inverse condemnation. In March 2012, the City filed a motion for summary judgment as to all claims. The City's motion was granted only as to the Bert Harris Act claims. The case proceeded to a non-jury trial on the inverse condemnation claims where the trial court ultimately entered judgment in favor of the City after determining that there had been no taking of Appellants' property. The trial court's judgment was affirmed in all respects.

While the appeal was pending, the City filed its motion for attorney's fees and costs. The trial court properly awarded the City attorney's fees for time expended in successfully defending Appellants' claims under the Bert Harris Act. The trial court further awarded the City its legal costs incurred from the inception of the lawsuit through May 18, 2012 — the date on which the trial court advised the parties of its intent to enter summary judgment on the Bert Harris Act claims. However, the trial court declined to award costs subsequently incurred by the City based on its conclusion that a governmental entity is not entitled to recover costs in an inverse condemnation action even where it is the prevailing party.

The District Court of Appeal affirmed the trial court's award of attorney's fees to the City. However, it found merit to the City's cross-appeal. Because the City was the prevailing party on Appellants' inverse condemnation claims, the court concluded that it was entitled to recover costs pursuant to section 57.041, Florida Statutes (2010).

District Court of Appeal holds that a governmental entity is entitled to recover costs in an inverse condemnation action where it is the prevailing party.

ZONING - LOUISIANA

Holy Cross Neighborhood Ass'n v. City of New Orleans

Court of Appeal of Louisiana, Fourth Circuit - September 9, 2015 - So.3d - 2015 WL 5272381 - 2014-1317 (La.App. 4 Cir. 9/9/15)

Neighborhood association and three individual neighbors brought action against city, city council, developer, and property seeking declaratory and injunctive relief related to city ordinance regarding proposed development of property. The Civil District Court granted preliminary injunction declaring ordinance ineffective. Intervening property owner appealed.

The Court of Appeal held that ruling on ineffectiveness of ordinance was beyond scope of

preliminary injunction proceeding.

Court's declaration of the ordinance's ineffectiveness was in effect a ruling on the merits of the property owners' petition for declaratory relief, and there was nothing in the record to suggest that the parties agreed to try the declaratory action at the hearing on the preliminary injunction.

ZONING - MASSACHUSETTS

Reynolds v. Zoning Bd. of Appeals of Stow

Appeals Court of Massachusetts, Middlesex - September 15, 2015 - N.E.3d - 2015 WL 5330370

Neighbor appealed issuance of comprehensive permit for construction of a low and moderate income elderly housing project. The Superior Court affirmed. Neighbor appealed.

The Appeals Court held that:

- Neighbor had standing to challenge the permit, and
- Waiver of the bylaw provision limiting the flow into waste disposal systems was unreasonable.

Neighbor, who presented expert testimony that well for proposed low and moderate income elderly housing project would have elevated nitrogen levels, had standing under "anti-snob zoning act" to challenge issuance of comprehensive permit for the project, even though the judge ultimately rejected the evidence, where judge's ultimate finding that the nitrogen would not reach the neighbor's well went to neighbor's success on the merits, and not his ability to challenge the acts of the zoning board of appeals.

Abutters have the benefit of a presumption of aggrievement, as would allow them to appeal waiver of local requirements and regulations pursuant to "anti-snob zoning act" regarding an affordable housing development, but if challenged by evidence warranting a contrary finding, the plaintiff must prove standing by introducing credible evidence of an injury special and different from the concerns of the rest of the community.

Waiver by zoning board of appeals of the bylaw provision limiting the flow into waste disposal systems within town's water resource protection district was unreasonable for proposed low and moderate income elderly housing project, and thus issuance of comprehensive permit for project was unwarranted, even though there was a local need for additional affordable housing, where it was more likely than not that the project would cause excessive nitrogen levels at neighboring well, and it was unreasonable to conclude that the local need for affordable housing outweighed neighbor's health concerns.

ASSESSMENTS - MINNESOTA

First Baptist Church of St. Paul v. City of St. Paul

Court of Appeals of Minnesota - August 31, 2015 - Not Reported in N.W.2d - 2015 WL 5089063

First Baptist Church of St. Paul and Church of St. Mary (the churches) challenged the 2011 right-o--way maintenance (ROW) assessment levied by respondent City of St. Paul (the city). The city

maintains all of the streets and sidewalks within the city limits and uses an annual ROW assessment to recoup the costs related to street maintenance. The amount the city assesses each property depends on the property location, size, street material, and services provided.

The churches challenged the district court's grant of summary judgment to the city, arguing that the city's right-of-way maintenance assessment (1) is a tax, (2) does not meet the special-benefit standard, (3) is improperly based on estimated costs, (4) fails to comply with respondent's charter and policies, and (5) is arbitrary and capricious.

The Court of Appeals affirmed, concluding that the assessment is a regulatory service fee, not a tax.

INSURANCE - MINNESOTA

American Family Ins. v. City of Minneapolis

United States District Court, D. Minnesota - September 8, 2015 - F.Supp.3d - 2015 WL 5228287

A water-main break occurred on October 20, 2013 in the City of Minneapolis, causing water to flow into a condominium building resulting in significant damage.

The City settled fourteen claims for losses that were not covered by insurance. The City paid these claims without requiring any evidence that the water main broke as a result of the City's negligence. The claims denied by the City were each submitted by insurance companies.

The insurance companies (Plaintiffs) sued the City, asserting claims for negligence, trespass, takings, and violation of the Equal Protection Clause.

Plaintiffs alleged that the City violated the Equal Protection Clause by agreeing to reimburse certain residents of the Sexton Condominiums for their uninsured losses while refusing to reimburse Plaintiffs. The City argued that it was entitled to summary judgment because there was no evidence in the record that the City treated Plaintiffs, as corporations, differently than it treated individuals. Rather, the City asserted, it made settlement decisions based on the nature of the loss—i.e., insured versus uninsured—rather than the type of person who made the claim.

The District Court found no Equal Protection violation by the City.

MUNICIPAL ORDINANCE - NEW JERSEY

Redd v. Bowman

Supreme Court of New Jersey - August 11, 2015 - A.3d - 2015 WL 4726557

Mayor and city council president brought action to declare invalid a petition submitted by city voters for adoption of proposed ordinance that would prohibit city from disbanding its municipal police department and joining newly-formed county police force.

The Superior Court ruled that proposed ordinance created undue restraint on future exercise of municipal legislative power. Voters appealed. The Superior Court, Appellate Division, reversed and remanded. Mayor and council president filed petition for certification, and voters filed cross-petition for certification, which were granted.

The Supreme Court of New Jersey held that:

- Appeal was not moot;
- Proposed ordinance did not constitute improper divestment of municipal governing body's legislative power;
- Proposed ordinance was not invalid by virtue of preemption; and
- Proposed ordinance was prohibited from being submitted to voters.

Appeal from determination that city voters' petition-initiated proposed ordinance that would have prohibited city from disbanding its municipal police department and joining newly-formed county police force did not constitute improper divestment of municipal governing body's legislative power was not moot in action brought by mayor and city council president to declare petition invalid, even though city had already disbanded its police force and contracted to receive its police services from county. Action was not direct action seeking to enjoin dissolution of municipal department and creation of county-wide police force, but rather question raised by parties was whether proposed ordinance was valid, which was justiciable issue to be resolved by court, and it was still possible to grant or deny remedy sought by mayor and council president.

City voters' petition-initiated proposed ordinance to prohibit city from disbanding its municipal police department and joining newly-formed county police force did not constitute improper divestment of municipal governing body's legislative power. Legislature authorized divestment, for prescribed period, of one aspect of succeeding governing body's authority when ordinance was enacted by initiative in accordance with statute governing petitions for proposed ordinances.

Local Budget Law (LBL), which required local municipalities to enact balanced budget every fiscal year, did not preempt properly-framed petition-initiated proposed ordinance under Faulkner Act to prohibit city from disbanding its municipal police department and joining newly-formed county police force. LBL imposed on municipalities detailed requirements with respect to process of enacting a municipal budget, but contained no evidence that legislature intended to preempt proposed ordinance at issue.

Special Municipal Aid Act (SMAA) and Transitional Aid to Localities program (TAL), pursuant to which city's transition from municipal to county police services were in part conducted, did not preempt properly-framed petition-initiated proposed ordinance under Faulkner Act to prohibit city from disbanding its municipal police department and joining newly-formed county police force. Although there was potential for dire fiscal consequences to result from municipality's failure to comply with state directives authorized by legislature under SMAA and TAL, neither statute barred municipality from enacting ordinances by initiative or referendum that contravened condition imposed be state.

Municipal Rehabilitation and Economic Recovery Act (MRERA), pursuant to which city's transition from municipal to county police services was in part conducted, did not preempt proposed ordinance, initiated by city voters under Faulkner Act, to prohibit city from disbanding its municipal police department and joining newly-formed county police force. Although it was possible that ordinance, however enacted, that undermined agreement reached by city pursuant to MRERA would prompt state to withhold municipal aid under MRERA, there was nothing in MRERA that expressed legislative intent to preempt Faulkner Act process, but instead, MRERA reaffirmed city's status as Faulkner Act municipality, and by inference, initiative and referendum procedure at Faulkner Act's core.

Police force statute did not preempt petition for proposed ordinance, initiated under Faulkner Act, to prohibit city from disbanding its municipal police department and joining newly-formed county

police force, since there was no legislative intent in statute to preempt police reorganization and there was noting in statute that precluded voter initiative and referendum procedures set forth in Act.

Proposed ordinance, initiated by city voters under Faulkner Act, to prohibit city from disbanding its municipal police department and joining newly-formed county police force was prohibited from being submitted to voters, since ordinance was out of date, inaccurate, and misleading. City had already disbanded its police force and contracted to receive its police services from county, voters who signed petition did so at time when police reorganization was in planning stage, and nothing suggested that those voters would have supported petition after city police force was disbanded, such that submission of ordinance to voters would have undermined objectives of Act.

BANKS - NEW YORK

New York Bankers Ass'n, Inc. v. City of New York

United States District Court, S.D. New York - August 7, 2015 - F.Supp.3d - 2015 WL 4726880

Association of commercial banks and federal savings associations brought action against city, alleging that city's Responsible Banking Act (RBA), which, inter alia, ranked and published information about banks with respect to certain criteria, including lending to low-income communities, was preempted by federal and state law. Association moved for summary judgment and city moved to dismiss for failure to state claim.

The District Court held that:

- RBA had regulatory, rather than proprietary, purpose;
- RBA conflicted with federal law; and
- Preempted provisions were not severable.

City's Responsible Banking Act (RBA) had regulatory, rather than proprietary, purpose, as required for RBA to be subject to federal preemption. RBA's stated purpose was to assess credit, financial, and banking services needs throughout city with particular emphasis on low and moderate income individuals and communities, legislators who sponsored RBA spoke about how federal and state laws were ineffectual in terms of both the collection of information and the influence over bank conduct regarding community reinvestment in city, RBA contained express procedures for adjudging, ranking, and publishing banks' efforts to comply with RBA's subjective criteria, RBA did not place conditions on deposits or transactions that city made as bank customer, city would not gain any discernible financial benefits from RBA, and RBA authorized city's Banking Commission to consider its rankings of banks when designating or de-designating banks that could hold city funds.

City's Responsible Banking Act (RBA), which regulated banks, conflicted with federal law, and thus was preempted. National Bank Act (NBA) stated that no national bank could be subject to any visitorial powers except as authorized by federal law, RBA authorized data and information collection from banks, and banks could be subject to de-designation as bank that could hold city funds if it declined to provide information to city or if it did not meet RBA's criteria, including benchmarks for lending to low-income communities that were more burdensome than those under federal Community Reinvestment Act (CRA).

Under New York law, city council would not have enacted Responsible Banking Act (RBA) without

provisions that were preempted by federal and state law, and thus preempted provisions were not severable. Provisions were subject of serious legislative debate concerning possibility of preemption, mayor initially vetoed RBA due to preemption concerns, council overrode mayor's veto and passed RBA as originally intended, RBA cost city more than $500,000 per year, and removal of preempted provisions would eliminate RBA's power to encourage certain behavior on part of banks, including lending to low-income communities.

EMINENT DOMAIN - NEW YORK

Incorporated Village of Westbury v. IACO Realty, Inc.

Supreme Court, Appellate Division, Second Department, New York - September 16, 2015 - N.Y.S.3d - 2015 WL 5436899 - 2015 N.Y. Slip Op. 06820

Village brought a condemnation proceeding, and bank, a nonparty, moved to enforce an equitable lien against the village and to hold the village jointly and severally liable for damages for the wrongful payment of condemnation proceeds. The Supreme Court, Nassau County, denied the motion, and bank appealed.

The Supreme Court, Appellate Division, held that:

- Notice of claim requirements of the General Municipal Law applied to bank's claims, and
- Claim accrued for limitations purposes on the date the condemnation proceeds were paid.

Bank's claims against village premised on the wrongful payment of condemnation proceeds sounded in tort, as required for the notice of claim requirements of the General Municipal Law to apply.

Doctrine of equitable estoppel did not apply so as to preclude the statute of limitations defense in bank's action against village premised upon the wrongful payment of condemnation proceeds, where bank did not allege any separate and subsequent act of wrongdoing that prevented it from timely bringing suit.

IMMUNITY - NORTH CAROLINA

Parker v. Town of Erwin

Court of Appeals of North Carolina - September 15, 2015 - S.E.2d - 2015 WL 5331924

Parents of almost four-year old pedestrian, who was killed in automobile accident after a parade, brought action individually and as administrator of pedestrian's estate against town and some of its employees in their official and individual capacities, chamber of commerce, landowners, and various emergency medical service providers for negligence and negligent infliction of emotional distress. The Superior Court denied town's motion to dismiss and granted motion to dismiss owner of the building located immediately adjacent to the site of the incident. Town and employees appealed, and parents cross-appealed.

The Court of Appeals held that:

- Trial judge was responsible to weigh evidence in determining if court had personal jurisdiction;
- Competent evidence supported trial court's determination that town did not waive sovereign immunity through the purchase of its insurance policy;

- Town had sovereign immunity from parents' claims with regard to services recognized as governmental functions;
- Remand was required for findings reflecting determination of the weight and sufficiency of evidence on sovereign immunity; and
- Parents failed to sufficiently allege that landowner breached duty to illuminate alley.

Competent evidence supported trial court's determination on ruling on motion to dismiss for lack of personal jurisdiction that town did not waive sovereign immunity through the purchase of its insurance policy. Evidence established that policy contained an express non-waiver of sovereign immunity endorsement.

A municipality's sovereign immunity is waived by the purchase of liability insurance only to the extent that the municipality is indemnified by the insurance contract from liability for the acts alleged; thus, a governmental entity does not waive sovereign immunity if the action brought against it is excluded from coverage under its insurance policy.

Remand was required in negligence action by minor pedestrian's parents against town for findings reflecting trial court's determination of the weight and sufficiency of evidence, and to determine whether parents established that alleged violations of statute requiring town to keep streets and alleys free from obstructions and gave it the power to close streets directly proximately caused driver to strike pedestrian such that dismissal of action against town on the basis of sovereign immunity was warranted, where trial court's order indicated that it considered evidence beyond allegations in parents' complaint.

The extent to which particular municipal streets and roads are kept open for use by members of the public is a governmental function such that governmental immunity is available to municipalities as a defense to damage claims arising from such discretionary road closure decisions.

MUNICIPAL ORDINANCE - OHIO

State ex rel. Szymanowski v. Grahl

Supreme Court of Ohio - September 11, 2015 - N.E.3d - 2015 WL 5448549 - 2015 -Ohio-3699

Relators filed action for a writ of mandamus to compel city auditor to transmit referendum petition and certified copy of ordinance regarding removal of dam that was the subject of the petition to the county board of elections. The Court of Appeals denied writ. Relators appealed.

The Supreme Court of Ohio held that auditor was required to transmit petition and ordinance to board.

City council ordinance authorizing mayor to proceed with process of removing dam was "first" ordinance necessary for removal of dam, and thus city auditor was required to transmit referendum petition and certified copy of ordinance to county board of elections under statute providing that statutory provisions governing initiatives and referenda applied to "first" ordinance necessary to make and pay for any public improvement, even though city had passed prior ordinances calling for removal of dam. City's authorization to remove dam under one ordinance had expired, thus requiring

new authorization restarting opportunity to pursue referendum, and other ordinances indicated city was not committed to the project and would not have called for vote on question of whether to remove dam.

BALLOT INITIATIVES - OHIO

State ex rel. Walker v. Husted

Supreme Court of Ohio - September 16, 2015 - N.E.3d - 2015 WL 5448584 - 2015 -Ohio-3749

Relators sought writ of mandamus to compel Secretary of State to reverse his decision sustaining protests against counties' petitions to adopt charters and compel placement of charter measures on ballots.

The Supreme Court of Ohio held that:

- Secretary lacked authority to invalidate petitions based on his own determination that measures were unconstitutional, if enacted;
- Secretary acted within his discretion in determining that petitions were invalid on ground that they failed to set forth form of government; and
- Relators' affidavits failed to comply with requirement that they be made on personal knowledge.

Secretary of State lacked authority to invalidate proposed county charter petitions based on his own assessment that measures, if enacted, unconstitutionally interfered with State's exclusive authority to regulate oil and gas operations by effectively banning high-volume hydraulic fracking as method of oil and gas extraction, and in some cases prohibiting new gas or oil exploration or extraction.

Secretary of State acted within his discretion when he determined that proposed county charter petitions were invalid on ground that they did not set forth the form of government. Although purporting to maintain the status quo on matters of county offices, officers, and their duties, and manner of election, proposed charters did not provide the form of government of the county or determine which of its officers would be elected and the manner of their election, thus requiring reference to sources outside the proposed charters to determine the form of government they purported to establish.

Affidavits by relators that were all made "to the best of my knowledge, information, and belief" were insufficient to comply with requirement that affidavits in original actions must be made on personal knowledge, in mandamus action seeking to compel Secretary of State to reverse decision sustaining protests to proposed county charter petitions and compel placement of charter measures on ballots.

UTILITIES - OHIO

Northeast Ohio Regional Sewer Dist. v. Bath Twp.

Supreme Court of Ohio - September 15, 2015 - N.E.3d - 2015 WL 5448303 - 2015 -Ohio-3705

Regional sewer district brought action against member communities, seeking declaratory judgment that district had authority to implement particular regional stormwater management (RSM) program. Property owners intervened. The Court of Common Pleas denied motion to dismiss,

granted partial summary judgment to sewer district and, after bench trial, entered judgment in favor of district. Communities and property owners appealed. The Court of Appeals affirmed in part and reversed in part. Sewer district appealed.

The Supreme Court of Ohio held that:

- District was authorized to implement the RSM, and
- District had authority to charge fees to landowners to fund it.

Charter governing regional sewer district specifically authorized it to implement a regional stormwater management program, where charter stated, "The District will plan, finance, construct, operate and control waste water treatment and disposal facilities, major interceptor sewers, all sewer regulator systems and devices, weirs, retaining basins, storm water handling facilities, and all other water pollution control facilities of the District."

Regional sewer district had statutory authority to charge fees to landowners to pay for regional stormwater management (RSM) program that it was authorized to implement. Governing statute provided that a regional water and sewer district may charge for the use or services of any water resource project, and statutory definition of water resource project included a facility that was "to be acquired, constructed, or operated" by the sewer district.

Broad language of regional sewer district's charter, which provided that "any projects not financed through the Ohio Water Development Authority would be financed in such a manner as may be deemed appropriate by the Board of Trustees," encompassed the assessing of fees to pay for a stormwater management system, and thus fees charged to landowners to fund district's stormwater management program were authorized by the charter.

UTILITIES - OHIO

In re Application to Modify, in Accordance with R.C. 4929.08, the Exemption Granted to E. Ohio Gas Co.

Supreme Court of Ohio - September 8, 2015 - N.E.3d - 2015 WL 5255264 - 2015 -Ohio-3627

Objectors appealed determination of the Public Utilities Commission modifying order exempting natural-gas utility from traditional commodity-sales service regulations.

The Supreme Court of Ohio held that:

- Commission did not ignore or rewrite prior exemption order;
- Utility's filing of motion to modify rather than separate application did not require reversal;
- Record supported Commission's determination that findings from exemption order were no longer valid;
- Commission's decision to modify exemption order was not against manifest weight of the evidence;
- Deference to Commission's findings was warranted; and
- Commission properly adopted stipulation.

ZONING - PENNSYLVANIA

Gorsline v. Board of Supervisors of Fairfield Tp.

Commonwealth Court of Pennsylvania - September 14, 2015 - A.3d - 2015 WL 5313639

Neighboring landowners sought review of decision of township board of supervisors granting application of limited liability company (LLC) for conditional use permit to locate natural gas well on land it leased from individuals. The Court of Common Pleas reversed. LLC and individuals appealed.

The Commonwealth Court held that:

- Proposed conditional use met threshold requirements set forth in township's zoning ordinance, and
- Evidence showed that well would not present detriment to health and safety of neighborhood.

Proposed conditional use, to locate natural gas well on land it leased from individuals, of limited liability company (LLC) that sought application for conditional use permit, met threshold requirements set forth in township's zoning ordinance. Ordinance permitted wide range of conditional uses in residential agriculture district, where land was located, proposed well would have presented low physical profile, would have involved small footprint on land, and was similar to public service facility, which was expressly allowed in district, and well would not have conflicted with general purpose of ordinance, which expressly authorized extraction of minerals.

Evidence showed that proposed natural gas well of limited liability company (LLC) would not present detriment to health and safety of neighborhood, in context of LLC's application for conditional use permit to locate well on land it leased from individuals. LLC's oil and gas engineering expert testified that, once well was constructed and drilling was completed, its operation would not create noise, light glare, or odors noticeable to township residents and that well would be drilled far below subsurface water that served neighboring landowners' wells, and township board of supervisors, in granting permit, responded to concerns of landowners by imposing numerous conditions related to roadway maintenance, traffic, and parking and by requiring LLC to provide emergency contact information upon request, to visually screen well from neighborhood, and to comply with all federal, state, and local permits and approvals.

MSRB: Consider the Risks and Opportunities of Interest Rate Movement.

Although interest rates are staying steady for now, the Municipal Securities Rulemaking Board (MSRB) reminds investors to consider the effects of interest rate movement on the price of municipal bonds.

Read about the risks and opportunities in the MSRB's new investor resource on the impact of market interest rate movement on municipal bond prices and yields.

SIFMA: Alternative Issue Price Method 'Not Workable' As Proposed.

WASHINGTON – The Internal Revenue Service's alternative method for determining issue price is "not workable," though the overall issue price rules proposed in June are a "significant improvement" over those floated in 2013, the Securities Industry and Financial Markets Association told the IRS.

SIFMA made the comments and recommended how the proposed rules can be improved in a comment letter sent to the IRS on Thursday.

