Local Government Investment in Water and Sewer, 2000-2015.

What investments will be needed to rebuild our national water and sewer infrastructure andprovide services to a growing and shifting population and an expanding economy?

Introduction

Will a new national infrastructure policy help or hurt city water and sewer services?
What is the role of the Federal Government in helping cities provide safe, adequate and affordable water and sewer in a national infrastructure policy?

Answers to these questions require knowledge of current public water and sewer economics and recent trends to help evaluate policy implications; this paper summarizes local and federal investment trends.

Congressional framers of the Clean Water and the Safe Drinking Water Acts promised local governments a technical and financial partnership to achieve national water goals. Those promises are long forgotten. Congress and the Executive branch have steadily retreated from responsibility for local water and sewer services, although they continue to stack up expensive regulatory mandates that trigger affordability burdens for low- and middle-income households. Current discussions of boosting infrastructure investments initiated by the Executive branch are long overdue; and the stated expectation that cities and states need to step up with more of their own money before they ask for federal financial assistance rings hollow in the case of local water and sewer where local government provides roughly 98 percent of the annual investments. Any major improvement in water and sewer infrastructure will rely on a new configuration of bonds, grants, loans and rate increases. A new infrastructure policy can get it right, if the new framers of the policy consider both achievements and systemic problems that have accrued over the last 40 years.

The case is well established that the federal financial partnership with cities died when Congress eliminated the construction grants program in favor of providing capitalization grants to states to disburse to local government as loans with capital and interest payments. Elimination of earmark grants for water and sewer construction soon followed, and local government picked up all the responsibility for providing local services and achieving national health and environmental goals, (Figure 1).

Continue reading.

The United States Conference of Mayors

By Richard F. Anderson, Ph.D.

Using Dollars with Sense: Ideas for Better Infrastructure Choices.

With infrastructure policy set for the spotlight in 2018, the Urban Institute is hosting this series to look beyond funding and into the way we choose which infrastructure projects are built and which are not.

On this page, you will find short essays about what criteria policymakers should keep in mind to make effective choices and what levers they can use to do so. Visiting fellow Shoshana Lew argues for one such tool in her new brief, calling attention to asset management plans.

Our authors hold various views and roles in our infrastructure system, and while they may not all agree, we hope their collective output will be a resource for infrastructure leaders to draw on as they make decisions that will reverberate in places and people's lives for decades.

We look forward to a thought-provoking and useful discussion.

Continue reading.

The Urban Institute

Fitch U.S. Not-For-Profit Hospitals and Health Systems Criteria Revision.

Fitch Ratings finalized its new criteria for U.S. not-for profit hospitals and health systems, the changes of which are detailed in a new report and companion piece. These revisions will facilitate a more forward-looking, predictable approach to ratings and better highlight differences among credits in the same category.

Anticipated Rating Impact Limited

Fitch expects criteria-driven rating changes to affect less than 15% of the portfolio, with a roughly equal mix of upgrades and downgrades. Upgrades are likely for issuers with enhanced revenue defensibility characteristics or less volatility in Fitch's through-the-cycle analysis, while downgrades are likely for issuers with elevated operating risk and leverage, which expose them to greater volatility in a through-the-cycle analysis.

Rating Changes More Predictable

In a sector characterized by low default risk, insight into an issuer's vulnerability to adverse conditions and credit deterioration is of paramount importance. The revised criteria more clearly define and communicate Fitch's expectations of the range of performance within which a rating is expected to be stable, versus conditions which could prompt a rating change.

New Through-the-Cycle Tools

Fitch is incorporating forward-looking tools into the rating process. Revenue sensitivity and scenario analysis tools work together to consider both the expected 'base case' financial performance within a typical business cycle and the 'rating case' potential financial performance given a moderate downturn. Known as FAST, this tool highlights how cycles affect issuers differently, and will be publicly available during the criteria comment period.

Experienced Analytical Judgment

Fitch's ratings will continue to be based on the judgment of a team of experienced analysts rather than model-based outcomes. Given the diverse characteristics and wide range of U.S. not-for-profit hospital and healthcare credits, Fitch believes there are clear limits to the degree to which data points and formulas can define them.

Clearer Communication of Credit Opinions

The goal of the revised criteria is to communicate Fitch's credit analysis more clearly, presenting well-defined opinions about both rating conclusions and the underlying fundamentals. This will provide greater differentiation among credits, increased insight into what could trigger a rating change, and facilitate comparison of Fitch's credit opinions with others in the marketplace.

Focused Key Rating Factors

Three focused key rating factors replace the traditional inventory of credit considerations to highlight the role that each plays in determining credit quality. The information that Fitch reviews is largely unchanged; however, the way this information is incorporated into integrated and transparent analysis is much improved.

Tailored Versus Generic Expectations

As part of an integrated analytical approach, expectations are linked to issuer-specific risk factors. For example, rather than having a blanket level of liquidity or leverage judged to be consistent with a given rating category, Fitch considers the issuer's fundamental financial flexibility and sensitivity to downturns against an issuer-specific operating cost flexibility assessment and the asset allocation of its unrestricted liquidity.

Bloomberg Brief Weekly Video - 1/18

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

Watch video.

Bloomberg

January 18th, 2018

House Panel Backs Bill to Scrap Floating Prices for Money Funds.

- Post-crisis rule raised municipal borrowing costs, critics say
- Key industry group opposes change, says markets have adjusted

The House Financial Services Committee has advanced a bill that would eliminate some of the strictures placed on the $2.8 trillion money market mutual fund industry in the wake of the financial crisis.

The legislation, which was opposed by Fidelity Investments, Vanguard Group., BlackRock Inc. and other major asset managers, would repeal a 2014 requirement that the riskiest funds allow their share prices to float, rather than maintain a stable $1 value. The panel's action clears the way for a House vote on the measure.

Representative Keith Rothfus, a Pennsylvania Republican who sponsored the legislation, said it aims to fix a "misguided Securities and Exchange Commission rule" that has disrupted markets and also caused municipal borrowing costs to rise. He said more than 60 lawmakers, both Democrats and Republicans, were co-sponsors of the bill.

While the prospects for passage in the Senate are dim, the 34-21 committee vote is a victory for Federated Investors Inc., which has a large money fund business and has been fighting the SEC regulation for years. The Pittsburgh-based firm joined with state treasurers, pension funds and other businesses to form the Coalition for Investor Choice to lobby for the bill.

Interest Rates

Other fund companies disputed the group's contention that the SEC rule was responsible for increased borrowing costs for cities and towns. In a paper distributed on Capitol Hill, Vanguard attributed the rise to the Federal Reserve's decision to boost interest rates.

"The coincidental timing of these increases and of money market reform has led to misidentification of the true causation of higher municipal yields," Vanguard wrote.

Mutual fund firms and their trade association, the Investment Company Institute, had mostly opposed the SEC's move to require the floating share price, but they told lawmakers changing the rule would be expensive and potentially troubling to the markets.

"The new regulatory regime involved substantial and costly operational changes implemented on a very aggressive timetable, but money market funds and the money markets have adjusted," ICI President Paul Schott Stevens wrote in a Jan. 12 letter to committee members. "The consensus of our member leadership is that reopening these reforms is not appropriate or desirable."

Clayton Warning

SEC Chairman Jay Clayton, in a letter last year to Representative Carolyn Maloney, also urged caution, noting that the agency's rule had only been fully put in place in October 2016. "I am concerned that making major changes at this time could be disruptive to the short-term funding markets," Clayton wrote.

The SEC's reforms came in response to a September 2008 run on the Reserve Primary Fund after its share price dropped below $1, causing investors to withdraw money at other funds and helping freeze credit markets. The Treasury Department was ultimately forced to stem the panic by temporarily guaranteeing shareholders against losses.

Among the lawmakers voting against the legislation were Representatives Bill Huizenga, the Michigan Republican who leads the Financial Services capital markets subcommittee, and New York's Maloney, the panel's top Democrat.

"I oppose this bill because I think it rolls back one of the most important post-crisis reforms we made," Maloney said.

Bloomberg Markets

By Robert Schmidt

January 18, 2018, 9:50 AM PST

[S&P Credit FAQ: Understanding Climate Change Risk and U.S. Municipal Ratings.]

The U.S. municipal market has always faced credit exposure to hurricanes, floods, drought, fires, tornados, earthquakes, and other catastrophes. In addition to episodic event risk from natural disasters, S&P Global Ratings believes it is important to consider the current long-term credit…

Continue Reading

Oct. 17, 2017

Moody's: Climate Change Adaption and Mitigation Could Affect Cities' Bond Ratings.

In December, Moody's Investors Service issued a report encouraging cities to invest in climate adaptation and mitigation. Cities will be evaluated in the future at least in part on how they prepare for both short-term climate "shocks" and longer-term trends associated with climate change.

Moody's is the largest credit rating agency to date to publicly outline how it evaluates climate change risk and integrates it into its credit rating assessments.

In the report, the United States is broken into seven "climate regions," identified by both geography and the type of mostly common regional impacts—for example, drought, extreme heat, and wildfires in the Southwest; rising sea level and its impact on coastal development in the Northeast; and flooding and other impacts on agriculture in the Midwest. The report stresses, "If federal, state, and local governments do not adapt, these risks are forecast to become more frequent and severe over time."

Cities that are already taking proactive steps to address climate change mitigation and resilience may welcome this additional level of scrutiny. A municipal credit rating based in part on climate change preparation could lead to a virtuous circle—cities that invest in climate preparedness would see a higher bond rating, allowing them to attract more low-interest capital to invest in a broader range of strategies to prepare for the short- and long-term impacts of climate change.

For cities that have not developed a climate action plan, or begun investing in climate change preparedness, Moody's report could be a wake-up call—if credit becomes harder to come by, these cities could be at a credit disadvantage to their peers, and find it hard to find the financing to catch up.

In the report, Moody's encourages cities to develop local adaptation and mitigation programs specific to their most likely short-term climate "shocks" and longer-term climate trends. In the Midwest, the report recognizes that "impacts on agriculture are forecast to be among the most significant economic effects of climate change." In the Southwest, the report recognizes that the region will become even more vulnerable to extreme heat, drought, rising sea levels, and wildfires. Rising sea levels and their effect on coastal infrastructure are the biggest projected long-term impact on the Northeast.

As Moody's recognizes climate change as a threat to municipal bond ratings, other debt markets have already begun integrating energy efficiency and climate change mitigation into their evaluation process. Fannie Mae is issuing green mortgage–backed securities for assets with a third-party green building certification or major energy efficiency improvements, and providing green financing loans to help drive these energy efficiency improvements. Earlier this year, a study by the U.S. Department of Energy and Lawrence Berkeley National Laboratory found that energy-efficient commercial buildings are less likely to default on their mortgages than their more energy-inefficient peers, further strengthening the case that commercial debt markets should incorporate energy efficiency into their underwriting process as well.

Urban Land

By Billy Grayson

January 17, 2018

Market Commentary: Munis Get Slammed in a Volatile Week.

Read the report.

Court Street Group's Perspective

by George Friedlander

Posted 01/16/2018

Market Commentary: Munis Outperform Treasuries as 10-Year UST Tops 2.60%

This Market Commentary is part of Court Street Group's Weekly Perspective.

This past week saw several milestones in broader markets with the Dow Jones Industrial Average crossing the 26,000 point mark for the first time and the U.S. Treasury 10-year yield topping 2.60% for the first time in nearly 4 years.

Pressure from sustained Treasury losses year to date and the crossing of the technical boundary of 2.60% did eventually put pressure on municipals but overall the theme of the week was outperformance.

Continue reading.

Neighborly Insights

by George Friedlander

Posted 01/19/2018

[Chicago Postpones $898 million Bond Sale, Eyes New Structure.]

CHICAGO (Reuters) – Chicago on Wednesday postponed an $898 million bond sale until next week at the earliest, citing weaker market conditions and the possibility of restructuring the deal to include taxable debt.

The revenue bond issue, which topped this week’s $3.45 billion supply calendar in the U.S. municipal market, was aimed at refinancing some of Chicago’s outstanding general obligation debt through a newly created Sales Tax Securitization Corporation.

Chicago Chief Financial Officer Carole Brown pointed to a weaker market tone and the fact that ratios between yields on tax-exempt muni bonds and comparable taxable U.S. Treasuries have risen since the city sold the first $743.7 million of bonds through the corporation in early December to refinance outstanding sales tax revenue debt. The ratios gauge the expensiveness or cheapness of munis versus Treasuries.

“We have the flexibility and the time to possibly evaluate some alternative structuring options and make sure we are offering the appropriate deal to the market given the current market environment,” she said in a telephone interview.

While the deal was meant to refund outstanding GO bonds callable within 90 days, the city could add a taxable component to refund debt callable beyond 90 days, according to Brown. The new federal tax law eliminated tax exemption for advance-refunded munis.

The tax-exempt bond deal was initially structured with serial maturities from 2031 through 2039 and a term maturity in 2042.

Chicago created the sales tax securitization corporation last year to refinance up to $3 billion of its sales tax revenue and GO bonds, and produce an initial $94 million in savings for the city’s fiscal 2018 budget.

A chronic structural budget deficit, as well as a huge unfunded pension liability that totaled $35.76 billion at the end of 2016, have led to low credit ratings and increased borrowing costs for the nation’s third-largest city.

The corporation is pledging Chicago’s state-collected sales tax revenue to pay off the new bonds. Investors will get a statutory lien shielding the debt from municipal bankruptcy, which is not allowed under Illinois law.

The bonds are rated AAA by Fitch Ratings and AA by S&P Global Ratings, both of which are several notches higher than the city’s GO ratings of BBB-minus by Fitch and BBB-plus by S&P.

Reporting by Karen Pierog; Editing by Matthew Lewis

JANUARY 17, 2018

The Week in Public Finance: Feds to Revisit Payday Loan Restrictions, a Pot Appeal and a Better Way to Do Property Taxes.

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

GOVERNING.COM

BY LIZ FARMER | JANUARY 19, 2018

Public-Private Partnership Withstands Court Challenge.

Attorney Mariah DiGrino of DLA Piper details a recent Illinois court case.

Housing for chronically homeless individuals in Lake County, Ill., has been preserved and expanded through a public-private partnership that recently withstood a court challenge by opposing residents. The Lake County Housing Authority is working with PADS Lake County, a local nonprofit homeless services provider, to provide permanent housing for chronically homeless individuals, using funding under the Department of Housing and Urban Development's (HUD's) Continuum of Care program.

The public-private partnership in this case uses a multifaceted approach to reach a narrow segment of the homeless population, whose unique challenges have proven difficult to address. This approach allows the housing authority to tap into multiple resources to reactivate a vacant facility: HUD funding, existing public housing tenant selection processes, and PADS' experience and expertise serving the chronically homeless. PADS itself is a nonprofit organization that engages a variety of community and financial resources to address homelessness.

The public-private partnership in this case follows a long history of government efforts to engage the private sector in housing programs, beginning with New Deal-era loan guarantees and subsidized loan programs. So-called P3s have evolved to include a variety of arrangements, but all share the common features of combining government resources and authority—such as public funding, public property or facilities, access to better financing, credits, or other incentives—with private-sector funding and expertise to achieve a government objective.

The Lake County case is a reminder that public-private partnerships remain a valuable tool for providing a coordinated and customized approach to housing. It's also a reminder that, while the public-private partnership framework encourages alliances and broad-based support, such projects are not immune from opposition. Local regulations and stakeholder dynamics are important considerations that can either support or hinder the public agency's objectives. In this case, local zoning regulations and building officials cleared the way for a project that would otherwise not be permitted absent the involvement of the housing authority but not before community opposition and a decision by a local zoning board delayed the project for two and half years. Given the cyclical and competitive nature of funding, justice delayed is often justice denied.

In recent decades, HUD has sought to use P3s to increase local control of housing efforts, partly in an effort to reduce the reliance on federal funds. The current administration's goals suggest that trend will continue. While there are unique challenges associated with negotiating and implementing a public-private partnership, P3s provide a unique opportunity to leverage private-sector expertise and resources to achieve a public objective.

PADS previously provided permanent housing for 13 chronically homeless individuals through a lease arrangement with a federal Veterans Affairs health-care center. Hospital administration notified PADS that it needed to reclaim the space, requiring PADS to relocate the residents. After looking for suitable replacement units for several years, PADS and the housing authority entered into a master lease, pursuant to which PADS would sublease units in a vacant facility, known as Midlothian Manor, to chronically homeless individuals, enabling PADS to preserve the existing 13 units and add a new unit. Midlothian Manor was acquired by the housing authority in 2001 as part of its non-federally funded housing inventory and was operated by the housing authority as an assisted-living facility for low-income seniors. Because it was never federally subsidized, the occupancy rate was perpetually low, and the housing authority closed the facility in 2010.

After PADS obtained permits for the proposed project from the local building department, nearby residents objected to the proposed reuse by filing a lawsuit seeking to stop the proposed project. The residents objected on the grounds that their homes and Midlothian Manor are located in the R-1 Residential District under the Lake County Unified Development Ordinance (UDO), which establishes zoning and development regulations throughout unincorporated Lake County. The R-1 district permits low-density, large-lot residential development. The objectors contended that re-occupancy of Midlothian Manor would be inconsistent with the R-1 district regulations.

After a two-and-a-half year battle, PADS, represented by DLA Piper LLP (US), successfully argued to the Circuit Court in November 2016 and then again to the Appellate Court in August 2017 that the project was permitted under the UDO as a "Government Use," which is a permitted use in all zoning districts under the UDO. "Government Use" is defined under the UDO as a "building or structure owned or leased by a unit of government and used by the unit of government in exercising its statutory authority." The effect of this definition is that a use which would otherwise be prohibited in a given zoning district is permitted when the governmental requirements of the definition are met, even though the uses may be functionally identical.

In upholding the building department's decision permitting the project, the Second District Illinois Appellate Court held in October that the housing authority's ownership of Midlothian Manor and the public-private partnership with PADS satisfied the definition of "Government Use." The objectors had argued that, with a public-private partnership arrangement, the property would not be "used by the housing authority," but would instead by used by PADS. The court rejected this argument and held that the public-private partnership leveraged the housing authority's express power to contract with and assist other entities—public or private—to reuse Midlothian Manor in a way that fits squarely within the agency's statutory purpose of providing safe and sanitary housing.

Affordable Housing Finance

By Mariah DiGrino

January 17, 2018

At DLA Piper, Mariah DiGrino concentrates her practice in the areas of land use and zoning, public-private financing, public incentives, historic preservation, and community and economic development.

Municipal Bond Funds See Record Inflows to Kick Off New Year.

Municipal-bond funds saw $3.1 billion of net new money last week, says ICI

It's only been a month and municipal bond funds are on a tear.

The Investment Company Institute estimated that muni bond funds saw net inflows of $3.1 billion for the week ending Jan. 10. That record-breaking sum is the biggest since the survey began in January 2007.

The bullish flows into munis represents a turnabout for the a sector that a few weeks ago looked bleak. As President Donald Trump's tax plans rushed toward completion, muni-focused mutual funds saw around $1.3 billion in net outflows in December.

At one point, the Republican tax bill threatened to do away with interest deductibility for municipal paper, which would have produced a major headwind for muni investing.

That's because the principal target investor for munis is wealthy individuals looking to cut their tax bill and earn tax-free interest income. Other measures included a repeal of private activity bonds, debt sold by municipalities to finance the projects of corporations like airports.

But sentiment over the sector swiftly turned bullish once the tax plan took its final and more benign form.

"Flipping that pancake to the other side, once the tax bill was finalized and signed, and once it became apparent that the tax rate for the top bracket was very high. Once that all became definitive, perhaps folks that took the outflow train took the inflow train," said Alan Shankel, municipal credit strategist for Janney Montgomery Scott.

Analysts now say negatives of the overall tax plan should be diminished. The Republican tax bill outlawed the use of so-called advanced refunding bonds, a roundabout way for municipalities to refinance their debt. Such bonds represented 15% of total issuance over the past decade, estimated Abigail Urtz, municipal strategist for FTN Financial.

The diminishing supply could give a boost to municipal bond-buyers and push yields lower. Debt prices rise as yields fall.

However, it may not all be rosy for munis.

Urtz said the outlook for demand could be a major wild card because one of the chief pieces of the bill was a cut to the corporate-tax rate to 21% from 35% this year.

The reduced corporate-tax rate may undercut appetite from banks and insurance companies, which have grown into significant players in the municipal-bond market (see chart lower). Banks now own more than $500 billion of the $3.8 trillion sector, according to Federal Reserve data.

"With banks the fastest growing buyers of municipals in recent years, fears about tax reform's impact on the municipal market have naturally focused on this provision," she said. "These buyers will be grappling with some sticker shock as previously cheap valuations start to look less appetizing."

Market Watch

by Sunny Oh

Published: Jan 18, 2018 7:32 a.m. ET

European Insurers Find Yield in U.S. Municipal Bond Market.

- **Higher credit quality than corporates fuels foreign interest**
- **Longer maturities are focus for European insurance companies**

The global hunt for yield is so vigorous that payments to protect against car losses, deaths and storms in Europe are helping to bankroll roads and utilities in the U.S.

The $3.8 trillion municipal-bond market, long the investment mainstay of U.S. residents, is seeing demand from European insurance companies drawn to higher yields and ratings than they can find closer to home. It's boosting the liquidity of a market where U.S. states and local governments raise money. And it's also providing a new source of business to asset managers.

"It's been very robust demand," said Ben Barber, head of municipals at Goldman Sachs Asset Management, which manages about $52 billion of the securities. "We're seeing brand new entrants into the market that are coming to institutional investors like us."

The interest from corporations such as Germany's Munich Re underscores the changing landscape in the municipal market, which is so U.S. focused that radio commercials for New York commuters tout local bonds. By the end of September, foreign buyers had increased their holdings of the securities to about $104 billion, more than double what they held a decade earlier, federal data show.

Municipals once held little allure overseas because federal tax breaks depress the yields. But in the era of low and even negative yields on global bonds, foreigners have taken a closer look, particularly in the taxable sector, where rates are higher.

Higher Quality

European insurers in particular are drawn to the higher quality of municipals compared with corporate debt. Sixty-seven percent of the Bloomberg Barclays Municipal Index is rated AA or higher, while just 11 percent of the comparable U.S. investment-grade corporate bond index is, according to an analysis by Matt Caggiano, who helps oversee more than $9 billion of insurers' municipal holdings at Deutsche Bank AG.

And for the higher credit quality, foreign investors are getting more in return, even considering currency fluctuations, according to an analysis from Bloomberg Intelligence.

To better match their liabilities, life insurers also favor longer-maturity bonds, which are more common in the municipal market than in the corporate world. And European Union regulations effective in 2016 allow insurers to put aside less in capital for holding infrastructure debt than corporate bonds.

"Municipals are an attractive investment, and we will use opportunities to accentuate our positions," said Josef Wild, a spokesman for MEAG, the asset manager for Munich Re, which provides reinsurance and insurance. The company likes municipals for their high ratings and spreads over

Treasuries and are using them to diversify its investments, he said by email.

New Funds

While Munich Re handles its investments internally, other insurers have outsourced their municipal strategies. Goldman Sachs Asset Management has seen its holdings of taxable municipals for European insurers increase by 89 percent in about a year. In September, Nuveen Asset Management launched a new high-grade municipal fund spurred by interest from clients outside the U.S., according to John Miller, co-head of fixed income. Overall, it's managing $2.5 billion in taxable municipals for foreign insurers as of the end of 2017 from nothing a little more than a year ago, he said.

To make room, some insurers are selling Treasuries, as well as European and U.S. corporate bonds, while others don't necessarily need to.

"There's a lot of cash being thrown off, and it's an easy way for them to make another allocation in decent yielding credit markets," said Jason Pratt, head of insurance fixed income at Neuberger Berman, which manages about $30 billion in assets for insurers.

Foreigners have made an impact: liquidity in taxable municipals has improved as trading activity shows, said Goldman's Barber. And new taxable deals have more potential buyers than bonds available than was seen in the past, said Deutsche's Caggiano.

The European insurers are likely to step up their purchases as they grow more comfortable with municipals, as yields remain competitive globally and as supply of taxable municipals picks up. Some analysts expect that the recent ban on advance refundings in the U.S., a previous source of tax-exempt debt, may compel issuers to refinance via taxable securities.

"We know from talking to potential clients that there's still capacity," Caggiano said.

Bloomberg

By Romy Varghese, Katherine Chiglinsky, and Julie Edde

January 19, 2018, 5:23 AM PST

Muni Bonds May Not Be the Reliable Bet They Once Were.

Investors should make sure to better understand the risks, and perhaps adjust their strategy accordingly

Can investors still use municipal-bond funds as core holdings in their taxable accounts?

For a long time, many have done just that—taking advantage of the bonds' big tax benefits, and using their low risk as a haven in times of stock-market turmoil.

But munis aren't looking like such a reliable bet anymore. Since the financial crisis, some big municipalities have defaulted on their obligations, while a number of states, cities and now Puerto Rico are currently facing financial woes. And bankrupt municipalities are increasingly making bondholders scrounge for what's left after paying employee pension funds.

So while it may still be possible to keep a muni fund as a core holding, investors should understand how the asset class has changed.

Price swings in the digital currency led to explosions in trading volume, assets under management and volatility at Bitcoin Investment Trust.

Municipal bonds offer investors interest that's tax-free at the federal level and at most state and local levels, if investors own bonds issued by any government entity within their state of residence.

When deciding whether to buy muni bonds, investors usually make a comparison between the yields of a muni bond and a U.S. Treasury note or bond of similar maturities. The "taxable yield equivalent" to a municipal bond is the municipal bond's yield adjusted for the investor's tax bracket.

So if an investor is hypothetically in a 50% bracket, including both federal and state taxes, a taxable yield twice that of a municipal yield—or a municipal yield half that of a taxable bond—would make two bonds equivalent. In that case, if a highly rated muni bond offered more than half the yield of a comparable U.S. Treasury, an investor could consider the muni bond the better choice in a taxable account.

A changed asset class

For decades, that was a reasonable comparison, and largely all that investors had to consider about munis. The chance of losing an investment was not even an issue: The historical default rate of the roughly $3.8 trillion market with more than 80,000 issuers has been low—0% for AAA-rated bonds and only 0.30% for AA- and A-rated bonds from 1970 through 2009, according to a Moody's study.

Unfortunately, municipal profligacy has begun to result in more high-profile distress and bankruptcy in recent years, including Jefferson County, Ala.; Detroit; Harrisburg, Pa.; Central Falls, R.I.; and Vallejo, San Bernardino and Stockton in California. Now the fate of more than $70 billion that creditors have lent to Puerto Rico is in doubt, as Hurricane Maria battered the island already struggling with manufacturing and population loss.

An updated Moody's study from 2016 notes that the "sector has changed over the past decade and more profound changes may be in the offing. The once-comfortable aphorism that 'munis don't default' is no longer credible, although default rates remain low."

In some cases, investors betting on munis have gotten burned. Recently, Franklin Double Tax Free Income fund merged with Franklin High Yield Tax Free Income fund (FHYVX) after it inflicted significant losses on investors. The fund had more than half its assets in Puerto Rico bonds.

Some analysts warn that many bond issuers are heading into precarious financial situations. In a 2016 research report from PNC Capital Markets, Tom Kozlik argues that around 20% of issuers haven't adjusted their spending to reflect diminished revenue after the financial crisis.

Mr. Kozlik doesn't cite names, but other observers have pointed fingers at issuers at risk.

"Though I'm not warning of an industrywide municipal-bond crisis, I think investors have to think carefully about individual credits and what, exactly, they're investing in," says Nicole Gelinas of the Manhattan Institute think tank. In the case of Chicago, "it's difficult to see, 10 years from now or even sooner, how, exactly, Chicago figures out [its problems with underfunded pensions] without bondholders having to take some sort of hit, as well." (Chicago officials declined to respond to a request for comment.)

And when a municipality goes bankrupt, investors aren't always first in line to recover their money.

Stockton and San Bernardino honored their obligations to state-employee pension funds at the expense of bondholders in their bankruptcies. “General obligation” bondholders, once thought to be above revenue bondholders in the case of defaults, aren’t necessarily ahead of unions.

Munis aren’t Treasurys
Not all municipal-bond experts are pessimistic. Tracy Gordon, a senior fellow at the Urban Institute think tank, says investors shouldn’t be alarmed about munis’ safety, emphasizing their low historical default rates. “It’s unfair to paint the whole sector with a broad brush,” she says.

But if investors choose munis as a core holding, many analysts advise using a diversified fund to lessen the risk of issuers defaulting. What’s more, investors shouldn’t expect the bonds to rally during a stock-market decline, as U.S. Treasurys often do.

That’s because munis have become closely tied to the health of state-employee pension funds. If stocks fall and pension funds lose money, the funds often turn to municipalities to make up losses—which makes muni bonds less attractive and hurts muni investors.

Indeed, the Bloomberg Barclays Municipal Index lost nearly 2.5% in 2008 during the stock crash—instead of providing municipal-bond investors with protection. That’s hardly catastrophic, but it might not have represented the resilience that the bond investors were expecting. And results might be less benign during the stock market’s next wipeout.

The Wall Street Journal

By John Coumarianos

Jan. 7, 2018 10:08 p.m. ET

Mr. Coumarianos, a former Morningstar analyst, is a writer in Laguna Niguel, Calif. He can be reached at reports@wsj.com.

SALT Shift Bolsters Munis' Appeal to Wealthy in High-Tax States.

- **With deductions capped, investors may look for new tax breaks**
- **Analysts expect uptick in demand from states like California**

Residents in New York, New Jersey and Connecticut who waited in queues to pay their property taxes early and take advantage of an expiring tax deduction may be lining up in 2018 to buy municipal bonds issued in their home states.

Strategists from Barclays Plc and Charles Schwab Corp. say demand for munis could increase from wealthy residents of high tax states this year because the Republican tax bill caps state and local property and income tax deductions at $10,000.

That kind of money doesn’t go a long way in Manhattan, where the average deduction per tax return is about $25,000 or Marin County, across the Golden Gate Bridge from San Francisco, where it’s about $17,000, according to the Tax Foundation. So residents may be eager to find other ways to reduce what they owe to the federal government.

“What are the remaining tax havens? Munis are still one of them,” said Mikhail Foux, the head of municipal strategy for Barclays in New York.

Californians, who pay a top income-tax rate of 13.3 percent or residents of New York City, which has a combined state and local rate of 12.7 percent, now have even more incentive to buy local debt because the interest is exempt from both state and federal taxes, he said.