“We believe that the 2015 proposed regulations are a significant step forward and with certain clarifications and modifications, can establish a regulatory structure that will impede neither the efficient and aggressive marketing of new issues nor enforcement of the limitations mandated by Congress,” SIFMA wrote in the letter, signed by managing director Michael Decker.

The general rule in the 2015 proposal is that the issue price of a maturity is the first price at which 10% is sold to the public. The public would be anyone other than the underwriters or a related party, with underwriters defined as the underwriting syndicate and anyone who enters into a contract or other arrangement to sell the bonds with any of the syndicate members.

If 10% of a maturity hasn’t been sold by the sale date, an issuer could use the alternative method to determine issue price. Under this method, the issuer could use the initial offering price as the issue price for bonds sold to the public as of the sale date as long as certain conditions are met.

One condition is that underwriters fill all orders placed by the public and received by the underwriter on or before the sale date at the initial offering price. Another is that the lead or sole underwriter certifies that no underwriter will fill an order from the public after the sale date, and before the issue date, at a higher price than the initial offering price unless the market moves after the sale date.

The 2015 proposal is markedly better than rules proposed in 2013 and then withdrawn because it provides an alternative way to establish issue price when there are unsold maturities as of the sale date, SIFMA wrote. But because of ambiguities and constraints, the alternative method, as proposed, “does not provide a workable alternative for establishing issue price, principally due to the requirement that lead underwriters certify as to the actions of others,” it added.

Lead underwriters can’t certify about actions that haven’t happened yet, and the lead underwriters can’t certify that the syndicate members actually won’t sell the bonds at a higher price during that period. Instead, SIFMA is recommending that under the alternative method, lead underwriters certify that all members of the syndicate have agreed in the agreement among underwriters or a related document to not sell bonds at a price higher than the initial offering price between the sale date and the closing date unless the market moves.

SIFMA also argued that it would be “exceedingly difficult” for the market change exception to be implemented, since there’s no effective way to demonstrate market movement. “Price indicators, such as the Thomson Reuters Municipal Market Data (MMD) AAA Curve, are not traded actively on a two-way basis and do not necessarily reflect actual sales, intraday market movement, or the localized nature of the tax-exempt market,” the group wrote.

Decker told The Bond Buyer that there’s no good way to clarify market movement, so SIFMA asked Treasury and the IRS to make clarifications about the period between the sale and the issue dates under the alternative method.

The group also wants Treasury and the IRS to clarify that underwriters are only restricted from selling bonds above the initial offering price during this period until 10% of the maturity is sold. SIFMA also wants the agencies to clarify that underwriters can fill orders at prices lower than the initial offering price during the period between the sale date and the closing date. Sales during this period should only establish the issue price under the general rule at a price lower than the initial offering price at the option of the issuer, SIFMA wrote.

SIFMA also had several suggestions for improvements to facilitate the application of the general rule.

One recommendation is for there to be a special rule for competitively bid and sealed bid offerings. It is common for bidders in these types of transactions to submit bids with little-to-no premarketing, and as a result, it is likely that many will not meet the 10% threshold on the sale date, SIFMA wrote.

For competitive and sealed bid transactions, SIFMA would like issuers to be able to treat the offering price specified in the winning bid as the issue price, without the restrictions on sales occurring between the sale date and the issue date that are set forth in the alternative method.

Other suggestions pertain to the definition of the public and the underwriter. SIFMA would like the agencies to include a provision similar to one in the 2013 proposal that would count as a sale to the public a sale to anyone, including an underwriter, who holds the bonds for investment and not for redistribution. SIFMA would also like Treasury and the IRS to clarify what is meant by an arrangement with an issuer to sell bonds, other than a contract, that would cause someone to be treated as an underwriter.

Additionally, SIFMA would like Treasury and the IRS to clarify the meaning of "the first price" at which 10% of the bonds are sold to the public.

THE BOND BUYER

BY NAOMI JAGODA

SEP 18, 2015 4:24pm ET

Should High-Risk Speculators in Puerto Rico Bonds Have a Seat at the Restructuring Table?

Summary

- Puerto Rico announced a five-year bond restructuring proposal.
- Bondholders will be forced to make concessions.
- U.S. House Democrats claim it's "unjust" for speculators to have restructuring input.

Puerto Rico last week said it had laid out a five-year plan for broadly restructuring its mammoth debt.

A significant question facing the politicians and bankers in charge of the debt reorganization is whether hedge fund investors, who recently bought the highly speculative bonds, should be treated the same as mom-and-pop retail investors. Those investors believed that they were investing in long term, safe and secure municipal bonds that their financial advisors at UBS (NYSE:UBS) and other firms recommended.

First, the plan.

> "The new plan calls for restructuring about $47 billion of Puerto Rico's $72 billion in bond debt and carrying out an ambitious package of economic changes under the eyes of an independent financial control board," reported Mary Williams Walsh of the New York

> Times. “Virtually every element of the plan requires either concessions negotiated from creditors or legislation enacted in San Juan or Washington, suggesting a long and difficult road ahead.”
>
> “Among the most striking aspects of the plan – and likely to be one of the most contentious – is the proposal to restructure Puerto Rico’s general obligation bonds, which were sold to investors with an explicit constitutional promise that timely repayment would take priority over all other expenditures on the island,” according to the Times report.
>
> “For decades, general obligation bonds have been marketed as virtually default-proof, and a major restructuring of them now by Puerto Rico would raise unwelcome questions about the credibility of the time-honored “full faith and credit” pledge that stands behind such bonds,” according to the Times. “Puerto Rico is not proposing to walk away from its bonds completely, but to pay its investors less.”

Remember, Puerto Rico defaulted for the first time in August when it paid just $628,000 of $58 million due from one of its agencies. Unlike U.S. municipalities, Puerto Rico cannot seek federal bankruptcy protection.

The five-year restructuring plan will entail significant concessions from bondholders and will likely spawn much litigation over general obligation bond guarantees, according to the Times.

It’s a dire situation. Puerto Rico and its agencies only have $5 billion to repay $18 billion of principal and interest over the next five years.

How will investors fare under the plan? That is one of the key questions raised by a policy paper called “Profit at Any Cost” prepared recently by U.S. House Democrats. The paper argues that it is “unjust and unrealistic” for hedge fund managers and other institutional investors to demand full repayment on what they knew to be junk bonds, according to an article by Billy House of Bloomberg.

The policy paper criticizes these investors’ opposition to proposed legislation that would allow Puerto Rico to file for Chapter 9 bankruptcy to restructure its $70 billion debt that the governor claimed could not be paid.

According to Bloomberg, the policy paper states that hedge fund managers are “now pushing teacher layoffs, pension cuts and other quality-of-life reductions for Puerto Ricans as the ‘solution’ to the crisis in a self-serving attempt to enlarge their profits.”

It seems clear that Puerto Rico bonds are heading for a massive default or restructuring that will result in pain for bondholders. While Puerto Rico is a mess and blood will flow, it seems unfair to treat all investors the same here.

We agree with the policy paper. All investors are not created equal. The little guy who bought Puerto Rico bonds as long-term investments deserves fair treatment while the institutions, hedge funds and other such big boys should take a seat at the back of the room during these negotiations.

Zamansky LLC are securities and investment fraud attorneys representing investors in federal and state litigation against financial institutions. For more information about Zamansky LLC, please visit here.

Additional Disclosure: Zamansky LLC represents investors in arbitration cases against UBS regarding Puerto Rico bonds and UBS closed end bond funds, Lehman structured products and other investments.

Jake Zamansky, Zamansky LLC

Sep. 16, 2015 6:27 PM ET

Posted on Seeking Alpha

IRS Rules that No Abusive Arbitrage Device Was Used in Connection With Bond Issue: Tax Analysts

In technical advice, the IRS concluded that no abusive arbitrage device was used in connection with bonds used to refund in advance a portion of the issuer's outstanding indebtedness.

Under section 148, the tax exemption for interest on state and local bonds does not apply to any arbitrage bond. Reg. section 1.148-10(a)(1) provides that bonds of an issue are arbitrage bonds if an abusive arbitrage device is used in connection with the issue.

The IRS found no evidence to indicate that any action was taken by the issuer to enable it to exploit the difference between tax-exempt and taxable interest rates to obtain a material financial advantage. Therefore, the IRS determined that no abusive arbitrage device was used in connection with the issue.

The IRS also concluded that neither the reserve portion nor the current portion of the bonds constitutes excess gross proceeds under reg. section 1.148-10(c)(2) because both are replacement proceeds in sinking funds for the refunding issue. Lastly, the IRS determined that the bonds were not an advance refunding in which a device was employed to obtain a material financial advantage apart from savings attributable to lower interest rates.

Summary by Tax Analysts®

Continue reading (subscription required).

Citations: TAM 201538013

SEPTEMBER 30, 2014

SEC Approves Stripping Credit Rating References from MMF Rule.

WASHINGTON – The Securities and Exchange Commission adopted amendments to its money market fund rule that would remove credit ratings references funds use to comply with the rule — an action many market participants applauded but others said could pose risks.

The approved late Wednesday of changes to Rule 2a-7 and Form N-MFP, which MMFs use to provide updates to the SEC, follow a Dodd-Frank Act mandate for federal agencies to review their policies and remove "any reference to, or requirement of, reliance on credit ratings" and substitute the requirements with a "standard of credit-worthiness as each respective agency shall determine as appropriate for such regulations."

The amendments will become effective 30 days after they are published in the Federal Register but

funds won't need to comply with them until as Oct. 14, 2016. MMFs previously could only invest in securities that were in one of the two highest short-term credit ratings, or, if they were not rated, in securities that were of comparable quality. Of the total number of securities in the fund, 97% had to be rated in the highest short-term category.

The amendments change the requirements to allow funds to invest in securities that present "minimal credit risks." The SEC said a fund's board should consider the following factors when determining if a security has minimal credit risks: financial condition; sources of liquidity; ability to react to future market-wide and issuer or guarantor-specific events, including ability to repay debt in a highly adverse situation; the strength of the issuer or guarantor's industry within the economy and relative to economic trends; and issuer or guarantor's competitive position within its industry.

The SEC removed credit rating references from several of its rules in 2011 to comply with the mandate, but decided to re-propose the more controversial MMF amendments in 2014 to solicit more comments. While the majority of the comments were supportive of the commission's proposed change, there were some concerns that Dodd-Frank was forcing the SEC to trade objective portions of the rule for more subjective ones.

Jane Heinrichs, Investment Company Institute associate general counsel, said ICI is still reviewing the changes but that the revised rule "retains a similar degree of high credit quality standards."

An industry source familiar with the SEC's work on the amendments said the changes will have little effect because asset managers will not alter the way they manage the funds despite the removal of reliance on credit ratings.

Asset managers "are going to manage [an MMF] today the same way they managed it a year ago, and two years ago," said the source, who did not want to be named. "The truth is that asset managers have their own systems of reviewing credit analysis and the way in which they manage these funds."

Stephen Austin, a spokesperson for Fidelity Investments, said the company welcomes the final rules and echoed the industry source in saying the company's MMFs already do not rely on credit rating agencies to make risk determinations but instead depend on "an experienced research team to analyze the credit-worthiness of each issuer or security purchased by the funds" the company manages.

But Robert Plaze, a partner at Stroock & Stroock & Lavan, said the rule change gives managers an option that they did not have before. He said maintenance of the status quo "may very well happen," but noted, "There may be some funds out there who decide to attempt to reach for yield by investing a greater percentage of their assets in second-tier securities, which had heretofore been prohibited."

He also said the SEC staff may find it harder to enforce the rules now that they are more subjective.

THE BOND BUYER

BY JACK CASEY

SEP 17, 2015 3:11pm ET

S&P: U.S. Public-Private Partnerships Encounter New Road Bumps as Political Appetite For The Projects Waxes And Wanes

After more than a year of positive momentum in public-private partnerships (P3) for U.S. infrastructure projects, shifting political winds are disrupting some plans for P3s, even as it becomes clearer that increased spending is needed to build and repair the country’s roads, bridges, and tunnels. Only a handful of states have used P3s in a significant way, with lawmakers in many states becoming wary of entering into such long-term contractual arrangements to finance, build, operate, and maintain infrastructure assets. In many cases, decision-makers are focused on short-term benefits–such as lower initial borrowing costs associated with tax-exempt financing and the traditional design-bid-build procurement route than the P3 route that has, particularly for larger, complex deals, the longer-term benefits of transferring performance…

The full report is available for purchase here.

Sep. 9, 2015

NABL: IRS Updates Sequestration Effects for FY 2016.

The Internal Revenue Service announced the FY 2016 updates on the effects of sequestration on State & Local Government Filers of Form 8038-CP. According to the IRS, refund payments processed on or after October 1, 2015 and on or before September 30, 2016 will be reduced by the fiscal year 2016 sequestration rate of 6.8 percent, unless a law is enacted that cancels or otherwise impacts the sequestration.

A press release from the IRS with more information can be seen here.

NABL: TEB Announces VCAP Changes.

The Internal Revenue Service Tax Exempt Bonds office (TEB) announced several changes to its tax-exempt bonds Voluntary Closing Agreement Program. The changes were announced during a September 3, 2015, webinar hosted by Karen Skinder, Acting TEB Program Manager for Compliance and Program Management.

The changes will be reflected in revised IRM sections 7.2.3 and 4.81.6, both of which will be published soon, according to the IRS. The changes include no longer providing relief for post-issuance compliance procedures (effective 6 months after publication in the IRM) and template agreements for certain violations.

The IRS TEB office will post the webinar, including copies of the slides, to their website here.

TAX - MASSACHUSETTS

Russell Block Associates v. Board of Assessors of Worcester

Appeals Court of Massachusetts, Suffolk - September 16, 2015 - N.E.3d - 2014 WL

10399795

City sought review of decision of the Appellate Tax Board, granting taxpayer an abatement of tax on its parking garage.

The Appeals Court held that:

- Evidence supported classification of parking garage as partially "residential" property, and
- The phrase "used exclusively," in statute defining accessory residential property to include property used exclusively by the residents of the property or their guests, refers to that portion of mixed-use property used exclusively for residential accessory purposes.

Parking garage was an "accessory" building "incidental to habitation" within the meaning of tax statute, thus supporting "residential" classification. Parking garage was part and parcel of residential development plan, residents of the development needed a place to park their vehicles, and garage was designed and built to serve the development's tenants' parking needs and was required to do so to meet zoning and lending requirements for the development of the project.

In the context of a multiple-use property classified as mixed use, the phrase "used exclusively," in statute defining accessory residential property to include property used exclusively by the residents of the property or their guests, refers to that portion of the property used exclusively for residential accessory purposes.

Puerto Rico Utility Fails to Extend Contract With Insurers.

Puerto Rico's main electricity provider failed to extend a contract with its bond insurers that has given the power company time to negotiate a way to restructure its $8.3 billion of debt.

The Electric Power Authority's failure to extend the forbearance agreement with the insurers marks a setback for the utility, which earlier this month struck a tentative deal with some of its bondholders to reduce its debt load. Insurers that guarantee $2.5 billion of the utility's debt balked at extending the talks. The forbearance keeps negotiations outside of court.

The bond insurers "are trying to apply more pressure on Prepa," Matt Fabian, a partner at Concord, Massachusetts-based Municipal Market Analytics, said in a telephone interview Saturday. "Now they have the ability to exercise remedies. They could look now to forming a bondholder committee to try and impose a receiver and raise rates."

Bondholders agreed to extend the forbearance contract to Oct. 1, while fuel-line lenders pushed the expiration deadline to Sept. 25. The agreement was set to expire late Friday night. The power provider will continue negotiations with its bond insurers even without a forbearance agreement, Lisa Donahue, Prepa's chief restructuring officer, said in a statement Saturday.

Making Progress

"We are making progress and will continue working towards a consensual resolution that benefits Prepa and all of its stakeholders," Donahue said in the statement.

A Prepa restructuring would be the largest ever in the $3.5 trillion municipal-bond market, surpassing Detroit's record bankruptcy in July 2013. Puerto Rico and its agencies owe $72 billion.

Commonwealth officials plan to offer investors a debt-restructuring proposal in the next few weeks that's separate from Prepa's negotiations and would reduce the government's obligations and delay payments to bondholders.
The utility, bondholders, banks and insurers have repeatedly extended the forbearance agreement, which was first signed in August 2014.

Assured Guaranty Ltd. and Syncora Guarantee Inc. declined to extend that accord beyond Friday. MBIA Inc. dropped out of the forbearance earlier this month. National Public Finance Guarantee Corp., an MBIA unit that insures Prepa debt, filed a petition Thursday to the island's energy commission, asking it to temporarily add at least 4.2 cents per kilowatt hour to the agency's base electricity rate so Prepa can repay its bonds, according to a copy of the request provided by the commission.

Exercise Authority

"While National is continuing its discussions with Prepa in good faith to accomplish a consensual restructuring of Prepa, National has petitioned the Puerto Rico Energy Commission to exercise its statutory authority to impose a modest and temporary rate increase and to impose deadlines for the completion of Prepa's rate case," Greg Diamond, a spokesman for MBIA, said in a statement.

The expiration with the insurers may imperil the tentative agreement that Prepa and some of its bondholders reached on Sept. 1 that would require investors to take losses of about 15 percent in a debt exchange.
Ashweeta Durani, a spokeswoman for Assured, and Michael Corbally, a spokesman at Syncora Guarantee Inc., didn't immediately respond to e-mails. Dan Zacchei, a representative in New York at Sloane & Co. for the forbearing bondholders, declined to comment.

Bloomberg News

by Michelle Kaske

September 19, 2015 — 9:19 AM PDT Updated on September 19, 2015 — 10:48 AM PDT

What Investors Can Learn From Puerto Rico's Bond Default.

Hint: It can happen again.

There was a point in time when buying Puerto Rico's municipal debt seemed like a good idea. Enticed by bonds offering relatively high yields and exemption from federal, state, and local taxes, many U.S. investors jumped at the chance to buy up the commonwealth's debt. But then things started going sour in Puerto Rico, culminating in the ultimate no-no on the part of any municipality: a default.

That's right: After periods of coming extremely close, Puerto Rico finally defaulted on its municipal debt, paying just $628,000 of the $58 million it was supposed to dish out to bondholders in early August. According to Governor Alejandro Garcia Padilla, the island's $72 billion in public debt simply isn't payable, and the general economic outlook is bleak. In fact, he has even gone so far as to say that Puerto Rico's economy is in a "death spiral." Talk about discouraging.

How we got here

In 2006, after Puerto Rico lost many of the federal tax advantages that attracted U.S. companies to the island, loads of businesses jumped ship, and things have gone downhill ever since. Unemployment is at 12% in Puerto Rico — more than double the average rate in the U.S. Residents, in turn, are saying adios to the island and seeking work on the mainland.

For years, Puerto Rico's municipal bonds have been trading well below par, and its credit rating is currently hovering in junk territory. The commonwealth has more debt than any U.S. state aside from California and New York, which both have significantly larger populations. During the past 10 years, the island has been forced to borrow at high rates and double its debt simply to stay operational.

What this means for muni bonds

A Puerto Rico debt restructuring would be the largest ever in the $3.7 trillion municipal-bond market. Because Puerto Rico is a commonwealth, not a U.S. city or state, it cannot, by law, file for Chapter 9 bankruptcy protection. It also, as the governor has so eloquently stated, cannot pay its debts, which means that if there is indeed a restructuring, it won't be the neat, orderly type we're all used to.

Rather, we're more likely to see a series of lawsuits brought by investors clamoring for their money. It's good news if you're a lawyer, but if you're a Puerto Rico bondholder, not so much. Furthermore, a restructuring that proves remarkably unfavorable to bondholders could leave a bitter taste in investors' mouths, which could, in turn, impact the municipal bond market as a whole.

What we've learned

The silver lining in all of this — and you really have to want to see it — is that individual investors are getting a nice little crash course on what to do differently the next time around. For starters, don't rely on the fact that municipal bonds boast historically low default rates. Though they are rare, we've seen more defaults happen in recent years. Remember Detroit, for example.

Secondly, in situations like the one Puerto Rico faces, don't count on a bailout. The whole "too big to fail" theory doesn't seem to be working thus far. In fact, Puerto Rico has been petitioning incessantly for Chapter 9 eligibility, only to have its pleas rejected.

Here's another takeaway: If you're going to tie up your money in long-term municipal bonds, you may want to choose issues that are insured. Most of Puerto Rico's debt does not fall into this category.

Furthermore, don't take comfort in the mistakes of the masses. Some investors chose not to sell their positions in Puerto Rico several years ago — before things got really ugly — because they assumed the hedge funds that owned large chunks of Puerto Rico's debt would either sue or demand favorable treatment for bonds in the event of a restructuring. But favorable treatment only goes so far when there's no money to go around. Holders of Puerto Rico's bonds are potentially looking at just $0.60 on the dollar following a restructuring.

Finally, pay attention to your investments. Many holders of Puerto Rico bonds, to this day, are unaware that these bonds are taking up valuable real estate in their investment portfolios. More than 20% of American bond funds own Puerto Rico's debt, and they could be in for an unpleasant surprise depending on how much of a haircut bondholders take in whatever slapdash restructuring the island manages to pull off.

Right now, we don't know what the future will hold for Puerto Rico or its bondholders. If you're

invested in the island's debt, however, it's fair to assume that you're in for a pretty rocky ride.

Find this article informative?

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The Motley Fool

Maurie Backman
Fool Contributor

Sep 17, 2015 at 7:07AM

DUDE, WHERE'S MY BOND? I'm Ashton Kutcher and I'm Here to Help.

I'm Ashton Kutcher. You might remember me from movies like the one where I couldn't find my car because I was too high and shows like the one where I replaced Charlie Sheen because he was too high, as well as marriages like, "Demi, are you too high?" Today I'm here to fix public finance across the United States.

I know what you're thinking: What does this Ashton Kutcher character know about municipal bonds? It may surprise you that the answer is: obviously, a fuckton.

I fly over highways all the time and think, man that highway looks like it sucks, what with the crummy asphalt and the having to drive and the needing to remember where your car is in the first place. I also walk by public sewers once in awhile when I'm in Los Angeles or Ibiza and think, could we organize, like, an epic sewer party down there? Probably not! Because the sewer is dirty and broken. Thanks, public finance.

Then I think longer term, about my planned space trip and I get a little bleary eyed. Or is it teary eyed? Whatever. I get water eyes.

That's because I think to myself: what happens when the government has to fund not only all these roads and sewers but SPACE HIGHWAYS?! Do I want my child dying in a space highway accident because the space authority didn't have enough funding??? I'm not 100% sure, but probably not.

The answer to all of this is Neighborly.

Neighborly isn't about all that Wall Street mumbo jumbo when it comes to financing crap you don't want to pay for. It's about neighbors! Neighbors paying for each other in a neighborly way in their neighborhoods. (As well as maybe the occasional sewer party together? Seriously, let's do this.)