Fewer Bargains

By increasing the cost of state and local taxes to wealthier residents, the federal shift may make it more politically difficult to raise taxes and curb the pace of bond sales backed by such revenue. Just four states — California, New York, New Jersey and Illinois — account for about 42 percent of long-dated, fixed-rate municipal bonds, Citigroup Inc. analysts led by Vikram Rai said in a Jan. 11 note to clients.

“A pullback on debt issuance by any of these states can cause a scarcity shock in the space for long-dated municipals,” they wrote.

At the same time, the increased demand for tax-free income may bring greater attention to mutual funds targeted at specific states.

Nuveen Asset Management’s California High Yield Municipal Bond is the best-performing open-end California municipal bond fund over the past 10 years, according to Morningstar Direct. It invests 36 percent of its assets in real-estate-related debt and has benefited from a run-up in property values since the Great Recession, said John Miller, Nuveen’s co-head of fixed income, who oversees $131 billion of muni debt.

Municipalities in California can sell bonds backed by assessments on homeowners to pay for roads and sewers in new neighborhoods.

“There’s really nothing that actually went into default in the last cycle in California in this type of bond,” said Miller, whose fund delivered annual returns of 6.25 percent for the 10-year period ending Dec. 31. “Some of these districts did trade 50-60 cents on the dollar. Now you have heavy, heavy overcollateralization.”

Miller said it will become harder to find bargains in the municipal market once the federal tax bill stokes even greater demand for higher-yielding California bonds. At the same time, limits on the ability of states and local governments to refinance their debt are promising to cut the pace of new sales.

“It’s going to get more challenging because pricing is tighter,” Miller said.

Low Defaults

Nationally, high-yield bonds offer a spread of about 2.7 percentage point more than AAA rated debt, but the premium is narrower for risky municipal debt issued in California, Miller said. And muni defaults remain low, with only $500 million defaulting for the first time in 2017, the least since 2008, he said.

“A growing economy tends to narrow spreads and low defaults tends to narrow spreads,” Miller said. “If spreads are narrowing, all else being equal, high-yield has an opportunity to outperform. You still have to pick the right credits.”

Delaware Funds Tax-Free New York Fund is the best performing New York retail fund over the 10-year period ending Dec. 31, returning 4.7 percent, according to Morningstar.

Almost half of the fund's assets are invested in bonds in the A or BBB category, with about 15 percent in junk-rated or non-rated bonds. The largest portion of its holdings, 23.1 percent, is in the education sector.

New York offers investors a diverse range of bonds, said Greg Gizzi, who helps manage Delaware's New York fund. For example, in the higher-education sector, the state has more than 100 private colleges and universities, from AAA rated Columbia University to BB rated Metropolitan College of New York.

"We're going to seek to diversify into those lower investment grade and those below investment grade categories despite the fact that we exist in a world that has constrained supply," Gizzi said.

Bloomberg

By Martin Z Braun

January 12, 2018, 7:34 AM PST

Bloomberg Brief Weekly Video - 1/11

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

Watch video.

Bloomberg

January 11th, 2018, 9:41 AM PST

Muni Market Set for Slow January After Tax-Fueled Rush to Market.

- **Citigroup says muni-bond sales unlikely to exceed $15 billion**
- **Muni market tends to outperform during January slowdown**

Municipal bond issuance could be poised for a multi-year low this month, setting up state and local debt to deliver hefty returns.

The drop in sales is expected to come after issuers rushed to sell a monthly record of bonds in December to avoid changes to the municipal market as part of federal tax reform. Municipal bond analysts say they expect very light issuance during what is typically a slow month for sales.

"I think you could see a record-low issuance," said James Dearborn, who oversees $29.5 billion as head of municipal bonds at Columbia Threadneedle Investments in Boston. "The forward calendar indicates it's going to be a very quiet month, if not quarter."

The 10-year low for January bond sales came after a similar rush to market when the Build America Bonds program was set to expire in 2010. Issuance totaled just $13.6 billion in January 2011, well below the $24.8 billion average for the month seen over the last decade, according to data compiled by Bloomberg.

Bond sales last month broke the previous monthly issuance record set in December 1985, which was driven by Congress' overhaul of the tax code. The next month, municipal bond issuance was a paltry $1.69 billion, according to Bond Buyer data. Bond sales are unlikely to fall below that figure, though, as $722 million in bonds have already been sold this month as of Jan. 5 and $3.6 billion in sales are scheduled for the week of Jan. 8 alone, according to data compiled by Bloomberg.

RBC Capital Markets is forecasting muni-bond sales of $10 billion in January, while Citigroup analysts say they would be "extremely surprised" if issuance exceeds $15 billion. Other analysts say they are hesitant to give a forecast for January given the mad dash to sell late last year.

"There are definitely deals that are going to be coming over the next couple of weeks, but it's difficult to figure out which issues are left to get done in January because of the deals that got accelerated," Tom Kozlik, managing director and municipal strategist at PNC.

The municipal bond market typically outperforms in January due to a drop-off in supply combined with investors looking to reinvest cash received from matured bonds and coupon payments.

While it's "nearly impossible" to predict supply this month, the drop-off in sales will cause this trend to continue, said Peter Block, managing director at Ramirez & Co. Net supply stood at negative $9.5 billion on Jan. 5, with $9 billion in bonds set to mature and $8.7 billion in bonds being called, according to data compiled by Bloomberg.

"Demand is going to be extremely high and you're going to see municipals outperform Treasuries because of the principal and interest that's been received," he said. "That's how the dynamic is going to be received."

Bloomberg Markets

By Amanda Albright

January 9, 2018, 4:00 AM PST

— With assistance by Elizabeth Campbell

[The Week in Public Finance: Deficits in 25 States, Exxon Sues California Localities, and New Jersey's Lottery Claim.]

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

GOVERNING.COM

BY LIZ FARMER | JANUARY 12, 2018

[Multifamily Housing Bond Issuance May Drop in 2018.]

WASHINGTON – Issuance of multifamily bonds may drop this year from the recent high of $14 billion in 2016, according to experts at a recent housing conference who were uncertain whether the decline will be significant.

Multifamily housing bond issuance had been expected to decline last year from the 2016 peak, but some projects were rushed to market at the end of 2017 when private activity housing were nearly terminated under tax reform.

"Part of the drop off, if there is one, might be that many states issued as many bonds as they could to make sure they preserved that bond authority," Garth Rieman, interim executive director of the National Council of State Housing Agencies, told The Bond Buyer.

Final Thomson Reuters' (TRI) data on housing issuance for 2017 won't be released until February.

Multifamily housing bonds have been the largest component of PAB issuance subject to state volume caps and Rieman expects that to continue.

The demand for affordable housing remains "extraordinary," Rieman said adding, "I think there are a lot of underlying reasons why production will remain high."

On the plus said, Rieman expects a pickup in use of mortgage revenue bonds by states to assist first-time homebuyers. "As interest rates rise, that creates a little bit more separation between tax-exempt rates and taxable rates which may allow tax-exempt bonds increase activity," he said.

Some of the MRBs used in early 2018 will be left over from late 2017, Rieman cautioned, but state housing finance agencies overall are likely to support more single-family home purchases this year.

Housing advocates remain hopeful that Congress may act on bipartisan bills to enhance the low-income housing tax credit which is linked to housing bonds in financing about half of the nation's multifamily housing rehabilitation and new construction.

The bipartisan Affordable Housing Credit Improvement Act (H.R. 1661) has 122 cosponsors in the House and the companion bill in the Senate (S. 548) has 22 cosponsors, including Senate Finance Committee Chairman Orrin Hatch, R-Utah.

Housing experts who attended a recent panel discussion here sponsored by the National Conference of State Housing Agencies also hope Congress and the Trump administration can be persuaded to include affordable housing in their plans for infrastructure spending.

"Elements like that might support more activity later this year," Rieman said.

For now, public housing agencies and developers are adjusting to the tax changes enacted by Congress that make housing bonds a less attractive investment.

The drop in the corporate tax rate to 21% from 35% is expected to make housing bonds less attractive as investments, experts agreed during the panel discussion.

There will be changes in housing bond pricing but nothing as extreme as what happened in the 2008-2009 Great Recession, said Anthony Freedman, a partner at Holland & Knight.

"The substance of the program hasn't changed at all," Freedman said.

"We weren't devastated, but we definitely were damaged," said Michael Novogradac, the managing partner in the San Francisco office of Novogradac & Co. His firm estimates the tax changes will produce a roughly a 14% drop in the value of investing in projects using the low-income tax credit which is often paired with housing bonds.

"In terms of what impact that is going to have coming up, I wish I knew," Novogradac said. "I know it's negative. I know it's adverse."

Foreign banks, in particular, are reassessing their investments because of complex new rules involving the base-erosion and anti-abuse tax (BEAT) said Priya Jayachandran, senior vice president for housing development at Volunteers of America.

Jayachandran, who is taking over as president of the National Housing Trust on Feb. 1, said another possible setback for affordable multifamily housing development this year would be if interest rates rise.

Scott Hoekman, senior vice president and chief credit officer of Enterprise Community Investment, said that despite the negatives of the new tax law, "The final changes are survivable."

The multifamily housing sector is flexible enough to figure it out how to cope, Hoekman said.

"What would have turned our world upside down was if private activity bonds had been eliminated," Hoekman said.

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 01/12/18 07:08 PM EST

Chicago Suburb Follows City with Securitization, Bypassing Junk Rating.

CHICAGO – A junk-rated Chicago suburb is following the city's lead by securitizing its state supplied sales tax revenue in a $47 million deal.

The bonds priced Wednesday, according to underwriter George K. Baum & Co.

The village of Bridgeview southwest of Chicago published an offering statement and investor presentation Monday. Fitch Ratings released its report assigning a BBB-plus rating to the deal on Tuesday.

At the same time, Fitch gave the village a first-time issuer default rating of BB-plus, one notch below an investment grade. S&P Global Ratings in March dropped the village to the speculative grade level of BB-minus when it cut its rating by four notches from BBB.

Chicago's Sales Tax Corporation received a AAA rating from Fitch ahead of its inaugural $575 million securitization earlier this month that refunded sales tax bonds. It returns next month with a $795 million issue to refund general obligation bonds.

The village has struggled to manage its debt burden after its investment in a stadium to house Major League Soccer's Chicago Fire has fallen far short of fiscal expectations.

The village of 16,000 issued $135 million for the stadium in 2005, which has been followed by tax increases, asset sales, refinancings and restructurings. Bridgeview, which has about $240 million of debt, had previously been considering restructuring debt beyond the useful life of the stadium, according to S&P.

The securitization sale included a tax-exempt A series for $26.6 million and a taxable B series for $20.4 million. The borrower is the special purpose entity Bridgeview Finance Corp.

Baum is the sole underwriter and Austin Meade is advising on the deal.

Proceeds will ease pressures on the village's balance sheet by refunding its 2008A-2 bonds, covering a debt service payment on the village's series 2005 bonds, and financing some capital projects. The B series will refund the village's series 2008B-1 and series 2008B-2 bonds, eliminating the village's floating-rate obligations.

The new securitization bonds hold a first lien on the village's state-collected portion of its home rule sales tax and local share of the statewide sales tax.

"The BBB-plus sales tax securitization bond rating is based on the bankruptcy-remote, statutorily defined nature of the issuer and a bond structure involving a perfected first lien security interest in the sales tax revenues," Fitch wrote.

The legal structure supports a true sale of the revenues and, in Fitch's opinion, insulates bondholders from any village operating risk. Under the structure, the village will sell all right, title and interest in the pledged revenues to the corporation and the state will direct all pledged sales tax revenues to the trustee.

Louis F. Cainkar Ltd. is bond counsel to the corporation. Burke Burns & Pinelli Ltd. is counsel to the corporation and Quarles & Brady LLP is disclosure counsel. Nixon Peabody LLP is special bankruptcy counsel.

Nixon Peabody gives its "reasoned and qualified opinion" in the offering statement that were the village to enter a bankruptcy – which is not currently allowed under state law – the corporation "would not be subject to substantive consolidation with the village nor would payments to bondholders be subject to the automatic bankruptcy stay."

The village's finance director referred calls for comment on the transaction to Dan Denys at Austin Meade but he did not return calls to discuss the deal.

The review of the pledged sales tax being leveraged drove the sharp contrast between the Bridgeview and Chicago ratings. Bridgeview faces stagnant growth prospects in its pledged tax revenue and the tax base faces risks from a concentration of the top 10 tax generators accounting for over half of pledged sales taxes.

The differential in ratings "proves the point that we look at the underlying sales tax base," Fitch analyst Matthew Wong said in an interview.

"It's a very stark contrast with Chicago," analyst Amy Laskey said.

Fitch said a severe decline would pressure the rating but collections have shown resilience through economic cycles. Coverage is strong and sales tax revenue is able to tolerate a 66% decline to 1 times coverage. No additional debt is allowed under the bond resolution.

Fitch's speculative grade issuer default rating reflects a "very high liability burden" that includes its bonded debt and pension liabilities which are at 61% of village personal income.

“The village has made several budget management decisions in the last several years that have eroded its ability to support operations, including general obligation backing of the Chicago Fire stadium,” Fitch wrote. “Fitch expects that ongoing budget management may be somewhat constrained by the sales tax securitization issuance as it diverts a portion of its sales tax revenue away from the general fund to pay for debt service and may require a corresponding increase in property tax rates.”

The Illinois General Assembly approved the new local borrowing program over the summer at Chicago’s behest as a means to bypass weak general obligation ratings by using a bankruptcy-remote structure.

Some market participants say the sturdiness of the new structure can’t truly be known until tested. They cite the ongoing challenge to some Puerto Rico’s debt. Others warn that the program could be abused by borrowers that lack fiscal restraint.

The stark rating differences between Chicago and Bridgeview provide “a great example of why techniques like securitization have to be viewed on an individual basis,” said Joseph Krist, a partner at Court Street Group LLC. “Securitization in and of itself is not a panacea for credits across the board.”

Krist said he sees why the securitization is attractive to the village because it provides a path to achieve some of its fiscal goals while addressing a market concern over its GO credit largely due its investment in a sports stadium that has disappointed.

When S&P junked the rating in March, it placed the rating on CreditWatch for a possible further downgrade due to concerns over market access and weakened liquidity. S&P removed the watch status and assigned a negative outlook in August after the village successfully modified its letter of credit with BMO Harris Bank NA. The village had been looking at borrowing to pay off $25 million of debt. BMO agreed to an extension of its amortization schedule. The securitization sale will allow the village to shed the floaters.

By Yvette Shields

BY SOURCEMEDIA | MUNICIPAL | 12/20/17 07:18 PM EST

S&P: U.S. Not-For-Profit Health Care Sector 2018 Outlook: Balance Sheet Strength Drives Stable Outlook Despite Expectations That Operations Will Weaken.

S&P Global Ratings has affirmed its stable outlook on the U.S. not-for-profit health care sector for 2018. Our view is based on the overall strength of balance sheets in the sector…

Continue Reading

Jan. 11, 2018

S&P: U.S. Local Government Sector 2018 Outlook: Resourcefulness Will Be Key To Managing New Obstacles.

Resiliency and resourcefulness will be increasingly important in U.S. local government credit analysis in 2018. When we published our 2017 U.S. Local Government Outlook in January 2017, we described the sector as stable and resilient.

Continue Reading

Jan. 10, 2018.

S&P U.S. State Sector 2018 Outlook: Short-Term Gain, Long-Term Strain.

Tightening labor markets and the increased business investment that could accompany corporate tax rate reductions have the potential to strengthen economic conditions in 2018. Subject to caveats related to geopolitical risk and ongoing policy uncertainty, S&P Global Ratings believes that on slightly firmer economic footing throughout the next year, U.S. states could enjoy an uptick in revenue…

Continue Reading

Jan. 9, 2018

NABL: House Problem Solvers Caucus Releases Infrastructure Report.

The bipartisan House Problem Solvers Caucus Infrastructure Working Group released its report on infrastructure policy recommendations. The report entitled, "Rebuilding America's Infrastructure," calls for, among other things, the preservation and expansion of "tax-advantaged infrastructure financing options by maintaining the federal tax-exempt status for municipal bonds and private activity bonds as well as increasing the private activity bond state volume cap for all infrastructure categories."

The report is available here.

Market Commentary: Issuance Stalls, Investors Take Profits on Instability.

Below we review the market this past week as well as how December was a record-breaking month for the municipal market. Next week, we will publish our full 2018 Outlook for the municipal industry.

Issuance Stalls and Investors Take Profits on Political Instability

Over the last week munis have outperformed Treasuries on most parts of the curve. While the Dow Jones Index hit all-time highs, we are seeing investors profit-take and move into safer assets given the political instability associated with the current Administration and international affairs.

The conflux of international politics and the historical record of economic trends in the United States, converging with Dodd-Frank regulations and an expected lower issuance flow for investors leads us to believe that outperformance to Treasuries and other domestic fixed-income asset classes is expected. Issuance thus far in January has been very low and expected issuance for the rest of the month confirms this expectation.

Continue reading.

Neighborly Insights

Posted 01/08/2018 by George Friedlander

This Market Commentary is brought to you by Court Street Group.

Market Commentary: The 2018 Outlook for Investors.

The start to this year is the most complex and uncertain transition in the municipal bond market since the 1986 Tax Reform, due to four main factors:

1) The impact of the Tax Reform Law on the supply/demand structure of the market

2) The continuing move toward higher short-term rates

3) The potential for an infrastructure bill of uncertain size and scope, and other concerns about infrastructure

4) Likely continued erosion in average credit quality.

Continue reading.

Neighborly Insights

Posted 01/09/2018 by George Friedlander

This Outlook is brought to you by Court Street Group.

Bipartisan Report Underscores Hard Truths About Infrastructure Funding.

"Our attention has been on that baseline has not really been adequately funded, or appropriately dealt with," according to U.S. Rep. Elizabeth Esty of Connecticut. "That needs to be addressed."

WASHINGTON — Recommendations for upgrading the nation's public works that a bipartisan group of House lawmakers released this week underscore the difficult budget math Congress will face coming up with the money for any eventual White House infrastructure plan.

The Problem Solvers Caucus, a group of 48 lawmakers, outlined their recommendations in a report issued Wednesday. Reps. John Katko, a New York Republican, and Elizabeth Esty, a Connecticut

Democrat, led a caucus working group that authored the report.

In the backdrop, is a yet-to-be-released proposal from the Trump administration for major new investment in the nation's roads, bridges, waterworks and other infrastructure.

Details that have surfaced so far suggest that the White House is aiming for $200 billion of direct federal investment, with the hope of attracting another $800 billion from state, local and private sources.

[Continue reading.]

ROUTE FIFTY

BY BILL LUCIA

JANUARY 11, 2018

[White House Updates Senators on Trump's Infrastructure Plan.]

Administration officials told the lawmakers to expect more details about the proposal around the time of the president's State of the Union address, Sen. John Barrasso said Wednesday.

WASHINGTON — The top Republican on the Senate's public works committee said Wednesday that Trump administration officials informed him and other lawmakers in a meeting Tuesday that the White House would release details about its infrastructure plan around the time of the president's Jan. 30 State of the Union address.

"Certainly within the next month," Sen. John Barrasso, the Wyoming Republican who chairs the Environment and Public Works Committee, told reporters, as he discussed when additional information about the proposal would be released.

White House officials previously signaled that they were aiming to release the long-awaited plan sometime in January.

Barrasso said that most members of his committee, both Republicans and Democrats, attended Tuesday's meeting. White House officials that were on hand included Secretary of Transportation Elaine Chao, chief economic adviser Gary Cohn and DJ Gribbin, who is a special assistant to the president on infrastructure policy, according to Barrasso.

The committee's ranking member, Sen. Tom Carper, of Delaware, described the meeting as civil and constructive.

Both he and Barrasso sidestepped questions about where lawmakers might find the $200 billion of federal funding the White House has indicated it would like to see included in its infrastructure package.

"We'll talk about it as time goes on," Barrasso said in response to a question about whether he had any preference for where the money could come from.

Asked if he had a favored approach for how to come up with the $200 billion sum, Carper responded: “Not today.”

Trump administration officials have previously described a plan that would involve $200 billion of direct federal spending over a decade, combined with $800 billion from private and state and local government sources. Carper said he and other Democrats are skeptical the $200 billion could be “leveraged” to come up with the $800 billion.

“Can we save some money on streamlining? Sure. We’ve already done that. Can we do more? Probably. Can we better leverage private sector money, and money from other sources? Probably,” Carper said. “Does it add up to $800 billion? I’m not sure that it does.”

The White House has also indicated that thinning down and speeding up federal permitting and approval processes for projects will be a part of its program.

Trump in a separate bipartisan meeting with lawmakers on Tuesday continued to tout the viability of his pending public works plan—one of his stated priorities since taking office.

“One thing that I think we can really get along with on a bipartisan basis—and maybe I’m stronger on this than a lot of the people on the Republican side, but I will tell you, we have great support from the Republicans—is infrastructure,” he said, according to a White House transcript of the meeting.

“I think we can do a great infrastructure bill,” the president continued. “I think we’re going to have a lot of support from both sides, and I’d like to get it done as quickly as possible.”

Carper noted that Republicans on the Environment and Public Works Committee are working on authorizing language that could guide new spending on infrastructure that is called for in the White House plan, and that Democrats are working on a similar package.

But he added: “We need for the administration to show us their proposal. Not just principles. But what do they actually want to do.”

ROUTE FIFTY

By Bill Lucia,

JANUARY 10, 2018

Whiplashed Planners Fear GOP Swerve on Infrastructure.

After close call on public-private financing tool, all eyes on 2018

Los Angeles has gained national notice for a series of ambitious projects affecting all facets of southern California’s transportation network, from the city’s light rail system to Los Angeles International Airport.

Many of the projects — a multibillion dollar expansion of the airport, work on roads leading to and from the busy ports of Los Angeles and Long Beach and a new light rail line, among others — were or will be financed with a tool called private activity bonds.

Known as PABs by those who use them, the bonds are issued by public-sector authorities to raise tax-exempt financing for private entities doing a project with a public benefit. Buyers of the bonds don’t have to pay tax on the interest income, allowing the issuer to borrow at a lower rate than would otherwise be available.

But Republican lawmakers sent a shudder through the groups that rely on the financing tool by proposing to eliminate the tax exemption in versions of the tax overhaul bill cleared by Congress just before Christmas.

“I think surprised is an understatement,” said Annie Russo, vice president of government affairs at Airports Council International-North America, a Washington group that describes itself as “the voice of airports.”

Congress eventually decided to keep the exemption, but the proposal to do otherwise put a spotlight on the importance that stakeholders give to private activity bonds. The proposal, which originated in the House tax bill and wasn’t matched in the Senate version, also raised questions about what could be included in Republican plans for infrastructure legislation in 2018.

President Donald Trump campaigned on a pledge to spend $1 trillion on infrastructure over 10 years. He had said most of that would come from the private sector, but has more recently been quoted saying he doubts the value of public-private partnerships. The administration is expected to deliver a plan early this year.

In and out of Washington, some who work in the transportation sector had hoped the tax bill would include provisions to help pay for infrastructure projects, or at least provide incentives for the private sector to do more. At one time in the run-up to the tax bill, Republicans even talked about encouraging corporations to repatriate profit held abroad and steering that money into infrastructure projects.

So the House Republicans’ proposed treatment of private activity bonds caught the industry off guard. Some saw the potential for hundreds of millions of dollars in additional interest costs on projects already underway. The House summary of its tax proposal — referring to the exemption as a giveaway — rang alarm bells on Republican thinking about the future.

According to Adam S. Wallwork, a public finance lawyer at Ballard Spahr, private activity bonds are a $102-billion-a-year business, representing 20 percent of the tax-exempt bond market.

Flying high on PABs

Airports in particular rely on private activity bonds for work on terminals.

Under the last major tax code rewrite in 1986, commercial U.S. airports — despite being almost universally owned and operated by public entities with bond-issuing authority — cannot issue standard municipal bonds for improvements to terminals because they benefit private companies like airlines and shops and restaurants.

But airport terminals have a clear public benefit, and therefore qualify for tax-exempt private activity bonds.

“Almost any” expansion or renovation of an airport terminal is financed through private activity bonds, Russo said.

Several parts of the Los Angeles airport’s multibillion-dollar overhaul — including a $5.5 billion “automated people mover” to connect the airport terminals to the city’s transit system, a new 18-gate international terminal and major renovations to other terminals — were financed through private activity bonds.

Mark Waier, director of communications for the Los Angeles airport, said PABs would finance about $5.1 billion of the roughly $8 billion of spending remaining to complete the project. Losing the tool could add $500 million just to interest payments on that total, he said.

Waier won't speculate on how the loss of that financing would affect the project, but said it would require either a new source of revenue or a smaller scope of one or more components of the program.

"If this was eliminated, we would need to either identify new sources of revenue or make a reduction to scope that would equate to $500 to $550 million out of our capital investment plan," he said.

A tool for transit

Unlike airport terminals, public transit systems haven't traditionally relied on private financing for expansions, but major projects in recent years included private partners, making private activity bonds an option for funding. Transit agencies that now have access to federal Transportation Infrastructure Finance and Innovation Act, or TIFIA, loans and local payments would be better positioned to work with a private partner.

"It's one more tool in the toolbox," said Rob Healy, vice president of government affairs for the American Public Transportation Association.

Denver's $2.2 billion Eagle public-private partnership project combined a number of development options. The project, which added two new light rail lines and the starting component of a third, got the bulk of its funding through a 2011 $1.03 billion grant from the Federal Transit Administration.

But its second-biggest source was private activity bonds, which provided $398 million for the project, according to the Department of Transportation. Other funding and financing sources for the Eagle project include new sales tax revenues, a TIFIA loan, other federal grants and private equity contributions.

A furious response

The House proposal to drop the tax exemption engendered a backlash in part because it contradicted one of Trump's early ideas for an infrastructure package — incentives for private sector involvement.

Private activity bonds have been used for "pretty much every project" that's part of a public-private partnership, said Robert Puentes, president and CEO of the think tank Eno Center for Transportation. So far, PABs have worked well and without much controversy. Taking them away wouldn't serve anyone's interest, he said.

"It doesn't seem to serve any public interest to get rid of it at this point, unless there are some kind of egregious problems," Puentes said. "But it's the opposite that we're seeing."

The near-universal outcry from infrastructure stakeholders that greeted the House proposal on PABs produced some echoes on Capitol Hill.

Senate Commerce, Science and Transportation Chairman John Thune, a South Dakota Republican who served on the conference committee that negotiated the final tax bill, told reporters during negotiations that PABs had fierce support in both chambers, leading to the removal of the House provision.

That account was backed up by a Dec. 13 letter from 39 House Republicans calling for members of the conference committee to protect private activity bonds. The letter nodded at Trump's onetime proclamation that private sector money would be a key part of his infrastructure plan.

"Given the administration's stated priority for increasing investment in infrastructure, we believe the elimination of tax exempt private activity bonds would be a step in the wrong direction toward fulfilling the president's goal," they wrote. "In fact, it will make infrastructure projects more expensive."

But the criticism of private activity bonds in some ways aligns with the critique of public-private partnerships generally. The difference is that Republicans were the critics of the interest exemption on PABs, while Democrats are more likely to criticize proposals that turn public infrastructure assets over to private operators in exchange for investment.

A summary of the original House proposal said PABs were essentially a giveaway to private interests that created an uneven playing field.

"The federal government should not subsidize the borrowing costs of private businesses, allowing them to pay lower interest rates while competitors with similar creditworthiness but that are unable to avail themselves of PABs must pay a higher interest rate on the debt they issue," the summary said.

The House proposal may also have failed to split some hairs among Republicans who like the bonds for transportation projects, but dislike their use for things such as sports stadiums and housing.

A 2016 Brookings Institution paper said private activity bonds are sometimes used to finance professional sports stadiums, a popular punching bag for those deriding "corporate welfare."

Small-government conservatives have issues with the use of private activity bonds for housing, which accounts for about 80 percent of the private activity bonds issued, said Marc Scribner, a senior fellow at the libertarian Competitive Enterprise Institute. When used for housing, the bonds can turn into tax breaks for well-connected developers without fixing the fundamental problems driving housing shortages, he said.

But in terms of transportation infrastructure, the bonds encourage private sector involvement, and CEI has supported them for transportation projects, especially highways, he said.

The House bill's solution to scrap the entire private activity bond function would hurt the ability of the private sector to spend on transportation infrastructure, he said. The system could be improved, but eliminating private activity bonds completely would be a mistake, tantamount to "throwing the baby out with the bath water," Scribner said.

"If you want to increase the private sector in the provision of public-sector infrastructure, eliminating private activity bonds is a really bad way to do that," he said.

The measure was "not very well thought out and certainly not thought out in terms of broader goals outside of tax issues," he said.

rollcall.com

by Jacob Fischler

Jan 10, 2018

Yearend Sales Boost 2017 U.S. Muni Bond Supply to $410 bln.

CHICAGO, Jan 2 (Reuters) – U.S. states, cities, schools and other issuers sold $410 billion of debt in 2017, with 14.5 percent of the total hitting the municipal market in December ahead of federal tax changes, according to Thomson Reuters data on Tuesday.

The supply, which was 3.2 percent lower than in 2016, got a last-minute boost from issuers racing to the market in late November and in December to sell certain types of tax-exempt bonds at risk in federal tax legislation signed into law on Dec. 22 by President Donald Trump.

December's $59.56 billion of long-term debt was a monthly record for the $3.8 trillion market, beating the $57 billion sold in December 1985 ahead of 1986 federal tax changes, Thomson Reuters data showed.

Bank of America Merrill Lynch was the top underwriter of municipal bonds last year with nearly $63.2 billion in 547 deals. Citigroup followed with $46.67 billion 518 deals.

California was 2017's biggest issuer with $8.87 billion of debt sold, followed by New York State Dormitory Authority with $7.43 billion, and New York City Transitional Finance Authority with $6.5 billion. Illinois ranked fourth with $6.25 billion. The state sold $6 billion of general obligation bonds in October to raise money to shrink its enormous pile of unpaid bills from vendors and service providers.

(Reporting by Karen Pierog; Editing by Tom Brown and Richard Chang)

Public Bank Movement Gains Ground in Cities and States across the US.