Have you ever looked at a broken stoplight and said to yourself, I wish I could just pay a startup to allow me to invest in a bond whose proceeds may or may not be used to fix that broken stoplight? I sure haven't! But that doesn't mean you shouldn't have that opportunity—and Neighborly is it.

At this point you might be wondering two things: why can't governments fund themselves without

Neighborly, and what, exactly, does Neighborly do? I'll answer these questions in two parts, unless I get distracted.

First: a lot of people think municipalities can't afford to fix their roads and sewers and space highways because 1) unemployment hurt tax revenue 2) a downturn in spending hurt tax revenue 3) a downturn in corporate income hurt tax revenue 4) local governments spent a lot of money on boneheaded projects 5) local governments entered boneheaded financing arrangements or 6) political nonsense in Washington with "fiscal cliffs" and "government shutdowns" hurt federal support of state and local budgets.

To all these ideas, I say: Pfft, whatever mom, you're not my boss.

The real reason for whatever we're talking about is that neighbors can't put neighbor money into a neighbor pot to support the neighborhood. It's sort of like when you put your keys into a "designated driver" bowl at a house party and the lady who owns the house won't let you leave with no pants on carrying a half-full bottle of Jack.

Anyway, the key bowl is a great idea for a public-finance startup because it can make money appealing to disillusioned young Americans who hate Wall Street, and want to be more directly involved in their local governments, without having to attend community board meetings. At least some guy told me that. Mainly, it's a great way for me to earn money doing the same thing Wall Street does, except cooler, with a smiley face: =:o]

I believe your second question was about how Neighborly works, or about how I manage to be so sexy and have amazing skin well into my 30s. The sexy-skin question was inappropriate—if omnirelevant. I'd answer the other one, except math is hard, and our "How It Works" section on Neighborly's web site doesn't offer much in the way of how it works.

However! It does include truisms such as "Investing in cities is hard." (I know, rite?) Besides that, I would suggest looking at the cartoons of a woman with hearts next to her head, as well as a guy surrounded by pine trees and wind turbines. All of this indicates that whatever we're doing is really "on fleek," as the kids say—and I have better skin than they do.

FUSION

by Lauren Tara LaCapra

September 16, 2015 10:53 a.m.

Neighborly Raises $5.5M from Joe Lonsdale's Formation 8, Ashton Kutcher to Transform the Municipal Debt Market.

For American cities that need to raise millions or billions of dollars to finance projects from local parks to suspension bridges, the fractal-like complexity of global financial markets means that funding is becoming ever more opaque and distant from the real-world work it supports.

A startup called Neighborly is hoping to narrow that gap with a $5.5 million round of funding from Joe Lonsdale's Formation 8 and Ashton Kutcher's Sound Ventures. An earlier incarnation of the product was about crowdfunding civic projects, kind of like a Kickstarter for your neighborhood.

That was an important niche, but large-scale and impactful projects require on the order of hundreds of millions or billions of dollars. For instance, the city of San Francisco is asking voters to pass a $300 million affordable housing bond this November amid a major shortage, and the regional transit system, BART, has more than $9 billion in maintenance needs through the next decade.

So Neighborly is shifting back to its original idea, which was to create a platform for retail investors to invest in municipal debt that actually affects where they live. It's an enormous market with a size of roughly $3.7 trillion.

The company's founder Jase Wilson grew up in a broken home in a poverty-stricken factory and farm town in the Midwest. But he had access to decent parks and a strong-willed mother, which helped him escape tough situations at home. Later on in college, he studied both engineering and urban planning and ended up working in civic software for city governments for about a decade.

Several years into the job, Wilson started getting to know municipal bond traders, who were exchanging and issuing the debt that cities need to fund projects. A trader walked Wilson through underwriting and compliance, and then over to a fax machine with stacks of papers and contracts. The trader explained to Wilson that just by switching from corporate to municipal debt, he could double his income without doing any extra work. This was because public city governments ended up with extra layers of fees throughout all the steps of municipal debt issuance that corporate issuers were more rigorous about holding accountable.

"I thought — why isn't there an AngelList for this?" Wilson said, adding that 2.2 percent of a cities' total debt issuance goes toward the cost of borrowing on top of interest. On top of that, city governments can end up on the bad side of a deal that they are unable to evaluate as well as investment banks, which see deals day after day.

After the last financial crisis, [Oakland got in a tussle with Goldman Sachs on an old interest-rate swaps deal]() that would have protected them if interest rates rose. Instead, interest rates fell after the housing market crashed, and the city ended up on the hook for $4 million in annual interest payments to the bank.

"There are a lot of inefficiencies that software can solve in the market as it operates today," he said. "The market fundamentally fails to connect people our age with the debt that goes toward funding projects in their neighborhoods."

On Neighborly, you can create a personal profile, listing out how much you want to invest and the kind of return and risk you'd want to assume. Then you can get notifications about upcoming sales and issuances. Neighborly can also use machine learning techniques to evaluate the risk of municipal bonds in addition to the analysts and rating agencies an investor would normally use. On the city side, government officials can store and manage all their documentation, cutting out legal and advisor work.

The hope is that if this behavior scales, Millennial retail investors buying municipal debt could drive down borrowing costs for projects in their own backyards. It could also crowd out the need for investment banks to package and distribute municipal debt to other investors — a process where they end up taking an estimated $60 billion cut off municipal issuance.

He added, "We are inheriting debt from the generation before us, and then we are going to be at the helm of this market that we have zero personal connection with."

TechCrunch

Posted Sep 15, 2015 by Kim-Mai Cutler (@kimmaicutler)

TAX - OREGON

City of Seattle v. Department of Revenue

Supreme Court of Oregon, En Banc - September 11, 2015 - P.3d - 2015 WL 5306744

Cities appealed from Tax Court's summary judgment ruling that their interest in electrical transmission capacity could be taxed by Department of Revenue as a property interest "held" by taxpayers.

The Supreme Court of Oregon held that:

- Cities' interest in electrical transmission capacity could be taxed, and
- Senate bill which repealed property tax exemption benefiting out-of-state municipal corporations was not a "bill for raising revenue" within meaning of state constitutional provision requiring that bill for raising revenue originate in House of Representatives.

Cities' interest in electrical transmission capacity, purchased from electrical cooperative and used to transmit electricity over region's federally administered power grid, could be taxed by Department of Revenue as a property interest "held" by the cities pursuant to statute under which real and personal property of the United States held by a taxpayer comes within exception of general exemption of federal property from taxation.

Senate bill which repealed property tax exemption benefiting out-of-state municipal corporations was not a "bill for raising revenue" within meaning of state constitutional provision requiring that bill for raising revenue originate in House of Representatives and pass by three-fifths vote, where bill, although generating revenue by removing a tax exemption, did not directly levy a tax.

S&P: Federal Fiscal Policy Discord Could Undermine the Economic and Budgetary Environment for States.

After a roughly two-year reprieve, U.S. state governments need to brace for the possibility of another federal government shutdown, Standard & Poor's Ratings Services believes. In addition, federal spending caps are scheduled to ratchet down again beginning in federal fiscal year 2016 (October 1). As we understand it, avoiding a shutdown may require that Congress and the President reach agreement on changes to the spending caps, no easy task given their stated policy positions. It's not a foregone conclusion, but we believe the state sector may be in for another episode of tumultuous federal fiscal negotiations, including the possibility of a short-term federal government shutdown.

In our view, most states can likely maintain their current rating levels with the slower economic growth rates that would result from a temporary shutdown. Appropriations for certain major federal grants to states are already in place, partially shielding state budgets from the immediate fiscal disruption that a short term federal shutdown would cause. However, from a macroeconomic standpoint, insofar as a shutdown translates to slower revenue growth or higher demand for state services, state fiscal margins could be narrower than presently forecasted. In our view, a shutdown could therefore absorb a portion of the states' budgetary capacity that would otherwise be available

in the event of unanticipated economic softening. This could leave states more vulnerable to downside pressure spilling over from a slowdown in the Chinese economy or elsewhere.

Continue reading.

14-Sep-2015

Dealers and Academics Square Off Over Data Proposal.

WASHINGTON – Dealer groups oppose a Municipal Securities Rulemaking Board proposal to provide academics with muni trade and pricing data with anonymous dealer identifiers while researchers contend the new data will add to market transparency.

The conflicting stances were taken in 12 comment letters from dealers, academics and others. Dealer groups argued the data would expose broker-dealers to business risks if the academics used the data to reverse engineer the trades.

Bond Dealers of America and Securities Industry and Financial Markets Association both said they were concerned the anonymized identifiers would open their members up to the possibility of having their identities, trading strategies and inventories discovered through reverse engineering.

"The potential impact of reverse engineering could be significant," said David Cohen, SIFMA's managing director and associate general counsel for municipal securities, and Sean Davy, SIFMA's managing director of the capital markets division. " Dealer trading strategies may be deciphered through reverse engineering of [municipal participant identifiers] and reviewing trading patterns and practices. If dealer trading strategies are publicly known they may significantly impact a dealer's ability to provide the market with liquidity."

Cohen and Davy said they would prefer to see dealers with similar characteristics grouped together instead of anonymized identifiers as well as an exclusion of all primary trades from the data.

Dealers currently are required to submit data from most of their trades to the MSRB's Real-time Transaction Reporting System within 15 minutes of execution. The trade data is made available in its entirety to regulatory and enforcement officials. Post-trade information is made public without the identification of dealers or customers. The public data does not distinguish between conditional trade commitments made before the bond purchase agreement is signed and the sale of new bonds after the BPA is signed.

BDA said the currently available data sets include "a sufficient level of detail to support rigorous study." The group said that if MSRB has to provide new data to academics, it should combine dealers into multiple groups based on size instead of applying anonymous identifiers.

Several academics disagreed with the dealer groups and argued the market would see more liquidity if they were allowed to access the proposed new data.

Larry Harris, chair of the University of Southern California's finance department, said the anonymized identities of dealers should be included so that academics can link multiple trades by the same dealer and analyze liquidity.

"The production of information about liquidity will lead to better policy decisions by the MSRB,"

Harris wrote. “Liquidity ultimately will be enhanced, which will benefit investors directly through lower transaction costs, and issuers through higher offering prices.”

The MSRB released the data proposal on July 16 and asked for public comments including, on a number of questions about whether its ideas to adapt the trade product to the market were sufficient. The originally proposed product would: require academics to agree not to engage in reverse engineering; cost $500 up front and then an additional $500 for each calendar-year data set requested; prohibit redistribution of data; mandate users disclose their specific intentions for requesting the information; and only be available to academics with institutions of higher education. Information would also have to be more than two years old to be eligible for release.

In addition to the debate about whether anonymous dealer identifiers should be used, academics and the dealer groups also disagreed about the right time period before data ccould be released. Academics thought the two-year wait was too long and could lead to stale data that would ultimately not be as useful in research.

“The 24 month delay for release of the data seems excessive and counter to the goal of promoting fair and efficient market practices,” James Ramsey, president of the University of Louisville, wrote. “A 12 month delay would be more reasonable.”

Most other academics thought 12 months was a fair amount of time to wait and would not expose dealers to significant business risks, but Harris said he thinks six months “would be optimal.”

“I do not think that much value can be inferred from reverse engineering dealer strategies, and I am concerned about identifying parasitic trading strategies as quickly as possible,” Harris said. Cohen and Davy recommended a four-year wait before releasing data. They said they believe that wait period “appropriately balances” their concerns “with researchers’ desire to have access to the data with anonymized dealer identifiers.”

Academics also raised an issue with restricting the audience for the possible new trade data to just those associated with institutions of higher education. They said higher level research requires a large number of people to review a study before it’s published and limiting the distribution to such a small group would limit the effectiveness of the research.

Ramsey, the Association for Budgeting & Financial Management, and Patrick Cusatis, an associate professor of finance, also raised concerns about a portion of the proposal that would hold a recipient of the trade information “liable for any action or inaction on the part of someone whom the recipient provides any derivative works.” They said it was unreasonable to hold an academic responsible for others’ actions, especially when sharing work is a large part of scholarship. They recommended the MSRB lessen the section of the proposal that would impose unlimited liability on researchers if they were to breach the data agreement.

THE BOND BUYER

by Jack Casey

SEP 15, 2015 4:25pm ET

SEC Urged to Disapprove Rule on MA Core Conduct.

WASHINGTON – Dealer, issuer and investment company groups are urging the Securities and Exchange Commission to disapprove a Municipal Securities Rulemaking Board rule that would impose core duties on municipal advisors, warning it is overly burdensome and anti-competitive. The groups made the requests in comment letters sent to the SEC regarding the MSRB's Rule G-42 on core duties of municipal advisors.

"The MSRB has made important strides in making proposed Rule G-42 workable since its original draft proposal," said Leslie Norwood, associate general counsel and co-head of municipal securities for Securities Industry and Financial Markets Association. But "SIFMA continues to have significant concerns regarding certain aspects of [the rule], which render it unreasonably burdensome and anti-competitive in ways that do not clearly promote the fundamental policies of the municipal advisor provisions of the [Securities and] Exchange Act" of 1934.

The rule states that MAs would owe a fiduciary "duty of loyalty" to their municipal issuer clients, requiring them "without limitation … to deal honestly and with the upmost good faith with a municipal entity and act in the client's best interests without regard to the financial or other interests of the municipal advisor."

The proposal also mandates a less stringent "duty of care" for all clients. The duty of care provision requires MAs to: exercise due care in their work; be qualified to provide advisor services; make a "reasonable inquiry" into the facts relevant to a client's request before deciding whether to proceed; and undertake a "reasonable investigation" to determine their advice is not based on bad information.

The SEC previously published the proposal for comment on May 8, but asked for an extension of up to 90 days on Aug. 6. The MSRB then published revisions to the rule and responded to earlier comments on Aug. 12. But Norwood said the MSRB response "in most regards simply dismissed commenters' concerns with conclusory and superficial responses that simply restate the MSRB's view that the particular provision is appropriate" without going further.

Several groups, including SIFMA, used their comment letters to address their ongoing complaint about the rule banning an MA from acting as a principal in a transaction with a muni issuer client that is directly related to a transaction on which the MA is providing advice. The ban is meant to prevent conflicts of interest.

Norwood said the ban is "more restrictive and inflexible than fiduciary obligations under any other financial regulatory regime." She added that the MSRB rejected proposed modifications to the ban, like limiting it to principal transactions that are directly related to the advice provided by the MA, including a separate registered municipal advisor exception, and allowing for incidental advice related to brokerage services.

Mike Nicholas, chief executive officer of Bond Dealers of America, suggested in BDA's comment letter the MSRB and commission would be better off addressing conflicts of interest through a disclosure and consent process, as is done with investment advisors and attorneys. Government Finance Officers Association Director Dustin McDonald agreed with Nicholas, saying the proposed rule removes issuers from the conflict review process. McDonald also reiterated an earlier concern that the ban would force small issuers to enter into more expensive arrangements with outside advisors.

GFOA, SIFMA, BDA, and the Investment Company Institute each urged the SEC to disapprove the rule.

SIFMA also said that the ban on principal transactions is already leading to a decrease in competition in the market as some firms associated with broker-dealers have stopped providing muni advisory services because they believe “the inability to enter into other business with the client makes the cost of providing municipal advisory services too high.”

BDA and SIFMA also said they are concerned about a lack of clarity in the rule’s documentation requirements, specifically those on documenting an advisor’s work to ensure a recommendation is suitable for its client. SIFMA said the rule does not make clear what constitutes a recommendation and thus what documents an advisor would need to retain to prove to a regulator that its recommendations were suitable for its client.

Nicholas said the MSRB should “state exactly what is expected of firms in the way of documentation” to help advisors engaged in deals that take multiple years to conclude. The suitability standard and documentation of recommendations is also one of multiple areas the National Association of Municipal Advisors requested additional clarity on from the MSRB and SEC, saying the clarifications “are essential for MAs to abide by the law because of the potential differences in interpretation that could occur between MAs and SEC examiners.”

NAMA did not ask the SEC to disapprove the rule, but said the rule should not go into effect until the MSRB gives additional guidance.

The group asked the MSRB to offer supplementary material, interpretive guidance and/or non-exclusive examples to help advisors understand the way they are expected to conduct and document reasonable due diligence, as well as alternative financings, and the duty of care provision. It also asked for clarification on any overlap between G-42 and Rule G-23, which prohibits firms from acting as advisors and underwriters on the same muni transactions. Without those clarifications, NAMA said the MSRB would place an undue burden on small advisors and violate the Exchange Act.

The Investment Company Institute also took issue with the documentation requirements, saying the requirement that an MA “affirmatively investigate the veracity of information provided to it” by its clients would be burdensome and “completely disruptive” to the long-term relationships that MAs advising on 529 college savings plans have with their clients.

THE BOND BUYER

by Jack Casey

SEP 14, 2015 3:42pm ET

Legality of Tax-Exempt Status for P3 Projects Scrutinized in Texas.

The long-standing practice of classifying student housing projects built through public-private partnerships on state university-owned land as tax-exempt is being questioned by a Texas county attorney’s office.

County Attorney Rodney Anderson of Brazos County has asked state Attorney General Ken Paxton to deliver a legal opinion on whether taxes should be levied on two Texas A&M student housing P3s in College Station, which collectively will house more than 4,500 students. The projects are among five P3s the university has negotiated and from which it expects to earn $900 million in revenues over several decades.

In his letter to Paxton, Anderson points out that each developer of the two projects will own the facilities and improvements they build, finance and operate during the 32-year and 40-year ground leases that were negotiated. After the leases expire the university will take ownership of the properties.

One of the P3 agreements stipulates that the student accommodations can be used only by people associated directly with the university. However, language in the other, more recent contract does not rule out the option to sublease the housing to "persons who are not faculty, staff or students of Texas A&M or [the university-associated] Blinn College," Anderson pointed out.

The county attorney questions whether these elements of the P3 agreements meet the requirement that, to be accorded tax-exempt status, the property must be both publicly owned and used for public purposes.

He also pointed out that the P3-developed projects will compete with private housing projects that do not enjoy tax-exempt status, which puts owners of non-P3 housing units at a "competitive disadvantage."

In defense of the P3s' eligibility for tax exemptions, the university has cited case law that favors its position, including a 1992 court ruling that improvements to state land are tax exempt even if the state doesn't hold legal title to their improvement, reported the Houston Chronicle.

NCPPP
By Editor September 17, 2015

Orrick Advises on First of a Kind Statewide Telecommunications Network in Kentucky.

Orrick, Herrington & Sutcliffe LLP represented KentuckyWired Operations Company, LLC, indirectly owned by Macquarie Infrastructure Developments, LLC, First Solutions LLC and Ledcor US Ventures Inc., as bond counsel in the US$300 million financing of a high-speed, open access, middle-mile fiber optic network with excess capacity with the Commonwealth of Kentucky. The project, which is expected to be completed in 2018, will add over 3,200 miles of fiber optic cable statewide.

Kentucky currently ranks 46th in the U.S. in terms of broadband availability, and approximately 23% of the state's population (mostly located in rural areas) has no broadband access at all. The statewide fiber optic network will make high-speed internet accessible throughout Kentucky's 120 counties by 2018, including 1,098 government and public facilities such as academic institutions, public libraries and governmental agencies, with the excess capacity to be made available through wholesale access to local Internet service providers who can extend fiber to homes and businesses. The project is a first of its kind in the U.S. in that it involves an underground fiber optic cable for part of the system, and was financed using a unique tax exempt structure that was designed by Orrick's Tax Group. In particular, the structure eased regulatory hurdles which enabled a statewide project to be completed in a short time frame.

"We are thrilled to handle such a unique and groundbreaking transaction," said Dan Mathews, partner and co-Head of Orrick's Energy & Infrastructure Group, who led the infrastructure team. "This project is expected to significantly improve Kentucky's education, health access and economy through increased connectivity to high speed internet, and we hope it will set precedent for

improvement of telecommunications networks in additional states."

"This deal was successful due to the cross-practice support of our Tax, Energy & Infrastructure and Public Finance Groups," said Chas Cardall, partner and Chair of Orrick's Tax Group and a member of the Public Finance group, who led the tax aspects of the transaction. "We were able to leverage the expertise of our lawyers in each of these areas to create a unique tax exempt structure, which was a key aspect of the transaction."

In addition to Dan and Chas, the team was comprised of Ken Schuhmacher, Susan Long, Benjamin Bass and Walter Alarkon of the Energy & Infrastructure Group, Sarah Rackoff, Marc Bauer and Jennifer Grew of the Public Finance Group and Greg Riddle, Wolfram Pohl, George Wolf and Ashley Rodriguez of the Tax Group.

About Orrick

Orrick is a leading global law firm focused on counseling companies in the Energy & Infrastructure, Finance and Tech sectors. The firm's client work is divided equally between transactional advice and litigation. Law360 recognizes Orrick among the "Global 20" law firms and named the firm a "Technology Practice Group of the Year" in 2014. The firm's platform includes offices across the US and in the UK, France, Switzerland, Germany, Italy, Belgium, Russia, China and Japan. The firm also has an affiliated office in Abidjan, Cote d'Ivoire. Financial Times consistently recognizes Orrick among the 10 most innovative North American firms, and BTI Consulting recently named Orrick to its Client Service All Star List.

Contact

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09-16-2015

S&P's Pubic Finance Podcast (The U.S. Health Care Sector Outlook and Special Tax Ratios).

In this week's Extra Credit, Senior Director Kevin Holloran explains what's behind our outlook for the U.S. health care sector and Director Russell Bryce discusses special tax ratios.

Listen to the Podcast.

Sep. 18, 2015

How Standard & Poor's Treats Public-Private Partnerships in U.S. State and Local Government Debt Analysis.

Although infrastructure needs in the U.S. — and worldwide -- are very high, in our view, the governments in many developed nations have cut back on infrastructure spending, in large part, we believe, because of budgetary concerns. In the U.S., government spending on projects, as a

percentage of GDP, has dropped to a two-decade low of about 1.7%, according to the Federal Reserve Bank of St. Louis. (See "U.S. Infrastructure Investment: A Chance To Reap More Than We Sow," published May 5, 2014, on RatingsDirect.) This limited infrastructure funding comes when the country's infrastructure has repeatedly received a near-failing grade from the American Society of Civil Engineers (ASCE) in the comprehensive assessment it issues every four years. The low grade reflects the enormous amount of capital needs, from bridges to levees. For example, according to ASCE, one in nine bridges in the U.S. is structurally deficient, and to eliminate the backlog of repairs or build replacements by 2028, local, state, and federal spending would have to increase by $8 billion per year.

As U.S. state and local governments look for alternative ways of delivering large infrastructure projects, interest has grown in using public-private partnerships (P3s), a risk-sharing method that governments have used globally for many types of infrastructure.

Standard & Poor's Ratings Services believes it will be useful to provide additional context about its views on P3s and to address how it incorporates P3 payment obligations into its debt statement analysis for U.S. state and local governments.

Frequently Asked Questions

What are public-private partnerships?

A P3 is a risk-sharing partnership–consisting of a government and a private business–that builds, finances, and operates an infrastructure project. In a P3, the roles and responsibilities of both the private-sector and government participants are typically specified in a contract, frequently referred to as a concession agreement. Under the concession agreement, the private entity is contractually obligated to deliver a service, typically to design, build, finance, operate, and maintain an asset for a specified fixed period, defined as the length of the concession. Concession periods of 30 to 40 years are common, but some are longer. These projects are arranged as either availability- or volume-based projects. For volume-based projects, the government typically receives an upfront payment in exchange for allowing the private entity to operate and collect the project revenues over the contract term. For availability-based projects, the government makes construction milestone payments and availability payments to support the new asset. In many, but not all cases, toll revenues, gas taxes, or appropriations back the government's availability payment commitment. Because of the issuance structure, the P3 debt issuances are often free from the constraints of a government's debt affordability models. We evaluate the nature of a government's obligation under the P3 agreements in determining whether we consider the obligation to be part of a government's tax-supported debt.

How prevalent is the use of P3s in the U.S.?

Although other countries have used P3s more widely, in the U.S. their use has been more recent and somewhat limited. However, interest in the P3 approach is growing in the U.S., and several states are developing programs. California, Florida, Indiana, Texas, and Virginia have participated in P3s. Currently, 33 states have authorized P3s, and others such as New York, North Carolina, and Pennsylvania are developing new P3 programs. The U.S. projects have primarily focused on transportation, such as roads, toll lanes, and transit projects. However, the Long Beach Courthouse in California is an example of a social infrastructure P3 project, and other states currently active in transportation P3 projects are also considering approving legislation allowing social infrastructure P3s. We expect that the states with established P3 programs will continue to use P3 financing. In our view, the large size and complexity of the projects and the concession agreements, as well as the lack of uniformity in the terms of these agreements–no two P3s are alike–have all created high start-

up costs and acted as a barrier to greater adoption of this model. This is particularly true when start-up process span different administrations, whose interest in P3s may vary. In addition, in the U.S. the municipal bond market has provided a readily available low-cost financing mechanism with long amortizations that are beneficial to many infrastructure financings, which has also limited the use of P3 financings in the U.S. In our opinion, recent problems regarding the Virginia Route 460 project, the Indiana Toll Road bankruptcy, and the federal judge's ruling on the Illiana Corridor project, regardless of these projects' ultimate outcome, might have created some headwinds for P3s in states that are unfamiliar or inexperienced with the P3 model. In our view, a more intrinsic barrier could be that despite a free market orientation in the U.S., governments don't have an evolved culture of public-sector agencies handing over these functions to the private sector. Whether this is because of political accountability, engrained views of the role of government, or other reasons is uncertain; however, we believe that at least in the near term, support for these projects will be mixed. (See "U.S. Public-Private Partnerships Encounter New Road Bumps As Political Appetite For The Projects Waxes And Wanes," published Sept. 9, 2015.)

How do the risks transferred differ from volume-based to availability-based P3s?

A P3 structure's benefits are that it includes some level of private investment and that there is, typically, a transfer of construction and/or operating risk to the private party. The private investment typically ranges from about 10% of total project cost for availability-based projects to about 30% in volume-based projects. In volume-based transactions, usage or volume risk, hence the name, is transferred to the private entity. For these, the government typically receives an up-front payment and/or payments over time in exchange for allowing the private entity to operate and collect the project revenues over the contract term. Funding usually comes largely directly from user fees or tolls and the private sector assumes most of the operating and volume risks, with very limited recourse to the government in case of lower-than-expected usage. Although in most cases toll road P3s are structured as volume-based projects, there are instances where concerns over the sufficiency of toll revenues to cover payment obligations could lead a government to use an availability-based model. For availability-based projects, the government typically transfers the construction and operating risks, but retains the risk of usage. In other words, the government's annual payments are for making the facility available for use, regardless of the actual usage (volume) or the amount of revenues derived from the project, if any.

How Does Standard & Poor's treat U.S. state and local governments' P3 payment obligations?

We might treat the government's P3 obligation as debt, as a contingent liability, or neither. The key determinants are the source of revenue to pay the P3 obligation and whether we consider the obligation self-supporting. Once we've determined to include all or a portion of the obligation as debt, we size the debt statement impact based on the type of payments (such as milestone, availability) and the net present value of the payments.

If we consider the revenue stream used to repay the obligation to be tax-backed revenue, then we'll include the P3 obligation as tax-supported debt, subject to adjustments mentioned below. Tax-backed revenues include tax revenues, appropriations, and special taxes. If the security for repayment is from a true enterprise operation or from a nontax-supported source, such as toll revenues or grant anticipation revenue bonds paid solely from dedicated federal funding, then we won't include it as tax-supported debt or contingent liability.

Does Standard & Poor's consider P3 availability payments to be debt-like?

While a unique structure, P3 availability payments have many features that make them debt-like.

Under an availability payment model, the government enters into a long-term contract or obligation to pay. In most cases, in addition to being long term, these payment obligations are fixed commitments with penalties, or termination payments, if the agreement ends. Often, the government pays these obligations from the same revenue sources as more traditional tax-exempt municipal debt. Furthermore, similar to debt, these payments fund capital improvements or meet other government purposes. Finally, generally, the sponsoring government owns the asset.

Does Standard & Poor's factor in self-support for P3 obligations?

In some cases, in addition to tax-backed revenues, pledges of nontax revenues, such as toll revenues, will support the P3 payment obligation. In these cases, we'll determine if these nontax revenues provide partial or self-support of the payment obligation and adjust the size of the obligation to include in our debt calculations. Our self-support analysis is based on historical coverage (see "Debt Statement Analysis"published Aug. 22, 2006), but we could adjust our view of self-support if we expect future coverage to be lower than historical.

Does Standard & Poor's make any adjustment to the availability payment obligations when including them as debt?

In deciding how much debt to include in debt statements, we evaluate milestone and availability payment obligations separately. Milestone payments are made in recognition of reaching a construction milestone and, in most cases, occur before the asset is available for use. Absent some form of self-support in the P3, we treat milestone payments as debt and add them at the P3's financial close. Availability payments include a fixed portion that represents both the capital portion of project-related debt issued by the partnership and equity partner's contribution and a variable portion that represents lifecycle operations and maintenance (O&M) expenses. In our view, adding the string of total future annual payments represents a more comprehensive estimate of a government's true obligation over the life of a project. However, because we view O&M costs for these projects as operating costs and to ensure equal treatment with other tax-backed debt, where a breakdown is available, we separate the O&M cost from the other components of the availability payment. We add availability payments as a debt-like obligation on delivery of the asset.

Because milestone and availability payments include either an interest component (for debt issued) or a return on investment (on the equity contribution), before adding the obligations to our debt statements, we discount the future payments to arrive at a net present value of the principal component of the P3 payment. Given that P3 projects are typically done in lieu of a traditional debt financing for a public entity, we estimate a discount rate that is representative of a public entity's cost of capital based on its rating category and length of the P3 contract. We would generally use Municipal Market Data or a similar data source to estimate the discount rate.

Under Standard & Poor's policies, only a Rating Committee can determine a Credit Rating Action (including a Credit Rating change, affirmation or withdrawal, Rating Outlook change, or CreditWatch action). This commentary and its subject matter have not been the subject of Rating Committee action and should not be interpreted as a change to, or affirmation of, a Credit Rating or Rating Outlook.

17-Sep-2015

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IRS Conducting Targeted Audit of Troubled Wayne County Jail Bonds.

WASHINGTON – The Internal Revenue Service is conducting a targeted audit of $200 million of recovery zone economic development bonds issued in 2010 by the Wayne County Building Authority in Michigan to finance a jail facility that was never completed.

The county disclosed the audit in an event notice posted on the Municipal Securities Rulemaking Board's EMMA system on Sept. 9 in the "Other Event-Based Disclosures," rather than the "Communication from the Internal Revenue Service" or "Adverse Tax Opinion or Event Affecting Tax-Exempt Status" categories of event notices. The IRS audit notice is the latest in a series of headaches for the county tied to the abandoned jail site in downtown Detroit, the county seat.

The authority received the audit notice from the IRS on July 28. The Service said it decided to audit the bonds "because of information we received from external sources or developed internally that causes a concern" that the bonds may fail one or more of the bond provisions in the federal tax code. Bond lawyers have said that language like this is an indication that the audit is targeted.

If the IRS determines that the authority's bond issue violates any tax requirements, the federal subsidy payments the authority receives for the bonds could be at risk. The authority could lose part or all of the subsidy payments, and those losses could be retroactive to the issue date, or prospective, or both. A loss of the subsidy payments "could materially adversely impact the county's ability to pay debt service with respect to the Series 2010 jail facilities bonds or other obligations of the county," the county said.

The authority receives subsidy payments equal to 45% of the interest costs, minus any reductions due to sequestration. As of the date of the event notice, the authority has received about $36.88 million from the Treasury. The event notice said that the county and the authority are currently unable to determine if the audit will lead to the loss of the subsidy payments.

The county said it has hired Miller Canfield to handle the IRS review. A spokesman also said the county is not aware of the information the IRS says it received that suggest the bonds may not be compliant.

"Nothing has come to our attention which suggests that bond usage was non-compliant," county spokesman James Canning said in a statement. "The full amount of authorized bonds have not been spent and are being held in the project fund," said Canning. "Wayne County is cooperating with the IRS and believes that it is in full compliance with all tax requirements."

The county's building authority floated the $200 million bond issue in 2010 to consolidate three aging jail facilities into one adjacent to the Frank Murphy Hall of Justice in downtown Detroit. The bonds were structured as RZEDBs, carrying the county's limited-tax general obligation pledge. RZEDBs are federally taxable, direct-pay bonds whose available project proceeds have to be spent

on purposes that promote development or other economic activities in recovery zones.

Wayne broke ground on the $300 million, 2,000-bed project in 2011 and halted it by the summer of 2013 as the estimated cost climbed to $390 million. The site has since sat vacant, with County Executive Warren Evans saying the cash-strapped county does not have the money to finish the project and cannot borrow the money without paying a hefty penalty. The county has the authority to issue another $100 million of bonds to complete the project.

Meanwhile, in 2014, the county's former chief financial officer and two others connected to the project were indicted by a grand jury for misconduct in office and willful neglect of duty tied to the jail financing.

Michigan Gov. Rick Snyder declared Wayne to be in a financial emergency in July, and the county is currently operating under a consent agreement with the state. As part of the decree, Wayne is required to present the state with a plan for the jail by Jan. 31. Officials are reportedly trying to sell the site to a local businessman.

Wayne is paying $14 million annually for the abandoned project, with debt service structured as cash rental payments from the building authority to the county, as well as an additional $3 million in storage costs.

Some of the bonds matured in 2014, and others mature in 2015, 2016, 2025 and 2040. Bonds maturing after 2021 have an optional redemption starting in December 2020. The bonds are also subject to an extraordinary optional redemption due to sequestration cuts to subsidy payments, but not due to any actions of the building authority.

The bulk of the $200 million of taxable bonds — $143.33 million — feature a 2040 maturity and a 10% coupon. The bonds were yielding 11.5% in Wednesday trading, according to EMMA. That's down from 12.3% on July 15 trading and up from a 7.5% to 8% yield in January.

Fitch Ratings has warned that the jail debt could be particularly vulnerable to cuts or default because it is not subject to abatement or appropriation and the project is politically controversial.

"Debt service comprises a relatively small share of governmental spending, but Fitch believes the jail debt could be vulnerable given the failure to complete the project," Fitch said in a March 2015 ratings commentary.

JP Morgan was the senior manager on the original deal. Government Finance Associates Inc. was the county's financial advisor, and Miller, Canfield, Paddock and Stone, PLC was bond counsel, according to the official statement for the bonds.

THE BOND BUYER

BY NAOMI JAGODA and CAITLIN DEVITT

SEP 16, 2015 4:07pm ET

Apples are Nice but Pensions are Better.

Two new research briefs this week fuel the argument that public pensions are only practical for the

small portion of workers who stick around in one place for their whole career. Nationally, fewer workers, particularly Millennials, are staying with a company for most of their careers. The research was conducted by TeacherPensions.org, Bellwether Education Partners and the Urban Institute and looks at how current pension plans in all 50 states serve short- and medium-term working teachers.

While it's a common assumption that public-sector teachers trade lower salaries for higher job security and more generous benefits, the briefs argue that trade only works well for the small minority of teachers who actually stick around until retirement. "Most teachers get the worst of both worlds — they earn lower salaries while they work and they forfeit retirement savings when they leave," the researchers said.

The first brief, Hidden Penalties, looks at short-term workers, or those who don't stay long enough to qualify for any pension. About half of all new teachers fall into this group and they forfeit thousands of dollars their employer contributed on their behalf.

The second brief, Negative Returns, looks at medium- and longer-term teachers. It found that because of the back-loaded nature of pensions benefits (meaning they ramp up in the final years of service), a teacher in the median state must serve 25 years before qualifying for a pension worth more than their own contributions. "Recent pension reforms, focused mainly on cutting costs, generally make this situation worse and force new teachers to work even longer before they benefit from their pension plans," the brief said.

GOVERNING.COM

BY LIZ FARMER | SEPTEMBER 18, 2015

Republican Governors Use Pensions to Oppose Iran Deal.

After Congress's deadline to block President Barack Obama's nuclear deal with Iran expired Thursday, Republicans are taking the fight to the states by vowing to preserve local sanctions.

Thirty states and the District of Columbia restrict investments by pensions and public entities in companies doing business in the country, according to the group United Against Nuclear Iran. Fifteen Republican U.S. governors, including four presidential candidates, last week sent a letter to Obama saying they would fight to keep their constraints if the administration lifts its nuclear-related sanctions.

A new nonprofit, Defund Iran, is also seeking state constitutional amendments next year that would mandate divestment. Florida alone has withdrawn more than $1.1 billion since 2007 from companies involved with Iran including Royal Dutch Shell Plc, Cnooc Ltd., and Daelim Industrial Co., according to Chief Financial Officer Jeff Atwater.

Republicans say Obama's agreement won't prevent nuclear proliferation, and will unleash Iran's economy and its ability to support terrorism. Focusing on states gives the party another angle of attack.

"It enables them to take a stand against President Obama and, in the bargain, take a stand for the rights of the states," said Jack Pitney, a political science professor at Claremont McKenna College near Los Angeles.

The lifting of federal sanctions would allow a few U.S. aerospace companies to seek business in Iran, such as Boeing Co. and General Electric Co., according to a report from Bloomberg Intelligence. Overseas firms including Shell and BP Plc also could seek business there, it said. States shouldn't help, said Sarah Steelman, chairwoman of Defund Iran and a former Republican candidate for U.S. Senate in Missouri.

The governors, including presidential aspirants Bobby Jindal of Louisiana, New Jersey's Chris Christie, John Kasich of Ohio and Wisconsin's Scott Walker, point to a provision in the deal that says the federal government will "actively encourage" state and local officials to "take into account" U.S. policy lifting some sanctions.

"We intend to ensure that the various state-level sanctions that are now in effect remain in effect," the governors said in their Sept. 8 letter.

BY TRIBUNE NEWS SERVICE | SEPTEMBER 18, 2015

By Mark Niquette

With assistance from Darrell Preston in Dallas.

Illinois Forces Towns to Either Eat Higher Costs or Avoid Market.

Illinois's budget stalemate is leading investors to demand higher yields to lend to its towns and villages, causing bond sales to tumble while borrowers outside the state rush to capture the lowest interest rates in a generation.

The drop in issuance this year stands in contrast to the rest of the $3.6 trillion U.S. municipal market, where bond offerings are on pace to reach the highest level since at least 2002, according to data compiled by Bloomberg. Illinois is one of only five states where they've fallen: issuers have sold $8.4 billion of debt through Sept. 11, down from $9.9 billion a year earlier. It's the biggest decline nationwide.

When municipalities do borrow, investors are requiring higher yields because of the association with the state, said Tim McGregor, head of municipals at Northern Trust Corp. in Chicago.

Illinois, with the lowest credit rating of any state, has been without a budget since the year began on July 1 because of a political standoff. That's forcing Illinois to leave some bills unpaid and casting doubt over how it will close a $6.2 billion shortfall.

"You're definitely getting a little extra yield as an investor, even in credits that may not have a direct link to the state," said McGregor, who oversees $27 billion of state and local government securities.

The financial pressure on the local governments has been underscored by Chicago, whose credit rating was cut to junk by Moody's Investors Service in May because of the soaring bills the city faces from its underfunded employee pension funds. It isn't alone: Half of the state's local retirement systems have less than 60 percent of the assets needed to cover all the benefits due as workers retire, according to a commission created by the legislature.

Bond buyers will have their choice of two large deals from the state this week. The Metropolitan Pier and Exposition Authority, which runs Chicago's convention center, is selling $223 million of bonds

Wednesday.

OSF Healthcare System, a hospital operator, plans to offer $368 million of tax-free debt through the Illinois Finance Authority on Thursday.

McGregor said Illinois hospitals are being penalized for the state’s crisis.

“Health-care bonds in Illinois are probably trading 25 to 50 basis points cheaper, just because of the situation in Illinois, than they would be otherwise,” said McGregor.

There’s no sign of a resolution to the budget impasse, which has lasted longer than any in the state’s history, according to the Civic Federation, a Chicago-based research group. Republican Governor Bruce Rauner and the Democrat-led legislature can’t agree on how to fix a deficit left after temporary tax increases expired.

Illinois’s bills are piling up without a budget, with the unpaid tab set to reach $8.5 billion by the end of the year from $5.5 billion in August, state comptroller Leslie Geissler Munger said last week. The state is paying about 90 percent of what it owes even during the standoff, she said.

The budget delay has already dealt a blow to the Metropolitan Pier and Exposition Authority, which was unable to make a deposit into its debt-payment fund in July because lawmakers hadn’t appropriated the money.

While lawmakers approved the funds last month, the lapse caused Standard & Poor’s to lower the authority’s rating seven steps from AAA to BBB+, three ranks above junk.

OSF, which operates 10 Illinois hospitals, hasn’t felt a direct impact yet, said Dan Baker, its executive director of Treasury services. Proceeds from its sale will be used in part to finance construction and renovation at medical centers in Bloomington, Peoria and Rockford, offering documents show.

“Most of the investors we talk to understand the situation,” said Baker. “There’s been a little delay in payment at times, though it’s not too far behind right now — although it may be without the budget being approved.”

Catherine Kelly, a spokeswoman for Rauner, declined to comment on the increasing borrowing costs for Illinois agencies and municipalities. She said on Sept. 2 that the state was “being cautious about bond sales” and plans to issue some debt this year, though it hasn’t announced any details. Illinois 10-year general obligations yield 1.94 percentage points more than benchmark munis, near the most since late 2013, Bloomberg data show.

Investors penalized local borrowers even before the new fiscal year began as Illinois lawmakers dueled over the budget deficit. A school district in Rockford, 88 miles (142 kilometers) west of Chicago, issued $40 million of debt in February, with 20-year bonds priced to yield 4.17 percent, Bloomberg data show. That compared with a 3.21 percent rate on an index of similarly rated AA bonds.

Lake County, which borders Chicago’s home county to the north, sold $90 million of top-rated general obligations in June. The portion due in about 30 years priced to yield 4.05 percent, compared with 3.43 percent for an index of top-rated municipals.

“Some of their headlines have caused Illinois spreads outside of the state and Chicago to widen out, and there are a lot of very strong municipalities within the state of Illinois,” said Rick Taormina,

head of municipal strategies at J.P. Morgan Asset Management, which oversees $56 billion in state and local debt.

"We're looking to take advantage of that widening if it occurs."

Bloomberg News

by Brian Chappatta

September 14, 2015 — 9:01 PM PDT Updated on September 15, 2015 — 5:55 AM PDT

Muni Debt Could Be a Bond Market Haven After Fed Hikes.

If the last time the Federal Reserve raised interest rates is any guide, U.S. state and local government bonds will be a refuge for investors once policy makers bring the era of nearly free money to a close.

When the central bank began tightening monetary policy in 2004, the $3.6 trillion market returned 5.5 percent, about 2 percentage points more than Treasuries, according to Bank of America Merrill Lynch Indexes. As the increases continued over the next two years, municipals kept outperforming.

Standish Mellon Asset Management Co., Neuberger Berman and Citigroup Inc. are among the firms saying municipal debt is poised for another round of standout returns if the Fed starts raising interest rates as soon as Thursday. That's because the securities are owned largely by buy-and-hold investors looking for steady tax-exempt income, which buffers them from the volatility elsewhere in financial markets. Higher yields tend to make the bonds even more attractive to those buyers.

"On a relative basis, munis should perform well," said Christine Todd, president of Boston-based Standish, which has $27 billion of munis under management. "Whether you're a taxable investor or not, you're better off in munis."

The securities aren't immune to losses, and the market trailed Treasuries as the Fed boosted rates during the 1990s. Yet a slide in prices this year, which pushed up 10-year yields by a half percentage point since February, may protect the market if the central bank moves slowly to avoid derailing the economic recovery, analysts said. It's held its benchmark overnight lending rate near zero since late 2008.

"Whether they do it September or December, they're going to then take a step back and and watch and really make sure they haven't moved too soon and haven't done anything to throw this economy off its moorings," said James Iselin, head of the municipal fixed income team in New York at Neuberger Berman, which oversees about $9.3 billion of munis. "That is somewhat supportive."

State and local debt is relatively cheap by one measure: 10-year munis yield 2.28 percent, about the same as similar U.S. government debt, according to data compiled by Bloomberg. The yields on munis have averaged 97 percent of Treasuries over the past decade because, unlike U.S. debt, the income they generate is exempt from the federal income tax.

The securities have outperformed other investments amid speculation about when the Fed will act. Munis have returned 0.8 percent this year, according to Bank of America Merrill Lynch indexes, almost twice as much as Treasuries. U.S. corporate bonds have lost 0.8 percent, while the Standard

& Poor's 500 Index is down by almost 4 percent.

Vikram Rai, head of municipal strategy in New York at Citigroup, said in an Aug. 31 report that munis maturing in 10 years or longer may rally if the Fed raises rates Thursday, given that yields have already climbed in anticipation. A year after the Fed's first increase in 2004, he said, top-rated 10-year yields declined by 0.56 percentage point and the 30-year slid 0.8 percentage point.

"Fed actions are perversely bullish for long-dated bonds," Rai wrote.

Investors may also seek protection from turmoil in equity and commodity markets. That would draw cash into the market, which continued to pull in funds from individual investors after interest rates began rising in 2004, according to Fed figures.

"Within fixed income, municipals continue to offer less volatility and the unique advantages of tax-free income," New York-based BlackRock Inc. analysts led by Peter Hayes wrote in a report Monday.