A growing number of cities across the US are considering launching city-owned "public banks," reports Deonna Anderson in Next City. Among these are Portland, Oregon; Seattle, Washington; Los Angeles, San Francisco, and Oakland, California; Philadelphia, Pennsylvania; Santa Fe, New Mexico; and Washington, DC. Nationally, the Public Banking Institute, an advocacy nonprofit, has been supporting these and many other campaigns.

At the state level, Anderson notes that in New Jersey, the governor-elect "expressed interest in establishing a state public bank during his campaign." Governor-Elect Phil Murphy's endorsement of the concept of a public bank may be a watershed of sorts. Murphy spent 23 years at Goldman Sachs, so he knows a thing or two about finance.

Actually, Murphy's rationale for supporting a public bank in New Jersey has a lot to do with what he learned on Wall Street. According to Katherine Landergan of Politico, on the campaign trail, Murphy noted that,

> When New Jersey collects taxes or fees, it currently deposits those funds in private banks—spreading the state's money across American and international institutions. Those banks, in turn, charge fees … and they use the capital from New Jersey's deposits

to provide loans or finance projects.

“They’re not being obligated to come back and do anything in New Jersey, and they don’t.”

Continue reading.

NPQ

By STEVE DUBB | January 2, 2018

The Biggest Issues for States to Watch in 2018.

Even though it’s an election year, these policies and problems are too important and timely for legislatures to ignore.

Nothing big happens in election years. At least, that’s the conventional wisdom on legislative action in many state capitols.

And in a year when 36 states will choose governors and 44 will elect state lawmakers, that feeling is understandable. Political paralysis in Congress is also keeping many states in a holding pattern, as their officials try to judge how best to react to potential changes from Washington.

But many state issues are simply too important or too timely to wait. Here are a few that will likely draw a lot of attention this year.

Continue reading.

GOVERNING.COM

BY NEWS STAFF | JANUARY 2018

Hatch Retirement Could Help Muni Market in 2019.

WASHINGTON – The outlook for the tax treatment of the municipal bond market could be brighter in 2019 when Senate Finance Committee will have a new chairman.

That’s because one of the leading candidates for the position is Sen. Mike Crapo, R-Idaho, who “the bond community would welcome,” said Chuck Samuels, a member of Mintz Levin who is counsel to the National Association of Health & Educational Facilities Finance Authorities.

“Crapo has been a stalwart supporter of municipal bonds both for private activity bonds and a supporter of liberalizing … bank qualified” bonds, Samuels told The Bond Buyer Wednesday.

Bank-qualified bonds were created by the Tax Reform Act of 1986 to encourage banks to buy tax-exempt bonds from smaller, less frequent issuers. Banks can buy these bonds from governments that reasonably expect to issue a total of $10 million or less of bonds in a calendar year and deduct a portion of the interest cost of carrying the bonds.

The annual limit was raised to $30 million from $10 million during 2009 and 2010 under the American Recovery and Reinvestment Act of 2009.

Bob Labes, a partner at Squire Patton Boggs in Cleveland, said Crapo has a record of supporting legislation to strengthen municipal bonds.

The Senate Finance Committee's current chairman, Sen. Orrin Hatch, R-Utah, announced Tuesday that he will not seek re-election next November. Hatch is expected to remain chairman for the remainder of his term, which ends in January 2019.

Hatch led the successful Senate effort last year to preserve the tax exemption for private activity bonds in the new tax reform law.

Democrats could regain majority control in the Senate in the November election, which would enable the committee's ranking Democrat, Sen. Ron Wyden of Oregon, to regain the chairmanship he previously held.

The municipal bond community also would be comfortable with Wyden as chairman, Samuels said, adding. "I don't think he will give anybody a free pass. He and his staff want an understanding of why things are the way they are and how they may be changed."

Crapo, 66, is serving his sixth term in the Senate and currently serves as chairman of the Senate Banking, Housing and Urban Affairs Committee.

Seven-term Sen. Charles Grassley, 84, has more seniority on the Senate Finance Committee than Crapo, but the Iowa Republican could choose to remain as chairman of the Judiciary Committee. In that role earlier this year, he oversaw the nomination and confirmation of Neil Gorsuch to be an associate justice of the Supreme Court of the United States as well as 12 federal appeals court justices.

Micah Green, a partner at Steptoe & Johnson, gave Crapo and Grassley similar ratings on their support for the muni market. "I don't look at them as, by definition, opposed to the municipal marketplace," he said. "In the end the Senate in the showed great support for private activity bonds and I think Crapo and Grassley were both supportive these."

Crapo, for his part, 'is not speculating on any transitions as this time as there are many factors that affect all this, not the least of which is which party controls the Senate," his spokesman Robert Sumner said in an email.

If Grassley should choose to take the top spot on the Finance Committee, he would only have two years remaining in the six-year term limit Senate Republicans has set for committee chairmen.

"Grassley has done it already and the question is, how does he balance it out with the judiciary process," said Green. "There will be a new senior Republican on the committee who, unless something changes, will be chair."

Labes said Grassley has supported legislation to expand the use of student loan bonds.

"Grassley was a very active chairman during the time he was chairman,'' said Howard Gleckman, a senior fellow in the Tax Policy Center. "He maintained to some degree a sense of bipartisanship but that began to change even while he was there."

Grassley's record on municipal bond issues is mixed, according to Samuels. Although Grassley "has many concerns and skepticisms about municipal bonds, he also is a strong protector" of Iowa's small rural hospitals and small private colleges, he said.

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 01/03/18 07:03 PM EST

2018 Outlook: More Tax Legislation and Possible Supreme Court Ruling.

WASHINGTON – Republicans in Congress expect the wide-ranging tax overhaul law just enacted will be followed by more tax legislation in 2018 that includes extensions for expired tax provisions such as one that would extend qualified zone academy bonds though 2017 and an excise tax on imported rum that benefits Puerto Rico and the Virgin Islands.

Senate Finance Committee Chairman Orrin Hatch, R-Utah, introduced the tax extenders bill the day after the Senate approved tax reform legislation.

The Senate extenders bill would continue for 24 months more than a dozen tax breaks that expired at the end of 2016, including a rum cover-over excise tax that produces revenue for Puerto Rico and the U.S. Virgin Islands to pay for local government operations.The QZAB extension only goes through 2017 because the new tax law terminates tax credit bonds after Dec. 31. Other extenders are energy-related, including a nuclear energy production tax credit.

Congress also will need to enact a technical corrections bill in the coming months to fix drafting errors and loopholes in the new tax law.

"It is inconceivable that Congress will not have to act early in the year on a technical reform bill," said Frank Shafroth, director of the Center for State and Local Leadership at George Mason University.

Shafroth said the "cataclysmic rush" to enact the legislation bore not even a remote comparison to the outreach and deliberations over the last tax reform bill in 1986.

"Because the legislation will have such a significant impact on increasing the federal deficit and debt, it seems certain that interest rates will rise, thereby increasing the cost of debt issuance for not just state and local governments but also for schools and universities," Shafroth said.

Meanwhile, the U.S. Supreme Court is expected to decide soon whether to consider a case involving South Dakota that would have nationwide impact on the ability of state and local governments to collect sale taxes on Internet purchases.

In addition, Congress may consider reforming the Internal Revenue Service to make it more customer friendly, according to House Ways and Means Committee Chairman Kevin Brady, R-Texas.

"My sense is that there could be broad bipartisan support for restructuring the IRS," Brady told reporters on Dec. 18.

Brady said the tax bill left out provisions that were dropped at the last minute because of the Senate's parliamentary Byrd rule as well as other proposals. Under that rule the Senate cannot include non-germane provisions without revenue implications via the reconciliation process or measures that would add to the federal deficit after the 10th year.

“This is not our last tax reform,” Brady said. “I’m going to recommend that we do have some form of tax reconciliation in future budgets because there are still areas of the tax code I think and we think can be improved whether it’s retirement savings, education, streamlining and we had a number of good ideas from our members we weren’t able to accommodate.”

Further tax legislation could provide an opening for municipal bond market issuers who think Congress left them in the lurch by not giving them a transition period before the termination of advance refundings and tax credit bonds.

Congress also will get pushback in 2018 from state and local governments on its controversial decision to limit to $10,000 per household the federal deduction for property and income or sales state and local taxes.

“Cities will continue to fight to fully restore SALT and the exemption for advance refunding bonds,” said National League of Cities President Mark Stodola, mayor of Little Rock, Ark.

U.S. Conference of Mayors President Mitch Landrieu, the mayor of New Orleans, described the tax legislation as “a full-fledged assault on cities and the families who live in them.”

“This bill will make our cities harder to live in and harder to run effectively -- all for the benefit of wealthy political donors,” Landrieu said.

Because Congress repealed the individual mandate requiring taxpayers to purchase health insurance, “Republican and Democratic mayors, not Washington politicians, will contend with emergency rooms filling up with the sick and the uninsured,” Landrieu said.

But repeal of the health insurance mandate won’t expire until the end of 2018.

The impact of the repeal could be partially offset before then if Congress enacts legislation to establish high-risk insurance pools at the state level and renews federal subsidies for low-income people to purchase health insurance. Republican lawmakers such as Sens. Susan Collins of Maine and Lamar Alexander of Tennessee are hoping Congress will enact bipartisan legislation with those fixes in 2018.

Congress, however, is expected to continue resist calls by state and local governments to enable to them to collect sales tax on Internet purchases.

The obstacle has been House Judiciary Committee Chairman Robert Goodlatte, R-Va., who has refused to consider legislation on Internet sales taxes authored by Rep. Kristi Noem, R-S.D.

Goodlatte has announced he won’t run for re-election in 2018, but relief could come sooner from the Supreme Court.

South Dakota Attorney General Marty Jackley announced Dec. 21 that the state filed its final reply in its request for consideration by the high court.

“Based upon the significant impact this issue has on every Main Street business, it remains my hope that our highest court will let us be heard,” Jackley said. “We have received extraordinary support from the State Attorneys General, the National Governors Association, educational leaders, and the business community in the national fight to bring tax fairness for our local retailers and to help support main street businesses."

South Dakota is hoping the Supreme Court will decide whether to take the case by the end of January, setting up the possibility of a ruling by the end of the court's term in late June.

The case is widely viewed as an opportunity for the Supreme Court to take into account technological advances since its 1992 ruling in Quill Corp. v. North Dakota, that sales tax collections for online sales can only be required if a retailer has a physical presence or "nexus" in a state.

South Dakota has no state income tax and is more reliant on sales taxes for its budget than most states.

A 2016 South Dakota law requires out-of-state retailers to collect and remit the sales tax similar to in-state retailers if the remote sellers have more than $100,000 in sales or complete more than 200 sales transactions per year within South Dakota.

After the law was enacted, the state contacted large remote retailers asking them to comply. The state then sued three that refused, resulting in the lawsuit, State of South Dakota v. Wayfair (W), Overstock and Newegg. South Dakota's highest court overturned the law, setting the stage for the appeal.

States and local governments lost an estimated $26 billion in potential sales tax revenue in 2015 because of online retail sales, according to the National Conference of State Legislatures and the International Council of Shopping Centers.

"I think the legislation, the way it is written, is actually a great opportunity for states and localities to address the collection of sales tax," said Emily Brock, director of the Federal Liaison Center for the Government Finance Officer Association.

While online merchandise sales have exploded, much of the sales tax is uncollectible, Brock said. "Local tax systems address local needs and so does the imposition of a sales tax," she said. "It's utilized effectively across the country."

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 12/29/17 07:08 PM EST

[S&P U.S. Public Finance Year In Review.]

As we reflect on the key credit events of 2017, we think it will likely go down as one of the most significant years in the municipal market. Despite the mature economic recovery, credit pressures were evident across many sectors and the outlooks identified a range of risks that we felt could affect credit for the year.

[Continue Reading]

[U.S. Tax Reform: What Will The New Law Do To Municipal Credit Quality?]

The tax bill adopted this week in Congress has significant implications for the municipal market, although the final bill looked rather different from the original House and Senate versions. The broad-reaching bill results in many changes for the U.S.

Continue Reading

S&P U.S. Charter Schools Sector Year In Review.

While we believe the Tax Cuts and Jobs Act, which has now been signed into law, should have little to no direct impact on the credit quality of charter schools, it still has the biggest potential to do so of any singular event in 2017.

Continue Reading

S&P U.S. Higher Education Sector Year In Review.

The ultimate credit impact of the Tax Cuts and Jobs Act on the sector remains to be seen, but we believe its provisions could have long-term operational impacts on colleges and universities throughout the country.

Continue Reading

How the New Tax Bill will Cut Infrastructure Investment.

By increasing the cost to finance infrastructure for states and local governments, the recently enacted Tax Cuts and Jobs Act (TCJA) will lower investment in our nation's infrastructure. This runs counter to President Trump's repeated desire to tackle the major problems associated with America's crumbling infrastructure through increased investment. The impact may be large and immediate enough to swamp the short-term impact of any infrastructure package Congress can put together in the immediate future.

Continue reading.

The Brookings Institute

by Aaron Klein

December 26, 2017

Muni Bonds May Not Be the Reliable Bet They Once Were.

Investors should make sure to better understand the risks, and perhaps adjust their strategy accordingly

Municipal bonds offer investors interest that's tax-free at the federal level and at the state and local levels, if investors own bonds issued by any government entity within their state of residence.

When deciding whether to buy muni bonds, investors usually make a comparison between the yields of a muni bond and a U.S. Treasury note or bond of similar maturities. The "taxable yield equivalent" to a municipal bond is the municipal bond's yield adjusted for the investor's tax bracket.

So if an investor is hypothetically in a 50% bracket, including both federal and state taxes, a taxable yield twice that of a municipal yield—or a municipal yield half that of a taxable bond—would make two bonds equivalent. In that case, if a highly rated muni bond offered more than half the yield of a comparable U.S. Treasury, an investor could consider the muni bond the better choice in a taxable account.

A changed asset class

For decades, that was a reasonable comparison, and largely all that investors had to consider about munis. The chance of losing an investment was not even an issue: The historical default rate of the roughly $3.8 trillion market with more than 80,000 issuers has been low—0% for AAA-rated bonds and only 0.30% for AA- and A-rated bonds from 1970 through 2009, according to a Moody's study.

Unfortunately, municipal profligacy has begun to result in more high-profile distress and bankruptcy in recent years, including Jefferson City, Ala.; Detroit; Harrisburg, Pa.; Central Falls, R.I.; and Vallejo, San Bernardino and Stockton in California. Now the fate of more than $70 billion that creditors have lent to Puerto Rico is in doubt, as Hurricane Maria battered the island already struggling with manufacturing and population loss.

An updated Moody's study from 2016 notes that the "sector has changed over the past decade and more profound changes may be in the offing. The once-comfortable aphorism that 'munis don't default' is no longer credible, although default rates remain low."

In some cases, investors betting on munis have gotten burned. Recently, Franklin Double Tax Free Income fund merged with Franklin High Yield Tax Free Income fund (FHYVX) after it inflicted significant losses on investors. The fund had more than half its assets in Puerto Rico bonds.

Some analysts warn that many bond issuers are heading into precarious financial situations. In a 2016 research report from PNC Capital Markets, Tom Kozlik argues that around 20% of issuers haven't adjusted their spending to reflect diminished revenue after the financial crisis.

Mr. Kozlik doesn't cite names, but other observers have pointed fingers at issuers at risk.

"Though I'm not warning of an industrywide municipal-bond crisis, I think investors have to think carefully about individual credits and what, exactly, they're investing in," says Nicole Gelinas of the Manhattan Institute think tank. In the case of Chicago, "it's difficult to see, 10 years from now or even sooner, how, exactly, Chicago figures out [its problems with underfunded pensions] without bondholders having to take some sort of hit, as well." (Chicago officials declined to respond to a request for comment.)

And when a municipality goes bankrupt, investors aren't always first in line to recover their money. Stockton and San Bernardino honored their obligations to state-employee pension funds at the expense of bondholders in their bankruptcies. "General obligation" bondholders, once thought to be above revenue bondholders in the case of defaults, aren't necessarily ahead of unions.

Munis aren't Treasurys

Not all municipal-bond experts are pessimistic. Tracy Gordon, a senior fellow at the Urban Institute think tank, says investors shouldn't be alarmed about munis' safety, emphasizing their low historical default rates. "It's unfair to paint the whole sector with a broad brush," she says.

But if investors choose munis as a core holding, many analysts advise using a diversified fund to lessen the risk of issuers defaulting. What's more, investors shouldn't expect the bonds to rally during a stock-market decline, as U.S. Treasurys often do.

That's because munis have become closely tied to the health of state-employee pension funds. If stocks fall and pension funds lose money, the funds often turn to municipalities to make up losses—which makes muni bonds less attractive and hurts muni investors.

Indeed, the Bloomberg Barclays Municipal Index lost nearly 2.5% in 2008 during the stock crash—instead of providing municipal-bond investors with protection. That's hardly catastrophic, but it might not have represented the resilience that the bond investors were expecting. And results might be less benign during the stock market's next wipeout.

The Wall Street Journal

By John Coumarianos

Jan. 7, 2018 10:08 p.m. ET

Mr. Coumarianos, a former Morningstar analyst, is a writer in Laguna Niguel, Calif. He can be reached at reports@wsj.com.

SIFMA Issues 2018 Municipal Issuance Survey.

Compiled from responses provided by seven municipal bond underwriters and dealers, SIFMA's Municipal Issuance Survey forecasts the type of activity that is expected in the municipal securities market in 2018. Highlights from the report include the forecast of total municipal issuance, both short- and long-term, to fall to $362.5 billion, down from $439.7 billion expected in 2017. The end of advance refundings (to expire December 31, 2017, based on the tax reform bill) is expected to have the greatest effect. While taxable municipal issuance is expected to rise by 54.7 percent to $47.5 billion in 2018 from $30.7 billion in 2017.

Municipal Issuance Survey 2018

Bloomberg Brief Weekly Video - 1/4

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

Watch video.

Bloomberg

January 4th, 2018

The Week in Public Finance: Tax Reform Hits Muni Market, California Plays Tax Games and Local Pensions Do Better Than State.

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

GOVERNING.COM

BY LIZ FARMER | JANUARY 5, 2018

4 Ways States will Fund Infrastructure Projects in 2018.

While the construction industry awaits the big reveal of President Donald Trump's long-anticipated infrastructure plan – promised to be introduced this month – state and local governments are likely wondering how the details will affect the way they finance repairs and construction of highways, bridges and other public projects. One thing that Trump made clear in his budget proposal – and most recently in his contention that that the federal government is not obligated to pay for half of the near-$13 billion NY-NJ Hudson River tunnel project – is that states and municipalities will have to dig deeper to finance projects that serve mainly local residents.

Continue reading.

Construction Dive

by Kim Slowey

Jan. 4, 2018

Fitch: Southern California Wildfires Unlikely to Affect U.S. Public Finance Credit Quality.

Fitch Ratings-San Francisco-20 December 2017: As with the October 2017 wildfires in northern California, Fitch Ratings sees no immediate credit impact on U.S. public finance credits from the Southern California wildfires which continue to rage in Ventura and Santa Barbara Counties. However, Fitch believes there could be short-term budgetary pressure for the most impacted governments.

Fires this month have impacted communities in Los Angeles, San Diego, Santa Barbara and Ventura counties. All except the Thomas Fire in Ventura and Santa Barbara counties are under control. The Thomas Fire started on Dec. 4 near the city of Ventura but has moved northwest into Santa Barbara County. As of Dec. 20, the blaze has burned over 272,000 acres.

The Thomas fire appears to be largely in the Los Padres National Forest and, as a result, about 1000 structures have been destroyed compared to over 3,000 structures, mostly homes, in the Napa, Sonoma and Mendocino county fires which destroyed over 200,000 acres in aggregate. Nevertheless, with 55% contained and possibility for continued dry and windy conditions, the final outcome could be different. Full containment is not expected until Jan. 8, over two weeks from now.

As with most natural disasters, Fitch believes the fiscal impact of the fires on rated entities in Ventura and Los Angeles counties will be largely mitigated by their financial flexibility and support from federal and state governments and private insurance policies. The local governments affected by the fires are likely to use a combination of federal relief funds, state support and insurance claims to pay for most fire-related damage. The Dec. 5 federal disaster declaration for the State of California enables individuals and local governments to seek individual assistance from the federal government. According to FEMA's website, the declaration applies only to the Thomas fire in Ventura and Santa Barbara counties.

Fitch maintains an 'AA+' Issuer Default Rating (IDR) on Ventura County (population of 849,000), which incorporates an 'aaa' financial performance assessment based in part on its substantial available liquidity. Fitch expects near-term budgetary fire-related impacts due to assessed valuation (AV) declines and the added cost of fire-fighting and clean-up. However, the county is part of a very large and diverse regional economy that Fitch believes should begin to recover promptly once the fires have been put out. Overall, we expect most damaged property in affected communities to be rebuilt, which will maintain tax bases, rather than residents and businesses leaving the areas. While we expect recovery efforts to follow historical patterns of disaster recovery, we will analyze any significant developments that might affect credit quality.

In addition to damage to residential properties, the fires have reportedly damaged avocado and lemon groves, but it is too soon to estimate the extent of the damage. According to the county's most recent crop report (2015), the total value of agricultural production in the county was $1.36 billion, with avocados and lemons combined representing about one third. Damaged trees could affect future years' output, though they would be eligible for crop insurance. However, the county's revenues are concentrated in property taxes (about 33% of general fund revenues) and intergovernmental sources (43%), so any material impact of the fires on the county's financial operations would be due to lower AV. This is likely to be temporary as owners rebuild damaged property, although it could be more extended for agricultural property. The breakdown of AV by land use was not immediately available.

No Fitch-rated public schools were reported as damaged due to the fires. However, a number of local school districts have been forced to temporarily close due either to fire damage or very poor air quality, including Hueneme Elementary School District (IDR 'AA-'/Stable Outlook) State law provides for school districts to be held harmless for impacts to attendance (on which state funding is based) due to natural disasters, including air quality.

Smaller fires broke out at the same time but have been largely contained: the Lilac fire in San Diego County (population of 3.3 million) burned 4,100 acres and damaged 157 structures, including a number of mobile homes. The Skirball fire in Bel-Air (Los Angeles County, population over 10 million) burned 422 acres and damaged or destroyed 18 acres. The Sylmar Fire (Los Angeles County) burned about 15,600 acres, and damaged or destroyed about 200 structures. The Rye fire near Santa Clarita (Los Angeles County) burned over 6,000 acres and six structures.

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Additional information is available on www.fitchratings.com

Bloomberg Brief Weekly Video - 12/22

Amanda Albright, a reporter for Bloomberg Briefs, talks with Joe Mysak about this week's municipal market news.

Watch video.

Bloomberg

December 21st, 2017

How GOP Tax Overhaul Makes it Harder to Pay for Infrastructure in U.S.

President Donald Trump promised during the presidential campaign and after his election to lead an upgrade in our nation's infrastructure, announcing in February 2017, for instance, that he would ask Congress to approve programs designed to stimulate $1 trillion in infrastructure investment across the country.

At least up to this point, the President's promises with respect to infrastructure remain unfulfilled. Furthermore, the recently passed tax bill that he signed last week may create some challenges for the municipal bond market and the infrastructure sector.

Continue reading.

By DANIEL BERGSTRESSER / ECONOFACT MONEYWATCH

December 28, 2017, 5:15 AM

Why Infrastructure is a Revenue Challenge for Cities.

Guest columnist Jen Mayer shares insights on revenue generation for infrastructure projects gleaned from city-led best practices and cutting-edge investment strategies.

Now that tax reform is over, Capitol Hill is likely to turn to the challenge of financing our nation's crumbling infrastructure. The trouble is, it's not really a financing challenge.

There are plenty of capital sources, domestic and foreign, eager to lend to infrastructure projects, including the U.S. municipal bond market, which emerged largely unscathed from tax reform. While the bill prohibited advance refunding of municipal bonds, the tax-exempt status of private activity bonds important for higher education, hospital and industrial developments was preserved.

Yet whatever happens next in Washington, DC.., it's not likely to resolve the decades-long need to raise the Federal gas tax or find another new source of revenue for infrastructure. Congress may well change how existing funding is allocated, expand Federal credit programs and facilitate public-private partnerships. But local governments will have to find the revenue to pay back any financing. That task may be exacerbated by the limits placed on State and Local Tax Deduction (SALT) deductions that could make raising local taxes even more difficult.

Continue reading.

efficientgov.com

December 22, 2017

How Trump's Infrastructure Plan Could Strain America's Cities.

A big investment blueprint is expected next month, and it might stretch local governments' already-stretched budgets.

President Trump took many opportunities in 2017 to rail against the state of U.S. infrastructure, most recently using the fatal Amtrak crash in Washington state to point out the country's crumbling bridges, roads, and railways. "[O]ur soon to be submitted infrastructure plan must be approved quickly," he tweeted, harkening back to his oft-repeated promise to invest $1 trillion rebuilding the country.

Little came of that plan in 2017. But come January, the White House will begin a push, in earnest, for a national infrastructure package that gets to $1 trillion in overall investment, using $200 billion in federal "seed" money, a senior official told Fox News last weekend.

Trump advisers had previously described an infrastructure package that would rely on the private sector to make up the $800 billion difference. In this version, most of the $200 billion would be rewarded on a competitive basis to states and localities that promise to raise new, infrastructure-dedicated revenue on their own, for a total of $1 trillion, according to The Washington Post. Some portion of the $200 billion would directly fund projects in rural areas.

Continue reading.

The Atlantic

by Laura Bliss

Trailing Deal Surge, Muni Market Heads into 2018 on Waning Supply.

NEW YORK, Dec 29 (Reuters) – The U.S. municipal bond market heads into the New Year with a thin number of deals after ending 2017 with a staggering upswing in supply as issuers raced to sell before a new tax law takes hold.

Roughly $934.7 million in municipal bonds and notes are expected to come to market next week, against a weekly average of more than $7 billion for the past 12 months, according to Thomson Reuters data.

In contrast, the month of December brought $62.1 billion in supply, far outweighing the average of $25.4 billion for the month over the last quarter-century.. The fourth quarter saw $146.2 billion in deals compared to $105.5 the same quarter in 2016.

Deals were issued at a breakneck pace as it became clear that a $1.5 trillion U.S. tax bill would clear the Republican-dominated Congress, limiting some types of muni offerings. President Donald Trump signed the legislation on Dec. 22.

Despite the eleventh-hour rush to market, 2017 produced an overall drop in muni deals compared to last year.

There were $453.5 billion in deals this year, a one percent decline from 2016, and 12,823 issues, a more than 12 percent fall.

The amount of refundings sank 16 percent to $221.2 billion as the number of those issues fell 31 percent.

New money issues, however, rose 19 percent year-over-year to $230.3 billion with a 3 percent increase in the number of deals completed.

Next week's largest deal comes from the New Jersey Economic Development Authority, which is set to sell $381 million in negotiated bonds. The state lease revenue bonds are rated BBB-plus and A-minus by S&P Global Ratings and Fitch Ratings, respectively.

A New Jersey assemblyman recently filed a lawsuit to block the bonds, which he said required a statewide vote to approve a sale. It was unclear whether the sale could proceed with the legal challenge.

The Town of Oyster Bay is expected to offer $10.5 million in general obligation district improvement bonds, the biggest competitive deal.

by Laila Kearney

Reporting by Laila Kearney; Editing by Daniel Bases and Alistair Bell

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In U.S. Tax Confusion, Muni Investors Take Refuge in the Known.

NEW YORK (Reuters) – As municipal bond investors try to understand how their portfolios will fare under the new U.S. tax code, some are maneuvering around the uncertainty by turning to one of the market's most stable options: state debt.

The appetite for state general obligation (GO) and revenue bonds will grow in 2018, investors said, as buyers seek near-bulletproof investments to keep their taxable income down as other options disappear.

That comes as the $3.8 trillion muni market is poised for significant shifts, with corporate demand seen slowing and the new tax rules limiting some types of supply. Meanwhile, bonds from high-tax states will likely see a jump in demand from in-state investors.

“The beginning of the year is going to be a period of confusion, of institutional components of the muni market figuring out where they stand … you’re going to have individuals go through the same thing,” said Christopher Mier, chief strategist and economist of Loop Capital’s analytical services division in Chicago.

“And with confusion, you get a certain amount of risk aversion,” Mier said.

Despite higher volatility in the sector this year, states’ financial flexibility and broad revenue-raising powers will allow them to adapt to federal tax changes while smaller governments and municipalities may flounder, Mier said.

State GO and revenue bonds made up $52.74 billion, or 11.6 percent, of overall municipal issuance in 2017 as of Wednesday, according to Thomson Reuters data.

MARKET CHANGES

The sweeping Republican-crafted tax overhaul, approved along party lines in Congress and signed into law by U.S. President Donald Trump on Friday, has several implications for the municipal bond market.

Among the biggest is its elimination of tax-exempt advance refunding bonds. Taking away advance refundings, which made up 30 percent of the market’s supply last year, would likely create more scarcity in what is expected to be an already dry year for muni supply.

Uncertainty over the tax plan had prompted a surge of muni record-breaking bond issuance totaling $58 billion for the month of December.

The most talked about change to the tax code in muniland is the $10,000 limit on state and local tax (SALT) deductions, which had allowed filers to reduce their federally taxable income.

With SALT now capped, investors are likely to seek the double-tax exemption from debt issued in their states, which also avoids federal taxation, said Alex Etzkowitz, senior associate, investment research and strategy, at Gurtin Municipal Bond Management in Solana Beach, California.

“It’s definitely going to make investing in-state more attractive for a lot of investors relative to just kind of buying a national portfolio,” Etzkowitz said.

That will be especially true for investors in states taxing income at more than 5 percent, including California, New Jersey and New York, said Beth Foos, a senior analyst at Morningstar Research Services in Chicago.

And investors starved for high-yield bonds could finally catch a break in 2018 as the Federal Reserve trims its massive balance sheet and accelerates interest rate hikes, Loop’s Mier said.

As the Fed dials back its monetary accommodation, there will be more market-determined yields and prices, widening credit spreads and boosting yields, he said.

Banks and insurance companies, the top corporate buyers of municipal bonds, might also reduce their muni debt holdings in response to tax changes, said Henry Cisneros, chairman of the executive committee at Siebert Cisneros Shank & Co.

The tax overhaul slashed the corporate income tax rate to 21 percent from 35 percent, potentially making muni investments less attractive to companies.