Bloomberg News

by Romy Varghese

September 15, 2015 — 9:01 PM PDT Updated on September 16, 2015 — 6:01 AM PDT

Chicago's Met Pier Pays the Price of Illinois Fiscal Stalemate.

Chicago's Metropolitan Pier and Exposition Authority, which runs the nation's largest convention center, is discovering the price of Illinois's political paralysis.

The authority sold about $220 million of federally tax-exempt securities Wednesday for yields of as much as 6 percent, according to preliminary data compiled by Bloomberg. Thirty-year bonds are being offered at 4.87 percent, about 1.6 percentage points more than top-rated securities.

It's the agency's first offering since skipping a July payment into its debt-service fund because lawmakers and Governor Bruce Rauner didn't appropriate the money amid a deadlock over the budget. As a result, Standard & Poor's slashed the authority's rating by seven steps from AAA to BBB+, three grades above junk.

The lapse highlighted the risk to investors from bonds with debt bills that depend upon the approval of lawmakers. While Rauner signed a bill last month to free up tax money for Met Pier, the agency's bonds haven't rebounded from the rout that followed the missed deposit.

"The downgrade, which resulted from the budget impasse, hurt them in terms of interest costs," said Alan Schankel, a managing director at Janney Montgomery Scott LLC in Philadelphia. "Investors realize probably it's a lot better than a BBB credit, but because of what's happened and because of the appropriation nature, it's a BBB and not much you can do."

Met Pier is among borrowers most affected by the impasse between the Republican governor and the Democrat-led legislature that's left Illinois without a budget for more than two months. The failure had led investors to push the difference between Illinois bond yields and top-rated debt near a record high.

Met Pier bonds maturing in 2050, its most actively exchanged securities, traded for an average of

100 cents on the dollar Wednesday, down from $1.02 on Aug. 4, the day before the rating cut. That's pushed the yield up about half a percentage point to 5 percent.

The securities offering is the authority's first since 2012, according to data compiled by Bloomberg, and illustrated how it's being penalized by investors. In 2012, its 30-year bonds were sold for yields as low as of 4.15 percent, about a percentage point more than top-rated debt at the time. That gap swelled to 1.6 percentage point Wednesday.

The proceeds will help pay for the construction of a 40-story hotel and refinance debt, bond documents show. The securities included zero-coupon bonds, which were offered at a top yield of 6 percent for those maturing in 2052.

"This transaction will lock up the financing" for the authority's projects, said Richard Oldshue, Met Pier's chief financial officer. He declined to comment on what kind of reception he's expecting for the deal.

Fitch Ratings gave the bonds a BBB+ rating, three steps above junk, with a negative outlook. The company said Met Pier's ability to make "full and timely" debt service depends on the Illinois General Assembly to appropriate the revenue, which ties the authority's credit to Illinois, the worst-rated state in the nation.

Met Pier never missed any interest or principal payments to investors and the agency now has the authority to tap tax money to cover its debts. The bonds are backed by authority taxes and state sales taxes. The authority taxes, which includes levies on hotels, reached $140.2 million in 2015, up 42 percent from 2010, bond documents show.

"This is still a solid credit backed by the economic activity in the city of Chicago in terms of sales taxes and hotel taxes — and all our indications are that business is booming in Chicago," said Paul Mansour, head of municipal research in Hartford, Connecticut, at Conning, which oversees $11 billion in state and local-government securities, including those sold by Met Pier. "It creates a buying opportunity for people willing to take the longer view."

Bloomberg News

by Elizabeth Campbell

September 16, 2015 — 12:00 AM PDT Updated on September 16, 2015 — 1:55 PM PDT

Drivers Decry Rise of Toll Lanes as Texas's LBJ Expressway Opens.

The 13 miles of rebuilt Interstate 635 in North Dallas offer something for everyone: express lanes for those who want to pay to bypass traffic, toll-free lanes for those who don't, no maintenance costs for the state and, officials hope, less congestion.

For investors in $615 million of private activity bonds sold for part of the $2.7 billion cost of the highway, also known as LBJ after former President Lyndon B. Johnson, all that matters is whether enough drivers use the express lanes to pay principal and interest coming through 2040. The road, which re-opened last week, is one of a handful in the country that charges tolls that adjust based on traffic volume, assuring those willing to pay as much as $9 during peak times to move quickly on a road that was once a parking lot at rush hour.

“The biggest risk from our perspective is the amount of traffic it will carry,” said Robert Amodeo, head of municipals for Western Asset Management Co., which has $452.5 billion under management, including LBJ bonds. “How many cars are going to jump on the road during peak pricing?”

The opening, which came ahead of schedule and below budget, will test a partnership between government and the private sector. The project only cost the state $496 million from gas tax collections, allowing it to improve traffic flow in a congested corridor nearly a decade earlier that it would have otherwise. But the tolling has sparked anger by some residents tired of seeing roads that were once free now have tolls.

“It’s offensive to make us pay to use roads that are being built with our tax dollars,” said Terri Hall, founder of Texans Uniting for Reform and Freedom, in San Antonio, which opposes new toll roads. “They’re letting a private company decide who gets to travel fast and who doesn’t.”

The new highway has four free lanes, as it had previously, in each direction, but in its new configuration it has two or three tolled express lanes each way. It’s those lanes that will pay back investors, cover maintenance costs and, officials said, reduce congestion for drivers who don’t want to use the tolled lanes.

The highway, part of a loop around Dallas, cuts a swath across the top of the city, linking businesses such as Texas Instruments Inc. and Brinker International Inc., parent of Chilli’s Bar & Grill, the Galleria Dallas and some of the city’s wealthiest neighborhoods. The highway is a crossroads for people heading to Dallas-Fort Worth International Airport and downtown.

Equity Investors

“Dynamic pricing gives users a choice of paying extra to cruise through or not pay,” said Michael Wilson, director of transportation for the North Central Texas Council of Governments. “The LBJ model is being looked at as the way to go because there isn’t enough money to build all the roads needed.”

The company that has been rebuilding the highway and will operate and maintain it is LBJ Infrastructure Group LLC, owned by the private-equity investors: Cintra Infraestructuras S.A., Meridiam Infrastructure Finance S.à.r.l. and the Dallas Police and Fire Pension System. The equity investors put $665 million into the deal. The rest of the financing comes from a $850 million Transportation Infrastructure Finance and Innovation Act loan from the Federal Highway Administration.

The tolls will generate revenue to repay bond holders, the federal loan and the private equity investors over the 52-year life of the agreement.

Failed Projects

Sometimes public-private projects don’t work out so well. For many failed highway projects, including some privatized toll roads, the cause is a lack of traffic. ITR Concession Co., operator of the Indiana Toll Road, sought to reorganize in bankruptcy last year after dwindling traffic undermined its $3.8 billion bet on a 75-year lease of the road. South Bay Expressway, a 10-mile toll road near San Diego, and the 16-mile Southern Connector in Greenville County, South Carolina, each filed for bankruptcy in 2010 after experiencing low traffic.

So far during construction of LBJ, the bonds have performed well, said Bill Delahunty, Boston-base director of municipal research for Eaton Vance Management, which also owns the bonds. Initially

priced in 2010 with tax-exempt yields of more than 7 percent, the series maturing in 2040 traded Sept. 15 at 17 percent over par. The bonds were initially priced at almost 3 cents under par.

Cash Flow

“This has been an absolute home run so far,” said Amodeo.

Over the life of the securities, the net cash flow available for payments on the bonds and the federal loan, after other expenses, is projected to increase to about $624 million in 2040 from an estimated $96 million in 2016, according to bond documents. Traffic is expected to increase 36.7 percent in that period, according to feasibly study by Arup North America Ltd.

Since the early 1990s and until construction began, most segments of the highway have carried more than 200,000 cars per day through North Dallas, according to data contained in bond documents.

“This is a very congested area,” said Delahunty. “The Dallas-Fort Worth area is doing very well from a demographic standpoint.”

Bloomberg News

by Darrell Preston

September 16, 2015 — 9:00 PM PDT Updated on September 17, 2015 — 6:42 AM PDT

Wayne County's $200 Million Debt for Jail Fiasco Audited by IRS.

The U.S. Internal Revenue Service is auditing $200 million of bonds that built an unfinished jail in Wayne County, Michigan, seeking to determine whether to revoke federal subsidies given to the cash-strapped government.

Wayne County, which includes Detroit, sold the federally taxable debt in December 2010 to build a new jail, only to shut down the project in the middle of construction about three years later because of cost overruns. The U.S. Treasury pays 45 percent of the interest under a program aimed at spurring development in economically distressed areas.

The IRS told the county it is scrutinizing the bonds “because of information we received from external sources or developed internally that causes a concern that the debt issuance may fail one or more provisions” of the tax code, according to a Sept. 9 filing with the Municipal Securities Rulemaking Board.

A move to revoke the subsidies could foist added costs on Wayne County, which is already operating under state oversight to avoid bankruptcy after years of budget deficits. The county has received $36.9 million in tax credits so far for the ill-fated project, according to the filing, and spends about $14 million a year on debt service for the securities.

The IRS could put a stop to the credits or seek to recoup subsidies if the county ran afoul of U.S. tax law. That could affect its ability to pay debt service on the jail bonds or other obligations, according to the filing. The county said it can’t determine “at this time” whether this audit will lead to a loss of funds.

Wayne is cooperating with the IRS, said James Canning, a county spokesman. Some of the money raised by the bond issue hasn't been spent and is held in the project fund, he said.

"Nothing has come to our attention which suggests that bond usage was non-complaint," Canning said in an e-mail. "Wayne County is cooperating with the IRS and believes that it is in full compliance with all tax requirements."

The disclosure of the audit hasn't affected the price of the bonds. A portion of the securities maturing in 2040 traded Wednesday at an average of 87 cents on the dollar to yield 11.6 percent, little changed from Sept. 8, the day before the filing.

Bloomberg News

by Elizabeth Campbell

September 17, 2015 — 9:16 AM PDT

Pennsylvania Bond Penalty Grows as State Budget Impasse Deepens.

Pennsylvania is facing rising penalties from investors as Democratic Governor Tom Wolf plans to veto a temporary budget being advanced by Republican legislators, promising to prolong a political impasse that's left the state without a spending plan for more than two months.

The state's 10-year bonds yield about 2.87 percent, about 0.59 percentage point more than benchmark municipal debt, according to data compiled by Bloomberg. That's approaching the 0.61 percentage point reached in July, which was the highest since the data begin in 2013.

"Each week and each month where they don't have a budget, that concern will increase," said Alan Schankel, a managing director at Janney Montgomery Scott LLC in Philadelphia. "They're playing a game of chicken."

Pennsylvania has been operating without a spending plan for the year that began in July because the Republican-led legislature and first-term governor have remained at loggerheads over proposed tax increases and overhauls to the public employee pension system.

The uncertainty led Moody's Investors Service last week to downgrade schools that issue debt through a state program that diverts aid to investors when needed.

The Pennsylvania Senate on Thursday is set to vote on a short-term budget that would provide state and federal funds to alleviate pressures on school districts and social service agencies.

Wolf told reporters Wednesday that he would veto the temporary spending plan because he wants them to consider his proposals for the full budget and concessions on the retirement system. He said the failure to compromise and balance the budget could imperil Pennsylvania's credit rating.

"We're going to continue to have the credit downgrades we've had because we're not doing anything else differently than we've done," Wolf said. "It's status quo."

The state's $53 billion unfunded pension liability has weighed on its bonds. The Keystone State is paying more to borrow than any other state except Illinois and New Jersey, according to data on 20 major states compiled by Bloomberg.

Standard & Poor's and Fitch Ratings cut Pennsylvania's rating last year to AA-, the fourth-highest level, citing the pension burden. Moody's grades Pennsylvania Aa3, also the fourth-highest rank.

Bloomberg News

by Romy Varghese

September 17, 2015 — 9:59 AM PDT

Bloomberg Brief Weekly Video - 09/17/15

Taylor Riggs, an editor at Bloomberg Brief, talks with reporter Kate Smith about this week's municipal market news.

Watch the video.

September 17, 2015

Puerto Rico Electric at Odds With Insurers on Debt Agreement.

The debt-restructuring agreement Puerto Rico's main electric utility unveiled with great fanfare at the start of the month is turning out to be far from a done deal.

The Puerto Rico Electric Power Authority, known as Prepa, still needs to come to terms with about two-thirds of creditors, including bond-insurance companies, or the agreement falls apart. An accord that keeps the negotiations out of court expires late Friday. All forbearing creditors except insurer MBIA Inc. are part of that contract, called a forbearance agreement.

"They still have to do quite a bit of work," said Mikhail Foux, a municipal-debt strategist at Barclays Plc in New York. "They have only about a third of the people on board. We're talking about monolines and bond funds that effectively bought at par."

The utility reached a tentative agreement on Sept. 1 with bondholders including OppenheimerFunds Inc., Franklin Advisers Inc., BlueMountain Capital Management and Goldman Sachs Group Inc. Investors agreed to take losses of about 15 percent under a debt exchange. Prepa, which has about $8.3 billion in debt, has been negotiating with creditors for over a year after saying it needed to reduce its obligations.

Some bondholders bought Prepa securities for as low as 33 cents on the dollar, giving them room to accept less than par. Bond insurers would have to make investors whole on any deferred payments or potential haircuts, making them less inclined to accept concessions, Foux said.

Forbearance Agreement

A Prepa restructuring would be the biggest ever in the $3.6 trillion municipal-bond market, surpassing Detroit's record bankruptcy filing in July 2013. The utility, which relies mainly on oil to produce electricity, is the largest U.S. public power provider, with 1.47 million customers and $4.68 billion in electric revenue in 2013, according to the American Public Power Association.

The utility has asked creditors to extend the forbearance agreement by two weeks, according to two people with direct knowledge who asked for anonymity because the talks are private. It first signed the pact in August 2014 with bondholders, banks and insurers after the agency used its capital budget to pay for fuel. Its been extended seven times.

Bond insurers Assured Guaranty and MBIA last week offered a proposal that doesn't include exchanging insured Prepa debt at a discount, according to a person with direct knowledge of the proposal. That would fit into the tentative plan with forbearing bondholders, the person said, without elaborating. Prepa has yet to respond to the proposal, the person said.

Greg Diamond, a spokesman for MBIA, Ashweeta Durani, a spokeswoman for Assured, and Michael Corbally a spokesman at Syncora Guarantee Inc. declined to comment.

Jose Echevarria, a spokesman in San Juan for Prepa, and Jenni Main, chief financial officer at Millstein & Co., an adviser on the utility's restructuring, declined to comment.

Governor Alejandro Garcia Padilla visited Washington this week as the island seeks to reduce its $72 billion debt load and delay payments to bondholders. A commonwealth agency, the Public Finance Corp., defaulted in August and September on debt payments, the first for a Puerto Rico entity. The administration plans to give commonwealth investors a debt-restructuring offer in a few weeks, after saying the government has only an estimated $5 billion to repay $18 billion of principal and interest coming due in the next five years.

After meeting with Garcia Padilla Thursday, U.S. Treasury Secretary Jacob J. Lew reiterated his support for legislation in Congress that would allow some Puerto Rico public corporations to file for bankruptcy.

"Given the commonwealth's projection that it will exhaust its liquidity later this year, Congress must act now to provide Puerto Rico with access to a restructuring regime," Lew said in a statement Thursday.

"Without federal legislation, a resolution across Puerto Rico's financial liabilities would likely be difficult, protracted, and costly."

Prepa bond prices show the difficulty the utility faces in reaching an agreement with creditors, Foux said.
Bonds maturing July 2040 traded Thursday at an average 60.1 cents on the dollar, according to data compiled by Bloomberg. That's higher than an average 53.5 cents on Aug. 28, the last time the bonds traded before the Sept. 1 agreement. But that's still lower than the 85 cents that bondholders would receive in a proposed debt exchange.

Legacy Debt

"One of the reasons they're trading substantially lower is that there's still quite a bit of an execution risk," Foux said.

Puerto Rico may ask holders of its general-obligation bonds and sales-tax debt, called Cofina, to take losses, and Prepa could again look to its investors if the proposed debt-exchange fails to improve the utility's finances, Matt Fabian, a partner at Concord, Massachusetts-based Municipal Market Analytics, wrote in a Sept. 14 report. That plan would swap existing bonds for new securitized debt repaid with a utility-customer surcharge.

"There is reasonably a risk that the commonwealth and/or Prepa would entertain a similar path

should Prepa's restructuring fail to be enough to achieve fiscal solvency," Fabian said.

Investors who haven't participated in the forbearance, such as individual bondholders and some municipal-bond funds, would also need to exchange their securities for new bonds, leaving no more than $700 million of legacy debt remaining, according to the agreement.

MBIA's National Public Finance Guarantee Corp. insures about $1.4 billion of Prepa debt, while Assured Guaranty backs $904 million, according forbearance documents. Syncora Guarantee Inc. insures $197 million.

Those firms must also take into consideration their exposure across all Puerto Rico securities. Assured guarantees $6.2 billion of Puerto Rico debt through 2047, as of June 30. National insures $4.5 billion through 2046, as of June 30.

"If monolines agree to some haircuts here, what would that mean for them with the rest of the bond stack?" Foux said.

Puerto Rico securities have lost 7.2 percent this year through Sept. 17, according to S&P Dow Jones Indices. The broader muni market has gained 0.9 percent.

Bloomberg News

by Michelle Kaske

September 17, 2015 — 3:47 PM PDT Updated on September 18, 2015 — 8:13 AM PDT

Possible Impact of a Fed Rate Hike on Municipal Bonds.

Bloomberg's Kate Smith reports on Fed policy and municipal bonds. She speaks on "Bloomberg Markets."

Watch the video.

September 17, 2015

Moody's: U.S. FY 2014 NFP Hospital Medians Show Stronger Profitability Margins and Revenue Growth.

New York, September 11, 2015 — The median annual revenue growth rate for not-for-profit hospitals and health systems in fiscal 2014 broadly surpassed the median expense growth rate, which reverses a two-year trend of expense growth outpacing revenues, Moody's Investors Service says in its annual medians for US NFP hospitals and health systems, "Strong Business Conditions Bolster Profitability and Growth, Moderating Fundamental Sector Risks."

"Notably, the spread in these growth rates is at a historic high," report author and Moody's VP — Senior Credit Officer Beth Wexler says. "The median annual revenue growth was 5.2%, while median expense growth was 4.6% in 2014."

Consolidation in the NFP sector, enrollment on the public health exchanges, and Medicaid expansion combined with generally favorable patient demand trends fueled the increase in revenues.

Moody's anticipates these favorable trends to continue in 2015 and into 2016, and supports Moody's stable outlook for the industry.

Balance sheets strengthened in 2014, with a 10% median growth in unrestricted cash and investments and a median decline in total direct debt of almost 2%. The median unrestricted cash and investments increased to $340 million in 2014 from $312 million in 2013.

However, the regional 2014 medians reveal varying market demographics, legislative oversight and strategic initiatives have resulted in a divergence of financial performance medians among the four US regions.

"The Northeast's performance is most striking, owing to its flat median operating cash flow margin, and reflects the difficult environment in which it operates," says Wexler in a related medians report, "Regional Hospital Medians Show Historically Weaker Financial Performance in the Northeast."

The Midwest has a history of consolidation and physician alignment which supports its high growth rates, over 18% in median absolute cash flow, well above the rest.

In the West, strong investment returns and robust profitability facilitated growth in liquidity, while the South reports the highest level of self-pay & other in the payor category.

The reports are available to Moody's subscribers here.

Fitch: Bill Could Challenge Some CA Public Power Utilities.

Fitch Ratings-New York-15 September 2015: California's public power utilities could face additional financial pressure over the medium to long term following the state legislature's passage of SB 350, Fitch Ratings says. The Clean Energy and Pollution Reduction Act of 2015 includes a number of provisions that are expected to increase direct costs for public power utilities. The bill's more notable provisions include an increase of the state's renewable portfolio standard (RPS) to 50% by 2030 and additional efficiency and conservation programs. Utilities have already begun to transition their power supplies toward lower emission resources due to other state regulations, including a RPS of 33% by 2020.

Fitch expects compliance with the more stringent environmental regulation will require the state's public power utilities to transition an even greater portion of their power supply to less flexible and potentially more costly renewable energy. Rate flexibility and the ability to preserve financial metrics in the face of these regulatory changes will be fundamental to maintaining long-term credit quality.

The higher RPS requirement will be phased in over a 10-year period, with utilities mandated to reach interim targets of 40% by 2024, 45% by 2027 and 50% by the end of 2030. This significant increase in renewable energy will push public power utilities to identify and acquire resources that are generally more expensive and less flexible than thermal resources. Positively, the bill allows for the indefinite banking of certain resources beginning in 2021, which will allow those utilities that exceed their annual target to roll over credits toward future compliance years.

SB 350 is expected to be signed into law as the bill conforms in large part to the governor's previously stated objectives of raising the RPS to 50% and reducing greenhouse gas emissions to 40% below 1990 levels by 2030.

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Fitch: Sea Level Rise May Challenge Some Local U.S. Governments.

Fitch Ratings-New York-16 September 2015: The rise in sea levels already impacts some communities and, in the long term, may pressure some local governments' operations, capital funding requirements and indebtedness, says Fitch Ratings. Such risks include heightened damage from episodic events such as hurricanes and storm surges (event risks) in addition to more chronic damage from pervasive flooding and permanent loss of land. Further, citizens living in flood plains are facing higher federal flood insurance rates.

Revised zoning ordinances are evolving that may impose coastal or low-lying development moratoriums or mandate modifications to existing housing to better withstand expected storm surges. These developments will change the nature of shoreline development and may negatively affect local government operations as home owner cost increases and restrictions on new development place limits upon taxable resource growth.

To date, the sea level rise has not played a material role in Fitch's assessment of the fundamental credit characteristics of any of its rated issuers. Fitch's special report, "Event Risk and Overall Credit Resiliency," dated December 2014, provides more detail. However, there are real threats faced by governments in coastal areas. As the effects of sea level rise upon issuers' credit fundamentals become known and measurable, over time, these considerations may take on greater importance as a credit factor in Fitch's rating decisions.

For more information, see latest Fitch Wire+ research on this topic.

NASACT and Deloitte Release 2015 Digital Government Transformation Survey.

View the Report.

NFMA Introduction to Municipal Bond Credit Analysis.

The National Federation of Municipal Analysts Introduction to Municipal Bond Credit Analysis registration is now open.

The course will be held at Le Meridien in Philadelphia on November 12 & 13, 2015.

The NFMA has offered this course annually since 1987. This year's course has been revamped, but attendees can still expect to be provided with an overview of the critical information to perform credit analysis on a variety of sectors. While traditionally an offering for those new to analysis, the course has also been used as a refresher to more seasoned analysts over the years.

Program link.

Register online.

MSRB to Create Investor Advisory Group.