Meanwhile, more supply could come if the Trump administration can secure an infrastructure spending deal, said San Antonio, Texas-based Cisneros, who served under former U.S. President Bill Clinton as Secretary of Housing and Urban Development. An infrastructure initiative in 2018 is "virtually certain," he said.

But while such a plan is possible, it may not involve the federal funds needed for programs that would stir the muni market, such as the subsidized Build America Bonds introduced following the 2007-2009 financial crisis, said Alan Schankel, a managing director at Philadelphia-based Janney Montgomery Scott.

"I imagine Congress will not be wild to increase the deficit further after the tax reform by actually putting money on the table for infrastructure improvement that's not already there," he said.

by Stephanie Kelly & Laila Kearney

DECEMBER 28, 2017

Reporting by Laila Kearney and Stephanie Kelly in New York; Editing by Daniel Bases and Meredith Mazzilli

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Municipal-Bond Supply Dries Up After Setting a Record December.

- **30-day visible supply down 40 percent from this time last year**
- **States and cities set to issue $5.3B in the next 30 days**

States and cities are set to issue about half the amount of debt at the start of 2018 compared with a year ago.

Issuers from California to Virginia plan to take on $5.3 billion of municipal debt in the next month; that's the lowest since June 30 and down from $8.9 billion of anticipated sales during a 30-day period beginning Dec. 27, 2016.

The dearth of supply comes as states and localities sold a record $55.6 billion of debt this month through Dec. 22 as they accelerated their offerings to avoid potential changes from the federal tax-overhaul bill.

The decline means fewer bonds for investors to choose from in early 2018. That may help generate gains in the tax-exempt market, which advanced each January for the past six years, according to Bloomberg-Barclay's Municipal Bond Index.

Bloomberg Markets

By Michelle Kaske

December 27, 2017, 11:01 AM PST

[Tired of Tax Reform? 3 Other Public Finance Trends to Watch in 2018.]

For one, many states have to figure out how to manage their marijuana revenue.

Tax reform has grabbed a lot of attention when it comes to big changes to watch in 2018. But there are plenty of other headline-worthy trends emerging. Here's a look at three economic and policy issues finance officials across the country will be dealing with next year.

Protecting Pot Revenue

As more states have legalized recreational marijuana, managing the taxes and revenues from it has proven dicey.

For starters, not every city or county in a state wants to take part in the nascent industry. These places have acted by banning pot sales within their borders. But should they still be entitled to the revenues coming in from marijuana sales? A few states don't think so. California, Massachusetts and Oregon are withholding marijuana tax revenues from these cities and counties.

Then, there's the fact that marijuana businesses deal largely in cash. The federal government regards marijuana as an illegal drug; banks are regulated by the feds. Most won't touch cannabis cash. For state and localities, this makes tracking the product and collecting the revenues difficult. Some solutions are emerging.

Community financial institutions, for one, have become more open to serving the cannabis industry after the feds said they won't go after institutions that keep a watchful eye on their clients and report suspected wrongdoing.

That's where a company called PayQwick comes in. It electronically transfers money between marijuana growers, sellers, customers and their financial institutions. It also offers services allowing businesses to electronically pay their taxes.

Another government security company, SICPA, is providing county governments in Northern California's Emerald Triangle track-and-trace services for cannabis products. Counterfeit-resistant tax stamps are placed on products and scanned at various points along the supply chain. The stamps, which the company has already developed for cigarette packs to prevent fraudulent sales, can help prevent revenue from slipping through the cracks. It also has the added benefit of helping regulators ensure that operators aren't producing more product than they are legally allowed to.

The savings can be significant, says Alex Spelman, SICPA's vice president of business development. In 2005, when the company first put tax stamps on cigarette packs in California, which has a high per-pack tax rate, it saved an estimated $90 million in revenue from going out the door. He adds it can also give governments more flexibility in deciding whether to adjust their taxes because they can more closely track what's happening at each stage of the product's life.

'Pay For Success' Coming to a Small Town Near You?

There are about a dozen so-called pay for success financing projects around the country, and all are with large governments such as states, counties and major cities. But 2018 is likely to see smaller cities finally get in on the action.

Pay for success programs attract money from private and nonprofit investors for public programs that seek to bettter outcomes in early childhood education, workforce development and opioid misuse, among other things. Governments only pay investors back if and when positive results, such as cost-savings or reduced recidivism rates, are achieved. As mayors and cities continue to face funding pressures, many more are starting to look at pay for success as a possible tool, says Justin Milner, a senior fellow at the Urban Institute.

The results of a project in Denver holds promise for smaller-tier cities looking to launch their own pay for success program. That city launched a program to provide permanent housing and support services to at least 250 chronically homeless people over five years. After 18 months, the city cut its first check — for $188,000 — to the program's financiers and put up an additional $670,000 in this year's budget to expand the program.

The Urban Institute advised on the Denver project and is now working with smaller cities such as Eugene, Ore.; Spartanburg, S.C.; and Tallahassee, Fla.

Elsewhere, a Baltimore-area hospital is developing a project to bring nutritious meals, in-home safety checks and case management services to vulnerable older adults. New Orleans' Mayor-elect Latoya Cantrell has said she wants to start a pay for success program aimed at creating jobs and reducing criminal justice costs. And projects to reduce children's asthma are being developed in places such as Springfield, Mass., and Memphis, Tenn.

"If the next tier can build upon some of the successes of Denver," says Milner, "if they can find that philanthropic interest and have the capacity to support launching a project, then I think you'll see that movement in even the third- and fourth-tier cities."

Increased Recession Worries

The U.S. economy is currently in one of the longest expansion periods in modern history — even though it doesn't quite feel like it. And it's that feeling, along with tight budgets and slow growth, that has many public officials worried that a recession is coming. "I think everybody is waiting, just holding their breath," says Mike McCann, a vice president at OpenGov.

That elephant-in-the-room feeling is playing out in a few ways. For one, state and local governments are saving big time. Cities' average savings level is at historic highs, according to the National League of Cities (NLC), equal to about one-quarter of annual budgets. Meanwhile, 26 states now have larger rainy day funds as a share of operating costs than they did before the recession.

When it comes to budgeting, governments are being extremely cautious in 2018. Municipal finance officers are expecting minimal growth this year — less than 1 percent — and far fewer of them believe they will be better able to meet the financial needs of their communities, according to NLC. At the state level, spending is expected to grow at the slowest pace since the recession.

Because of the pressure, McCann expects to see officials demand more transparency and accountability when it comes to budgeting. "I think people are increasingly unwilling to take a black box number out of a budget module and not be able to challenge it," he says. "Old-school budgeting was so technical and some of the calculations so obtuse, that normal people weren't allowed to see that. People just aren't tolerant of that anymore."

GOVERNING.COM

BY LIZ FARMER | DECEMBER 29, 2017

December Muni Volume Hits Record $62.5B Ahead of Tax Overhaul.

Municipal bond issuance set a new single-month record in December as issuers rushed to close deals before the new tax law took effect with the New Year.

Data from Thomson Reuters (TRI) shows volume in December ballooned to $62.50 billion in 1,168 transactions from $20.81 billion in 780 deals from the last month of 2016. The issuance surpassed the previous record of $54.7 billion of deals in Dec., 1985, just before the last comprehensive tax overhaul took effect.

Back then, issuers rushed to market on fear of tax reform only to have the legislation delayed until September. This time around, the frenzy started in early November on concern that the municipal market would lose the tax exemption on both private activity bonds and advance refundings.

The flood of issuance also resulted in a 2017 total of $434.76 billion, closer than expected to the yearly issuance record, of $451.65 billion that was set in 2016. Of the 2017 total, $144.61 billion came in the fourth quarter.

"By our estimate, the tax bill rush resulted in about $35 billion of issuance was pulled forward in 2017 and taken away from 2018," said Sean Carney, director and head of municipal strategy at BlackRock (BLK). "It begs many questions about the New Year, including what it means for the overall market performance and volume in 2018 but also volume in the first quarter of the year."

Tom Kozlik, managing director and municipal strategist at PNC, said he wasn't surprised by the surge in November and December and that volume would have been even greater if there'd been more time.

"For months, tax reform had been in the pipeline and no one could have guessed a threat to the tax exemption would have emerged for a tax cut," he said. "Issuers responded how I think they should have, by assuming the worst case scenario. And they were able to mobilize and execute some financings before year end. Investors soaked up several weeks of $20 billion-plus supply easier than expected."

Carney agreed, saying that what surprised him the most, was how easily digested the volume was, as many deals were oversubscribed. He predicted issuance will fall to about $335 billion – down 21% year over year, but only 13% off from what the market was on pace for this year, before the tax reform rush.

"It's harder to predict what it means for performance," he said. "The month of January over the past five years turns in about 45% of all returns but it looks like 2018 will bring a net negative year by about $50 through $60 billion, taking us back to a year like 2011. We will be going from a growing market in to a shrinking one in 2018. Returns from municipals were phenomenal in 2017, as rates did not move as much as people anticipated. 2018 will be a year of carry and more reliant on coupon."

The new tax bill was signed into law by President Trump on late December, keeping PABs as is for now, but ending advance refundings, a popular and important cost-saving instrument.

"Advance refundings over the past 5 years account for around 22% of all issuance," said Carney. "One highlight of the whole situation could be how PABS were saved. Maybe it means that Washington views the muni market as an avenue to fund infrastructure. Down that road, PAB s could get redefined, especially the alternative minimum tax portion."

Kozlik bank product solutions, like derivatives or interest rate swaps, could be employed effectively as an alternative to in certain situations.

"It would make sense for some issuers to lock in forward rates with derivatives when appropriate," he said. "It is also possible that the uses of synthetic advance refundings are structured by using fixed payer swaptions. It is quite possible that municipal entities begin to use these types of strategies more often.

Issuers might also toy with a five-year call, instead of the traditional 10-year call, to offset the loss of advance refunding.

"Demand, creates supply. If there is demand for issuers to come with shorter call dates, then its quite possible we could start seeing more of that," said Carney. "That being said, the muni market is very traditional and accustomed to certain 10-year non-call structure."

Refundings accounted for $28.49 billion in 492 deals, up from $5.57 billion in 227 transactions during December of 2016. New money deal volume grew to $27.31 billion in 595 sales from $13.02 billion in 502 deals.

The value of combined new money and refunding deals for the month rose to $6.69 billion from $2.22 billion a year earlier. Issuance of revenue bonds increased to $48.29 billion, while general obligation bond sales gained to $14.21 billion from $8.33 billion.

Negotiated deals jumped to $52.69 billion from $14.16 billion, while competitive sales increased to $6.83 billion from $3.91 billion. Taxable bond volume vaulted to $6.79 billion from $2.29 billion, while tax-exempt issuance expanded to $52.84 billion.

Deals wrapped by bond insurance rose 70.2% year-over-year to $2.92 billion in 121 transactions from $1.72 billion in 123 deals.

California remained the state with the most volume. Issuers in the Golden State have sold $67.59 billion this year. New York came in second with $48.45 billion, followed by Texas with $41.62 billion. Illinois was fourth with $21.57 billion and Pennsylvania rounds out the top five with $20.47 billion.

"The threat to the tax exemption is now very elevated," said Kozlik. "If Washington lawmakers can put the municipal bond tax exemption on the chopping block for a tax cut, what happens when they get serious about deficit reduction?"

By Aaron Weitzman

BY SOURCEMEDIA | MUNICIPAL | 12/29/17 07:07 PM EST

Bond Insurer MBIA Targeted by Short Sellers After Puerto Rico Hurricane.

Hedge funds are again betting against the company

Hedge funds are increasingly betting on whether bond insurer MBIA Inc. can survive heavy losses expected from Puerto Rico's bankruptcy in the wake of Hurricane Maria.

Short sellers have borrowed about 40% of the firm's stock since September, wagering that it will drop, while value investors Fine Capital Partners L.P. and EJF Capital LLC have taken the opposite side, buying millions of MBIA shares. Credit hedge funds like Mill Hill Capital LLC have bought credit default swaps, or CDSs, that gain value as the probability of an MBIA default rises.

Bond insurers charge premiums to companies and governments that issue bonds and agree to take over interest and principal payments if the borrowers default. That business model backfired during the financial crisis, when the insurers took billions of dollars in unexpected losses on mortgage bonds. Bets against MBIA became a lucrative trade among hedge-fund managers, most famously Bill Ackman.

MBIA recovered by focusing on insuring municipal bonds but defaults in that market have mounted, calling the firm's business into question once again. Bearish investors doubt the firm has set aside enough capital to cover likely payouts, especially now that Hurricane Maria has crippled Puerto Rico, where MBIA insured $3.4 billion of bonds.

"It's not something we've asked for or created," said MBIA's head of investor relations, Gregory Diamond, about the attention from hedge funds past and present. "We are here to operate our company as best we can and to satisfy our obligations."

Mill Hill founder David Meneret said he started buying MBIA CDS—derivatives that pay out if a bond defaults—before the hurricane struck because he believed the insurer was undercapitalized given its exposure to cash-strapped Puerto Rico and financially troubled states like Illinois and Connecticut.

"We didn't know when something bad was going to happen but with a company that has so much leverage, anything bad could be very damaging," Mr. Meneret said

By one measure, MBIA has done less to prepare for Puerto Rico-related losses than its competitors. MBIA's most recently reported loss reserves amount to about 10% of its exposure to Puerto Rico, compared with about 20% for Assured Guaranty Ltd. and about 40% for Ambac Financial Group Inc., according to data from S&P Global Market Intelligence.

The difference in reserves reflects the fact that most of the Puerto Rico bonds MBIA insured were issued by different entities and government agencies than the bonds insured by its competitors and the likelihood that recoveries will vary accordingly, Mr. Diamond said.

Puerto Rico owes investors about $70 billion of bonds and had begun restructuring the debt in court when Hurricane Maria struck in September, destroying much of the island's infrastructure and drastically reducing forecasts for how much bondholders will recover. Benchmark bond prices dropped to about 23 cents on the dollar from 60 cents as expectations of bondholder recoveries fell.

The net dollar amount of CDS contracts purchased on MBIA after the hurricane hit Puerto Rico increased by $267 million to $1.13 billion through Nov. 21, the most recent date for which data are available, according to data from the Depository Trust & Clearing Corporation. The percentage of MBIA stock sold short surged to 43% on Dec.19 from 14% in September, according to data from S&P Capital IQ.

Buyers of CDS have made large returns on their trade so far—prices of the derivatives have tripled since September, according to IHS Markit. Movement of the stock has been more erratic, falling about 40% to $6.22 in October from about $10 in early September, before rebounding to about $9 in November, when MBIA announced a $250 million share buyback. Shares closed at $7.49 Wednesday, and many of the recent short sales in MBIA stock were executed when the stock traded for $8 or more, implying a modest gain, according to data from the Depository Trust & Clearing Corporation.

Sunesis Capital LLC founder Manal Mehta, a longtime investor in MBIA, says the market is again underestimating the firm's resilience. The insurer will have decades to pay off the Puerto Rico bonds it insured, which is ample time for the island's economy to bounce back and for MBIA to recover money through litigation and debt restructurings, he says.

Some funds viewed the share drop as a buying opportunity. Fine Capital Partners L.P. and EJF Capital LLC have collectively bought about 5.6 million MBIA shares since the end of September, according to data from S&P Capital IQ. An official at Fine Capital declined to comment, while EJF couldn't be reached for comment.

The investor face-off reprises the debate over the viability of MBIA and other bond insurers that Mr. Ackman started in 2002, when he announced his short bet against the company.

The key to the bond-insurance business is reserving enough cash to cover losses from bond defaults, and to maintain a high enough credit rating to keep selling new policies. Mr. Ackman argued that MBIA had far too little capital relative to potential losses from the hundreds of billions of dollars the firm insured.

Fallout from the financial crisis forced regulators to intervene with two of the largest bond insurers—Ambac Financial Group Inc. and Financial Guaranty Insurance Co.—while others stopped writing new policies. MBIA's market capitalization dropped about 95% from precrisis levels and Mr. Ackman made about $1 billion from his trade.

Still, MBIA weathered the financial crisis by suing banks that structured the mortgage bonds it insured, and its stock recovered modestly, generating gains for hedge funds like GSO Capital Partners that bet the firm would survive.

That could happen again, Mr. Mehta says, forcing short sellers who borrowed MBIA stock to scramble to buy shares. "If you are short the stock and there's a positive piece of news, the stock will go vertical and you'll be caught with your pants down," he said.

The Wall Street Journal

By Matt Wirz

Dec. 21, 2017 5:30 a.m. ET

Write to Matt Wirz at matthieu.wirz@wsj.com

GASB Issues Implementation Guide on Other Postemployment Benefits.

Norwalk, CT, December 19, 2017 — The Governmental Accounting Standards Board (GASB) has issued a new Implementation Guide that contains questions and answers about the GASB's new standards on accounting and financial reporting for postemployment benefits other than pensions. Those benefits (primarily retiree healthcare) are referred to as other postemployment benefits (OPEB).

Implementation Guide No. 2017-3, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (and Certain Issues Related to OPEB Plan Reporting)*, provides answers to questions intended to clarify, explain, or elaborate on the requirements of GASB Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions.

The document also addresses a limited number of issues related to Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*.

The guide is available for download at no charge on the GASB website, www.gasb.org. Printed copies will be available through the GASB Store in the coming weeks.

The questions and answers contained in GASB Implementation Guides constitute Category B authoritative guidance under generally accepted accounting principles (GAAP). The guidance is applicable to all state and local governments that follow GAAP when preparing their financial statements.

Broken Bonds: The Role Wall Street Played in Wiping Out Puerto Ricans' Savings.

When residents of Puerto Rico funneled their life savings into funds that were largely made up of the island's bonds, they were told their money would be safe.

They were told that they would receive interest payments that were higher than many comparable opportunities. They were told income would be tax exempt.

And when those investments began to evaporate four years ago, they were told not to sell, that the market would rebound, and they would recoup their losses — eventually.

This year, eventually became never after Puerto Rico triggered bankruptcy-like proceedings, and the island began restructuring its debt to seek protection from creditors — pushing the already depreciated bond prices within the funds lower. Then came Hurricane Maria, and those prices plummeted even further.

Continue reading.

CNBC

Dawn Giel | Leslie Picker | Scott Zamost

18 Dec 2017

Moody's: Local Government Pension Liabilities Soar in Fiscal Year 2016.

Adjusted net pension liabilities for the 50 largest local governments totaled $456 billion in at the end of fiscal year 2016, up from $390 billion the previous year, said a report from Moody's Investors Service.

The $456 billion is more than double the size of debt and reported other post-employment benefit liabilities for the local governments combined, Moody's said in the report.

On an individual basis, only 14 of the 50 municipal entities reviewed had less pension debt than bonded debt in fiscal year 2016.

Moody's uses a market interest rate to calculate pension liabilities rather than a discount rate. Often times, Moody's adjusted net pension liabilities are higher because it's using an interest rate closer to 4% than the 7% or 7.5% that pension funds use.

The five entities with the highest adjusted net pension liabilities as a percentage of operating revenue were Chicago at 703%, followed by Dallas at 609%; Houston, 606%; Phoenix, 494%; and Los Angeles, 432%. That ranking remains unchanged from last year's report, with the exception of Phoenix and Houston, which switched places.

On the flip side, local governments reporting the lowest adjusted net pension liabilities as a percentage of operating revenue were Wake County, N.C., at 24%; Houston Independent School District, 46%; and Washington D.C., 50%.

Regarding pension contributions, only 16 of the 50 entities surveyed contributed enough to stem unfunded pension liability growth, down from 26 in fiscal year 2015.

Moody's noted in the report that 42 of the 50 entities reported pension funding information that lagged their fiscal-year end. Under GASB 68, governments are permitted to report net pension liabilities up to one year prior to their fiscal-year end, said Timothy Blake, managing director, public finance at Moody's.

As a result, the rating agency predicts that adjusted net pension liabilities for the 42 entities will increase an additional 33% in their fiscal year 2017 reporting due to their "lagged recognition" of weak investment returns and declining discount rates in calendar year 2016. Moderate declines in adjusted net pension liabilities are expected in fiscal 2018, however, due to stronger returns in 2017.

Moody's report also looked at the probability of pension investment losses in a given year amounting to 25% or more of a government's operating revenue. For seven of the 50 entities reviewed, the probability of this happening was 10% or greater in fiscal year 2016 due to the size and estimated volatility of their pension assets, the report said. Houston and Los Angeles faced the highest probability.

PENSIONS & INVESTMENTS

BY MEAGHAN KILROY · DECEMBER 19, 2017

U.S. Municipal Bond Issuance Totals Nearly $12 Billion Next Week.

NEW YORK (Reuters) – U.S. municipal bond and note issuance were expected to total about $11.77 billion next week, according to Thomson Reuters data, a larger-than-usual amount ahead of the holiday season as issuers mull potential changes to the federal tax code.

This past week, U.S. municipal bond market supply totaled more than $20 billion for a second straight week as investors accelerated debt sales in case the U.S. Congress votes to eliminate federal tax breaks for private activity bonds (PABs) and advance refunding bonds starting in 2018.

The elimination would mean higher borrowing costs for nonprofits and other entities that issue PABs. It would also remove a way that all muni issuers can take advantage of lower interest rates to save money.

"Really it has been the concern about whether (there will be) a repeal of private activity bonds and advance refunding that has just driven a surge in volume during what is typically a quiet time," said Erin Ortiz, a managing director and municipal research analyst at Janney Montgomery Scott in Philadelphia.

Republican lawmakers are expected to release details on a final tax bill later on Friday.

Muni bond and note issuance from the beginning of the year to Thursday totaled about $434.2 billion, according to Thomson Reuters data. November and December issuance accounts for nearly 20 percent of that total even though December is only half over.

A $1 billion bond sale by Houston pricing through Barclays tops next week's negotiated deal calendar.

The taxable pension bonds, which were approved by Houston voters last month, are a critical part of a 30-year cost-saving plan signed into law in May by Texas Governor Greg Abbott to address the city's $8.2 billion unfunded pension liability.

The bonds, rated Aa3 by Moody's Investors Service and AA by Fitch Ratings, are structured with serial maturities from 2020 through 2032 and term bonds due in 2037 and 2047, according to the preliminary official statement.

A handful of negotiated deals on next week's calendar total more than $600 million.

The Railsplitter Tobacco Settlement Authority in Illinois will issue about $678.6 million of revenue bonds, the Metropolitan Transportation Authority in New York will sell $608.8 million of transportation revenue refunding bonds, and Virginia's Housing Development Authority is set to issue $600 million in rental housing bonds.

The week's largest competitive deal comes from the City of Virginia Beach for $69.7 million of general obligation public improvement refunding bonds, expected to sell Tuesday.

By Stephanie Kelly

(Reporting by Stephanie Kelly; Editing by Daniel Bases and J.S. Benkoe)

Dec. 15, 2017, at 2:18 p.m.

[There's No Holiday Slowdown in the Municipal-Bond Market This Year.]

- **'All hands on deck' as issuance surges even during holidays**
- **About $9 billion in issuance planned for next week alone**

It's the most wonderful time of the year — and usually the quietest — for the $3.8 trillion municipal-bond market, but not so much in 2017.

States and localities typically sell very little debt during the second half of December, but the potential congressional tax-code overhaul that threatens to wreak havoc on tax-exempt borrowing for municipalities has led to a surge of deals coming to market at year-end, disrupting the usual holiday pace.

Preliminary numbers indicate that at least $9 billion of municipal debt is expected to be issued during the week of December 18 alone, according to data compiled by Bloomberg. That's more than double the average issuance during the last two weeks of December in 2014, 2015 and 2016, when about $3.4 billion of bonds were sold, and leaves this month on track to approach or top the record of $54.7 billion hit in December 1985.

"A lot of new issues are coming in, and they're looking to price next week," said Eric Friedland, director of municipal research in Jersey City, New Jersey, for Lord Abbett, which holds about $20 billion of municipal debt. "It's usually unheard of to price the week before Christmas."

Lawmakers in the House and Senate are still hammering out the details of tax legislation that could curb subsidies for a large swath of the municipal market in 2018. The House version repeals the tax-exemption for so-called private activity bonds that help entities like hospitals and airports finance projects at a lower cost. The Senate bill doesn't end those deals. But both chambers' proposals repeal the use of tax-exempt bonds for advance refundings, a tool that lets localities refinance debt and save tens of billions of dollars a year. The risk of those changes sparked a rush to market.

Friedland said he wouldn't be surprised if deals came in between Christmas and New Year's. He noted that the calendar could also shrink if deals get pulled because of less interest.

"Until there's clarity, everyone's going to be trying to get to the market," said Friedland, who noted that it'll probably be too busy for him to take time off. "It's all hands on deck right now."

Bloomberg clients: We'll be doing a TOPLive Q&A on Thursday, December 14 at noon ET, moderated by Taylor Riggs, in which you can ask Joe Mysak questions about the municipal supply deluge, tax reform, what next year may hold for the sector and more. You can watch it here. If you want to ask a question, please send it to TOPLive@bloomberg.net

Bloomberg Markets

By Elizabeth Campbell

December 13, 2017, 6:30 AM PST

— With assistance by Danielle Moran

Commentary: Holiday Wish List for Muniland.

There is no doubt that this year has created many highs and lows in the municipal market. We have many reasons to be grateful. One of the high points is that for most of the year money has flowed into mutual funds and ETFs except for a periodic single down week.

Another wonderful element this year has been the strong bid for municipals from all demand sides of the market. We have even experienced a spike in the amount of foreign buying in the market. The latter is rare indeed given foreign buyers do not benefit from the tax exemption. These buyers have been participating in municipals because our market has higher rates than in their home markets and our creditworthiness is relatively strong and stable despite the handful of problematic credits.

Although not as strong as last year, refunding activity has been steady. There have been a fair number of transactions that have been over $500 million that have been distributed with ease. The long end of the curve continued to rally despite an overall flattening of the curve. Long bonds at the offer have frequently been oversubscribed 3x's to over 10x's.

So what more could we desire? Why are we so cranky? Is it just because spreads are narrow and everyone is generating less revenue or is it something more? Why does it take 3 to 5 rounds of interviews to hire someone when there are enough qualified candidates?

Or, perhaps, the regulatory requirements have just become more burdensome, including issue price rules and ever more disclosure requirements. Tax Reform clearly has many troubling aspects to a municipal professional. We do not have one answer to the rhetorical question but we are certain that you have your own answer.

We think it is an appropriate time to ponder the Wish List in earnest. Herein is my humble attempt.

- Please, provide us with an Infrastructure Plan that we can embrace fully. Our appetites were whetted with the promise of a new bold plan last year. The infrastructure initiative was quickly overwhelmed by other priorities. It would appear that tax cuts and reforms were much higher on the priority list than getting more folks to work in necessary public works projects. There has been some very recent discussion that a plan may emerge again as soon as in January. However, according to reports the version that may be floated this time will allegedly put more pressure on state and local governments to provide matching funding of some kind. How will that work? Have they been reading that Connecticut, one of the wealthiest states in the nation, has a budget gap and has a challenge in its transportation funding because it is not keeping pace when the economy is at a high mark. Asking states and localities to do more is acceptable, but, these governments do not have unlimited resources.
- How about assisting the effort with some clearly identified and unencumbered revenue streams from the federal level that can be leveraged in an efficient way. We have no qualms about issuing debt, especially, revenue debt that is backed by user fees and not general taxation. But additional revenues are required. Not many projects can be well funded with "smoke and mirrors."
- Ratings should be assigned with well researched conclusions and rationales. Criteria have to be as clear and transparent as possible. Assessment of the long haul in ratings is essential, while it is good practice not to ignore the realities of the present. Although matrices and other tools may be useful in attaining good judgments, there should not be an overreliance on these tools. Also, three notch downgrades should happen less frequently assuming reviews are being done in timely fashion.
- Adding regulations at the pace of a few major initiatives a year may be important, but it does have an impact on the functioning of the market. We keep moving toward a fully regulated market, but no participants would be satisfied with that outcome. Refining what is on the books already is a worthy goal, but brand new aspects should be sparse.
- We all have a great deal of information to review each and every day. The Bard of Avon suggested that "Brevity is the soul of wit". We cannot agree more. We know that some technical aspects require longer explanations with certain critical passages and caveats. But, we hope that if there is a more direct way to present the information that path will be taken.
- Those who have the data prevail and those who do not are challenged. If you have access, there is a level playing field. We also believe that data that is painstaking to gather and labor intensive

should be paid for without hesitation. The Bond Buyer has added MBIS data to its platform. We are working to make this service an increasingly useful tool.
- Do not forget the needs of the small Issuer. One of the greater and more democratic principles of the municipal market is that the small Issuer has as good access to the market as the large Issuer. We are not clear that this condition is the case in all markets. We continue to be champions of this principle in the municipal market.
- An informed market is a more efficient market. We fully appreciate the necessity of the Compliance function in the market. But we do believe that being able to discuss critical matters that are important to the business is quite essential to the proper functioning of the market.
- Tax Reform is a defining moment for this market. We appreciate that the tax reductions are designed to be a catalyst for GDP growth. But, let's not forget the poor, the sick, and the needy. Pass the CHIP funding. And we trust we will find our way in issuing more taxable paper if need be. We just lament the higher costs. We stand for fairness and efficient markets. We want to remain the best market we can be.

The Bond Buyer

By John Hallacy

Published December 11 2017

The Bond Buyer Celebrates City of Cambridge's Collaboration with Neighborly at Annual 'Deal of the Year' Awards.

SAN FRANCISCO, Dec. 11, 2017 /PRNewswire/ — Neighborly, the San Francisco-based fintech company focused on modernizing public finance by empowering investors to fund positive change in communities, today announced that The Bond Buyer has recognized the firm's 2017 partnership with the City of Cambridge, Massachusetts, as its 'Non-Traditional Deal of the Year.' The accolade was announced at The Bond Buyer's recent Deal of the Year Awards ceremony, held in New York City.

Now in their 16th year, the Deal of the Year Awards reward innovation in municipal finance. Winners, which are determined by a panel of Bond Buyer editors, are deemed to have exhibited noteworthy innovation, successful execution of complex transactions under oftentimes challenging conditions, an ability to serve as an exemplary model for future financing, and proven impact factor – i.e., the public purpose for which a deal's proceeds were used.

The City of Cambridge was lauded for its February 2017 issuance of General Obligation Series 2017 A Minibonds, which leveraged Neighborly's accessible online platform to sell bonds directly to Cambridge residents. The bonds, offered in affordable denominations of $1,000 to encourage participation, presented a unique opportunity for individual investors to earn tax-exempt interest while advancing positive projects in their own community. The funds raised, totaling $2 million, have since been utilized to renovate school buildings, upgrade municipal facilities, and advance implementation of Cambridge's "Complete Streets" plan.

"Neighborly heartily congratulates the City of Cambridge on this accolade, which reflects its leadership's commitment to residents," said Pitichoke Chulapamornsri, who led the deal as director of business development at Neighborly. "Our work with Cambridge is a prime example of how technology can reduce the cost and complexity associated with public finance to produce powerful results. As a result of our engagement, the City Manager's office was able to raise capital and shape

Cambridge's future by connecting with a previously untapped audience of engaged, impact-driven residents."

Cambridge's initial bond offering generated a significant amount of interest, selling out within six days. Thirty-seven percent of buyers were first-time bond investors; more than 30 percent were under the age of 40.

Issuers who are interested in learning more can contact the team via neighborly.com/issuers, while potential investors can learn more about the Cambridge offering at https://neighborly.com/cambridge.

About Neighborly

Founded in 2012 and headquartered in San Francisco, CA, fintech company Neighborly is on a mission to modernize public finance. This civic-minded team of technologists and finance professionals is united by the belief that the humble municipal bond can once again be a singularly important force in solving economic, educational, healthcare and environmental issues – one community at a time. Positioned at the intersection of technology, government, and finance, Neighborly reduces the cost and complexity associated with municipal bonds by directly connecting fiscally responsible issuers with investors who want to earn returns while effecting positive change in the world.

Neighborly Corporation has built bank-grade technology, and its wholly-owned broker-dealer subsidiary, Neighborly Securities, is a member of FINRA, SIPC, and the MSRB. Neighborly Investments is an SEC-registered investment adviser; registration as an investment adviser does not imply any level of skill or training. This material is for informational purposes only and should not be considered investment advice or recommendation to invest. The information on this page does not constitute a solicitation to buy or sell securities.

When Climate Change Becomes a Credit Problem.

Climate change is now a credit issue for city and state governments vulnerable to extreme weather events and natural disasters made worse by global warming. And that will make a complicated problem a lot easier for people to understand, because it could hit them where they feel it: in their wallets.

In a welcome but long overdue development, one of the world's leading credit-rating agencies, Moody's Investors Service, announced recently that it would give more weight to climate change risks in evaluating the creditworthiness of state and local governments.

Coming in the aftermath of hurricanes that severely damaged parts of Houston and much of the United States Virgin Islands and Puerto Rico this year, the message from Moody's was clear. Governments must prepare for heat waves, droughts, flooding and coastal storm surges or face credit downgrades that will make it more expensive for them to borrow money for public services and for improvements in roads, bridges and other infrastructure.

That could mean higher taxes for the people who live in those communities. Even for governments that act to reduce their exposure to climate risks, the costs of doing so "could also become an ongoing credit challenge," Michael Wertz, a Moody's vice president, said.

And there are many communities in harm's way: Just in terms of coastal flooding, for instance, Moody's reports that 43 percent of coastal homes in Georgia lie in floodplains vulnerable to inundation; in Florida and Mississippi, the number is 38 percent; in Louisiana, 34 percent and in Texas, 26 percent.

Credit agencies have been under pressure for years to give greater weight to the dangers posed by climate change as they evaluate the risks of government bonds. As Moody's put it: Climate change is expected to increase the nation's "exposure and vulnerability to a range of factors such as severe heat, changes in precipitation patterns and rising sea levels." And those factors, the rating agency said, "are projected to drive an increased frequency of extreme weather occurrences, or climate shocks," like droughts, wildfires, flood and storms.

In short, Moody's is making it clear that there is a potential climate risk bubble in which an extreme weather event causes damages so catastrophic that taxpayers, insurers, lenders, states and municipalities suffer damages or losses of hundreds of billions of dollars and local and state government face downgrades in their credit worthiness, affecting their ability to borrow money.

This scenario isn't outlandish. In Puerto Rico, it could cost up to $95 billion to pay for and repair the damage caused by Hurricanes Irma and Maria. What if a storm of Maria's ferocity had hit South Florida dead on?

Smaller credit-rating and bond investor firms are already taking climate risks into account. But the Big Three rating agencies (the other two are Standard & Poor's and Fitch Ratings) have been slow to take climate risks seriously.

Perhaps Moody's decision might also strengthen the hand of activist shareholder groups that maintain fossil fuel-related industries may see their oil, coal and natural gas assets stranded below ground as efforts to combat climate change ramp up.

Moody's is trying to get ahead of the curve. The company and the other major credit-rating firms badly missed the subprime housing bubble that helped push the economy into recession and were widely criticized for it.

Now the agency is warning, "Long-term climate changes, including rising global temperatures and sea levels, are forecast to drive increased extreme weather patterns and other vulnerabilities like flooding that might put negative credit pressure" on municipalities and states.

Moody's warnings go beyond the risks of coastal storm damage, more frequent and severe droughts, wildfires and heat waves.

The company put it this way: "In addition to loss of life and threats to public health and safety, these events present a multitude of challenges in the form of compromised crop yields, economic disruption, damage to physical infrastructure, increased energy demand, recovery and restoration costs, and the cost of adaptive strategies for prevention or impact mitigation. These challenges can result in lower revenue, increased expense, impaired assets, higher liabilities and increased debt, among other effects."

As one of the Big Three credit rating agencies, Moody's credit advice to individual and institutional investors carries enormous weight in the lending and capital markets.

If the other major ratings agencies follow, the pressure will be on municipal and state governments around the country to address the underlying climate risks they face or confront the very real possibility that the costs of borrowing money will suddenly become a lot more expensive.

And that’s not something taxpayers will like.

THE NEW YORK TIMES

By JEFF NESBIT

DEC. 13, 2017

Fitch: U.S. State Pension Burdens Trending Higher Than Debt.

Fitch Ratings-New York-12 December 2017: U.S. states continue to keep overall debt largely in check, though their pension burdens are larger and rising according to Fitch Ratings in a new report.

Fitch’s calculations showed a modest year-over-year increase in median state long-term liability burdens at 6% of 2016 personal income compared to 5.6% one year earlier. Fitch attributed the entire year-over-year increase to defined benefit pension liabilities versus bonded debt. Nonetheless, Fitch still deems the median state liability burden low relative to state resources.

A different picture emerges when assessing liability burdens for individual states. Fitch calculated that six states have liability burdens eclipsing 20% of personal income. Illinois tops the list with a total liability burden equal to 28% of personal income, followed by Connecticut, Kentucky, New Jersey, Alaska and Massachusetts. By contrast, 38 states carry liability burdens below 10% of personal income, with Nebraska the lowest at 1.4%.

The disparity in liability burdens is driven mostly by pension obligations. Many states with elevated pension burdens provide pensions not only to state retirees but also to local teachers. Additionally, a history of weak contribution practices has resulted in actuaries forecasting that pension assets will be depleted for many states with the highest pension burdens. This requires a more conservative calculation of pensions under current accounting rules.

“Unlike bonded debt, state pension burdens continued to rise,” said Senior Director Douglas Offerman. “Factors driving this growth include weaker than expected asset performance during the most recent reporting period, inadequate contributions by some governments, long-term demographic trends and the continued shift by states toward lower discount rates.”

‘Pensions Driving State Liability Burdens’ is available at ‘www.fitchratings.com’

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Bloomberg Brief Weekly Video - 12/15

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

Watch video.

Bloomberg

December 14th, 2017, 1:28 PM PST

Muni Debt That Beat Stocks Likely Won't Deliver Repeat Next Year.

- **Tobacco sector may return 5 percent in 2018, Barclays says**
- **Cigarette tax and smoking age increases will weigh on prices**

High-yield municipal bonds backed by legal-settlement payments from tobacco companies have returned 20.4 percent this year, more than the S&P 500 index. Don't expect a repeat in 2018.

Investors in the sector may have to settle for the income they get from interest payments — instead of price gains — as higher tobacco taxes in California and the U.S. Food and Drug Administration's plans to cut the nicotine in cigarettes to non-addictive levels threaten to weigh on the industry's sales. The payments that back tobacco bonds are based on cigarette shipments, which are affected by the overall economy, government regulation and excise taxes.

"They don't have a lot of upside left in them," said Guy Davidson, director of municipal fixed income for AllianceBernstein LP.

Junk-rated tobacco bonds have beaten the S&P 500 index three of the last five years, though almost all of the sector's gains this year came in the first half. The securities rebounded after money managers dumped the securities — among the most liquid high-yield municipal bonds — to meet redemptions during the bond-market rout that erupted after President Donald Trump's victory.

Refinancings by New York City and California that reduced the amount of debt and lower-tha--forecast smoking declines have also boosted prices.

Since the FDA announced its plan to lower nicotine levels in cigarettes in late July, the sector has returned 1.6 percent, lagging the 2.1 percent gain for the the broader high-yield muni market over the period. Junk-rated tobacco bonds make up about 20 percent of the Bloomberg Barclays Municipal High Yield Index.

The largest single tobacco bond, issued by an Ohio agency and maturing in 2047, trades at about 96 cents on the dollar, or a cent less than the 2007 issue price, and is up more than 50 percent since

Sept. 2013. Many tobacco bonds can be bought back at par from investors before maturity, which may limit further upside because the securities are already trading close to 100 cents on the dollar, Davidson said.

Even though the FDA proposal may take more than a year to enact, performance next year will be hindered by other factors, Mikhail Foux, the head of municipal strategy for Barclays Plc, said in an interview. Tobacco sales may be curbed by a $2 per-pack tax increase in California that took affect April 1 and a raising of the minimum smoking age to 21 in that state as well as New Jersey and Oregon, Foux said.

The production of cigarettes has declined 2.5 percent through September 2017 compared with the same period last year, according to data from the Alcohol and Tobacco Tax and Trade Bureau.

An improving U.S. economy may blunt the impact of cigarette tax and smoking age increases, said Foux, who predicted tobacco bonds may return about 5 percent in 2018.

AllianceBernstein reduced tobacco-bond holdings in its muni high yield fund to 4.3 percent from 7 percent in June.

“The best scenario for the 2007-vintage tobacco bonds is a stable market where investors earn the yield on their bonds,” Davidson said.

Bloomberg Markets

By Martin Z Braun

December 14, 2017, 8:53 AM PST

[The Week in Public Finance: Tax Reform Games, a Mad Rush to Issue Muni Bonds and Pension Fees.]

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

GOVERNING.COM

BY LIZ FARMER | DECEMBER 15, 2017

[State Spending Grows at Lowest Pace Since Great Recession.]

Amid uncertainty about federal tax reform, states are exercising caution with their fiscal 2018 budgets.

After several years of moderate spending growth, states are dialing it back amid federal policy uncertainty and unpredictable revenues.

States’ general fund spending is projected to total $830.2 billion in fiscal 2018, which represents just 2.3 percent growth and the lowest spending increase since the Great Recession. Twenty-six states have already enacted budgets with general fund spending growth below 2 percent, and 15 states are cutting spending in fiscal 2018.

The [new survey data]() was released Thursday by the National Association of State Budget Officers' (NASBO).

The shift comes amid uncertainty about how federal tax reform will ultimately affect states' revenues and taxpayer behavior in 2018. Meanwhile, two straight years of an unusually high number of states resorting to mid-year spending cuts has many policymakers taking a more conservative approach to this year's budget.

"There's plenty of reasons for caution at this point," said Michael Cohen, director of the California Department of Finance, on a call with reporters. "And we've not been willing to overcommit to ongoing spending."

Underscoring that caution is the fact that, for the first time in five years, states have collectively budgeted for revenue growth to outpace spending growth in fiscal 2018. Most states are forecasting general fund growth of 4 percent. Roughly a quarter of this growth can be attributed to tax and fee increases and other revenue measures enacted by states in the 2017 legislative session, often in the face of budget deficits.

Those increased revenues, said NASBO Executive Director John Hicks on the same call, are a way of "catching up" budgets to reality after many states employed one-time fixes to balance past budgets.

Many states are also continuing to strengthen their reserves, despite the recent revenue slowdown. Rainy day funds as a percent of general fund spending is now at 5.2 percent, compared to less than 2 percent in 2011.

State by state, the financial picture varies widely.

Some states have repeatedly turned to their rainy day funds to help address shortfalls. Connecticut, for example, is battling a weak local economy and has just over 1 percent of general fund spending in its reserves after withdrawals in recent years.

Alaska, New Mexico and North Dakota passed their third straight budgets with spending cuts thanks to weak oil and other energy-related revenues.

Meanwhile, 11 states, mostly in the faster-growing regions of the Southeast and West, increased general fund spending by more 4 percent.

When it comes to where states targeted their spending, most of the focus went to K-12 education, the largest single portion of state general fund spending. A total of 38 states increased education spending, while 10 states made cuts, resulting in a net increase of $8.6 billion this year.

Medicaid was also a big driver of spending with states collectively spending $2.6 billion more this year from their general funds than in fiscal 2017. (NASBO notes that figure is actually more than $5 billion when including Medicaid spending in Ohio that is now being withdrawn from special funds.)

GOVERNING.COM

BY LIZ FARMER | DECEMBER 14, 2017

S&P: Southern California Fires Again Test Local Government Credit Resilience.

After a difficult October for California that brought major fire damage to mostly northern areas of the state such as Santa Rosa and the iconic wine-growing communities in Napa and Sonoma Counties, December has brought major fires to Southern California, particularly in areas surrounding Ventura (western Ventura County).

Continue Reading

Dec. 12, 2017

P3 Digest for December 15, 2017

Innovative U.S. 36 Express Lanes Project Reduces Traffic Congestion by Offering Mobility Choices

Editor's Note: The following article is one in a series of six profiles of winners of NCPPP's 2017 National Public-Private Partnership Awards, which recognize organizations and individuals that have gone above and beyond to advance the concept and implementation of P3s across the country. The winners will be honored during P3Connect in Miami Beach in January.

If you asked David Spector which of the improvements made to U.S. 36 in Colorado have benefited the most travelers, you might expect him to pause and ponder because there are so many choices.

Would he mention the new walking, cycling or bus rapid transit (BRT) options on this 18-mile segment? Or would he single out the increased safety provided by a new diverging diamond interchange at a bridge that crosses U.S. 36? Maybe top billing would go to the ability of the state's first active traffic management system, which monitors traffic flow and speed limits, to provide traveler information and improve incident analysis.

Continue reading.

NCPPP

S&P: U.S. Not-For-Profit Acute Health Care Stand-Alone Hospital Median Enterprise Statistics.

S&P Global Ratings considers the assessment of enterprise profile characteristics in conjunction with its evaluation of financial profile attributes when rating acute-care stand-alone hospitals. Our assessment of the enterprise profile includes evaluation of the operating environment, organization-specific characteristics, and broad industry conditions–all of which can influence financial perform

Continue Reading

Dec. 11, 2017

Securitized Muni Bonds Can Make Good Sense.

The assertion that Chicago and Connecticut are borrowing a "debt trick from Puerto Rico" is misguided.

Regarding your editorial "Have They Got a Bond for You" (Nov. 21 and the Letters of Nov. 28): The assertion that Chicago and Connecticut are borrowing a "debt trick from Puerto Rico" is misguided. Municipalities and states across America have used secured debt offerings to access the capital markets at a lower cost than unsecured bonds for decades.

Secured debt backed by a dedicated revenue stream, such as local sales taxes, typically comes with a higher rating and lower interest rate than unsecured debt. Chicago's new tax-backed bond issuance is expected to be 200 to 300 basis points cheaper than its general obligation debt, saving the city and its citizenry up to $100 million a year.

Investors will accept a lower interest rate in exchange for property interest in collateral that will remain intact following any default or bankruptcy filing. In fact, effective use of tax-backed secured debt, combined with renewed emphasis on fiscal discipline, allowed Washington, D.C., and New York City to raise affordable capital following downturns and avoid bankruptcy restructurings.

Your editorial misrepresents the separate collateral pool for Puerto Rico's Cofina bondholders and overlooks that the VAT proposed by the island's last governor was voted down by the legislature before it ever went into effect. The editorial also omits that Detroit's secured creditors received par recoveries precisely because our laws protect property interests.

We cannot forget that not all bonds are created equal.

by Matt Rodrigue

Dec. 3, 2017 3:50 p.m. ET

The Wall Street Journal

The writer is financial adviser to a coalition of investors holding $2.6 billion of Cofina senior bonds.

Fitch: Some Smaller U.S. Colleges May Face More Pressure in 2018.

Fitch Ratings-Chicago-07 December 2017: The outlook for ratings in the U.S. colleges and universities sector is stable headed into next year, though the gap is widening between larger, stronger universities and some of their smaller counterparts, according to Fitch Ratings in its 2018 outlook report.

"Operating revenue pressures will likely intensify for small, tuition-dependent schools in demographically declining areas or highly competitive regions," said Director Emily Wadhwani. "Barring those outliers, operating performance is expected to remain strong sectorwide, which coupled with steady student demand and enrollment and solid financial resources supports a stable sector outlook.'

Operating revenue also stands to be affected by recently proposed tax reform legislation, with annual charitable gift revenue and both state and federal funding to feel those effects most acutely. Most vulnerable are institutions already facing revenue pressures related to enrollment, tuition dependency, or those with limited liquidity profiles lacking material foundations or endowments. “Proposed bills have served to sustain national focus on the value proposition of higher education, which could have a more lasting impact over time,” said Wadhwani.

Nonetheless, U.S. colleges and universities by and large enjoy ample financial flexibility and have been proactive in minimizing the volatility of investment returns and increasing the overall liquidity of their total holdings. Well-positioned institutions retain meaningful balance sheet resources, solid demand and increasing tuition revenue while keeping leverage in check. Most colleges are also effectively balancing the desire to maximize long-term investment returns and the need for capital investments against the need for sufficient working capital and liquidity.

Fitch’s ‘2018 Outlook: U.S. Colleges and Universities’ is available at www.fitchratings.com.

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Fitch: Outlook for U.S. Local Government Ratings Stable in 2018.

Fitch Ratings-New York-06 December 2017: Numerous questions concerning Federal policy and infrastructure adequacy will not impede the financial resiliency of U.S. local government ratings next year, according to Fitch Ratings in its 2018 outlook report.

Fitch’s stable outlook for U.S. local government ratings remains in place for 2018 thanks in large part to their financial dexterity in uncertain times, both economic and otherwise.

“Local governments have long demonstrated the ability to close budgetary gaps throughout economic cycles,” said Managing Director Amy Laskey. “Also helping matters are reserve levels, which going into next year are well in excess of what is needed to offset a recessionary revenue decline.”

Federal policy uncertainties around Medicaid, the federal tax system and international trade could heighten the risks associated with local government non-property tax revenue. Depending on the outcome of each of these areas, school districts would be most at risk as a result of changes to Federal policy since they are most reliant on state aid. Also worth watching are localities bordering Canada and Mexico that would be vulnerable to loss of direct revenues resulting from changes in trade policy.

Infrastructure remains an ongoing concern and more so in light of Hurricanes Harvey, Irma and Maria, which caused widespread damage in parts of Texas, Florida, and much of Puerto Rico and the Virgin Islands. That said, local government ratings should remain well insulated from ongoing rebuilding costs as they are largely shouldered by the federal government.

"Local governments will not have to issue much debt that is not reimbursable by the federal government, so the recent storms should not affect debt service or long-term liability burdens," said Laskey.

Another area of note in the coming year is the desire by some local governments to create structures that protect bondholders from a government's general operating risk. One such structure is securitization, as evidenced by the recent creation of Chicago's Sales Tax Securitization Corporation.

"Several California issuers along with the Chicago Board of Education have also issued bonds secured by tax revenues that lead Fitch to analyze the debt without regard to operations, and increased interest among some other local government entities is a real possibility headed into 2018," said Laskey.

The report "Fitch 2018 Outlook: U.S. Local Governments" is available at 'www.fitchratings.com'

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Fitch: Budget Challenges Await Some U.S. States in 2018.

Fitch Ratings-New York-06 December 2017: U.S. states are well positioned to meet budget forecasts next year so long as the economy continues to grow, though five states could run into some issues, according to Fitch Ratings in its 2018 outlook report.

The Rating Outlooks for most U.S. states are Stable and expected to remain so over the next 12 months. Federal action remains the pre-eminent factor driving state credit ratings in the coming year. Decisions around Medicaid and tax policy present the most immediate risks while infrastructure, trade and other policy areas will affect economies and budgets over time, all with varying degrees by state.

Nearly one year into the new federal administration, many areas of policy remain unresolved. Throw in increasingly contentious state budgeting sessions and policy becomes more of a challenge for states next year. However, "state budget makers are historically conservative, which should make budget forecasts attainable for the vast majority of U.S. states," said managing director Laura Porter.

Helping matters is the likelihood of the broader economy continuing to grow next year, which is what Fitch is projecting. "Changes to federal funding could present a challenge without mandate relief, though states would likely rely on their strong ability to manage budgets and download fiscal challenges were federal changes to take place, protecting ratings," said Porter.

The overall stable outlook for the sector, however, is not without its outliers. Not surprisingly, Illinois and New Jersey are once again on Fitch's "states to watch" list in 2018 along with Connecticut, Kentucky and Louisiana. "Illinois will enter 2018 with an enacted budget for the first time in nearly three years, though whether the budget will be successfully implemented remains a lingering question mark," said Porter. "If Illinois reverts back to a pattern of deferring payments for near-term budget balancing, their credit rating could face more immediate pressure."

The full report, '2018 Outlook: U.S. States' is available at 'www.fitchratings.com'

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Fitch: U.S. Not-for-Profit Hospitals Face Rising Challenges in 2018.

Fitch Ratings-New York-06 December 2017: Regulatory, political and competitive challenges will intensify for U.S. not-for-profit hospitals and healthcare systems headed into next year, according to Fitch Ratings in its 2018 outlook report.

While Fitch has a Stable Rating Outlook for the not-for-profit healthcare sector in 2018, the sector outlook is negative. "Growth in Medicare and Medicaid volumes are weakening provider payor mixes at a time when providers are moving from volume-based to value-based reimbursement in greater numbers," said Senior Director Kevin Holloran.

Profitability will also continue to weaken gradually for the sector next year, although operating performance should by and large be stable, similar to what was seen in 2017. That being said, "growing pressure on salaries and wage expense and continued erosion in payor mix could adversely affect operating performance for lower-rated hospitals," said Holloran.

Another area worth close watch in 2018 will be the proposed tax-overhaul bill, which would hamper hospitals' and health systems' ability to issue tax-exempt revenue bonds and in turn likely drive up issuance costs and further pressure the industry.

Fitch maintains its stable outlook for ratings of healthcare issuers, with affirmations and Stable Outlooks to dominate most rating actions in 2018. Fitch anticipates our revised criteria for the acute care sector will be published early next year, which should lead to an above-average, but still balanced, degree of rating movement during the year.

“Fitch 2018 Outlook: U.S. Not-for-Profit Hospitals and Healthcare Systems” is available at www.fitchratings.com.

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[Fitch: EPA's LCR Changes Will Not Deter U.S. Water/Sewer Stable Outlook in 2018.]

Fitch Ratings-Austin-06 December 2017: Uncertainties around the regulatory environment will not deter the stable outlook for the U.S. water and sewer sector next year, according to Fitch Ratings in its 2018 outlook report.

The U.S. Environmental Protection Agency’s (EPA) Lead and Copper Rule (LCR) may roll out revisions next year following numerous stops and starts. Added capital and operating expenses could be meaningful depending on how significant the changes to LCR are. That said, any costs would likely be phased in over several years. ‘Wastewater utilities will continue to face pressure from enhanced nutrient removal requirements as discharge permits are renewed periodically,’ said Managing Director Doug Scott.

Despite the regulatory uncertainty, water and sewer municipalities have strong balance sheets that give them flexibility should capital demands increase. What’s more, Fitch’s latest medians point to slightly lower capital spending next year and beyond from recent levels. Over time, however, ‘sustained capital investment increases will be necessary to address deferred maintenance and preserve service levels over the long term for water and sewer municipalities,’ said Scott.

Also solidifying the sector’s stable outlook in 2018 will be a manageable debt profile, with Fitch projecting growth in debt to be muted. The likelihood of water and sewer utilities keeping new debt issuance modest in the coming year will also keep the debt profile sustainable even if interest rates rise.

The full reports, ‘2018 Outlook: Water and Sewer Sector’ and ‘2018 Water and Sewer Medians’ are available at www.fitchratings.com.

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Fitch: Tax Reform May Curb Capital Spending for U.S. CCRCs in 2018.

Fitch Ratings-New York-06 December 2017: A stable outlook remains in place for U.S. continuing care retirement communities (CCRCs) next year though the recently enacted tax reform bills could moderately reduce what has normally been a healthy capital spending environment, according to Fitch Ratings in its 2018 outlook report.

The potential loss of tax-exempt financing from federal tax reform proposals would reduce access to capital and increase borrowing costs or CCRCs. As a result, “CCRCs would have to use taxable bank financing and other more expensive forms of capital that may have less favorable terms and conditions,” said Director Paul Rizzo. “Additionally, many borrowers may opt to use equity or downsize capital projects that require higher levels of debt.”

Regardless, the potential short-term hit to capital spending will not dramatically affect the sector’s credit profile thanks to consistent operating profitability, high occupancy and good demand for services. CCRCs will look to remain competitive and address such service-line needs as memory care and/or unit-mix issues. The tight labor market, however, may lead to higher construction costs for some communities along with delayed starting dates for certain large-scale projects.

Also bolstering the sector’s stable outlook next year is the healthy U.S. housing market. Nominal home values are steadily increasing and housing affordability remains favorable relative to historical levels. “The housing market will remain healthy in 2018, which should support ILU occupancy and net entrance fee receipts for CCRCs in the coming year,” said Rizzo.

As far as challenges for 2018, CCRCs are experiencing pressure in post-acute care census and tightening employment markets that are increasing staffing costs. Post-acute care management and reimbursement modifications are changing the care for short-term rehabilitation patients in skilled nursing centers. Further, growth in healthcare employment levels is leading to harder recruitment of certain positions and expense pressures.

‘Fitch 2018 Outlook: Nonprofit Continuing Care Retirement Communities’ is available at www.fitchratings.com’

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Fitch: U.S. Public Power Set for Stable 2018 amid Regulatory Uncertainty.

Fitch Ratings-New York-06 December 2017: Uncertainties around the fate of the Clean Power Plan (CPP) and the Trump administration's withdrawal from the Paris climate agreement will not detract from U.S. public power sector's stable outlook next year, according to Fitch Ratings in its 2018 outlook report.

Fitch's 2018 rating and sector outlook for the public power and electric cooperative sector is stable thanks largely to autonomous rate-setting authority, the essential nature of electric service and reliable cash flow. The stability of the sector is in contrast to the future of environmental regulations aimed at reducing carbon dioxide (CO2) emissions, which is uncertain at best in light of both aforementioned market developments.

One segment already seeing a near-term boost off of Trump's proposed CPP repeal is coal-dominated public power entities according to Managing Director Dennis Pidherny. "The economics of coal-fired generation have improved this year with coal-fired generation likely to surpass natural gas-fired generation for the first time in over a decade," said Pidherny. This boost, however, figures to be fleeting for coal-fired generation with other EPA rules likely to weigh on coal-fired generation over time.

Also buoying the sector's stable outlook next year is electric cost affordability, which is now at pre-recession levels. "Strong growth in household income has eased rate pressures for most public power and cooperative issuers," said Pidherny. "A willingness to increase electric rates to preserve margins along with modest economic growth should help sustain the sector's trend of improving financial metrics."

'Fitch 2018 Outlook: U.S. Public Power and Electric Cooperative Sector' is available at 'www.fitchratings.com'

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Massive Muni Rally Not Enough to Prevent Fund Outflows.

- **Muni yields had fallen to 15-month low against Treasuries**
- **Pullback may test demand for $18 billion of deals next week**

Municipal bond buyers are taking a breather after the market's biggest rally since August 2011, with firms reporting that investors pulled over $800 million from state and local bond funds over the course of a week.

The yields on benchmark 30-year bonds edged up 0.05 percentage points on Friday to 2.61 percent, stepping back from the price gains that had sent yields tumbling by 0.35 percentage points in the five days through Wednesday. That had left tax-exempt securities less of a draw by reducing their yields to the lowest relative to Treasuries since September 2016.

"Ratios to Treasuries have dropped to levels that present less value for crossover investors and they probably fueled the pace of the recent rally," said Daniel Solender, head of municipals at Lord Abbett & Co., which manages about $20 billion of state and local government securities.

State and local governments are planing to sell $18 billion in debt next week, continuing a potentially record-setting wave as the tax-overhaul legislation in Congress threatens to pull the subsidies from a large swath of municipal securities beginning next year.

Investors have so far eagerly snapped up the new offerings, anticipating that the supply of tax-exempt bonds will fall next year, making them more valuable to investors.

But some buyers have shifted money away from the market. Investors yanked $807 million from municipal bond funds during the week ended Dec. 6, the biggest weekly outflow since June, according to Lipper US Fund Flows data. The outflows this past week reverse a four week-long streak of inflows.

Solender said some of the outflow may have been driven by withdrawals from funds focused on shorter-dated bonds, a segment that would be particularly affected by rate increases from the Federal Reserve.

"Given the heavy forward supply, uncertainty about flows and lower relative value, there is probably a slight pause to see how the next few deals do and to see whether the pace of selling by funds increases," he said.

Bloomberg Markets

By Martin Z Braun and Amanda Albright

December 8, 2017, 9:36 AM PST

Bloomberg Brief Weekly Video - 12/8

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

[Watch video.]

Bloomberg

December 7th, 2017

[The Week in Public Finance: Deduction Loss May Cause Real Pain, the St. Louis Blues Win and Working Around Bad Ratings.]

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

GOVERNING.COM

BY LIZ FARMER | DECEMBER 8, 2017

[A Tale of Two Recoveries a Decade Since the Recession.]

The largest metro areas and those with highly educated workforces have rebounded well, but many other regions have struggled to recover job losses.

Like many smaller economies, the Binghamton, N.Y., region has seen its workforce slowly dwindle since the arrival of the Great Recession. Its large manufacturing sector was hit hard as companies lost defense contracts and a nearby IBM facility implemented multiple rounds of layoffs. Over the past decade, the region shed nearly 9 percent of its workforce — one of the largest declines of any metro area in the nation.