Alexandria, VA – The Municipal Securities Rulemaking Board (MSRB) today announced that it will establish an investor advisory group to provide the MSRB's Board of Directors with additional expertise on municipal market practices, transparency and investor protection issues.

"The creation of an investor advisory group will provide the Board of Directors with a formal mechanism for accessing the expertise of active municipal investors," said MSRB Board Chair Kym Arnone. "As the Board considers significant market structure proposals, we can ensure that our deliberations include the perspectives of a broad investor group."

The MSRB Board earlier requested comment on a proposal to modify the application of the standard of independence for the one public member of the board designated to represent institutional or retail investors in municipal securities. The goal of the proposal was to allow the MSRB to identify an investor representative with significant knowledge of the municipal securities market from a broader group of applicants. The Board determined not to pursue changes to the rule regarding the standard of independence at this time.

"We are satisfied that the creation of the advisory group will address our current concerns and provide an excellent way for us to access the knowledge of experienced municipal securities investors," Arnone said.

Names of members of the investor advisory group will be announced at a later date.

Date: September 17, 2015

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- NFMA Releases Final Best Practices for State GO Bond Disclosure After Public Comment.
- SEC Asks: Should Muni Bond Pricing Change in Wake of Edward Jones?
- MSRB: Best-Ex Rule Will Not Be Implemented Before Release of Guidance.
- BDA Submits Letter to SEC on MSRB Proposed Rule G-42 Regarding the Core Duties of Municipal Advisors.
- Hedge Funds Fill Gap in the U.S. Municipal Bond Market.
- Bond Ruling Emboldens Abusive Scheme, Former IRS Official Says: Tax Analysts
- *Emmet & Co., Inc. v. Catholic Health East* – Appeals court holds that issuer's coupling of tender offer with redemption of municipal bonds, as well as issuer's synthetic sale of bonds to financial advisor through total return swap, violated indenture.
- And finally, "Now Where Did I Leave My Keys?" is brought to us this week by *Caramanno v. City of New York*, in which a paving contractor sued the city after it relocated, and subsequently destroyed, an item of contractor's personal property. The item, you ask? A steam roller. An honest-to-god steam roller. Answers to the absolutely dumfounding questions regarding how one might possibly misplace, relocate, or destroy such an item are far, far beyond the purview of this publication. Our deepest apologies.

EMINENT DOMAIN - CALIFORNIA

Rancho de Calistoga v. City of Calistoga

United States Court of Appeals, Ninth Circuit - September 3, 2015 - F.3d - 2015 WL 5158703

Owner of mobile home park filed petition for writ of administrative mandamus against city and administrative hearing officer, asserting regulatory takings and separate "as-applied private takings" challenges to city's mobile home rent control ordinance, as well as due process and equal

protection claims against officer. The United States District Court granted city's motion to dismiss. Owner appealed.

The Court of Appeals held that:

- Owner's claims were ripe;
- Even if owner's claims were construed as an as-applied attack, no regulatory taking occurred here;
- Owner's self-styled "private takings claim" was not a separately cognizable claim but, rather, was part of its larger regulatory takings claim, which, viewed in this context, failed; and
- Officer's decision, rejecting owner's rent-increase application, did not violate equal protection.

BONDS - CALIFORNIA

City of Petaluma v. Cohen

Court of Appeal, Third District, California - July 30, 2015 - 238 Cal.App.4th 1430 - 190 Cal.Rptr.3d 703 - 15 Cal. Daily Op. Serv. 8389 - 2015 Daily Journal D.A.R. 8699

City brought a petition for a writ of mandate, seeking an order to require the Department of Finance (DOF) to approve expenditures for an interchange and roadway under-crossing that had been approved by the city's redevelopment agency prior to the redevelopment agency's dissolution. The Superior Court denied the petition. City appealed.

The Court of Appeal held that:

- City's planned expenditures were not an "enforceable obligation" under redevelopment agency dissolution law;
- DOF's disapproval of expenditures did not violate the covenant of good faith; and
- DOF's disapproval of expenditures did not result in an unconstitutional impairment of city's contract rights.

City's planned expenditures for an interchange and roadway under-crossing that had been approved by the city's redevelopment agency prior to the redevelopment agency's dissolution were not "payments required under the indenture" and thus were not an "enforceable obligation" under the redevelopment agency dissolution law, even if city's failure to use its bond proceeds for the roadway project would result in the bond losing tax-exempt status and the interest rate on the bonds being increased, where nothing in the language of the first supplement to indenture required that the roadway project actually be funded or constructed, absent evidence of whether the indenture itself contained such a requirement.

The provision of the redevelopment agency dissolution law requiring a redevelopment agency, until a successor agency is authorized, to preserve the tax-exempt status of interest payable on outstanding agency bonds did not preclude the Department of Finance (DOF) from disapproving items on a recognized obligation payment schedules (ROPS) submitted by a redevelopment agency's successor agency.

Department of Finance's (DOF) disapproval from city's recognized obligation payment schedules (ROPS) of expenditures for an interchange and roadway under-crossing that had been approved by the city's redevelopment agency prior to the redevelopment agency's dissolution did not violate the covenant of good faith in the first supplement to indenture, even if the failure to use bond proceeds to fund the roadway project would result in the loss of tax-exempt status and defeasance of the bonds, where those two potential consequences were expressly provided for in the supplement.

Department of Finance's (DOF) disapproval from city's recognized obligation payment schedules (ROPS) of expenditures for a bond-funded interchange and roadway under-crossing that had been approved by the city's redevelopment agency prior to the redevelopment agency's dissolution did not result in an unconstitutional impairment of city's contract rights in impairing the security of the bonds, where city was not a bondholder, absent evidence of a "present, specific and substantial impairment."

ANNEXATION - INDIANA

American Cold Storage NA v. City of Boonville

Court of Appeals of Indiana - August 28, 2015 - N.E.3d - 2015 WL 5081405

Landowners who owned property in annexed territory brought declaratory judgment action and written remonstrance, asserting that city's annexation should not take place. The Superior Court entered partial judgment in favor of city on city's motion to dismiss and determined landowners had standing to pursue declaratory judgment action. City brought interlocutory appeal.

The Court of Appeals held that:

- Evidence supported finding that over 60 percent of the territory was subdivided, and
- Evidence supported conclusion that territory was both "needed" and "can be used" in the reasonably near future.

In determining whether territory had been sufficiently subdivided to permit annexation by municipality, trial court properly refused to limit the definition of "subdivided" to parcels of land that had actually gone through process set forth by county subdivision control ordinance, in finding that 60 percent of annexation territory was subdivided as required by annexation statute.

Evidence supported trial court's conclusion in bench trial that city had met its statutory burden that annexation territory was both "needed" and "can be used" for city's development in the reasonably near future. City needed the annexation territory to be able to grow and attract new business, city had plans for bringing new development to the territory, including sewer services and a major transportation linkage, and city provided fire protection an police patrols to the territory.

FORUM SELECTION - NEW MEXICO

Presbyterian Healthcare Services v. Goldman, Sachs & Co.

United States District Court, D. New Mexico - August 14, 2015 - F.Supp.3d - 2015 WL 4993571

On February 10, 2014, Presbyterian Healthcare filed a claim against Goldman Sachs with the Financial Industry Regulatory Authority ("FINRA") Division of Arbitration in New Mexico. The claim alleged the standard-issue ARS claims.

Goldman Sachs challenged the arbitrability of the matter, citing the forum selection clause (and the attendant broad merger clause) in the parties' Broker-Dealer Agreement. Goldman Sachs moved to transfer the case to the United States District Court for the Southern District of New York. Presbyterian Healthcare argued that Goldman Sachs was required to arbitrate pursuant to a written agreement it entered into when it became a FINRA member.

Presbyterian Healthcare contended its grievances arise from Goldman Sachs' role as an advisor, and thus its arbitration claims related to transactions not contemplated exclusively by the Broker–Dealer Agreement.

The District Court concluded that:

- Presbyterian Healthcare's claims 'arise out of' the Broker–Dealer Agreement, because the claims concern Goldman Sachs' actions pursuant to that agreement; and
- Goldman Sachs' motion to transfer the case to the United States District Court for the Southern District of New York would be granted.

BONDS - NEW YORK

Emmet & Co., Inc. v. Catholic Health East

Supreme Court, New York County, New York - August 28, 2015 - N.Y.S.3d - 2015 WL 5122314 - 2015 N.Y. Slip Op. 25293

Holders of municipal bonds filed putative class action against issuer, claiming breach of contract and breach of duty of good faith and fair dealing based on issuer's coupling of tender offer with redemption of bonds that allegedly violated trust indenture governing bonds, after issuer defeased bonds so that issuer no longer had any payment obligations but bonds remained callable by compelling holders to sell their bonds to issuer at price set forth in indenture. Issuer moved to dismiss for failure to state claim, and holders moved for partial summary judgment on liability.

The Supreme Court, New York County, held that:

- Coupling of tender offer with redemption of bonds breached indenture;
- Issuer's synthetic total return swap with financial advisor breached indenture;
- Breach of covenant of good faith and fair dealing claim was duplicative; and
- Award of punitive damages was not warranted.

Issuer's coupling of tender offer with redemption of municipal bonds issued to refinance hospital's debt and subsequently defeased by issuer but remaining callable was impermissible under trust indenture provision, allowing issuer to redeem any percentage of outstanding bonds, but requiring issuer to randomly select which bonds to redeem if less than 100% of bonds were redeemed, where tender offer allowed bondholders to either tender their bonds at 101% or see them redeemed at 100% of bonds' principal amount, and issuer redeemed only 45% of non-tendered bonds after other 55% were tendered, so issuer effectuated non-random redemption of less than 100% of bonds by excluding its own tendered bonds from redemption.

Issuer's synthetic sale of municipal bonds to financial advisor through total return swap, after impermissible non-random redemption of bonds by coupling tender offer with redemption, was prohibited under trust indenture, providing that all bonds "paid, redeemed or purchased, either at or before maturity, when such payment, redemption or purchase is made, shall thereupon be cancelled by the Trustee and shall not be reissued but shall thereupon be destroyed by the Trustee," since bonds had to be cancelled and could not be resold once acquired by issuer.

Bondholders' claim for breach of implied duty of good faith and fair dealing by issuer of municipal bonds was duplicative, after holders prevailed on their express breach of contract claim against issuer regarding trust indenture that governed bonds, since breach of implied covenant was intrinsically tied to damages resulting from breach of indenture.

Issuer's coupling of tender offer with redemption of municipal bonds that resulted in non-random redemption and subsequent synthetic total return swap with financial advisor, in breach of trust indenture, did not justify award of punitive damages, since issuer's conduct was not intentional, deliberate, fraudulent, or conducted with evil motive, and even if intentional, controversy was between highly sophisticated financial professionals who disagreed about complex issues without clear precedent to guide them.

LIABILITY - NEW YORK

Caramanno v. City of New York

Supreme Court, Queens County, New York - September 3, 2015 - N.Y.S.3d - 2015 WL 5166177 - 2015 N.Y. Slip Op. 25301

Paving subcontractor brought action against city, city department of sanitation, and owner of junkyard after department removed subcontractor's legally parked steam roller following completion of paving work and subsequently sent it to junkyard, where it was destroyed. City and department moved for summary judgment.

The Supreme Court, Queens County, held that:

- Genuine issue of material fact as to whether department's actions were discretionary or ministerial precluded summary judgment, and
- Even if department engaged in ministerial act, subcontractor adequately alleged that it had special relationship with city and department, giving rise to a special duty supporting imposition of municipal liability.

Even if city department of sanitation engaged in ministerial act when it removed paving subcontractor's legally parked steam roller following completion of paving work and subsequently sent it to junkyard, where it was destroyed, subcontractor adequately alleged that it had special relationship with city and department, giving rise to a special duty supporting imposition of municipal liability. Subcontractor alleged that defendants affirmatively acted on its behalf by assuming control of its vehicle, that it had direct contact with department's employees, and that it detrimentally relied on employees' representations that department did not have the roller.

ANNEXATION - NEW YORK

Commandeer Realty Associates, Inc. v. Allegro

Supreme Court, Orange County, New York - August 18, 2015 - N.Y.S.3d - 2015 WL 4920070 - 2015 N.Y. Slip Op. 25276

Property owners commenced Article 78 proceeding seeking writ of prohibition temporarily restraining three municipalities from taking any action on two petitions to annex territory that overlapped with territory proposed for annexation in another municipality's prior annexation petition, on grounds that municipalities lacked jurisdiction to entertain those two petitions, under prior jurisdiction rule, pending final determination of prior petition, and also claiming two petitions were filed for illegitimate purpose of attempting to block prior petition. Municipalities asserted counterclaims and cross-claims for declaratory relief. Individual signatories to two petitions moved to dismiss.

The Supreme Court, Orange County, held that:

- Owners had standing to maintain Article 78 proceeding;
- Writ of prohibition was available for jurisdictional claim;
- Writ of prohibition was not available for illegitimacy claim;
- Article 78 proceeding was ripe;
- In matter of first impression, prior jurisdiction rule applies to municipal annexation proceedings; and
- Prior jurisdiction rule barred processing of two later-filed petitions.

ELECTIONS - OHIO

State ex rel. Morris v. Stark Cty. Bd. of Elections

Supreme Court of Ohio - September 9, 2015 - N.E.3d - 2015 WL 5255463 - 2015 -Ohio-3659

Challengers filed writ of prohibition to prevent Secretary of State and county board of elections from placing mayoral candidate on ballot as an independent candidate.

The Supreme Court of Ohio held that:

- Secretary acted within his discretion in determining that candidate had established a conforming residence within city, and
- Evidence supported finding that candidate had disaffiliated from political party.

Secretary of State acted within his discretion in concluding that mayoral candidate established a conforming residence within city, even though candidate ultimately spent only four consecutive nights at that residence before moving to another residence within city. Candidate moved into first residence without knowing when second residence would become available, and candidate had intended to reside at first residence indefinitely.

Evidence supported finding that mayoral candidate who wished to run as an independent candidate had disaffiliated from political party of which he had been a member, even though candidate did not resign his seat on county board of commissioners. Seats on county board were not assigned by political affiliation, and candidate took affirmative steps to resign from political party.

PENSIONS - OREGON

Moro v. State

Supreme Court of Oregon - April 30, 2015 - 357 Or. 167 - 351 P.3d 1

Active and retired members of the Public Employee Retirement System petitioned for judicial review of legislation aimed at reducing the cost of retirement benefits, which eliminated income tax offset benefits for nonresident retirees and modified the cost-of-living adjustment.

The Supreme Court of Oregon held that:

- Tax offsets were not contractual as required for their repeal to violate Contract Clause;
- Cost-of-living adjustment requirement was a term of the Public Employee Retirement System benefit offer;

- Public employers could revoke offer of cost-of-living adjustment to Public Employee Retirement System benefit for future work without violating the state Contract Clause, abrogating *Oregon State Police Officers' Ass'n v. State of Oregon*, 323 Or. 356, 918 P.2d 765;
- Legislation reducing cost-of-living adjustment cap and bank and imposing fixed rates on benefits received impaired the contractual obligations of public employers in violation of the Contract Clause;
- Supplemental payments were void in whole; and
- Prohibiting payment of tax offset benefits to non-residents did not violate the Privileges and Immunities Clause.

Tax offsets of 1995, which were calculated by applying a formula intended to negate from Public Employee Retirement System benefits the maximum Oregon personal income tax rate, were not contractual, as required for repeal of the tax offsets to violate state Contract Clause, even if the 1995 Legislative Assembly expected that a future legislature would repeal that provision. The legislature had not, in fact, repealed it, statute expressly stated that it was not contractual, and, thus, legislature clearly intended that the 1995 offset would not be contractual.

Tax offsets of 1991, which provided a benefit to both active and retired members of Public Employee Retirement System based on years of service, were not part of the Public Employee Retirement System contract, as required for repeal of the tax offsets to violate state Contract Clause, although it was intended to compensate Public Employee Retirement System members for the losses that they would incur when the state repealed the income tax exemption, as required by federal law. Statute itself was, neither an offer that members had accepted by rendering services nor initially supported by an exchange of consideration, and instead, legislature enacted offset as a type of pre-emptive damage payment to mitigate a claim for breach of Public Employee Retirement System contract that no court had yet sustained, and, thus, it was not a component of the type of employment compensation benefits otherwise found in the contract.

Cost-of-living adjustment requirement for Public Employee Retirement System benefits was a term of the Public Employee Retirement System benefit offer, as required for its amendment to violate the state Contract Clause, rather than merely a continuation of the discretionary dividend payment benefits system that preceded the requirement. By enacting the cost-of-living adjustment system, the legislature made the Public Employees Retirement Board's function ministerial and the application of the adjustment automatic, and legislature continued to make additional discretionary ad hoc payments during periods of particularly high inflation so that employees could reasonably expect that adjustment statute codified some minimum automatic protection of the purchasing power of their future benefits that was separate from any discretionary and gratuitous ad hoc benefits that the legislature might otherwise have provided.

Public employers could revoke offer of cost-of-living adjustment to Public Employee Retirement System benefit for future work without violating the state Contract Clause; benefit was not an irrevocable term of Public Employee Retirement System benefits offer such that it could not be changed prospectively; abrogating *Oregon State Police Officers' Ass'n v. State of Oregon*, 323 Or. 356, 918 P.2d 765.

Legislation that reduced the cost-of-living adjustment cap for Public Employee Retirement System benefits from plus or minus 2% to plus or minus 1.5% for 2013, and, beginning in 2014, eliminated the cap and bank and imposed a fixed rate of 1.25% on benefits received by retired members up to $60,000 and a fixed rate of 0.15% on retirement income in excess of $60,000 impaired the contractual obligations of public employers to apply cost-of-living adjustment provisions to Public Employee Retirement System benefits earned before the effective dates of those amendments in violation of the state Contract Clause. Case involved public employers's financial obligations and,

thus, did not automatically fall within reserved powers that could not be contracted away, public employers failed to establish that funding was so inadequate as to justify allowing the state to avoid its own financial obligations.

Amendments to cost-of-living adjustments for Public Employee Retirement System benefits were void as violative of the state Contract Clause only to the extent that they applied retrospectively to benefits already earned, and, thus, Public Employee Retirement System members who earned a contractual right to benefits by working for participating employers both before and after the effective dates of the amendments were entitled to receive during retirement a blended cost-of-living adjustment rate that reflected the different cost-of-living adjustment provisions applicable to benefits earned at different times. Prospective application of amendments was consistent with the legislative intent, because amendments provided employers with long-term savings.

Legislature could change prospectively, for benefits earned by Public Employee Retirement System members on or after the effective date of statutory amendments, cost-of-living adjustment for Public Employee Retirement System benefits without violating state Contract Clause.

Supplemental payments provided for in legislation amending cost-of-living adjustments for Public Employee Retirement System benefits by reducing cap and imposing a fixed rate could not be severed from the unconstitutional retrospective application of legislation to benefits already earned in violation of the state Contract Clause and were, therefore, void in whole, even though the supplemental payment provision itself was not unconstitutional. Impact on the benefits Public Employee Retirement System members would have received was adverse.

Prohibiting payment of tax offset benefits to non-residents of Oregon, who were members of Public Employee Retirement System, to compensate them for limitations to cost-of-living adjustments for retirement benefits did not upset the substantial equity between resident and non-resident members in violation of the federal Privileges and Immunities Clause, where nonresidents were not subjected to the tax that the tax offsets were intended to offset.

Prohibiting payment of tax offset benefits to non-residents of Oregon, who were members of Public Employee Retirement System, to compensate them for limitations to cost-of-living adjustments for retirement benefits did not violate the Equal Protection Clause. Objective was to remedy damages resulting from the imposition of Oregon income tax, and it was rational to provide that remedy to only those who suffered the damages by paying Oregon income tax.

UTILITIES - SOUTH CAROLINA

Azar v. City of Columbia

Supreme Court of South Carolina - September 9, 2015 - S.E.2d - 2015 WL 5247144

Objectors brought action against city, alleging city’s expenditures of water and sewer revenues were unlawful. The trial court granted city summary judgment, and objectors appealed.

The Supreme Court of South Carolina held that:

- Genuine issue of material fact as to what nexus, if any, existed between economic development costs and city’s provision of water and sewer services, precluded summary judgment, and
- Genuine issues of material fact as to whether city adequately funded ongoing operating and maintenance expenses, and satisfied the specific statutory set-asides, as a precondition for diverting $4.5 million from its water and sewer enterprise fund into its general fund each year,

precluded summary judgment.

Can Social Impact Bonds Help Reduce Homelessness?

On any given night in Santa Clara County, Calif., more than 6,000 people are homeless. Annually, that's costing the county more than $500 million. To Dave Cortese, president of the Santa Clara County Board of Supervisors, such a high cost should come with better results. The solution, he says, is obvious: "Devise a program that rapidly treats those folks and turns some from persistently homeless to consistently housed, and you cut down on the safety net they're using."

But that kind of prompt and comprehensive response is difficult for local government, in part because of the high upfront costs. Three years ago, Cortese heard about a new financing tool that tapped into the private and philanthropic sectors for early investors for otherwise cost-prohibitive public programs. If the program worked, the government would use future years' revenue to pay back its investors. The tool, known as a social impact bond or "pay for success" program, was new to Cortese. Even though it was called a "bond," it was more of a public-private partnership for experimental and expensive interventions in human services.

Last month, Santa Clara County announced Project Welcome Home, the latest local government initiative that leverages the social impact bond model. In the next six years, a nonprofit called Abode Services will provide housing and support services to between 150 and 200 long-term homeless people. The nonprofit will assign small caseloads to a multidisciplinary team with training in psychiatry, substance abuse, social work, nursing and vocational rehabilitation. The approach represents a combination of evidence-based practices, and is backed by academic research and recommended by the U.S. Department of Housing and Urban Development.

A group of funders is providing $6.9 million — mostly in loans — to make the project happen. Project Welcome Home's goal is to house at least 80 percent of participants for a year or more. If the program is successful, the county will reimburse its lenders as each person hits certain tenancy milestones. For example, lenders will initially be paid $1,242 for every individual who stays housed for three months. The largest reimbursement comes after a formerly homeless person remains in housing for a year:

Payment to Lender per Program Participant Milestone	Participant Milestone
$1,242	3 months of continuous tenancy
$1,863	6 months of continuous tenancy
$2,484	9 months of continuous tenancy
$6,831	12 month of continuous tenancy
$1,035	Each month after the first year of continuous tenancy

In the next six years, the county has agreed to set aside about $8 million from its general fund to pay

back its lenders if Abode is successful in keeping people housed.

Part of the appeal of social impact bonds is that they force local governments to account for current public spending on a problem and estimate cost savings if it reduced the problem using a relatively new and expensive intervention. That logic is driving the Santa Clara project as well. A study published in May by the Economic Roundtable, a policy research nonprofit in California, found that more than 2,800 people are chronically homeless in Santa Clara County, and each of them costs about $83,000 a year in public spending. Cortese and the rest of the Santa Clara County Board of Supervisors are betting that as the homeless population drops, some of that $83,000 in spending at local jails, emergency rooms and shelters will drop as well.