Elsewhere in the state, the sprawling New York City metro area and the state capital of Albany have experienced much stronger recoveries — up about 9 percent and 4.4 percent, respectively.

[Continue reading.]

GOVERNING.COM

BY MIKE MACIAG | DECEMBER 5, 2017

[Green Bond Market Heats Up.]

Issuance of the bonds has reached record levels this year and looks set to accelerate, market watchers say.

Issuance of so-called green bonds reached a record $110 billion through mid-October this year, according to a recent report, signaling the fast-growing popularity of an asset class that was created just a few years ago.

The report — released by Scandinavia's SEB, a leading global green bond underwriting institution —

revealed that this figure topped the $97 billion in total issuance last year. SEB predicts that total issuance for the full year could reach $125 billion.

Though the concept is only about a decade old, green bonds — corporate or government-issued debt that is used to finance various environmental or climate-related projects — are becoming a credible asset class as more asset managers are increasing portfolio allocations to them.

Take, for instance, AMP Capital, a leading Australian fund management firm with A$179 billion ($138 billion) in assets under management. Lydia Serafim, a senior portfolio manager with AMP Capital, says the Sydney-based firm takes environment, social and governance investing seriously — so seriously that managers decided last year their $180 million Responsible Investment Leaders Diversified Fixed Income Fund must have a 15 percent allocation to green bonds.

"Green bonds are a small part of the overall bond market, but it's a growing area," Serafim said in an e-mail to Institutional Investor. "As the investment metrics around 'what is a green bond' become more standardised and refined, investment in the area will increase as the benefits become more transparent to clients."

AMP Capital's decision to include green bonds in its portfolio undoubtedly pleases Christopher Flensborg, the head of climate and sustainable financial solutions at SEB. Flensborg has been called the father of the green bond because he proposed the creation of one to the World Bank back in 2007.

Since then, he has worked with many issuers around the world to launch such bonds. According to SEB, the U.S. has been the top green bond market in 2017, with $25.4 billion in issues through Oct. 10, while China came in No. 2 with $19 billion in issues. France came in at No. 3, with $17 billion in issues.

"In the coming four to five years, I see 10 percent to 20 percent of all new issuance having the 'green' label," Flensborg said in a phone interview. He expects global issuance to top $300 billion by 2020. "We're taking about trillions of dollars a year sometime in the future."

Matthew Kuchtyak, a New York-based analyst specializing in project and infrastructure finance at Moody's Investors Service, also thinks the sector has room to grow.

"Although green bonds will remain a niche segment of the global fixed income market for the foreseeable future, we expect robust issuance growth as market awareness increases and issuers seek greater investor diversification," he said in an e-mail to Institutional Investor. Moody's expects global green bond issuance to top $120 billion in 2017, a 24 percent year-on-year increase.

Many of the 2017 issues came from utility companies. Take U.K.-based water treatment company Anglian Water, which in October issued a £250 million ($336 million) green bond to finance a range of projects in some of the driest regions of the United Kingdom.

Will Oulton, the global head of responsible investment at Australia-based First State Investments, which is a substantial shareholder in Anglian, says he expects that green bonds will become a key feature of the asset manager's portfolio allocation strategy in the future.

"We are watching the development of the market and are always seeking a competitive market return as well as assurance that the proceeds are being utilized for the environmental purposes as stated and not for other non-environmental projects," he said in an e-mail to Institutional Investor.

SEB's Flensborg says he believes that China will become the world's largest green bond market in a few years. Chief among the major global partners who worked with him in designing policies that support green bonds have been policymakers at China's central bank.

Laurence Brahm, a Beijing-based American lawyer who acted as an adviser to China's Ministry of Environmental Protection, says the nation is in the process of changing its power grid away from a reliance on fossil fuels. Officials are determined to reduce coal and fossil-fuel-generated electricity from 70 percent of the power grid supply to 50 percent in the coming decade, Brahm says.

In addition, according to Brahm — who helped the government draft its green investment policy known as "Ecological Civilization" — the government is determined to promote electrical vehicles so that 30 percent of all vehicles on the road will be electric by 2025. By 2030, all new sources of energy will be green, he says, adding that by 2050, 80 percent of China's national grid will be green.

"That kind of scale of transition in a nation of 1.3 billion people can only happen if the financial services sector drives it," Brahm said in a phone interview. "Green finance is critically important, as it is at the core of determining future infrastructure away from fossil fuel economies."

Institutional Investor

Allen T. Cheng

December 05, 2017

U.S. Municipal Bond Supply to Top $20 Billion for Second Week.

CHICAGO (Reuters) – U.S. municipal bond market supply will top $20 billion for a second straight week as issuers scramble to sell debt ahead of potential federal tax changes, according to Thomson Reuters estimates on Friday.

Next week's supply of bonds pricing in the $3.8 trillion market is estimated at $22.88 billion, more than three times the average weekly muni issuance between 1990 and the end of November.

In addition, billions of dollars of more debt is bypassing the market and being sold directly to banks, according to a top-ranked financial advisory firm.

Many states, cities, schools, hospitals and other issuers are accelerating their debt sales in case the U.S. Congress eliminates federal tax breaks for private activity and advance refunding bonds starting in 2018.

That move would saddle nonprofit and other entities that issue tax-free private activity bonds (PABs) with higher borrowing costs and eliminate a way all muni issuers can take advantage of lower interest rates to save money.

The feared loss of advance refundings is accounting for a lot of the market's surging supply, according to John Bonow, CEO of Public Financial Management, a municipal finance advisory firm.

"It's not exclusively advance refundings, but by and far it's driven by advance refundings," he said, adding that some issuers are combining those refundings with new money debt sales.

A provision in both the U.S. House and Senate tax bills would end the practice of refinancing bonds on a tax-exempt basis beyond 90 days from their call date for interest rate savings.

Current refundings of debt within the 90-day call date window would remain tax exempt. The tax bill passed by the House last month would get rid of tax exemptions for new PABs issued to fund hospitals, affordable housing, airports and other projects that benefit private entities. The Senate's bill did not include that provision.

Given the time crunch for getting a deal to market by year end, many issuers are privately placing debt with banks or turning to so-called committed underwritings with banks that lock in interest rates at a spread to current market rates with a plan to reoffer the debt to investors early next year, Bonow said. This means that the surge in debt issuance is even bigger.

"If the weekly calendar says $20 billion I think it could be as much as double that," he said, adding he is aware of one bank that has set aside $20 billion for committed underwritings.

Market demand has been strong, sending prices higher and yields lower on Municipal Market Data's (MMD) benchmark triple-A yield scale for five straight sessions.

But the market began reversing direction on Thursday followed by a larger downward price move on Friday that pushed yields up as much as 9 basis points. The yield on top-rated, 10-year bonds climbed 7 basis points to 1.95 percent and the 30-year yield also went up 7 basis to 2.56 percent, according to MMD.

By Karen Pierog

Dec. 8, 2017, at 2:50 p.m.

(Reporting by Karen Pierog; editing by Daniel Bases and Andrew Hay)

Here's Why Muni Bond Prices Rally Even as Market Is Deluged.

- **Steady amortization provides shock absorber for new supply**
- **Maturing bonds, calls means money is always looking for a home**

Everyone's marveling this week because the municipal market is rallying in the face of a $21 billion-plus wave of new supply, almost triple the $7.3 billion average this year, as issuers look to get ahead of Congress's tax reform.

The yield on the Bloomberg BVAL 10-year triple-A benchmark has fallen from 2.25% on Nov. 29 to 1.94%, even below the 2.03% it posted on Nov. 2, when the House GOP unveiled their version of tax reform and set off the bond-issuance stampede.

How was this even possible? Munis are bulletproof!

Well, yes. I hadn't fully grasped the nature of the market until the rally this week. If anything, I took for granted what we all know in the municipal market, and which mystifies tourists in MuniLand.

And that's the conservative debt management of most of the nation's states and municipalities.

Back in the days of the financial crisis, even before Meredith Whitney's famously off-target prediction about a wave of coming defaults, I remember reading some blogger who asked what municipalities were going to do when it came time to rollover all their maturing debt — a routine ingredient of sovereign debt crises. The implication was that states and cities all faced imminent financial oblivion.

But that’s not how munis work — then or now. There is no big rollover, as is also common in corporate finance. I got really angry because someone was making an assertion and they didn’t know what they were talking about. This sort of thing used to bother me.

States and municipalities borrow with bonds that mature serially (every year) and in terms (think of single-bullet maturities). They pay off their debt steadily over time, just as homeowners do with their mortgages. Because of that, even with a steady thrum of borrowing, for much of this year, and for the past few, the municipal market had actually been shrinking.

Until relatively recently, issuers have been retiring more debt than they sell. This year, for example, long-term issuance stands at $357.8 billion. There have been $439.7 billion in bonds maturing and being called.

Let’s see how this works in practice. In November, $20.9 billion in bonds matured. Another $10.5 billion was called. That means $31.4 billion was looking for a new home, presumably back in the municipal market.

But November was a very busy month, as private-activity bond issuers and all issuers who wanted to use advance refundings, both of which would be prohibited under the House GOP version of tax reform, rushed deals to market. States and municipalities sold $42.7 billion in long-term debt, both fixed-rate and variable.

Now let’s look at December. At the beginning of the month, the amount issuers planned to sell over the next 30 days was calculated at $29 billion, the highest it’s been since 2005. Municipalities are rushing to beat the Jan. 1 effective date of the House GOP version of tax reform. They are even moving up deals they had planned to sell in early 2018.

So: $29 billion in new deals are planned. There’s $27.7 billion in debt maturing; another $12.5 billion is being called. So $40.1 billion is looking for a new home. There’s your rally.

Now, the visible supply figures don’t capture every planned bond issue; in fact, they basically capture about half. It’s almost like a weather forecast — very accurate up front, less so the further out you go. If we see $58 billion in sales this month, won’t yields go higher?

And the answer is: Perhaps. But keep in mind, investors know that issuance in early 2018 will be down, maybe because of new prohibitions on tax-exempt debt, definitely because so many 2018 deals were moved into 2017. Plus, $21.7 billion in municipal bonds mature in January. We don’t know yet about how many will be called; calls are announced 30 days in advance. And in February, another $26 billion matures. And so on.

This amortization schedule is why the municipal market is bulletproof.

Bloomberg

By Joe Mysak

December 7, 2017, 4:00 AM PST

[Investors Can't Buy Munis Fast Enough.]

- **Even as supply surges, many deals coming in oversubscribed**
- **'We've all gotten a fraction of what we'd hoped to get.'**

Congress has set off a feeding frenzy for municipal bonds.

Investors are rushing to buy debt being issued by state and local governments, leaving banks with far more orders than they can fill, despite a potentially record-setting flood of new sales this month. Some firms are borrowing so they can purchase more. And even cash from overseas is coming into a market dominated by Americans seeking income that's exempt from federal taxes.

"Firms are taking up leverage, drawing down cash, extending duration — everything they can do to be as aggressive as they can in their portfolios," Peter Hayes, head of municipal bonds at BlackRock Inc., said in an interview with Bloomberg radio on Thursday.

The spree was triggered by the U.S. tax-overhaul legislation that would pull the subsidies from a vast swath of the municipal-bond market starting next year, which investors and analysts say could cut the supply of new bonds by as much as a third. Faced with that scarcity, prices have rallied, sending the yields on 10-year benchmark debt on their biggest six-day drop since 2009, according to data compiled by Bloomberg.

Both the House and the Senate legislation would eliminate tax-exempt bond sales for advance refundings, a technique governments use to refinance tens of billions of dollars of debt each year. The House bill would also prevent businesses such as hospitals, airports and privately owned power companies from borrowing in the municipal market, where interest rates are lower. The two bills are currently in the process of being reconciled.

Guy Davidson, director of municipal fixed income for AllianceBernstein LP, said the buying has come from mutual funds, individual investors and banks.

"It's been a wall of money coming in and coming from a number of different directions all at once," he said. "We've been frustrated because we've all put in for a lot of bonds. But because there's so much competition for the bonds, we've all gotten a fraction of what we'd hoped to get."

Kyle Gerberding, director of trading at Atlanta-based Asset Preservation Advisors, said he could only get a small sliver of what he wanted from the University of North Georgia's $88 million bond issue this week. "Unfortunately, it's all been like that," he said.

He's been told by underwriters that deals have typically been 10 to 15 times oversubscribed, meaning that an investor who places an order for $1 million bonds would end up with $100,000 or less. He said he was "in an uphill battle" with larger firms, some of which are try to buy every bond in an entire deal when it comes to market.

But there's plenty of securities still in the pipeline for December, with issuers already scheduled to sell over $17 billion of bonds next week alone, more than twice what comes during a typical week, according to data compiled by Bloomberg. BlackRock's Hayes said he expects this month's issuance to eclipse the 1985 record of $54.7 billion.

Investors are especially clamoring for higher-yielding tax-exempt hospital and airport securities, which would disappear after this year under the House bill. In the Long Island Power Authority's

$350 million issue last week, 10-year securities were priced at yields of 0.33 percentage point over the benchmark, down from 0.53 percentage point when it sold debt last year.

“It’s been a fever pitch up and down the credit spectrum,” said Tom Casey, a senior portfolio manager at Standish Mellon Asset Management, who said he expects strong returns to continue in the first quarter of 2018 due to a decline in bond sales. He said there’s been “tremendous appetite” from foreign investors.

It’s not only supply that the tax plan could change. By scrapping the deduction for state and local income taxes, the overhaul would increase taxes on wealthy residents of states such as New York, California and New Jersey. That has led some analysts to predict that bonds from those states may outperform, since residents may look for new ways to drive down their federal tax bill.

“Someone who knows the market should be paying attention to high tax states, if they’re not,” said Sandy Panetta, a portfolio manager at Evercore Wealth Management in New York. “They should be getting the most attention because, for sure, they will be in higher demand next year.”

Bloomberg Markets

By Rebecca Spalding, Amanda Albright, and Danielle Moran

December 7, 2017, 9:48 AM PST

U.S. Muni Bond Yields Fall for Fourth straight Session.

Dec 5 (Reuters) – U.S. municipal bond prices rose for a fourth-straight session on Tuesday, dropping yields as much as 8 basis points on Municipal Market Data’s benchmark scale.

The yield on top-rated bonds due in 10 years fell 6 basis points to 1.99 percent and the 30-year yield tumbled 8 basis points to 2.58 percent, according to MMD, a unit of Thomson Reuters.

(Reporting By Karen Pierog; Editing by Steve Orlofsky)

Developers, Banks Push to Close Bond Deals.

It’s crunch time as the industry tries to stay ahead of potential tax reform changes.

Affordable housing developers and their financial partners are working hard to close private-activity bond (PAB) deals in the final weeks of the year.

The fourth quarter is typically a busy time for the low-income housing tax credit (LIHTC) industry, but there’s even more urgency this year. The tax bill passed by the House eliminates PABs, a critical tool in financing the production and rehabilitation of affordable housing. The Senate tax bill retains bonds, so it’s left up to members of both houses to reconcile their differences.

Concerned about the fate of PABs, developers and bond financiers are attempting to close those deals in 2017.

Roughly half of all low-income housing tax credit (LIHTC) developments utilize tax-exempt bonds and 4% credits, and losing the use of the bond program could mean roughly 60,000 fewer affordable homes are built or rehabilitated each year, estimate authorities.

Dominium, a leading affordable housing developer and owner, has approximately 13 deals that it’s trying to complete the financing on in some capacity.

“Some will close in normal course, but we’re doing everything we can that come the end of December we are in a position to capture as many deals as we can,” says Chris Barnes, vice president and senior project partner at the Minnesota-based firm.

In prior years, Dominium has typically had between one to six bond deals set to close at the end of the year.

In addition, the company has about another 11 projects that have bonds that remain to be drawn. “We’re trying to get those drawn ahead of schedule in case the worst-case scenario comes out. We’re working with our lenders, fiscal agents, and issuers to get that done,” Barnes says.

If the House tax plan passes, housing officials hope that Congress will adopt transition rules that would allow deals that have closed earlier to go ahead and complete their draw down in 2018 and 2019 on a tax-exempt basis so long as a draw down is consistent with the original documents and are not modified in a way that triggers a tax law reissuance. But, concerns that transition rules may not cover this issue have developers and their financial partners looking at drawing down bonds this year.

People have been a little hesitant to bring up transition rules because they don’t want to appear to be conceding defeat on tax-exempt bonds. No one is ready to give up on PABs. Affordable housing supporters have been urging members of Congress to preserve the bond program.

Working on deals

In the meantime, bank and other financial leaders are doing what they can on bond deals.
“An affordable housing transaction is far more complex than a typical real estate transaction,” says Richard Gerwitz, managing director and co-head of Citi Community Capital. “It takes time to structure and process. It’s hard to ‘push’ a transaction before its time. But to the extent that our clients have projects that were already in process and were planning to close sometime in the beginning of 2018, it hasn’t been unusual for them to ask if we could facilitate a closing this year. We’re doing everything we can to accommodate them.”

The situation also depends on how much bond cap states have available. “Some utilize all of its PAB allocation on current year transactions while others states have bond allocation available and are dispersing as much as they possibly can to projects that qualify,” Gerwitz says.

While it is still undetermined how many transactions Citi Community Capital will close in the final four weeks of the year, the number of deals may increase by as much as 50% over what was originally planned for the month, estimates Gerwitz.
Bank of America Merrill Lynch and Wells Fargo officials also are working on bond deals.

“We are pushing to close those deals that were originally scheduled to close in 2017 and that are appropriately structured in light of concerns raised by the House bill,” says Michael Lavine, head of Wells Fargo’s LIHTC program.

The bank has a slightly higher number than usual, according to Lavine. “The higher number is more due to the general delays the market suffered during 2017 in the aftermath of the election, rather than the more recent House bill," he says.

The latest efforts are broader than just closing on new deals by the end of the year, adds Iris Bashein, senior vice president, community development banking group, at Bank of America Merrill Lynch. Like Dominium's Barnes, she points to earlier bond deals that still have proceeds that need to be drawn.

"We're also trying to make sure that any deals that did not fully draw at closing will draw all of their bond proceeds by the end of the year," she says. "That's significant."

Anything that the bank has in the pipeline that was planning to close, officials are working to hit that closing date and make sure those deals don't slip into next year, Bashein says.

"There are a handful of deals that are fully baked, but, given where they are in the closing process, there's a chance they might not make it before year end," she says. "At the advice of counsel, we're looking at doing bond-only closings before the end of the year for those few deals and then wrapping up the real estate closings in the new year."

Bond participants will be closely watching how tax reform efforts proceed.

"If we see something happen in the near-term and the House and the Senate agree on a tax bill where PABs are retained, I expect that developers will be willing to wait until next year to secure an allocation of bonds; they'll continue with business as usual," Gerwitz says. "However, if we go into the end of the year without an agreement between the House and Senate, I think developers will continue to ask us to close their deals early."

Affordable Housing Finance

By Donna Kimura

October 5, 2017

[P3 Digest for December 8, 2017]

Michigan's Freeway Lighting Upgrade P3 Improves Efficiency and Safety

Editor's Note: The following article is one in a series of six profiles of winners…

[Read the Digest.]

NCPPP

December 8, 2017

[S&P Municipal Portfolio Review (September 2017): Tax-Secured Bonds Maintain Their Prevalence While Total Issuance Declines.]

S&P Global Ratings is providing its first comprehensive study of enhanced and unenhanced primary market municipal bonds and notes for September 2017.

Continue reading.

Dec. 3, 2017

Tax-Secured Bonds Maintain Their Prevalence In The Muni Market While Overall Issuance Declines: S&P Video

S&P Global Ratings published its first comprehensive study of enhanced and unenhanced muni bonds and notes across all public finance sectors. In this CreditMatters TV segment, analysts Shirley Zhang, Lawrence Witte and Joshua Saunders project the issuance volume rally late in 2017 and overall decline in 2018, due to pending tax reform and slowing of refunding, among other factors.

Watch Video

Dec. 4, 2017

S&P: Pension Obligation Bonds' Credit Impact On U.S. Local Government Issuers.

U.S. state and local governments can use pension obligation bonds (POBs) to address the unfunded portion of their pension liabilities. In certain cases, POBs can be an affordable tool to lower unfunded pension liabilities. But along with the issuance of POBs comes risk.

Continue Reading

Dec. 6, 2017

S&P Criteria FAQ: What Does The Focus On Credit Fundamentals Mean For Proposed U.S. Public Finance Tax-Secured Criteria?

S&P Global Ratings has recently released several requests for comment (RFCs) on proposed criteria changes in U.S. public finance. While each RFC covers a distinct type of credit pledge or security, all of them have in common an increased focus by S&P Global Ratings on fundamental credit quality rather than legal provisions and structural features.

Continue Reading

Dec. 4, 2017

The Muni Market Hasn't Rallied This Much Since the U.S. Was Downgraded.

- **Prices gain, despite flood of borrowing to beat Congress**
- **'I'm buying as many bonds as I can,' says Deutsche's Pollack**

In the municipal-bond market, investors are buying now while supplies last.

As municipalities rush to sell tens billions of dollars of securities before Congress enacts legislation that would dramatically cut the size of the tax-exempt bond market after this year, prices are rallying, sending the yields on benchmark ten-year debt down by the most since S&P downgraded the U.S. in August of 2011. On Wednesday, those yields dropped 0.09 percentage point to 1.95 percent, according to data compiled by Bloomberg.

That's defying the initial expectations of analysts and investors that a potentially record-setting borrowing wave would depress prices through the end of the year. But such short-term considerations have been overridden by the prospect that new sales of tax-exempt debt could fall by a third or more starting next year, which would made the securities more valuable to investors.

"There's a fear that there's going to be a scarcity of municipal bonds going forward," said Gary Pollack, a managing director who handles fixed-income research and trading for Deutsche Bank AG's private wealth division in New York, which holds about $6.5 billion of state and local debt. "I'm buying as many bonds as I can."

The tax-cut bills that were passed by the House and the Senate would strip the tax-exemption from bonds in so-called advance refundings, a technique that governments used to refinance tens of billions of dollars in debt last year alone. The House version would also prevent hospitals, airports and other private borrowers from raising money in the tax-exempt market. The two bills are now in the process of being reconciled.

The changes have led state and local governments to move swiftly to sell debt by the end of the year, putting the market on track to approach or eclipse the monthly record of $54.7 billion in 1985. By late November, borrowers had already scheduled $29.4 billion of sales over the next month, the most since 2005. That captured only a portion of the supply, since many sales are set with less than a 30-day notice.

So far, there's been plenty of demand. "It's a grab fest," said Adam Buchanan, senior vice president of municipal sales and trading at Ziegler Capital Markets Group in Chicago.

Bloomberg Markets

By William Selway and Brian Chappatta

December 6, 2017, 10:18 AM PST Updated on December 6, 2017, 11:37 AM PST

— With assistance by Martin Z Braun

Muni Market Goes on Hot Streak Even as All Signs Suggest Selloff.

As municipal bond issuers stampede to borrow before Congress enacts sweeping changes to the $3.8 trillion market, investors are stampeding right back at them.

Yields on 30-year municipal bonds fell for a fourth straight day to the lowest level of 2017. It's a shock to investors who have been bracing for a supply glut that has pushed the volume of planned issuance in the coming weeks to almost $28 billion.

"I'm trying to wrap my head around it," said Matt Dalton, chief executive officer of Rye Brook, New York-based Belle Haven Investments, which manages $6.5 billion of municipal bonds. "Stuff's running pretty hot right now."

Yields on top-rated 30-year municipal bonds fell on Tuesday by about seven basis points to 2.67 percent, the lowest since November 2016. Issuers that benefited from the demand include New York, Texas's Harris County and a newly created corporation in Chicago.

Dalton said one possible reason for the rally was that investors are anticipating a big drop off in issuance in the first quarter of 2018, given how states and local governments are pulling deals forward before year-end. Muni yields have declined in each December over the past three years.

The House tax-cut plan would end the tax break for interest on private activity bonds sold by nonprofits, hospitals and private colleges. The House and Senate bills would also end a debt refinancing tool called advance refundings that states and cities use to save money.

"I'm shocked at how well the market has absorbed this supply so far," said Nicholos Venditti who oversees $11.5 billion of munis at Thornburg Investment Management in Santa Fe, New Mexico.

Bloomberg Markets

By Martin Z Braun

December 5, 2017, 2:08 PM PST

Inside the Tax Reform-Fueled Muni Market Frenzy at MuniOS.com.

- **Sales in November hit $44.5 billion, up 45% year-on-year**
- **December 1985 is all-time record for issuance at $54.7 billion**

Rescheduled vacation time, all-nighters and plenty of coffee and pizza: these are the scenes from the front lines of municipalities' push to sell bonds before Congress overhauls the tax code.

MuniOS.com, operated by Ann Arbor, Michigan-based tech company ImageMaster, is the platform that thousands of issuers spanning the $3.8 trillion municipal market use to showcase their bond offering documents. Since the release of the House and Senate tax bills in November, MuniOS has processed preliminary and final official statements for the billions of bonds sold by issuers hoping to avoid being affected by tax bills going into effect Jan. 1.

The website was launched in 1999 and is used by issuers to distribute and print their bond offering documents. The service has a 72 percent market share among issuers. It's popular with other municipal market participants, too: MuniOS has over 28,000 active members and over 7,600 people have signed up to receive emailed filing notifications from MuniOS. Over 500 users were listed as active on the website on Tuesday morning.

Long and short-term municipal bond sales surged 45 percent year-over-year in November to $44.5 billion, the month that both chambers released their tax plans, according to Bloomberg data. The

House plan would end the tax break for interest on private activity bonds sold by nonprofits, hospitals and private colleges. The House and Senate bills would end a debt refinancing tool called advance refundings.

MuniOS has been helpful for municipal bond trader Chip Peebles during the rush to market. Once bond offering documents are up on the website, it means the deal is on its way to pricing soon rather than just being under consideration, said Peebles, who is a senior vice president for retail trading at Raymond James.

"It's very helpful," said Peebles, who is based in Memphis, Tennessee. "As a trader, you hear a lot of rumors about deals. But until you see the papers on it, you can't do much with the rumors."

Peebles, who has worked in municipals for over 30 years, said he's been a user of the site since it was created. Raymond James traders and underwriters use the site's customization features to receive emailed bond offering documents for the regions or sectors they trade in, he said.

The only time comparable to this year's surge in bond sales was in late 2010, when the Build America Bonds program was set to end its subsidies on taxable bonds, said Dan Rodriguez, a vice president at ImageMaster who has worked there for 27 years. While the Build America Bonds supply surge started in September until the end of 2010, this year's flurry of bond sales is being consolidated into a shorter time period, he said.

When MuniOS receives a bond document from an issuer, it vets the document with a 64-point checklist system that takes about two hours or less to complete, said Marianne Shiff, vice president of operations at ImageMaster. Then, staff members will give their feedback to the issuer, which could take anywhere from a few hours to a day to be completed, she said.

That means lots of long hours lately for the 30 people who work on MuniOS.com, which has people on staff from 7 a.m. to 11 p.m. EST. It also offers a 24/7 on-call service issuers can arrange ahead of time, Shiff said. Last weekend, before issuers were set to sell as much as $21 billion in bonds, there were eight different people on call, Shiff said.

"Everybody's all in and we take care of each other," Shiff said. "It'll be over in a few weeks."

A boon in municipal bond sales is good news for ImageMaster, which receives fees from processing the offering documents and printing them. The company's roadshow service — which features recordings of issuers' presentations to investors — had its biggest month ever in November, Rodriguez said.

"With the large saturation of deals in the market, we see that a lot of clients are trying to stand out by providing these online roadshow presentations," he said. The service has also gotten new clients during the past month, Rodriguez added.

Still, the official statement hustle and bustle has required some sacrifice. Production supervisor Jennifer Braun was going to take off for her birthday on Monday, but decided not to because it's one of the company's busier days. In the past few weeks, some employees have worked through the night until their coworkers came into the office the next morning.

Shiff said she's looking forward to recharging come Jan. 1, 2018, when the proposed tax changes would go into effect. MuniOS also plans to re-launch the site in early 2018 to be more mobile-friendly.

Bloomberg Markets

By Amanda Albright

December 6, 2017, 4:00 AM PST

Seeking Solutions for the 'Water Infrastructure Death Spiral'

It's a problem communities can face when populations and property values decline.

WASHINGTON — Cities with shrinking populations and aging water infrastructure can face tough choices when it comes to paying for waterworks upgrades and keeping service affordable.

This has some experts and lawmakers raising concerns. They caution that there are localities around the U.S. that could be at risk of problems similar to those that bedeviled Flint, Michigan, where residents were exposed to lead-contaminated drinking water.

"Communities that are struggling begin to make sacrifices, budgetary decisions, based on what they can afford and what their immediate needs are," Rep. Dan Kildee, a Michigan Democrat whose district encompasses Flint, said at an event on Capitol Hill on Wednesday.

Continue reading.

ROUTE FIFTY

BY BILL LUCIA

DECEMBER 7, 2017

U.S. Municipal Bond Market Shrinks to $3.803 trln in Q3-Fed.

Dec 7 (Reuters) – The U.S. municipal bond market shrank to $3.803 trillion in the third quarter of 2017 after growing to $3.827 in the previous quarter, according to a quarterly report from the Federal Reserve released on Thursday.

Households, or retail investors, held $1.562 trillion of debt sold by states, cities, schools and other muni issuers in the latest quarter, down from $1.612 trillion in the second quarter, the Fed report said.

U.S. banks' muni bond buying fell to $7.1 billion in the third quarter from $10.9 billion in the second quarter. Property and casualty insurance companies also acquired fewer munis in 2017's third quarter at $3.4 billion versus $5.8 billion in the second quarter. Life insurance companies picked up $5.4 billion of the bonds.

(Reporting By Karen Pierog Editing by Chizu Nomiyama)

GASB Proposes Guidance on Capitalization of Interest Cost and Implementation of Recent Pronouncements.

Norwalk, CT, December 8, 2017 — The Governmental Accounting Standards Board (GASB) has issued two Exposure Drafts proposing accounting and financial reporting guidance—a proposed Statement related to capitalization of interest cost and a proposed Implementation Guide that addresses multiple topics.

Capitalization of Interest Cost

The Exposure Draft, *Accounting for Interest Cost during the Period of Construction*, proposes guidance that would enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period. It also would simplify accounting for interest cost incurred during the period of construction.