While the Santa Clara County social impact bond is certainly an effort to control spending on homeless services, local officials have been careful not to make reduced costs the sole objective. “We are not predicating success based on the amount saved,” says Greta Hansen, a county attorney overseeing Project Welcome Home. The primary goal, Hansen says, is to house people and keep them housed for a long time. The project also may bring other benefits that county officials consider desirable even if they don’t translate into direct cash savings. For example, wait times at emergency rooms may go down as fewer homeless patients make frequent and repeat visits. That’s a “noncashable” improvement in service delivery, Hansen says.

Another noncashable benefit is the increased focus on data collection and performance measurement in a human services context. Independent researchers from the University of California, San Francisco, have designed an evaluation tool to track treatment groups and control group to determine if Project Welcome Home can be credited for improvements in participants’ health or decreases in their use of social services. “For so long, it’s been a bit of mystery how impactful the [support] services we deliver are,” Hansen says. “We were paying the same amount for a service provider who was extremely effective as one that was less effective. We want to tie our expenditure of public dollars to the outcomes we want to see.”

Santa Clara County’s Project Welcome Home comes at a difficult time for social impact bonds: It launched less than two months after the first and most famous social impact bond in the United States came to an early end. Group therapy for juvenile inmates, the intervention being tried in Rikers Island, N.Y., proved to be ineffective, so the primary funder, Goldman Sachs, pulled the plug. The contract in Santa Clara County includes a similar clause that allows funders to discontinue the project if Abode doesn’t meet its housing targets. “There is risk,” says Cortese. “No one is saying there isn’t risk.” But, he counters, anyone questioning the net benefit of the project should consider the counterfactual, “what you would spend on homelessness if you kept doing what you’ve been doing.” That’s about $3.1 billion over six years, according to the Economic Roundtable study.

While failure is a possibility, so is expansion. The initial project only deals with a small slice of the county’s overall homeless population, but that could change. If enough participants reach their first set of tenancy milestones, Cortese says he would want to explore ways to scale up the program as early as June of next year.

Santa Clara County is one of eight U.S. jurisdictions with a social impact bond project that is up and running. The other seven are in Massachusetts, New York, Ohio and Utah. While they are alike in using nongovernmental funding to cover high upfront costs for an intervention, they seek to address different issues, such as disparities in early childhood education, high prisoner recidivism and chronic homelessness. Other than the Rikers Island project, none have reported final results.

GOVERNING.COM

BY J.B. WOGAN | SEPTEMBER 8, 2015

SEC Asks: Should Muni Bond Pricing Change in Wake of Edward Jones?

CHICAGO – Securities and Exchange Commission lawyers pushed municipal market participants meeting here on Thursday to consider whether industry practices on the pricing of new bonds should change in the wake of the SEC's enforcement case against Edward Jones.

"It's a legitimate, open question as to whether industry practices need to change here," Mark Zehner, the deputy director of the SEC enforcement division's municipal securities and public pensions unit, said after a panel discussion of hot topics in municipal securities law at the National Association of Bond Lawyers' Bond Attorney's Workshop. "Is Edward Jones an aberration or is it a symptom of a larger problem in the municipal market?" he asked.

In its first enforcement case on primary market pricing of bonds, the SEC last month ordered the St. Louis based, retail-oriented dealer Edward Jones to pay more than $20 million for overcharging retail customers for new munis. The commission found that instead of selling new bonds to customers at the initial offering price as required, Edward Jones, acting as a co-underwriter, and the former head of its syndicate desk, took bonds into the firm's own inventory and then improperly sold them to customers at higher prices. In some cases, the firm failed entirely to underwrite and offer the new bonds to investors until secondary market trading began.

Zehner said this is "a very important case" that shows the levels to which some underwriters will go to make money. Before the case, there was an assumption that underwriting syndicate members would adhere to both the bond purchase agreement and agreement among underwriters requirements to sell bonds at the "initial offering price" negotiated with the issuer. But after the case, Zehner said he is "not sure that is a good assumption moving forward."

He encouraged bond and tax counsel to think through what they want to see in issue price certificates, in which the senior managing underwriter certifies the issue price – the price at which at least 10% of a maturity is sold to the public in a bona fide public offering.

Stressing that these are his personal views and not necessarily those of the SEC, Zehner said he is just posing the question of what changes the Edward Jones case might lead to, not answering it.

Rebecca Olsen, deputy director of the SEC's office of municipal securities, raised the same question in an earlier underwriters' counsel roundtable. She asked if the senior managing underwriter can continue to rely on co-managers to comply with their obligations under both the BPA and AAU. Olsen also asked whether bond counsel can continue to rely on issue price certificates executed by the senior managing underwriter on behalf of syndicate members without making inquiries about the pricing of those members' bond sales.

She also asked whether the senior underwriter in a syndicate should start asking co-underwriters to sign the issue price certificate and whether bond counsel should be getting on the Municipal Securities Rulemaking Board's EMMA system and looking at prices at which new bonds were sold. The other panelists, who included a lawyer for a broker-dealer, said a strong no to both questions.

Ernesto Lanza, a panelist and shareholder with Greenberg Traurig in Washington D.C., said the Internal Revenue Service has learned that EMMA is not designed to capture information for purposes of determining the issue price or whether bonds are initially being sold at the issue price.

Lanza said it would be “inefficient” and “ultimately ineffective” to have all syndicate members sign the issue price certificate. Leon Bijou, senior vice president and municipal general counsel with Jefferies in New York, said the likelihood of that happening “seems remote.” Bijou noted that the SEC did not go after the senior managing underwriters in the bond issues where Edward Jones committed pricing abuses.

Lanza said, “everyone should be aware that there is significant evolution going on” following the Edward Jones case, but added it won’t be clear for many months what, if any, changes will occur.

“Expect change in the next year or two in terms of the degree to which syndicate members can trust each other, the degree to which issuers can trust members of the syndicate, and the degree to which lawyers will be pulled into the process,” Lanza said.

Bijou said that underwriters do not have the resources to check what other syndicate members are doing and they assume that the other underwriters are complying with regulations.

“It would be very difficult for us to tap a co-manager on the shoulder and say, ‘By the way, did you comply?'” Bijou said. “We get their signature on the AAU and to go beyond that in the industry process would be considered inappropriate and highly intrusive.”

At least one panelist said syndicate members may be more closely scrutinized by the lead underwriter, but Bijou and others pointed out that issuers sometimes put firms in the syndicate and that lead underwriters do not have the capability or desire to kick them or other firms out.

Paul Maco, a partner with Bracewell & Giuliani, said the senior managing underwriter that signs the issuer certificate can only do so much and that the Edward Jones case showed the SEC looks at each member of the syndicate as being responsible for its own compliance.

An audience member later asked Zehner whether the SEC was concerned that issuers, not just investors, were hurt by Edward Jones. Zehner said the SEC focused on investors, who were clearly hurt by Edward Jones’ actions, in part because the issuers got the deal they thought they were getting. They helped negotiate the initial offering price. “I’m not saying they weren’t victims,” Zehner said, referring to the issuers.

In the earlier session, Maco made the point that when Edward Jones was violating the MSRB’s syndicate rules, it was also violating the securities laws.

“The sea change here” is that the SEC now has a large group of enforcement staff that understand how muni bond pricing and trading desks work and they will be watching this area of the market, Maco said. In addition, the Financial Industry Regulatory Authority will start paying attention to these issues and will probably start looking at syndicate practices and pricing in their examinations of broker-dealers, he said.

THE BOND BUYER

BY JACK CASEY

SEP 10, 2015 4:02pm ET

MSRB: Best-Ex Rule Will Not Be Implemented Before Release of Guidance.

WASHINGTON – Implementation of the Municipal Securities Rulemaking Board's best-execution rule will start four months after the board releases guidance on the rule, instead of Dec. 7 as originally planned.

The MSRB announced the later date on Thursday in an effort to give dealers adequate time to review the guidance before the rule becomes effective. The guidance will be a collection of answers to frequently-asked-questions.

"Linking the effective date of the best-execution rule to the publication of the guidance will establish a clear implementation period and ensure that dealers have adequate time to review and make use of the guidance as they continue to prepare to comply with the new rule," the MSRB said in a news release.

Rule G-18, on best execution, requires dealers to use "reasonable diligence" to determine the best market for a security and to then buy or sell the security in that market so the price for the customer "is as favorable as possible under prevailing market conditions." The Securities and Exchange Commission called for the adoption of such a rule in in its 2012 Report on the Municipal Securities Market.

Dealers would have to take into account a list of factors to meet the diligence requirement under the rule, including: the character of the market for the security; the size and type of transaction; the number of markets checked; the information reviewed to determine the current market for the subject security or similar securities; the accessibility of quotations; and the terms and conditions of the customer's inquiry or order.

The MSRB filed the best-ex rule with the SEC in August 2014 and the commission approved it later that year on Dec. 8. The effective date for the rule was to be one year from the SEC's approval, but the need to coordinate between the MSRB, SEC and the Financial Industry Regulatory Authority, which has its own best ex rule for corporate bonds, caused the guidance process to take longer than expected.

"The MSRB is continuing to coordinate with the SEC and FINRA with the goal of publishing best-ex implementation guidance in short order," said MSRB executive director Lynnette Kelly. "Facilitating dealers' compliance with their new obligations and ensuring that retail investors consistently receive the benefit of fair handling of their orders to buy or sell municipal securities is a top priority for the MSRB."

Dealers had expressed concern that the implementation date for the rule was looming and the MSRB still had not provided them with answers to questions they felt they needed to know to for compliance. There had been questions about how dealers could prove they had used "reasonable diligence" or had found a price that was "as favorable as possible."

Jessica Giroux, senior counsel and senior vice president of federal regulatory policy for Bond Dealers of America, said BDA was concerned about the short period of time that remained before the previous implementation date. But she added that, "since the MSRB has announced it will delay the implementation date to coincide with the delay in anticipated guidance, we are pleased that our members will have additional time to read, comprehend and put in place processes and systems to ensure compliance with the rule."

David Cohen, a managing director and associate general counsel with the Securities Industry and

Financial Markets Association, said, "SIFMA welcomes the delay, as it will allow dealers time to amend and further refine the implementation of policies and procedures that have been under development. We also welcome the coordination with FINRA. SIFMA has concerns, however, that four months is not a sufficient amount of time for dealers to design, test, and implement any changes to their systems as a result of the guidance."

THE BOND BUYER

BY JACK CASEY

SEP 3, 2015 4:48pm ET

Bond Ruling Emboldens Abusive Scheme, Former IRS Official Says: Tax Analysts

A recent private letter ruling has emboldened the use of an abusive arbitrage scheme and should be withdrawn, says William Mark Scott, former director of the IRS Office of Tax-Exempt Bonds.

Summary by Tax Analysts®

September 8, 2015

William J. Wilkins, Esq.
Chief Counsel, IRS Office of Chief Counsel
1111 Constitution Ave., NW
Washington, DC 20224
Re: Priv. Ltr. Rul. 201502008

Dear Mr. Wilkins,
I write to you to lend my voice to the discontent over Priv. Ltr. Rul. 201502008 (dated May 21, 2014, and released Jan. 9, 2015). I believe your office erred when it issued this ruling, and that the ruling should be revoked per Rev. Proc. 2015-1, § 11.04. And, with full knowledge of the errors, I am hopeful you will act accordingly.

Priv. Ltr. Rul. 201502008 addresses the use of a total return swap (TRS) in conjunction with an issue of tax-exempt bonds. In the ruling, one party wears 2 hats as both the swap counterparty and the holder of the tax-exempt debt. Because of this dual role, the swap counterparty/bondholder, through pricing terms applicable to the "total return" portion of the TRS, can lower its taxable income in exchange for greater tax-exempt income. The ruling, therefore, describes an arbitrage scheme that is quite easy to abuse.

Continue reading (subscription required).

Hedge Funds Fill Gap in the U.S. Municipal Bond Market.

Besides shouldering risks on municipal paper that mutual funds won't take, hedge fund firms are pushing for better disclosure from issuers.

At the end of July, Wells Fargo & Co. analysts Natalie Cohen and Roy Eappen published a research note suggesting that hedge fund buyers are becoming bigger players in the $3.6 trillion U.S. municipal bond market. But as the New York–based researchers pointed out, there's no clear way to see what those firms are buying and why.

Tracking players in the market is tough because of a quirk in how the U.S. Federal Reserve Board counts what it calls household investors. "The Federal Reserve (sadly) includes both non-profit organizations and hedge funds in the Household category" of bondholders, Cohen and Eappen wrote.

Still, a scan of the headlines suggests that hedge funds are going all in on obvious U.S. distressed plays like Puerto Rico, any issuance coming out of Illinois and, more recently, the city of Hillview, Kentucky. (Hillview has filed for bankruptcy, but there's some question about whether it will be able to proceed.)

Hector Negroni, co-founder, co-CEO and CIO at New York–based Fundamental Credit Opportunities, an $800 million municipal finance fund, says the opportunity set for hedge funds is much larger than distressed debt. Although people think municipal bonds are just for mom-and-pop investors, he explains, before the financial crisis proprietary trading desks at the U.S. bulge-bracket banks and even foreign banks were big players.

"Hedge funds have stepped into that gap," says Negroni, who ran Goldman Sachs Group's municipal desk until he founded Fundamental Credit Opportunities within New York–headquartered, $2.2 billion alternative-asset manager Fundamental Advisors in 2012. "It's a liquidity option to be in municipal bonds."

For hedge funds, the municipal bond market is still a bit small for the block trades and other big moves they often make. However, munis have emerged as a viable opportunity for a modest bond sleeve within multistrategy funds or as part of a diversified credit exposure. In Negroni's experience, the types of bonds available within the municipal market vary widely, and they're responsive to ebbs and flows in the market.

Hedge funds create demand for municipal bonds that mutual funds and other retail investors won't touch, notes Vikram Rai, a New York–based analyst and head of municipal strategy at Citigroup. "Hedge funds have longer holding periods as well and are thus willing to take their chance on the steps of the bankruptcy court, whereas mutual funds do not want to see a disruption in their coupon income," Rai says, adding that hedge funds also see liquidity opportunities in municipal bonds owing to the market's overall strength.

That relative strength appears to be bringing foreign banks back too, as regulations permit. According to Wells Fargo's Cohen and Eappen, international buyers have boosted their holdings by 144 percent since 2006: "These investors find municipal securities attractive when they are cheap relative to Treasuries, and the spread effectively overcomes the U.S. tax code." This move to munis is most common during so-called flight-to-quality events like the one that has roiled international markets in recent weeks. Munis even saw increased interest from international buyers on the heels of the U.S. credit rating downgrade in 2011.

The price is right when the current yield on an index of triple-A-rated municipal bonds beats that on equivalent Treasuries. For example, the yield on municipal bonds is hovering around 3.82 percent, according to the Bond Buyer Go 20–Bond Municipal Bond index. As of September 10 the highest yield on U.S. government bonds was 2.98 percent on 30-year paper, the Department of the Treasury reports.

The growth of nonretail interest in municipal bonds has come with pushback from critics who say that hedge funds are just in the market to speculate, but Negroni disagrees. “Hedge funds are professionalizing the municipal bond market,” he says. “Hedge funds are the ones putting bond issuers’ feet to the fire and asking for better disclosures. That’s not a bad thing.”

Alternative-investment firms may get some help from the Securities and Exchange Commission on this score. Municipal bond underwriters are on the agency’s radar as part of its Municipalities Continuing Disclosure Cooperation Initiative. Under this effort the SEC is bringing administrative actions against brokerages selling bonds to investors at inflated prices. On August 13 Edward D. Jones & Co. settled with the regulator on exactly this issue. The St. Louis–based brokerage had to pay a fine of more than $20 million but did not admit or deny wrongdoing.

More surprising is that after the settlement, SEC commissioners issued a separate statement calling for new and clear rules for municipal bond dealers that would require them to disclose markups and markdowns on trades. Taken together, the two actions signal that the agency is keeping a close eye on the municipal bond market and potential pricing violations.

So, why weren’t mutual funds and asset managers already pushing for all of this? The short answer is, mandates. Mutual funds and other retail investment vehicles in the municipal bond market are tasked with generating the most tax-exempt coupons. By contrast, hedge funds must provide the best risk-adjusted returns.

“Hedge funds have deep pockets and a higher appetite for risk,” Citi’s Rai says. “They typically step in at certain price points and provide demand for paper that mutual funds and other real money investors don’t want to hold. This has happened in the case of Puerto Rico and other credits as well, like Detroit.”

Alternative-investment firms with the right expertise are also providing specialty finance and municipal financing. Those packages can include bridge loans and municipal bond offerings around the same projects to create comprehensive solutions.

Rai believes the municipal bond market is strong enough to withstand “a handful” of defaults and subsequent distressed-debt interest without creating havoc. “I am quite optimistic about the overall credit landscape for munis,” he says.

Institutional Investor

By Bailey McCann

SEPTEMBER 11, 2015

Nerd-vana: Giving Fellow Reporters Tips on School Bond Sales Statements.

On Tuesday I tried to pass along everything I know about reporting on school bonds to education reporters around the country as a panelist on an Education Writers Association webinar.

The session focused on the wonky topic of official statements, those compendiums of financial information and legal jargon that come with every public bond issue. Those, plus annual financial updates on the debtor agency, are free and available on the Electronic Municipal Market Access portal.

I discovered this treasure trove of source documents while staring at a 2-inch thick stack of spreadsheets I had been given by a school district that seemingly did not want any clear information on its debt to surface. Burying data in bullpucky appeared to be the strategy – and it was working.

But then I found EMMA and, eventually, the district's debt schedule showing year-by-year what it owed on all its bonds. Clarity had arrived.

EMMA expert Leah Szarek, communications manager for the Municipal Securities Rulemaking Board, was a fellow panelist Tuesday. I learned a lot from her presentation, and hope reporters did not get lost in mine as I went down a rapid-fire list of potential stories. Nichole Dobo of The Hechinger Report moderated.

School bond stories are back in the news in this area. First, after the recession wreaked havoc on normal bond financing, those who can are restructuring their debt to take advantage of lower rates.

The Yosemite Community College District has saved taxpayers $12.5 million with a new issue to restructure $120.2 million in debt from its Measure E bonds. That comes on top of $4.5 million it trimmed from its debt obligations with a 2012 sale.

Checking the statement, I see that property owners will still pay another $800.5 million through 2042 on the district's total debt. But, checking their property-valuation schedule, I can also see that is spread over nearly $54 billion (note the "b") worth of real estate over the far-flung district covering part or all of six counties.

Taxpayers pay roughly $25 per $100,000 valuation each year for the bond, which has remade Modesto Junior College with cutting-edge classroom space in its health sciences building, the Community Science Center and its newly opened Center for Advanced Technologies.

Another upcoming story will be Turlock Unified making plans to float a bond in 2016.

Turlock trustees will hold a special meeting at 6:30 p.m. Wednesday to talk over the idea of a school bond measure. They will meet in the school district main office at 1574 E. Canal Drive, Room 102.

After years of declining enrollment, Turlock schools are growing again and proposed development in the south area of town would overcrowd its existing schools there. With the state no longer offering to provide half the funding for new schools, Turlock must figure out how to raise all the money on its own if it wants to create a new school for those new neighborhoods.

The district has also recently refinanced its debt. That should lower its annual debt payment, which in fiscal year 2014-15 cost property owners $4.2 million, according to its bond statement on EMMA. That money went toward outstanding debt for the work finishing at Turlock High School, upgrades the district made to older elementary schools, and the bond to build Pitman High.

Expect to see other school districts weighing bond measures by next year as the rebounding economy brings more families to the area. If you want to know what they already owe or how their finances are doing, check out EMMA.

THE MODESTO BEE

SEPTEMBER 8, 2015

BY NAN AUSTIN

Nan Austin: 209-578-2339, naustin@modbee.com, @NanAustin

Fed Rate Increase Too Late for BlackRock, Alpine Muni Cash Funds.

Whether the Federal Reserve’s first interest-rate increase since 2006 comes this week or not, it won’t be soon enough for Alpine Funds’ municipal money-market fund.

Alpine Woods Capital Investors closed the $120 million fund in April after more than 12 years of operations, joining seven other tax-exempt money-market funds that have liquidated in the last 12 months, according to data compiled by Bloomberg. That number is set to grow. BlackRock Inc. in July said it would close its New Jersey, North Carolina and Virginia money funds by the end of year, leaving it with 15.

“It’s tough times in the muni market,” said Peter Crane, president of Westborough, Massachusetts-based Crane Data, a money-fund researcher. “Rates are so low that nobody cares about the taxes on them, because there’s no income to be taxed.”

Caught in a vice of the Fed’s zero interest-rate policy and the cost of implementing new government regulations, fund companies are culling their offerings through liquidations and mergers. Municipal money-fund assets have plunged by half since peaking in August 2008, to $250 billion. The falloff has far outpaced taxable money-market funds, which dipped 20 percent in that period, to $2.4 trillion as of Sept. 10, according to the Investment Company Institute.

Municipal funds have been hit harder than prime money funds because the tax-exempt market is dominated by individual investors, while the taxable market is led by institutions which have been holding cash, said Crane. Tax-exempt seven-day money funds currently yield an average of 0.01 percent, while taxable funds yield 0.02 percent, according to iMoney.Net.

“Retail investors have options, whereas institutional investors are dealing with other people’s money, so they can’t afford to take risks,” he said. In particular, assets in brokerage sweep accounts are moving to bank deposits from muni money-market funds, Crane said.

Tax-exempt money-market funds, which invest in high-rated, short-term debt and are treated like cash by investors, may still recover as rates rise. Balances in tax-exempt funds more than doubled from the early 1980s through 2008, with faster inflows when the Fed funds rate was rising than it was declining, according to Moody’s Investors Service.

Alpine Woods, based in Purchase, New York, said its fund wasn’t big enough to justify additional expenses resulting from U.S. Securities and Exchange Commission rules that take effect in October 2016 aimed at preventing a run on the funds. Costs for lawyers, technology, disclosure and stress testing are going up, fund managers said.

In September 2008, the $62.5 billion Reserve Primary Fund “broke the buck” because of losses on Lehman Brothers Holdings Inc. debt. Its move to reprice shares below $1 sowed panic among investors, who pulled $310 billion from money funds in a single week, helping freeze credit markets.

“Clearly there are some organizations where the cash product is essential to their product line-up and they have the scale to weather the storm,” said Steven Shachat, who managed the Alpine fund. Alpine still has a $980 million “ultra short” municipal fund, whose holdings have an average maturity of about 90 days.

Some bigger fund companies are also trimming product lines. In July, Western Asset Management, a Legg Mason Inc. affiliate, merged its $540 million Institutional AMT Free fund into the $1.3 billion Institutional Tax Free Reserves Fund, citing similar objectives and investment strategies.

"A shift in assets resulting from the low interest rate environment coupled with money market reform, gave us the opportunity to assess our platform and determine how best to continue to meet the investment needs of our clients," Katherine Ewert, a BlackRock spokeswoman, said in an e-mailed statement.

Money-market fund revenue declined almost 60 percent, to $3.6 billion from December 2009 to December 2014, Crane estimates.

Under the new SEC rules, institutional taxable and municipal money market funds will move from a stable $1 price per-share to a floating share price.

In addition, funds may impose liquidity fees of as much as 2 percent and/or temporary suspensions of redemptions if weekly liquid assets fall below 30 percent. If weekly liquidity falls below 10 percent, money market funds must impose a 1 percent liquidity fee.

By contrast, retail funds, which are limited to individuals, can maintain a stable $1 per share price, although they are still subject to redemption restrictions and fees if they drop below liquidity levels. More than 70 percent of the $250 billion in tax-exempt money-market assets are classified retail by the Investment Company Institute. The new rules don't apply to U.S. government money-market funds.

Even as investors fled tax-exempt money funds, yields on short-term municipal bonds have averaged 0.07 percent over the last three years as state and local-government issuance of the debt has shrunk.

Municipalities are locking in 30-year fixed rate bonds for as low as 3.2 percent rather than issuing floating-rate bonds backed by bank credit facilities. In addition, as the improving economy boosts tax receipts, state and local governments' need for short-term financing has declined.

Government officials are also focusing more on the risks related to issuing floating-rate bonds and entering into swap agreements. Municipalities may be forced to unwind the deals and buy back their debt at great cost if their credit rating is lowered below investment grade.

Chicago faced as much as $2.2 billion in payments to banks after Moody's cut the third-largest U.S. cities debt to junk in May. The city has approved borrowing $1.1 billion to convert floating-rate bonds into longer-term fixed-rate debt and terminate interest-rate swaps, where floating and fixed-rate payments are exchanged.

"There's a propensity for issuers to say, you know, the last thing we want is some sort of downgrade event to trigger a swap termination," said Lyle Fitterer, who helps oversee $38 billion of munis at Wells Capital Management in Menomonee Falls, Wisconsin.

Bloomberg News

by Martin Z Braun

September 13, 2015

SEC Won't Be Pinned Down on MCDC Continuing Disclosure Violations.

CHICAGO – Securities and Exchange Commission officials repeatedly rebuffed bond lawyers' attempts to pin them down on the specific parameters of continuing disclosure violations based on the commission's settlements in June with 36 underwriters under the Municipalities Continuing Disclosure Cooperation initiative.

The initiative allows underwriters and issuers to receive lenient settlement terms from the SEC if they voluntarily self-reported any instances during the past five years in which they falsely claimed in official statements to be in compliance with their self-imposed continuing disclosure agreements.

Panelists at the National Association of Bond Lawyers' Bond Attorneys' Workshop here persistently questioned commission officials about whether an issuer who said it had complied with its continuing disclosure obligations materially violated those obligations if it was 14 days late in filing its annual financial disclosures. They also asked about whether the lack of violations involving the failure to file material event notices means the SEC does not consider these to be material to investors.

But LeeAnn Gaunt, chief of the SEC enforcement division's municipal securities and public pensions unit, told conference attendees that the commission described examples of violations in its settlements with underwriters to provide market participants with broad guidance, especially after they complained the earlier Kings Canyon Unified School District case failed to do so.

"We were genuinely in good faith trying to make these orders something that would be useful to you," Gaunt said during one of the panels on hot topics in municipal securities law. "Hearing the concerns expressed about the opacity of the Kings Canyon order and understanding that people genuinely in good faith were wanting to have a bit more texture on the nature of the violations that were reported and that were independently determined," the muni enforcement unit worked to ensure the order provided some guidance, she said.

But she said the examples cited reflect a range of conduct that fit the submissions the SEC received and that nobody should be "trying to find a bright line" in the order.

"What we tried to do in part in the spirit of the MCDC initiative, which was voluntary and cooperative, was not to necessarily lay bare every failure everybody reported," Gaunt said. "We wanted this to be a set of orders that were helpful to the industry, helpful to the market but didn't unduly [and] unnecessarily belabor failures, some of which were very repetitive in nature."

Elaine Greenberg, a panelist, partner with Orrick, Herrington and Sutcliffe, and predecessor to Gaunt at the SEC, sat on one of three hot topics securities law panels and tried to get more clarification on the SEC considers to be material violations under the initiative. Alexandra MacLennan, a partner with Squire Patton Boggs, similarly sought clarification from Mark Zehner, deputy chief of the SEC's muni enforcement office, during a different hot topics panel, but neither Greenberg and MacLennan made much headway with the SEC officials.

In response to Greenberg's questions on materiality examples, Gaunt said each example bullet point in each order is considered material, but she cautioned that if multiple events are mentioned in one bullet point, only the cumulative actions mentioned in the one point should be considered material.

Gaunt also said the absence of any examples involving failures to file material event notices does not mean they will not show up in future settlements.

“Nobody should take from that fact that we have decided that the failure to file material event notices is absolutely never actionable,” Gaunt said. “We’re not setting a floor, we’re not setting a ceiling.”

The examples are “not the universe of everything that could be,” Rebecca Olsen, deputy director of the SEC’s Office of Municipal Securities, said during another panel.

Zehner echoed Gaunt during his panel: “Those are only examples. They are not floors, they are not ceilings,” he said, adding, there is no “magic line drawing.”

Both Zehner and Olsen separately stressed that market participants should not be looking at the SEC to determine whether disclosure failures are material. They said materiality is always a facts and circumstances determination of what a reasonable investor would want to know when buying or selling bonds. “The market should not be looking to the SEC … to say what is material,” said Olsen.

Gaunt did not rule out the possibility that there could me more than one more set of underwriter settlements, saying “there will be at least one more group” of underwriter settlements but that she could not “say for sure if there will be another one after that.”

Some sources have said issuer settlements will not be released until next year. Asked about that by a reporter, Gaunt said she could not say.

Both Olsen and Jessica Kane, director of the SEC’s OMS, said that the MCDC initiative has served an important purpose in focusing market participants’ attention on the commission’s Rule 15c2-12, on disclosure. Kane said the initiative has provided “valuable insight into how 15c2-12 is working.” Both she and Olsen suggested that the settlements will allow them to determine whether further changes to the rule or other actions are needed.

One bond lawyer in the audience noted that most continuing disclosure agreements provide remedies for bondholders if issuers fail to meet their obligations. Zehner replied the SEC’s focus during the investigation was not on issuers’ failure to file disclosures but rather on whether they made false or misleading statements when they said they were meeting their obligations. Zehner added, however, “I think one of the issues that the industry has to wrestle with is whether current remedies on disclosure failures are adequate.” Continuing disclosure agreements are essentially contracts between the issuer and the bondholders subject to state contract law. In theory, if the bondholders are upset that an issuer has failed to meet its continuing disclosure obligations and want to force the issue to remedy the situation, they can sue the issuer under state law. But in reality, a bondholder typically does not know the identities of other holders of the bonds and small holders do not have the financial resources to file a lawsuit.

Zehner said after the panel that if bondholders had an adequate enforcement mechanism to force issuers to comply with their disclosure obligations, the SEC would not need to bring enforcement cases in this area.

“In a perfect world, we should never have to show up,” he said.

The MCDC also may already be changing some market practices. Until the initiative, most offering documents contained language saying the issuer had complied in all material respects with its continuing disclosure undertakings. If this language was included in an official statement and the issuer did not meet its undertakings, then the SEC could easily show the issuer made a false representation. As a result, many of the lawyers on panels said issuers may no longer include these statements in their offering documents.

"MCDC made issuers aware that those statements have risk," said Barron Wallace, a partner at Bracewell & Guiliani and a panelist on an underwriter's counsel roundtable. Paul Maco, a former OMS director from the same firm who was also a panelist, pointed out that these statements are not required by Rule 15c2-12 but rather have been a "construct that was developed by the bar."

Another member of the audience asked Zehner what trends or patterns he sees in the market that bond counsel and underwriter's counsel should pay attention to. Zehner said there are so many areas that it is hard to think of a list, but responded to the question by warning that "if you are participating in a higher risk, higher yield transaction, you need to be more careful."

After the panel he explained that issuers need to be sure they are disclosing all of the risks in these kinds of deals. The SEC for example brought enforcement action against Allen Park, Mich., its former mayor, and its former city administrator in connection with $31 million of munis sold in 2009 and 2010 to finance a movie studio project in the city. The SEC found that offering documents contained false and misleading statements about the scope and the viability of a questionable movie studio project as well as Allen Park's overall financial condition and its ability to pay debt service.

THE BOND BUYER

BY JACK CASEY

SEP 11, 2015 11:15am ET

UBS wins Puerto Rico Bond Fund Arbitration After Spate of Losses.

UBS AG has prevailed against an investor's multi-million-dollar arbitration claim for losses tied to the firm's Puerto Rico bond funds, following a string of investor victories.

A Financial Industry Regulatory Authority (FINRA) arbitration panel ruled that investor Berta Ganapolsky relied on advice from her family's "outside counsel" and an accountant, instead of her UBS broker, when she chose to remain invested in a bond fund that was underwritten and sold by UBS's Puerto Rico arm. The ruling, dated Wednesday, was posted to FINRA's website on Friday.

"We believe that justice was not done here," said Charles Lichtman, a lawyer in Boca Raton, Florida, who represented Ganapolsky. "Our client is a 78-year-old widow, whose UBS broker put all of her money into one investment," Lichtman said in a statement.

Ganapolsky, who filed the case last year, had sought a total of $9.1 million in relief.

Many of the Puerto Rico funds sold by UBS were highly concentrated in the debt of the Caribbean island's government and related entities. UBS is defending against hundreds of arbitration claims filed with FINRA, which collectively seeking more than $900 million in damages.

Some of the funds lost half to nearly two-thirds of their value between March 2011 and October 2013, amid fears about the size of Puerto Rico's debt burden and the weakness of its economy. They have failed since to recover.

"UBS is pleased with the arbitrators' decision in this matter," a spokesman said.

The panel's decision follows a series of recent UBS losses. On Aug.31, arbitrators ordered UBS to

pay $2.9 million to two Puerto Rican investors. And Aug. 11 arbitrators ordered UBS to pay two investors $2.5 million.

In May, arbitrators ordered UBS to buy back an investor's Puerto Rico bond fund portfolio for $1 million. As the value of the investor's portfolio plunged, a UBS manager told him that "even a skinny cow could give milk," the ruling said.

The panel, in reaching its decision on Wednesday, also recommended removing details about Ganapolsky's complaint from the public record of her broker at the time, David Jose Lugo.

FINRA rules require that summaries of investors' arbitration complaints appear in the public records of brokers who are either named in a case or facilitated a transaction.

Lugo's public record reflects dozens of such complaints about the funds and also notes that he left UBS in May. Lugo's lawyer was not immediately available to comment.

REUTERS

SEPT 11 | BY SUZANNE BARLYN

(Reporting by Suzanne Barlyn; Editing by Leslie Adler)

Markets Provide a Reality Check for the Risky Bet of Pension Obligation Bonds.

The scary stock market that we've seen since mid-August is a classic example of how reality keeps intruding on theory. And it shows how there really is no such thing as free money on Wall Street, no matter how beguiling the sales pitch.

The case in point: pension obligation bonds — a supposedly magic solution to the problem of underfunded government pensions. The idea is that governments with badly underfunded plans can borrow money at historically low rates, invest the borrowed cash in the stock market, and earn much more on stocks than the bonds cost in interest.

I wrote a skeptical article about these bonds in July, with Cezary Podkul of ProPublica as co-author. "Governments can borrow cheaply these days — but the risks of investing pension bond proceeds are unusually high," we said. Recent weeks have proved us right.

We warned that potential pension bond issuers such as Colorado and Pennsylvania would be taking a huge chance by selling billions of dollars of bonds at seemingly low rates and investing the cash in the then-stable stock market.

The idea, as presented by investment banks (which get fees for doing deals), is that pension bonds can be a magic elixir. For two groups in particular, they profess, it's just the thing: employee unions worried that underfunded pension plans could lead to benefit cuts, and public officials who want to improve pension-funding ratios without raising taxes or cutting benefits.

After all, the argument goes, you can't go wrong selling bonds at about 5 percent interest to raise money to buy stocks, which have historically produced returns exceeding 10 percent.

Oops. Timing is everything. Had a government sold pension bonds on July 10, the day our article appeared, it would have suffered a double whammy. The Standard & Poor's 500-stock index has dropped 6 percent since then, and interest rates on the kind of municipal bonds that make up a large piece of pension issues have fallen.

Had Colorado sold its proposed maximum of $12 billion in pension bonds on July 10 and put the proceeds into the S&P 500 that day, its portfolio would be about $700 million underwater. What's more, its bonds would probably be carrying a somewhat-higher-than-current-market interest rate.

That's because the rate on 30-year AA-rated taxable muni bonds, a major component of pension bond issues, was 4.74 percent Thursday, according to Bloomberg, down from 5 percent on July 10. Rates on the 20-year version of the bond, another major pension bond component, were down slightly, to 4.46 percent from 4.49 percent.

So Colorado — which fortunately for its taxpayers deferred the pension bond issue after state legislators got nervous — would have had a large paper loss and would be paying what at least for now is an above-market rate on much of the borrowing.

"Recent market behavior has reminded us that markets have volatility and uncertainty and may not provide the returns we want, no matter how badly we need them," said Ben Valore-Caplan, a Denver-based adviser to institutional investors who quit as vice chairman of the Colorado Public Employees' Retirement Association board rather than be involved in a pension bond issue.

"Markets don't care that a pension is underfunded," he told me. "Pensions don't get secret access to higher returns or lower risk. When they forget their place, the markets sooner or later will remind them."

The S&P 500 has produced an average of 10.6 percent in price increases and reinvested dividends over the past 45 years. But that doesn't mean you are guaranteed a double-digit return if you invest on a particular day. It's about statistics: You can drown in a pond that's an average of one foot deep if you happen to step into a 10-foot-deep part.

It's one thing to invest in stocks over the long term. But investing gradually, over time, is a lot different than hocking yourself to the eyeballs and putting the borrowings into the market in one shot.

No, I'm not saying that stocks won't recover and go on to new highs. What I am saying is that any government — or any retail investor — borrowing a ton of money and putting it all in the stock market at once is taking an enormous risk. It's not a risk I would take myself. As recent weeks have shown, it's not a risk that governments should take, either.

The Washington Post

By Allan Sloan

September 10, 2015

Research for this column was provided by Cezary Podkul of ProPublica.

Detroit Schools Paying Penalty in Bond Market Post Bankruptcy.

Detroit's schools are paying a hefty penalty for persistent financial woes as the district taps the tax-exempt debt market in the wake of the city's record bankruptcy.

The $121 million in notes maturing in August being sold through the Michigan Finance Authority were priced to yield 5.75 percent, according to preliminary data compiled by Bloomberg. That's about 5.5 percentage points more than one-year benchmark municipal bonds.

"The market pricing is just reflective of many buyers' uncertainty regarding the legal standing of this type of security package for a name that has suffered so much fundamentally in recent decades," said Gabe Diederich, a Menomonee Falls, Wisconsin-based money manager at Wells Capital, which manages about $39 billion of municipals, including some Michigan school holdings.

The proceeds of the deal will refinance debt to help cover the district's budget deficit, according to bond documents. The district, which has been run by a state-appointed manager since 2009, is in Wayne County, which entered into a consent pact with the state last month to try to mend its own spiraling finances.

Michelle Zdrodowski, a spokeswoman for the schools, said in an e-mail that the district was not going to make any comment during the pricing period.

Detroit Public Schools' financial problems mirror a shrinking population, a trend that has contributed to slumping enrollment. The "severe declines" in the number of students enrolled at Detroit schools has limited state aid available for debt payments, according to Standard & Poor's, which rates the notes SP-3, its lowest short-term grade. The schools saw average annual enrollment declines of more than 12 percent from 2007 to 2012, according to S&P.

In May, the Michigan Finance Authority sold $82.8 million of notes maturing in June 2016 at a yield of 4.75 percent.

The district is behind on its pension payments by about $92 million, bond documents show. The state's office of retirement systems can ask the Michigan treasurer to intercept state aid to the schools to get the funds. While the director of the pension system has said that he doesn't plan to do that as long as the district sticks to its plan to make payments in October, the pension costs remain a drag on school finances.

The state is working to ease the district's fiscal woes. In April, Gov. Rick Snyder proposed a restructuring of the school system into two parts. One district would be charged with paying off the $483 million of operating debt using an existing property tax, and the other would be tasked with educating students and collecting state aid funds, according to bond documents. Legislation on the plan is expected to be introduced in the coming months, according to bond documents dated Sept. 4.

"Ultimately there just doesn't appear to be a near-term catalyst for boosting enrollment and changing the trajectory of the trends of Detroit public schools itself," said Diederich, who passed on the note sale Thursday.

Bloomberg News

By Elizabeth Campbell

September 11, 2015

[Orrick: SEC Expands its Focus in the Municipal Bond Market, Bringing First-Ever Charges Against an Underwriter for Pricing Violations Related to Primary Offerings.]

Coming on the heels of the SEC's first wave of settlements with underwriters as part of its Municipalities Continuing Disclosure Cooperation ("MCDC") initiative, the agency has brought yet another precedent-setting enforcement action against an underwriter in the municipal bond market. On August 13, 2015, the SEC brought a settled enforcement action against the brokerage firm Edward Jones, in which the firm agreed to pay more than $20 million to settle charges that it overcharged customers in connection with the sale of municipal bonds in the primary market. Edward Jones settled without admitting or denying the SEC's findings.

According to the SEC, Edward Jones regularly underwrote—usually as part of an underwriting "syndicate" or group—and sold municipal bonds to the public through negotiated offerings. Underwriters of municipal bond offerings are generally required (as part of an agreement between the members of an underwriting syndicate) to offer municipal bonds to the public at the "initial offering price," which is the price negotiated between the issuer and underwriter. To compensate the underwriter for its services, the issuer typically sells the bonds to the underwriter at a price below the initial offering price.

The SEC charged that, on numerous occasions, Edward Jones violated its agreements with both bond issuers and its fellow underwriters by improperly reselling municipal bonds to its customers at prices above the initial offering price. The SEC found that between 2009 and 2012, Edward Jones overcharged its customers in 75 different negotiated offerings, netting the Firm more than $4.6 million in additional revenue.

The SEC also found that Edward Jones regularly purchased bonds without disclosing to the underwriting syndicate that the purchases were for Edward Jones' own inventory. While underwriters are permitted to make orders for their own inventories, the SEC contended that they are required to disclose that fact, as customer orders are given priority over orders for an underwriter's own account. Consequently, the SEC found that Edward Jones' failure to disclose this information enabled it to purchase bonds that it otherwise may not have been able to purchase.

In addition, with respect to Edward Jones' trading of municipal bonds in the secondary market, the SEC separately charged the firm with failing to establish an adequate supervisory system to determine whether the markups it charged on certain transactions were reasonable.

The SEC ordered Edward Jones to cease and desist from future violations of Sections 17(a)(2) and (3) of the Securities Act, Section 15B(c)(1) of the Exchange Act, and a number of rules promulgated by the Municipal Securities Rulemaking Board ("MSRB"), which regulates dealers of municipal securities. Edward Jones agreed to pay $5.2 million in disgorgement, as well as a $15 million penalty. It also undertook a number of remedial measures, including: (i) hiring a dedicated compliance officer for its fixed income desk; (ii) adopting new procedures for the sale of municipal bonds, including a requirement that bonds acquired in new issuances may only be sold at the initial offering price; (iii) disclosing in writing the amount of any markup or markdown on all fixed income trades; and (iv) making restitution to affected customers.

This action sends a signal to municipal market participants that the SEC continues to be on the lookout for violations of securities laws or MSRB regulations in connection with both disclosure and pricing. Indeed, as Andrew Ceresney, the SEC's Director of Enforcement, stated in the SEC's press

release announcing the Edward Jones case, the enforcement action "reflects [the Commission's] commitment to addressing abuses in all areas of the municipal bond market." Moreover, in the aftermath of the case, four SEC commissioners took the unusual step of issuing a separate statement calling for the completion of clear rules requiring dealers to disclose markups and markdowns on municipal securities trades.

Article by William J. Foley Jr, Kevin M. Askew and Elaine Greenberg

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The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

TAX - WASHINGTON

Automotive United Trades Organization v. State

Supreme Court of Washington, En Banc - August 27, 2015 - P.3d - 2015 WL 5076289

Industry group brought action challenging agreements under which Indian tribes agreed to buy taxed fuel and State agreed to refund portion of fuel tax receipts to tribes. The Superior Court granted summary judgment in favor of state. Industry group appealed.

The Supreme Court of Washington, en banc, held that:

- Fuel tax refund agreements between Indian tribes and State did not violate constitutional provision governing fuel tax receipts, and
- Agreements did not violate separation of powers provision of state constitution.

Agreements under which Indian tribes agreed to buy taxed fuel and the State agreed to refund a portion of the fuel tax receipts to the tribes did not violate state constitutional provision that limited use of state fuel tax receipts to highway purposes, where refunds were paid to tribal governments under contracts that limited their use to various government purposes, and governor was statutorily authorized to enter into such agreements.

Legislative authorization for executive to enter into agreements under which Indian tribes agreed to buy taxed fuel and the State agreed to refund a portion of the fuel tax receipts to the tribes did not constitute delegation of legislative authority in violation of separation of powers doctrine of state constitution, where legislature had provided fairly detailed standards and guidelines for such agreements, legislature defined objective of agreements, and legislature required regular audits and reports regarding agreements.

TAX - PENNSYLVANIA

GAI Consultants, Inc. v. Homestead Borough

Commonwealth Court of Pennsylvania - July 8, 2015 - A.3d - 2015 WL 4095523

School district brought declaratory judgment action against redevelopment authority, other taxing

bodies, and waterfront partners, asserting authority had the contractual duty to direct bank holding tax increment financing (TIF) fund to pay any assessment appeal refunds on properties pledged to waterfront district at the direction of the taxing body, regardless of tax year.

Owner of parcel pledged to waterfront district brought action in assumpsit in order to recover $34,535 from borough taxing authority following assessment appeal. The Court of Common Pleas entered order declaring authority had a contractual duty under TIF agreement to direct payment of assessment appeal refunds, and ordered authority to direct reimbursement to county and school district of refunds paid to owner of pledged parcel. Borough appealed.

The Commonwealth Court held that four-year statute of limitations for contract actions did not bar claims of taxing authorities for pre-2010 property tax assessment appeal refunds.

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