For financial statements prepared using the economic resources measurement focus, interest cost incurred during the period of construction would be recognized as an expense in the period in which the cost is incurred. Such interest cost would not be capitalized as part of the historical cost of a capital asset.

For financial statements prepared using the current financial resources measurement focus, interest incurred during the period of construction would continue to be recognized as an expenditure on a basis consistent with governmental fund accounting principles.

Implementation Guidance

The proposed Implementation Guide, *Implementation Guidance Update—201Y*, contains questions and answers intended to clarify, explain, or elaborate on GASB Statements. It proposes guidance on a range of topics, including pensions, other postemployment benefits, the statistical section, regulatory reporting, and tax abatement disclosures. The proposed Implementation Guide also includes amendments to previously issued implementation guidance.

Both Exposure Drafts are available on the GASB website, www.gasb.org. Stakeholders are encouraged to review and provide comments on the Exposure Drafts.

Comments are due on the Exposure Draft, *Accounting for Interest Cost during the Period of Construction*, by March 5, 2018.

Comments are due on the Exposure Draft of Implementation Guide No. 201Y-X, *Implementation Guidance Update—201Y*, by February 16, 2018.

Muni Buyers Are Handed a Holiday Bounty With Governments Rushing to Market.

- **New offerings hold near 13-year high in usually slow month**
- **Issuance may break $54.7 billion monthly record seen Dec. 1985**

For municipal-bond buyers, December is providing the chance for a rare holiday shopping spree.

Spurred by legislation in Congress that would end the tax-exemption for a big share of the market starting next year, state and local governments are rushing to borrow, turning a typically sleepy month into a potential record-setter.

That's created some discounts, too: In anticipation of the deluge, prices have dropped, sending the Bloomberg Barclays Municipal Bond Index 0.54 percent lower in November, its worst monthly performance in a year.

"It is significantly busier," said David Mullen, senior vice president and director of public finance at Dougherty & Co., a Minneapolis based investment bank and financial advisor. "The feeling in the office is hectic."

The volume of sales scheduled over the next 30 days currently stands at $26.9 billion, holding near its highest in almost 13 years. That's already more than was sold in all of last December, and the final tally is likely to be considerably higher because many deals are planned with less than a month's notice.

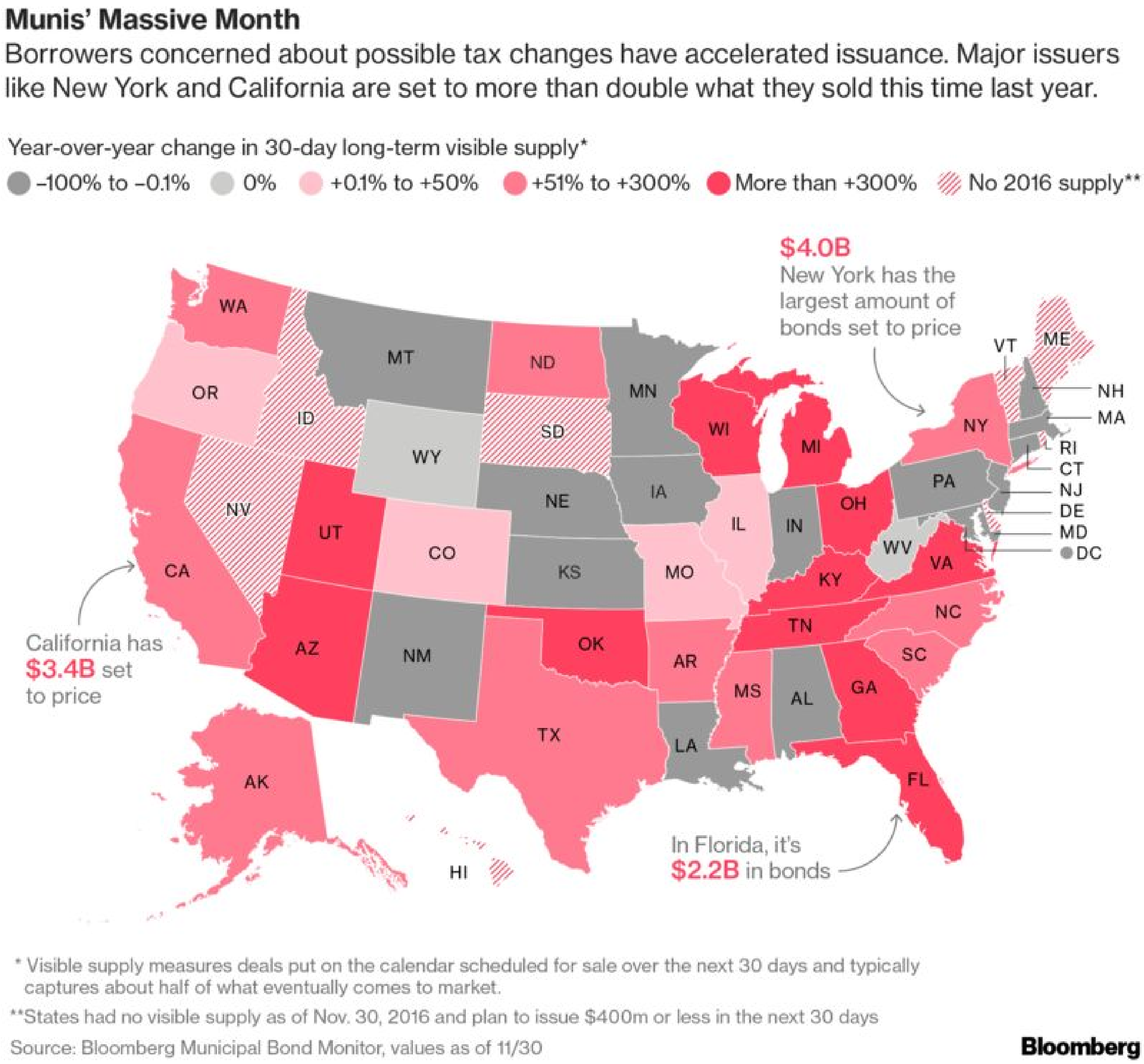
The tax bills in Congress — which propose scrapping subsidies for advance refundings and, in the House's version, private activity bonds as well — would reduce tax-exempt issuance significantly starting next year. Those two categories accounted for about 40 percent of total new supply over the past three years, according to Peter Block, managing director of credit strategy at Ramirez & Co.

Hence a rush that recalls the scramble to issue seen in December 1985, ahead of the last major overhaul of the U.S. tax code. Governments in New York are leading the charge with $4 billion of borrowing planned, followed by California, Texas and Florida.

Should December issuance top $54.7 billion, it would be the biggest month in the market's history. Mikhail Foux, head of municipal strategy at Barclays Plc, estimates that $40 billion to $50 billion will be sold, in line with other forecasts. That compares with about $32 billion in November.

The dramatic increase in supply has driven municipal prices down and yields up, with the Bloomberg Barclays municipal index loosing about 0.8 percent last month, the worst monthly showing in a year.

"I'm getting the impression that there is a lot of general market distortion that prices are significantly different than what they were two or three weeks ago," said Scott Stevenson, a managing director at D.A. Davidson, an underwriter.



The uncertainty is due partly to the discrepancies between the House and Senate tax bills, with the Senate proposing to leave the private activity bond market intact.

“One pivotal question, one key uncertainty to this whole equation is the degree to which what’s eventually passed. Is it the House version or is it the Senate version?” said Brett Wander, chief investment officer of fixed income at Charles Schwab.

For the moment, that’s sending underwriters into overdrive. And buyers are busy shopping.

Bloomberg Markets

By Danielle Moran

December 1, 2017, 6:00 AM PST

Every Basis Point Counts to Muni-Bond Issuers Rushing to Market.

- **Difference in rates between taxable, tax-exempt would add up**
- **A-rated 30-year G.O. bond issue would cost $12 million more**

What’s the difference between selling municipal bonds that are tax-exempt and taxable? While a few fractions of a percentage point might not seem like much, it can cost taxpayers millions of dollars.

For example, an A-rated municipality that issues $100 million in 30-year general-obligation bonds in the taxable rather than the tax-exempt market would see an additional cost of 0.40 percentage points, or $12 million over the next three decades, according to calculations based on Bloomberg’s indexes.

That’s why states and local governments are rushing to sell billions of dollars of bonds this month, in case Congress enacts legislation that would tax the income from a big chunk of the municipal securities that are sold after this year.

The U.S. House of Representatives’ bill would pull tax-exemption from refinancings known as advance refundings and from private activity bonds, which are used by colleges, hospitals and airports, among other borrowers. The Senate’s would leave private activity bonds intact, though that could change when the two chambers negotiate a compromise.

Borrowers aren’t waiting to see. Wheaton College, the Norton, Massachusetts-based liberal arts institution, plans to offer $56 million revenue bonds next week, some of which will be used for an advance refunding. If the deal was sold at taxable yields, the higher interest costs would be equivalent to about $200 of additional tuition per year from each of its students under a 30-year maturity, said Brian Douglas, executive vice president for finance and administration.

The college was planning to sell the bonds anyway, but once tax reform came under discussion, the university decided to move quickly, he said.

Wheaton, which has over 1,650 students, is rated A3 by Moody’s Investors Service. Taxable A-rated revenue bonds with a five-year maturity would cost about 90 basis points more than their tax-exempt counterparts, according to data compiled by Bloomberg.

Over 65 percent of students receive need-based aid at Wheaton. Annual tuition cost $50,520 for the 2017-18 year. “We try every way we can to lower the costs for our students,” Douglas said, “and this change would have the opposite effect, it would force us to increase costs for students.”

Other entities face a similar hike in borrowing costs. Dennis Hunt, executive vice president and manager of public finance at Stephens Inc., said municipalities that sell tax-exempt bonds with a top yield of 4 percent would pay 5.5 percent if bondholders had to pay tax on the income.

If the proposed limit on tax-exempt private activity bonds goes through, many issuers would likely curb their borrowing because of the the higher interest rates, he said. That would cut into spending on infrastructure projects, putting the tax bill at odds with President Donald Trump’s stated goal of pumping more money into public works.

“It would be a very significant difference,” he said.

Bloomberg Markets

By Amanda Albright

December 1, 2017, 8:50 AM PST

House Approves Legislation to Reauthorize Flood Insurance Program.

House Republicans voted to reauthorize flood insurance for five years with heavy reforms including new reporting requirement for FEMA

Although the House and the Senate remain at odds over how to advance legislation that would reauthorize the National Flood Insurance Program (NFIP), the House on Nov. 14 approved its measure by a vote of 237–189 along party lines.

The legislation, the 21st Century Flood Reform Act (H.R. 2874), combines a series of bills that, in addition to reauthorizing the NFIP, would bring about considerable reforms to the program. Some of the proposed reforms could raise premium rates for flood insurance policyholders and make insurance less affordable for homeowners. As lawmakers respond to the aftereffects of this year's severe storms, some expressed hesitation to attach controversial reforms to a must-pass reauthorization bill, which the White House had urged Congress to consider earlier this year.

The NFIP is currently operating under a temporary extension that will expire on Dec. 8 if Congress does not act. Facing a busy congressional calendar, the House may have to pass an additional short-term funding extension through the end of December until a longer-term package is approved.

H.R. 2874 includes the following provisions:

- Reauthorize the NFIP for five years, from its Dec. 8, 2017 expiration through Sept. 30, 2022
- Lower the annual cap on premium increases from 18 percent to 15 percent
- Create a new flood insurance affordability program that allows states to subsidize premiums for low-income policyholders
- Require property owners to disclose any known flood damage prior to selling or renting a property, and
- Direct the Federal Emergency Management Agency (FEMA) to provide a mitigation credit for homeowners who have made improvements to their property to reduce the impact of flood damage.

The bill would also enact new reporting requirements for FEMA, which would require the agency to disclose to policyholders the formula used to determine insurance rates and provide property owners with information on flood risk and previous claims. Important to note for counties, the bill would create a new voluntary Community-Based Flood Insurance Pilot Program, which would allow local governments to purchase flood insurance for a portion of properties within their jurisdiction or for all of them.

The bill also contains several provisions of concerns to policyholders, including:

- An increase in the threshold of premium increases from 5 percent to 6.5 percent, meaning whenever rates increase for policyholders, they would do so at no less than 6.5 percent; this represents an increase from what is currently authorized under federal law;
- The cap on annual premiums is set at $10,000, which could limit affordability of the program to homeowners, and decrease the overall risk pool; and
- The implementation of a $25-$250 surcharge for policyholders who elect to make monthly

installments on their annual premiums.

During a Nov. 13 hearing about the bill in the House Rules Committee, Rep. Garret Graves (R-La.) voiced concerns with the legislation, which he said did not adequately address the long-term solvency of the NFIP or the program's leftover debts from the costs incurred by superstorms such as Hurricanes Sandy and Katrina. Graves also argued that much of the NFIP's $24 billion in debt was a result of levee failures, and not due to a lack of coverage among property owners in New Orleans, who could face higher premiums that would go toward paying off the program's debts.

The measure must now be considered in the Senate, which remains divided on significant issues with the NFIP, such as the program's long-term solvency and premium increases for policyholders.

Although NACo applauds lawmakers' efforts to reauthorize the NFIP and implement reporting standards that are beneficial to homeowners, counties remain concerned with proposals that could make flood insurance less affordable, especially at a moment when communities across the country are still engaged in recovery efforts.

NATIONAL ASSOCIATION OF COUNTIES

By JACOB TERRELL Nov. 22, 2017

Fitch U.S. Water and Sewer Rating Criteria.

View the criteria.

30 Nov 2017

S&P Request for Comment: U.S. Municipal Retail Electric And Gas Utilities.

S&P Global Ratings is requesting comments on proposed changes to its methodology for assigning ratings and related credit products to U.S. retail electric, retail gas, steam, chilled water, and combined utility systems where electric and/or gas is the predominant service…

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Nov. 27, 2017

S&P Criteria FAQ: Proposed Criteria For U.S. Municipal Retail Electric And Gas Utilities.

On Nov. 27, 2017, S&P Global Ratings published a request for comment (RFC) on revised criteria for U.S. municipal retail electric, retail gas, steam, chilled water, and combined utility systems where electric or gas is the predominant service ("U.S. Municipal Retail Electric And Gas Utilities").

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The Week in Public Finance: Controversy at the Consumer Protection Agency, Education Funding Still Lags and Tax Reform's Blow to Puerto Rico.

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

GOVERNING.COM

BY LIZ FARMER | DECEMBER 1, 2017

Fate of Special Purpose Tax Districts Tied to Reform Bill.

Think local impact fees are high now? Eliminate private activity bond deductibility, and then see what happens

U.S. Senate lawmakers, back in Washington after Thanksgiving holidays, are working on the double to fast-track a major tax code overhaul through to a vote on the floor this week. The aim is to take a passed Senate bill to conference–a committee of both Senators and House members–for reconciliation of its bill with legislation voted on two weeks ago in the House.

As is widely reported, the current Senate version of tax reform may need revisions–both in its cost implications and in whom it's benefits impact–to successfully navigate push-back from Senators who could deter its passage. Word is, if the Senate passes an amended bill by just a vote or two, its compromises may be so stretched to the limit that it may simply hand the bill over to the House with a "take it or leave it" message.

Continue reading.

Builder Digital

by John McManus

November 28, 2017

P3 Digest for November 30, 2017

Dominique Lueckenhoff Brings a P3 Approach to Community-Based Stormwater Management

Editor's Note: The following article is one in a series of six profiles of winners of NCPPP's 2017 National Public-Private Partnership Awards, which recognize organizations and individuals who have gone above and beyond to advance the concept and implementation of P3s across the country. The winners will be honored during P3Connect in Miami Beach in January.

"Innovation is taking two things that already exist and putting them together in a new way." — Tom Freston

States and localities throughout the nation are struggling to find reliable, cost-effective ways to prevent stormwater runoff from reaching — and polluting — major waterways. Failure to address this major cause of water pollution is endangering health and safety, while increasing the liabilities of communities with permit compliance requirements under the Clean Water Act. However, local government efforts to develop solutions often have been hampered by limited public funding for construction or capacity to implement larger scale projects. This is particularly true for greener stormwater infrastructure projects.

Continue reading.

NCPPP

Neighborly Insights: Tax Outlook and Mueller Investigation Roil the Bond Markets, Taking Munis for a Ride.

Municipals had a rough week to start but ended on a more positive tone, following Treasuries to lower yields as the tax reform debate moves along. Although issuance could be as much as $50 billion for December, real money accounts (especially funds) appear to have been well positioned coming into this heavy period, and there is also going to be an especially heavy bond call/maturity period from December 1 through February 1 with proceeds that need to be reinvested somewhere.

Continue reading.

by George Friedlander

Posted 12/01/2017

Neighborly Insights

This post is adapted from the Court Street Group Weekly Perspective. Download the full report.

Commentary: How the Puerto Rico Dispute Threatens Bond Holder Rights.

The municipal bond market, for borrowers and investors alike, is fundamentally changing. Municipalities across the U.S. are struggling to provide essential services on top of skyrocketing pension and benefit obligations. In addition, although bankruptcy and default remain minimal, the Detroit bankruptcy case had a profound and sobering impact on the market, leading participants to reevaluate what a general obligation (GO), full faith and credit pledge actually means. Logically, there has been a market shift to bonds secured by a specific revenue stream – a securitized loan – as a means for issuers to enhance the attractiveness of their bonds and lower borrowing costs.

The outcome of a highly publicized court case currently being heard by Judge Laura Taylor Swain in U.S. Municipal Bankruptcy Court under Title III of PROMESA (No. 17-00257-LTS), COMMONWEALTH of PUERTO RICO vs. COFINA, is likely to set the course for where the municipal market goes from here.

COFINA bondholders are renouncing actions taken by the Commonwealth to impair or eliminate its debt. Clearly, this would be devastating for investors, including the Puerto Rican citizens who own approximately $2.8 billion of the bonds. Impairing this debt may also impede, if not eliminate, access to funding via securitized loans.

The background: The Puerto Rico Sales Tax Financing Corporation — in Spanish, Coporacion del Fondo de Interes Apremiante or COFINA — was created by PR Law No. 91, as amended, to establish an entity that was independent and separate from the Commonwealth in order to address one of the worst fiscal crises in Puerto Rico's history. In consideration for COFINA's help in this crisis, the legislature established and assigned to COFINA a priority lien on a newly imposed, island-wide sales and use tax (SUT). A summary of Puerto Rico Act No. 56., describes the bargain:

"A special fund is hereby created to be known as the Dedicated Sales Tax Fund. The Dedicated Sales Tax Fund and all of the funds deposited therein and all the future funds that must be deposited in the Dedicated Fund pursuant to this law are hereby transferred to, and shall be the property of COFINA. This transfer is made in exchange for COFINA's commitment to pay, all or part of the extraconstitutional debt outstanding as of June 30, 2006. The Dedicated Sales Tax Fund shall be funded each fiscal year from the first revenues of the SUT, deposited at the time of receipt and shall not be deposited in the Treasury of Puerto Rico, nor shall it constitute resources available to the Commonwealth of Puerto Rico, nor shall be available for use by the Secretary of the Treasury."

COFINA – revenue analysis: The Sales and Use Tax (SUT) pledged to COFINA is very strong, as reflected in all but one of the elements credit analysts consider when evaluating a bond.

- *Demographics and Economic Base* – **Poor.** The island has a declining population, low income levels, and high unemployment relative to the U.S. mainland.
- *Nature of the Dedicated Revenue* – **Superior.** The SUT applies to a very broad list of services and essential consumer goods, is very stable, and is enforced throughout the entire island.
- *Revenue Analysis and Fund Flows* – **Superior.** Fiscal year 2017 collections were a record high and double 2013 levels. A priority lien exists on collected taxes, going first to bondholders.
- *Debt Service Coverage* – **Superior.** The ratio of pledged revenue to annual debt service on the senior lien bonds was 11x in fiscal year 2017.

The problem: After following the law and the set-forth payment mechanism for many years, as well as countless legal opinions attesting to COFINA's property rights, multiple opinions rendered by the Commonwealth's own Department of Justice, year upon year of statements by Governors, Legislators, and Development Bank officials attesting to COFINA's rights the Commonwealth provided the following statement as part of its complaint filed with the bankruptcy court (Under Title III of PROMESA) on Sept. 8:

"This adversary proceeding is being commenced to resolve the Commonwealth-COFINA Dispute. As set forth, in this complaint, the SUT revenues, wherever located and whenever arising, are the exclusive property of the Commonwealth."

With 25 years of experience as a municipal bond analyst and portfolio manager, I have never witnessed such apparent disregard for property rights, existing statutes, and Constitutional law. Since July 2015, while remaining current on debt payments, the Commonwealth has increasingly made bondholders uneasy by their actions and inactions with regard to COFINA's rights and priorities. With this complaint, however, they essentially deny COFINA's existence altogether. Even in Title III bankruptcy, the Commonwealth's actions appear almost contemptuous of US Municipal Bankruptcy law as amended in 1988, which had the sole purpose of distinguishing between certain revenue bonds and general obligation (GO) debt. At least in this matter, it appears that promises, obligations, commitments, liens, contracts, and bargains carry little weight with the Commonwealth government.

The ramifications: Should the Commonwealth of Puerto Rico prevail, I foresee it setting a disastrous precedent.

- Access to the securitized loan market could be restricted for all borrowing municipalities. This would be most damaging to state and local borrowers with weak GO ratings. Over time, this may affect higher-rated issuers as well.
- Local governments and municipalities could be forced to choose between default and austerity.
- The ratings of some existing revenue bonds may see multiple downgrades.
- Future Puerto Rican bonds will necessitate a specific revenue pledge separate from their general fund. Oddly, this is the COFINA bond structure the Commonwealth is arguing against.
- Rating agencies will have the challenge of squaring up ratings among different securitized bonds.
- An alarming moral hazard would be created if interest rates (borrowing risk) are determined based on the political and judicial landscape – eschewing property rights and collateral.
- Bankruptcy will become a more popular option for politicians as an "easy" short-term solution to more difficult long-term problems.
- There could be a significant impact on the U.S. municipal market if the control board and the Commonwealth push through a Detroit-like bankruptcy result favoring pensioners over secured borrowers and other creditors with constitutional priority.
- If a borrower's ability to repay is in doubt, and complying with the law is optional, that borrower could be forced to pay higher interest rates, which could be a budget-busting proposition for financially fragile municipalities.
- Higher government borrowing costs may crowd-out the ability to provide and maintain essential services. This could lead to higher taxes or a reduction of services, resulting in a U.S. taxpayer bailout nonetheless.

The numbers: Consider the Virgin Islands Electric and Water Authority. In July 2017, it was shunned by "once burned, twice shy" municipal investors leery of a Puerto Rico-like restructuring, leaving officials no choice but to issue a three-year note paying 10.85% interest. Contrast this with Philadelphia Gas Works Authority, which issued three-year notes yielding 1.2%. That is an interest penalty spread of 9.65%. Applying this to half of Puerto Rico's estimated outstanding debt of $60 billion equates to an annual financial impact of $3 billion.

The bottom line: I cannot begin to imagine the current struggles for the people of Puerto Rico. Without electricity, adequate shelter, and dependable water supplies, I am at a loss to relate to the challenges people on the island face today, and for the foreseeable future. Yet, I firmly believe that if debt relief is the action taken by the Commonwealth against COFINA, it will only hurt, not help, the territory as it emerges from this crisis. The ability to raise funds to deliver needed services is one of the most broadly essential functions a government can provide, and the cost of those funds affects all citizens.

All things considered, I'm an understanding holder of Puerto Rico general obligation debt, but I'm an angry COFINA bondholder.

Policymakers and the public must recognize that bonds are not all structured the same. Each bond has very separate and unique security features which need to be considered and respected, not just in the case of COFINA, but for the overall health of the municipal bond market. For if all bonds are treated the same, and politics trump property rights and the sound application of bond analysis, then the unintended consequences will be costly and far-reaching.

In closing, as a Chartered Financial Analyst and Certified Financial Planner®, I pride myself on taking a long-term view, doing extensive research, and adhering to a moderately conservative risk profile. My clients are accepting of lower returns in lieu of lower overall portfolio volatility — and like me, they are pleased to provide capital to state and local governments in need of infrastructure development. They are not vultures or unscrupulous speculators, and I take offense to the generalization by public officials and others who insist they are – and the last thing any of us expects is to be “wiped out.” Risk is certainly a part of this business, but my hope is that we will all look to the future and craft solutions that protect not only investors and borrowers, but also our fellow citizens of Puerto Rico who desperately require our help.

The Bond Buyer

by Glenn E. Ryhanych

Glenn Ryhanych CFA, CFP is an investment advisor representative of Spire Wealth Management, LLC, an SEC Registered Investment Advisor, and is president and founder of BlueList Partners, LLC, a municipal bond management firm in Northern Virginia.

November 29 2017

The views expressed in this article are the author’s own and do not in any way reflect the opinions of Spire Wealth Management. Mr. Ryhanych personally owns General Obligation, Highway & Transportation, and COFINA bonds issued by the Commonwealth of Puerto Rico.

What Do Muni Bonds Have To Do With Medicare? Here's Why You Should Care.

It’s that time of year again. No, I don’t mean the holidays. It’s that window in time when those who just turned 65 can sign up for Medicare.

You’re probably asking why a bond manager is writing about Medicare and what this has to do with anything. Simple. The law requires some people to pay higher Medicare premiums than others. Simply stated, this is the government’s way of saying that Medicare is means tested. Those who earn more, pay more. Tax-free income from municipal bonds is included in your modified adjusted gross income.

Here’s the rub. You may own a large municipal bond portfolio of all high coupon munis: maybe 5.50%, 5.00%, perhaps some 4.00% coupons. If you purchased bonds over the last four years with maturities 12 years or less, you paid high premium prices for each. Your actual yield based on cost is most likely one-half that of your coupon. However, your brokerage firm reports the gross coupon income on your Form 1099, which is also reported to the IRS, and then reported to the Social Security Administration for use in means testing your Medicare premiums. By definition this overstates your income, thus possibly placing you in a higher Medicare means testing category than is appropriate.

The bummer here is that if your muni portfolio is large enough and populated with high coupon bonds, the gross income grotesquely overstates what you are actually earning. You should care because it may increase your Medicare premiums. This is due to the difference between coupon cash flow versus real yield based on cost.

This coupon tragedy is much more prevalent in Muniland as opposed to corporate bonds. That’s because when a state, city, county or municipality comes to market with a new issue there usually is a reverse inquiry. That is, several municipal bond fund managers may be queried as to what structure they may be interested in having. All high coupons? Current coupons? Zero coupons? From what I understand of the process the underwriters take that information under advisement then decide with the issuers the best structure.

Take a look at Illinois—the most dysfunctional state government. To help pay down their $16 billion in unpaid bills over the past two years the state issued $4.5 billion bonds. The 5.00% municipal General Obligation bonds due November 1, 2022 was one maturity size. This portion of the 2022 maturity size represented $500 million of the $4.5 billion. The dollar price at the new issue was 108.465, or $1084.65 per bond yielding 3.15% to maturity.

This means at maturity you'll hopefully get back $1,000 face value for every bond. Do the math. The state immediately took in a premium of $84.65 per bond equaling $42,325,000 more than it will pay at maturity while paying a 5% coupon rather than the 3.15% yield to investors based on the bond's cost.

Forbes

by Marilyn Cohen

NOV 28, 2017

Bloomberg Brief Weekly Video - 11/30

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

Watch video.

Bloomberg

November 30th, 2017, 5:27 PM PST

Moody's Warns Cities to Address Climate Risks or Face Downgrades.

- **Communities in Texas, Florida, other coastal states at risk**
- **Credit rating agency says it's adding climate to credit risks**

Coastal communities from Maine to California have been put on notice from one of the top credit rating agencies: Start preparing for climate change or risk losing access to cheap credit.

In a report to its clients Tuesday, Moody's Investors Service Inc. explained how it incorporates climate change into its credit ratings for state and local bonds. If cities and states don't deal with risks from surging seas or intense storms, they are at greater risk of default.

"What we want people to realize is: If you're exposed, we know that. We're going to ask questions about what you're doing to mitigate that exposure," Lenny Jones, a managing director at Moody's, said in a phone interview. "That's taken into your credit ratings."

In its report, Moody's lists six indicators it uses "to assess the exposure and overall susceptibility of U.S. states to the physical effects of climate change." They include the share of economic activity that comes from coastal areas, hurricane and extreme-weather damage as a share of the economy, and the share of homes in a flood plain.

Based on those overall risks, Texas, Florida, Georgia and Mississippi are among the states most at risk from climate change. Moody's didn't identify which cities or municipalities were most exposed.

Bond rating agencies such as Moody's are important both for bond issuers and buyers, as they assign ratings that are used to judge the risk of default. The greater the risk, the higher the interest rate municipalities pay.

Bloomberg News reported in May that towns and counties were able to secure AAA ratings despite their risks of flooding and other destruction from storms, which are likely to be more frequent and intense because of climate change. If repeated storms and floods are likely to send property values — and tax revenue — sinking while spending on sea walls, storm drains or flood-resistant buildings goes up, investors say bond buyers should be warned.

Jones said Tuesday that the company had been pressured by investors to be more transparent about how it incorporates climate change into the ratings process. Some praised the move, while also urging it to go further.

Think Harder

"This kind of publication shoots for municipalities to think harder about disclosure," Adam Stern, a senior vice president at Breckinridge Capital Advisors in Boston, said in an interview. "The action would start to happen when and if you start seeing downgrades."

Jones, the Moody's managing director, said he couldn't recall any examples of the company downgrading a city or state because it failed to address climate risk.

Eric Glass, a fixed-income portfolio manager at Alliance Bernstein, said real transparency required having a separate category or score for climate risk, rather than mixing it in with other factors like economic diversity and fiscal strength.

Still, the new analysis is "certainly a step in the right direction," Glass said by email.

Others worried that Moody's is being too optimistic about cities' desire to adapt to the risks associated with climate change.

Shalini Vajjhala, a former Obama administration official who consults with cities on preparing for climate change, says that won't happen on a large scale until cities start facing consequences for failing to act — in this case, a ratings downgrade.

"Investors and governments alike are looking for clear market signals to pursue, and perhaps even more importantly, to defend investments in major adaptation and resilience projects to their constituents and taxpayers," Vajjhala, who now runs Re:Focus Partners, said in an email. "Outside of the rating agencies, it is not obvious who else could send a meaningful market-wide signal."

Rob Moore, a senior policy analyst at the Natural Resources Defense Council, said increased attention from rating agencies could push cities to reconsider where they build.

"If I was a city official, I'd be asking a whole lot of questions about what vulnerabilities their community has, and how each new proposed development adds to that vulnerability," Moore said in an email. "Because at some point, your creditors certainly will."

Bloomberg

By Christopher Flavelle

November 29, 2017, 1:00 AM PST

— With assistance by Tiffany Kary

California's Post-Redevelopment Tools are Getting a Test Drive.

LOS ANGELES — California cities are beginning to figure out how to use economic tools created to fill a gap left when redevelopment agencies were dissolved in 2012.

La Verne city leaders have spent the past 18 months coming up with a plan to redevelop 100 acres into a mixed-use development involving housing, infrastructure and a parking structure for a train station on the Foothill Gold Line, a light rail extension into the San Gabriel Valley, said Larry Kosmont, founder of Kosmont Cos., a consultant on the project.

That plan uses the Enhanced Infrastructure Financing District legislation that was adopted in 2014, and further refined in 2015.

La Verne, a city of about 30,000 about 30 miles east of downtown Los Angeles, is among the first cities to create such an improvement district.

It took La Verne 18 months to come up with an infrastructure financing plan, Kosmont said. The city went to Los Angeles County with the idea of improving the area around the proposed transit station. The county owns the nearby Los Angeles County Fairgrounds and Brackett Field Airport. The county, which doesn't have an EIFD process, hasn't decided whether to join, Kosmont said, but participants can decide to contribute their money at a later date, he said.

The city made a decision to move ahead with its own share and activated the EIFD as of Oct. 30. Making the decision to do it now enables the city to set a baseline for tax increment for the tax rolls in 2018.

"The county is still reviewing," Kosmont said. "I hope they will come in next year."

The new light rail line is key to the plan. The Los Angeles County Metropolitan Transportation Authority has a groundbreaking ceremony planned Dec. 2 for the $1.5 billion Foothill extension. Metro issued Nov. 8 the request for qualifications for the 12.3-mile project that will add six new light rail stations in Glendora, San Dimas, La Verne, Pomona, Claremont and Montclair.

The debate in Congress over the future of private activity bonds could make things harder for the city; the GOP tax bill in the House of Representatives would eliminate them, while a Senate Republican plan keeps them.

The elimination of PABs won't stop the project, but it takes away another avenue to encourage public-private partnerships in the state, Kosmont said.

The infrastructure La Verne is building would be funded with public money generated by the tax increment the district generates.

Any potential EIFD bonds wouldn't be affected, but Kosmont said the elimination of PABs could make it hard to do a public-private project on the parking structure next to the transit station, because it would then have to be funded with taxable bonds or as a stand-alone parking bond. The parking structure for the district isn't likely to be constructed for a couple of years, because rail line construction has to be completed first.

Gov. Jerry Brown signed legislation eliminating some 400-plus redevelopment agencies in 2011. Prior to that, cities and counties could use tax increment financing – the increase in tax revenues generated by new development – to repay bonds issued to finance development and infrastructure in project areas deemed "blighted." The RDAs were also required to set aside 20% for affordable housing.

Two laws passed in 2015 sought to restore some of the economic tools used by the former RDAs. The laws allow cities, counties and special districts to form EIFDs under specific circumstances. Once the districts are formed, local government can use tax increment to finance infrastructure improvements.

The initial EIFD statute, Senate Bill 628 was passed in 2014. Assembly Bill 313 approved in 2015 added refinements.

EIFDs are separate government entities, formed through a joint powers authority consisting of cooperating cities, counties, and special districts. They can finance traditional public works, such as transportation, transit, parks and libraries, water and sewer facilities, solid waste disposal, and flood control and drainage.

A primary difference between EIFDs and the former redevelopment agencies is the new districts can't just capture all the tax increment created with new development. The district's authority can designate its own tax increment, but it then has to ask other municipalities in the district if they would like to contribute their increment to the project.

That authority has to create an infrastructure financing plan that will attract private investment and reduce the carbon footprint, Kosmont said.

The authority establishes a boundary and identifies infrastructure improvements that could occur over the next 45 years. The La Verne project involves the creation of three new districts on 110 acres in the city's downtown area, two adjacent to the rail station, and one bracket near the airport.

La Verne's financing plan has a 10-year outlook horizon that determines how much tax increment will be generated from new development, Kosmont said.

Improvements planned around the Gold Line station include sustainable water and utility projects and a parking garage. The city rezoned a number of properties around the transit station to build affordable housing and other amenities by working with private developers, Kosmont said.

Voter approval is not required to form an EIFD, but there is a 55% requirement to authorize bonds. Where an IFD makes the tax increment available for up to 30 years, the EIFD extends that timeline to 45 years.

"I am calling EIFDs sustainability and housing districts, because they are used for sustainable infrastructure," Kosmont said.

Another difference between redevelopment agencies and EIFDs is that a blight study is not required, but an infrastructure plan is, Kosmont said. The former redevelopment districts had to be created in blighted areas as they were designed to bring economic development to areas unable to attract new projects – and also to provide funding for and encourage affordable housing development.

When Brown pushed to eliminate redevelopment agencies, the governor's argument was that they were taking away money needed for school districts.

"The school district tax increment is not eligible to be part of EIFDs, as they were with redevelopment agencies," Kosmont said.

"That wipes out 50 cents on the dollar," he said. "It's why RDAs were so powerful. They took everyone's increment and used it for redevelopment. The RDAs came into the sandbox and took everyone's toys. The EIFDs come into the sandbox with their toys, and then ask if they can share everyone else's toys."

The districts can include brownfield restoration and other environmental mitigation; affordable housing development, and transit-oriented development.

Even as cities are beginning to figure out how to use EIFDs, two candidates for governor – California Treasurer John Chiang and former Los Angeles Mayor Antonio Villaraigosa are talking about bringing back redevelopment agencies if they are elected.

"I believe that more tools to facilitate development and redevelopment are better than less, particularly in Los Angeles as the region is preparing for the Olympics, addressing the evolution of mobility and catching up with years of deferred infrastructure projects," said Timothy Reimers, a principal with Polsinelli, a law firm.

The Bond Buyer

By Keeley Webster

Published November 16 2017, 2:00pm ES

How Cash-Strapped Chicago Snagged a Triple-A Rating for Its New Bonds.

Chicago is running a multimillion-dollar deficit and faces a pension-funding crisis that dwarfs many others around the country.

Yet the nation's third-largest city is on the verge of selling as much as $3 billion in bonds at a triple-A rating, the latest twist in the tale of cash-strapped U.S. municipalities adopting Wall Street financial engineering in their struggle to raise money in the market.

Echoing methods adopted by Puerto Rico and New York, Chicago has created a new company to sell debt, offering a tempting pledge to investors: a dedicated first claim to the city's sales-tax revenue.

In theory, that should make the debt as secure as U.S. Treasury bonds. But there is a catch: analysts and investors say in the scenario of a bankruptcy, it is difficult to predict whether owners of the new bonds would get paid back ahead of other creditors, pensioners or even police and emergency services workers.

The deal tests whether years of near-zero interest rates will send yield-starved investors into complex bond structures. And Chicago — with a school system that has teetered near bankruptcy and greater expenses than its revenues — could still face a funding gap down the line even if it manages to lower its borrowing costs, analysts say.

For the $575 million in bonds being priced this week, Jefferies LLC is the underwriter, while Goldman Sachs Group Inc. will lead the next batch, according to city presentations. Carole Brown, chief financial officer of Chicago and a former banker at Barclays PLC, told investors that she devised the plan to create the corporate entity to issue the bonds, according to a person who attended an investor luncheon for the sale.

Through the sale, Chicago is tapping a tool New York's leaders developed in the 1970s as the city faced the specter of a bankruptcy. Back then, Felix Rohatyn, a famed mergers and acquisition banker at Lazard, led an entity called the Municipal Assistance Corp., which allowed New York to borrow money even after major banks had choked off financing.

Puerto Rico sold more than $15 billion in sales tax bonds over the past decade. Rating firms considered the debt to be the island's safest offering, and it was snapped up by investors. Now those bondholders are fighting in court against creditors owning general-obligation bonds, who say their claim on the island's full faith and credit should include sales taxes also. Known by the acronym Cofina, those bonds recently traded at pennies on the dollar.

"Sometimes greed overtakes fear" in the market, said Chris Ryon, a portfolio manager at Thornburg Investment Management, which oversees more than $10 billion in municipal bonds. "It's a function of investors' desire for income."

Earlier this year, Chicago issued more than $1 billion in bonds, with part of the deal yielding 6%, far higher than most tax-exempt municipal credits. The coming deals would allow Chicago to refinance some of its over $9 billion in debt with lower interest costs, city officials have said.

The new debt, the first portion of which has maturities up to 26 years, could save the city more than $90 million in borrowing costs next year, according to the city. Chicago's leaders emphasize in bond filings that the new company, dubbed the Sales Tax Securitization Corp., is separate from the city.

Illinois currently doesn't allow its municipalities to file for bankruptcy, though lawmakers introduced legislation in recent years that cleared the way for Chicago or its school system to file.

Chicago declined to comment on the debt deal. Robert Christmas, a partner at law firm Nixon Peabody, which is advising the city on the sale, said investors shouldn't compare Puerto Rico's sales-tax bonds with Chicago's offering, in part because the city has stronger protections for investors than the island territory had.

Chicago's deal also sheds light on how widely diverging views can emerge from credit-ratings firms in the municipal bond market. Moody's Investors Service has graded the city's debt as junk, but S&P Global Ratings, Fitch Ratings and Kroll Bond Rating Agency have given Chicago investment-grade ratings.

For this latest issuance, Fitch and Kroll gave Chicago's corporate entity an additional boost: a AAA rating, the highest possible grade and equivalent to U.S. Treasurys.

S&P scored it two grades lower, although the firm still rates it five notches higher than other Chicago bonds. S&P also said in November it could change how it evaluates debt like Chicago's latest issuance, meaning investors could end up with bonds that are later downgraded by the firm.

In 2015, two years after it defaulted on its debt, Detroit snagged an investment-grade rating from S&P on new bonds by promising investors they would have first claim on income-tax revenues, although it didn't create a new corporation like Chicago.

Thornburg's Mr. Ryon said Chicago's new entity doesn't deserve separate credit ratings from the city's other debt. "It's a bit of smoke and mirrors," he said.

Moody's, which lowered the city's general-obligation bonds to junk in 2015, doesn't have a rating for the city's new debt. Chicago asked Moody's to withdraw the junk ratings on the general-obligation bonds, the firm said.

Bond ratings are also important because they can dictate money flows. Fund managers are often restricted to buying bonds with certain grades.

Other cities and states will be watching Chicago's bond sales. Illinois passed a special statute allowing the city to issue the bonds, and now other municipalities in the state can do the same.

States including California, Nebraska and Rhode Island have passed laws in recent years aimed at giving bondholders first claims on some taxes even if the issuer is in financial distress. Illinois and Michigan have also proposed similar laws.

Investors say municipalities with weaker financials will continue to try to woo bondholders with proposed safeguards, especially with the market rattled by Puerto Rico's restructuring.

"The idea is to provide a little more reassurance to potential creditors that they've got first crack at the money," said Glenn Weinstein, a Chicago attorney at Pugh, Jones & Johnson P.C., who has advised the city in the past.

At the same time, Mr. Weinstein said, "if you don't have financial difficulties and your credit is good, you don't need this."

Dow Jones Newswires

By Gunjan Banerji

Published December 03, 2017

Write to Gunjan Banerji at Gunjan.Banerji@wsj.com

KBRA Friday Read: 2017 Project Finance Update New Market Developments, Sector Overview, and Looking Forward to 2018.

In case you missed it, KBRA published an article discussing some recent project finance market trends, credit performance of certain sectors and its expectations for 2018.

The Project Finance Group has seen a significant increase in requests for Project Finance ratings in 2017. So far, it has provided ratings on 25 projects. It believes the significant increase in number of transactions and rated debt amounts can be attributed to a shift in financing strategies from the bank market to the capital markets –both public and private—due to the forced deleveraging of banks following the financial crisis, the longer tenors the bond market offers relative to the bank market, the increased amount of private capital that has needed to be deployed, and general yield-hunting behavior exhibited by investors given the current low interest rate environment.

To access the full report, please click on the link below:

New Market Developments, Sector Overview, and Looking Forward to 2018

If you have any difficulties accessing the report, please contact info@kbra.com or visit www.kbra.com

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Have They Got a Bond for You.

Connecticut and Chicago borrow a debt trick from Puerto Rico.

State and local governments pledge their full faith and credit to repay general obligation bonds, but politicians in Chicago and Connecticut realize their word is depreciating in value. Thus they're pitching a debt arbitrage to reduce their borrowing costs.

As part of Illinois's slow-rolling bailout of Chicago, Democrats in Springfield this summer allowed the city to issue bonds securitized with $700 million or so in annual sales tax revenue. Creditors would have a legal lien on the revenues. Chicago plans to start floating the sales-tax bonds next month to refinance existing debt.

The bonds will be cheaper to finance than Chicago's junk-rated GO bonds, which carry a 3.5% premium over top-rated municipal securities. Fitch has rated Chicago's sales tax bonds AAA, which is an insult to every triple-A issuer including the U.S. Treasury. (Fitch still rates Treasurys triple-A, unlike Standard & Poor's.) While the city noted in a recent presentation that "ratings agencies rate bonds issued by special-purpose corporations highly because they are more legally secure than a normal bond," that hasn't historically been the case.

Securitized bonds issued by special public corporations were once considered less safe than GO bonds because their revenue bases are narrower and can shrink over time. Consider the 2011 bankruptcy of Jefferson County, Alabama, which resulted from political corruption at its over-leveraged sewer system.

Detroit's Chapter 9 bankruptcy in 2013 set a precedent by subverting GO bondholders to pay public workers and retirees. Prior to Detroit, creditors considered GO bonds sacrosanct and figured courts would compel local governments to raise taxes or cut pensions to repay them. That assumption proved incorrect. So creditors are now demanding higher yields for GO bonds issued by fiscally irresponsible governments.

Hence, Connecticut lawmakers recently authorized bonds backed by state income taxes as a substitute for GOs. The budget noted that "the new type of borrowing authorized in the bill may be viewed more favorably in bond markets because it is linked directly to a large and relatively stable revenue source." Hmmm.

Income-tax revenues in Connecticut have repeatedly fallen short of estimates due to tepid economic growth. Last year they were off by $530 million. Perhaps Democrats consider this a rounding error on a $3.5 billion deficit. Chicago has reassured investors that the new "corporation would be considered bankruptcy-remote" (our emphasis). However, "in the unlikely event of a municipal bankruptcy, bondholders would still be paid." Not so fast.

Puerto Rico likewise established a special public corporation in 2006 to issue sales-tax "Cofina" bonds, which were billed as more secure than debt paid from the commonwealth's operating fund. And for a time that appeared true as politicians raised the sales tax (which was later converted into a VAT) to repay creditors.

But last year Puerto Rico's governor issued a debt moratorium, which led Congress to impose a fiscal control board and create a quasi-Chapter 9 bankruptcy process. Cofina and GO bondholders are now vying for the same, small pool of money, and both will be lucky to get half of what Detroit bondholders recovered.

Illinois could authorize Chicago to declare bankruptcy in the future, and while states can't declare bankruptcy, Connecticut could try to renegotiate the terms of its debt. In the event of a default, GO bonds in both places would be less secure because of competing creditor claims.

Investors thirsty for yield may take Chicago and Connecticut up on their proposition, but they shouldn't complain later if these bets turn out to be bad political risks. Caveat creditor.

The Wall Street Journal

By The Editorial Board

Nov. 20, 2017 7:12 p.m. ET

[Fitch Focuses on Rental Car Facilities in Revised Airport Criteria.]

Fitch Ratings-New York-27 November 2017: Fitch Ratings is enhancing its rating criteria for airports by adding key risk factors associated with airport stand-alone car financed projects, as per the rating agency's new criteria report.

Link to Fitch Ratings' Report: [Airports Rating Criteria]

Consolidated car rental projects, or CONRACs, are typically financed and secured by the levy of a surcharge on car rental contracts called Customer Facility Charges (CFCs).

"More airports are finding the need to do standalone financing in order to develop efficient car rental facilities," said Senior Director Seth Lehman. "CONRACs are helping to consolidate and make airport operations more seamless in the grander plan of streamlining airport services overall."

A burgeoning subset of the airport finance market, Fitch currently rates eight CONRACs including the first projects in Hawaii and San Antonio, Texas.

Fitch's key financial performance metrics for CONRACs will be based on volatility of cash flow derived from the combined assessments for both Revenue Risk – Volume and Revenue Risk – Price. Volume and price revenue risk remain the key factors Fitch will use in its analysis of airports going forward, along with criteria mainstays like infrastructure development/renewal, debt structure and the financial profile of an airport.

The full criteria report is available at www.fitchratings.com.

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Additional information is available on www.fitchratings.com

Fitch: FACT Shows Large Hubs Again Driving Traffic for U.S. Airports.

Fitch Ratings-New York-27 November 2017: Annual passenger traffic at U.S. airports grew at an even greater rate in 2016 while airport debt remained relatively flat, according to Fitch Ratings in its latest interactive peer study for standalone U.S. airport credits.

Median enplanements grew again yoy, rising by over 5% to 4.71 million for fiscal 2016 compared to 4.16 million in fiscal 2015. Large hubs and international gateways again drove most of the growth yoy. “The vast majority of Fitch-rated U.S. airports saw higher passenger traffic last fiscal year,” said Senior Director Seth Lehman. “Conversely, only four airports saw declines in passenger traffic in fiscal 2016.”

Strongest performers among the large hub airports include Orlando, FL; Broward County (Ft Lauderdale), FL; Seattle, WA; and Los Angeles, CA. Weakest performers included several airports such as Dayton, OH and Buffalo, NY.

The Fitch Analytical Comparative Tool (FACT) contains key financial information for Fitch-rated standalone airport issuers in the U.S.; a graphical plotting function for five-year annual and median performance; and a radar chart that indicates key risk levels. FACT also features a peer analysis tool, which allows users to review and compare summary credit profiles for selected individual issuers. The median charting tool allows users to generate a graphic representation of how specific metrics for individual airports compare to sector medians.

“Fitch Analytical Comparative Tool – U.S. Airports” is available at www.fitchratings.com. Fitch has also updated its interactive map detailing the financial profiles of its rated U.S. airports.

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[Bloomberg Brief Weekly Video - 11/24]

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

[Watch video.]

Bloomberg

November 22nd, 2017, 1:04 PM PST

[Can Other States Tap Tennessee's Secret Sauce for Government Efficiency?]

Once seen as a laggard in public administration, the state is now a leader.

Derek Young is no stranger to the C-suite. As he waits for a client in his 10th-floor corner office in downtown Nashville, he talks about his passion for culture change. One of the services he offers companies is as a motivational speaker and executive coach who charges "anywhere from one to six thousand dollars" a pop.

This morning, Young is meeting with Marcus Dodson, who manages IT operations for a large financial institution. When he arrives, Dodson updates Young on the project he is currently working on. He's been trying to get everyone in his 250-person organization up to speed on Microsoft Excel. But the project isn't going well. Dodson wasn't as prepared as he had wanted to be, and as a result, the first round of reviews from participants let him know that. But then, Dodson worked to improve his presentation, and his subsequent reviews were dramatically better.

Having a coach help an executive work through challenges is common in corporate America. But Dodson doesn't work in the private sector. He works for the state. He's responsible for infrastructure and security at the Tennessee Department of Treasury. He's receiving coaching through an innovative leadership development program known as LEAD Tennessee.

[Continue reading.]

GOVERNING.COM

BY JOHN BUNTIN | NOVEMBER 2017

Why Does Some Available Capacity for New CREBs Go Unused?

WASHINGTON – The Internal Revenue Service is accepting applications from public power providers through June 19, 2018 for $379.5 million of unused volume cap for New Clean Renewable Energy Bonds.

Congress authorized $2.4 billion of New CREBS during the Obama administration and divided the amount into $800 million each for issuers in three categories — public power authorities, electric cooperatives and state and local governments.

New CREBs are taxable and issued as either a refundable tax credit to the bondholder or in a direct-pay mode to the issuer with a direct subsidy from the federal government that reduces the interest costs. The direct-pay subsidy equals 70% of interest costs minus or 70% of a credit rate determined by Treasury, whichever is less. Both are subject to sequestration, which is a 6.6% reduction in the current 2018 fiscal year.

Cooperative electric companies had $179.36 million in unused allocations as of July and governmental bodies had $150.3 million, as well as public power providers that had the $379.5 million, according to the IRS.

Those allocations are being made on a first-come, first served basis.

White House emphasis on renewable energy sources such as solar, wind and hydro-electric has fallen with the change in administrations, but the New CREBs program is continuing to allocate unused bond authority.

Some New CREBs bond authority has not be used, in part, because of the peculiar idiosyncrasies of the authorizing law, according to those familiar with them.

Electric cooperatives and state and local governments have been limited to allocations of no more than $40 million, which limits the size of the projects unless they are packaged with other financing.

Public power companies have only 180 days to issue New CREBs after the date they receive a notification of their award from the IRS.

“Energy financings take more time than perhaps other types of financing to get the bonds issued,” said Ed Oswald, an attorney with Orrick Herrington & Sutcliffe here. “If someone is looking to do a wind project, wind typically takes a long time to do, and it could just be within a particular time frame of use-or-lose. I don’t think that’s the whole story but at least a part of it.”

“New CREBs obviously help reduce the cost of financing renewable energy projects,” said John Godfrey, senior director of government relations at American Public Power Association. “New CREBs are good if you can get them and I am glad to see that some of our members have been able to make real use of them.”

Godfrey said the federal law authorizing New CREBs for public power authorities, hamstrings how they are used.

“You have to get a prior allocation of bond volume, bond volume itself is limited and, in the case of public power, even if you get an allocation you may only get a fraction of what you need,” Godfrey said. “Bluntly, being forced to wait around for a fraction of ‘too little’ is not a good way to run a program. If Congress wants these incentives to work — if they want public power utilities to directly invest in renewables – these barriers need to be lifted."

A 2009 round of new CREBs for public power agencies was over-subscribed. According to the APPA, there were 38 applications for $1.446 billion.

The IRS prorated the allocations and set a 180-day deadline for their use.

Many of the projects were not undertaken by the 180-day deadline, however, so there was a reallocation round in 2015 round for the remaining $516.56 million.

That second round for public power companies ended June 3, 2015 with only $137 million in New CREBs bond authority used. The IRS has not disclosed how much bond authority was requested or how much may have been forfeited by not meeting the 180-day deadline.

The new round announced by the IRS on Oct. 19 faces the same hurdles.

Public power authorities once again will be awarded pro-rata shares of the $379,549,691 if the requests are larger than the allocation and will have 180 days to issue bonds after receiving a letter of notification.
The Grant County Public Utility District in Washington State has been the nation's largest user of New CREBs, according to a database maintained by Thomson Reuters (TRI).

The Grant County PUD issued $222.4 million in low-cost New CREBs to "help modernize turbines and generators at Wanapum and Priest Rapids Dams,'' spokesman Ryan Holterhoff said. Wanapum Dam produces 1.1 million kilowatts of electricity and Priest Rapids Dam produces 956,000 kilowatts.

The two other New CREBs issuances that were among the three largest also were for hydro-electric projects.

American Municipal Power Inc., which serves 135 public utilities in nine Midwest and Southeast states, issued $136 million. The money went for the Meldahl Hydro Project and the Combined Hydro Project, which includes development of new hydro-power at the Smithland, Cannelton and Willow Island Locks and Dam, said spokesman Michael Beirne.

Seattle City Light used $84.9 million to rebuild hydro-electric generators at the Diablo Dam and Boundary Dam.

By Brian Tumulty

BY SOURCEMEDIA | MUNICIPAL | 10/31/17 07:11 PM EDT

Neighborly Insights: Flattening Treasury Curve and Tax Reform Concerns Outweigh Temporary Spike in Muni Supply.

According to Bond Buyer data, muni new-issue supply in the upcoming week is expected to reach nearly $12 billion, as a number of issuers rush deals to market to avoid potential deadlines in House and Senate Tax Cut Bills, which would eliminate both advanced refundings and Private Activity Bonds (PABs) on the House side, but potentially preserve PABs on the Senate side. What the outcome will be after a) a Senate vote and b) some form of Senate/House negotiations, if we get that far, remains uncertain. Nevertheless, some issuers are in a hurry to get their deals done before a potential 12/31/17 deadline, just in case prohibitions of advance refundings and PABs actually make it to a final law. Such a law could be signed after 12/31, but with a year-end effective date.

So, we expect issuance in vulnerable sectors to remain heavy right through year-end, unless it becomes clear that the Tax Cut bill in the Senate is foundering — a distinct possibility. Of the 26 major negotiated deals this week, 20 are revenue-based issues. Many have noted that generic revenue bonds have outperformed high-grade GOs by 50 basis points. Additional concession can be expected in the sector with the influx of supply and should offer interesting yield options (5 year 2%s, 15 year 3%s). The 5-year AAA has moved 20 basis points higher, while intermediate yields are nominally higher and 20 year-plus yields have seen a modest rally. Short munis are looking the most attractive to short U.S. Treasuries in nearly a year.

Continue reading.

by George Friedlander

Posted 11/27/2017

Neighborly Insights

[Trump's Vow to Fix 'Third-World' U.S. Airports Is Hurt by Tax Bill.]

- **House measure would end tax-free bonds used to fund projects**
- **Infrastructure advocates lobby to kill measure in final draft**

President Donald Trump has compared landing at Los Angeles International and other U.S. airports to arriving in a third-world country. But a provision in the tax bill passed by the House of Representatives would eliminate a tool central to his $1 trillion pledge to upgrade airports and other public works.

The House measure would eliminate a form of tax-exempt debt called private-activity bonds. That would leave Los Angeles World Airports, which runs LAX, with the choice of scaling back projects in its $14 billion modernization plan or finding $500 million in new revenue because of higher borrowing costs, Chief Financial Officer Ryan Yakubik said in a interview.

"Certainly, it had been made clear that infrastructure was a great priority, and that finding ways to do that was important," Yakubik said. "This doesn't seem pointed in that direction."

While the Trump administration has called for expanding the use of the bonds to attract more private investment in U.S. infrastructure, the House tax bill passed on Thursday would eliminate them after Dec. 31. Airport executives, state transportation officials and other advocates unsuccessfully lobbied lawmakers to remove the provision. It's not in the current Senate plan, and they're pushing to keep it out of any final bill.

Fewer Projects

Advocates say losing the tax exemption would mean airports, port authorities, state and local governments and other entities would complete fewer projects or face higher costs at a time the American Society of Civil Engineers has said the U.S. needs an additional $2 trillion for infrastructure by 2025. Trump has promised to invest $1 trillion over 10 years.

“They just won’t be able to do these deals,” Toby Rittner, president and chief executive of the Council of Development Finance Agencies, said by phone. “At the end of the day, you just hope smart-minded people in the House and Senate see the ramifications of this.”

Private-activity bonds, or PABs, are issued by state and local governments and other public authorities to give private entities access to tax-exempt debt to increase their participation and lower costs for qualified projects. They’re also used by hospitals, universities and other non-profit groups.

Without the tax exemption, borrowing costs for state and local governments would rise by as much as 35 percent, Ritter said in a Nov. 3 letter to congressional leaders on behalf of more 200 cities, banks and other entities nationally and in 39 U.S. states and territories.

The impact would be especially felt at LAX and other U.S. airports, where PABs accounted for 60 percent of bonds issued for terminal renovations and other capital projects during the past decade, according to Airports Council International – North America. The group represents owners and operators of commercial airports in the U.S. and Canada.

Cancel or Delay

Airports have an estimated $100 billion in infrastructure needs by 2021, and financing that work without PABs could increase costs to the airport industry by $3.2 billion over the life of the bonds, according to a Nov. 13 letter sent to Senate Finance Committee leaders by the Council and the American Association of Airport Executives. Some airports may have no choice but to cancel or delay projects, the groups said.

Voters in Kansas City approved a new $1 billion terminal on Nov. 7, and the elimination of PABs could throw the project’s future into question because of higher borrowing costs, Mayor Sly James said. Philadelphia International Airport would have to re-evaluate the sequence of about $377 million in planned projects, Chief Executive Chellie Cameron said in a statement. Denver International Airport would have to evaluate other financing options if the bonds were eliminated because it had expected to use them for about three-quarters of a planned $3.5 billion capital improvement program, Chief Financial Officer Gisela Shanahan said.

Borrowing Costs

Republican tax-writers said the federal government shouldn’t subsidize the borrowing costs of private businesses when their competitors must pay higher interest rates on debt. Eliminating the tax exemption also would increase federal revenue by $38.9 billion through 2027 to help pay for tax cuts, according to the Joint Committee on Taxation.

Still, there’s a misperception about PABs because the bulk of the deals are for assets that the public uses, said Susan Monteverde, vice president for government relations at the American Association of Port Authorities.

“We are building a transportation hub for trade, which everyone sees as a valuable public asset,” Monteverde said.

Advocates also were surprised by the provision because the Trump administration had proposed expanding the bonds as a way to tap more private capital for the president’s infrastructure plan, which is expected after the tax overhaul. The White House has called for allocating $200 billion in federal funds to generate $800 billion in spending by states, localities and the private sector.

“Any objective assessment would conclude that terminating the use of PABs will make these levels of infrastructure investment much more difficult to achieve, if not impossible,” associations representing state transportation officials, construction companies and other contractors said in a Nov. 3 letter to leaders of the House Ways and Means Committee.

More Expensive

Without the tax-exempt bonds, projects such as the $3 billion Interstate 66 project in Virginia, which includes new express lanes and relies on about $737 million of PABs, may not get off the ground or would be more expensive, said Aubrey Layne, the Virginia secretary of transportation.

“If they truly are serious about infrastructure, then this is not helping,” Layne said.

The Trump administration “strongly” supported passage of the House bill and didn’t publicly object to the provision eliminating PABs. The White House said Trump is committed to generating $1 trillion in infrastructure investment.

“We are confident that when the debate on tax reform is complete, we will be well positioned to make American infrastructure once again the envy of the world,” White House spokeswoman Lindsay Walters said in a statement. Walters didn’t specifically address the potential elimination of the tax-free bonds as a financing source.

’Third-World Countries’

Trump has said multiple times during the presidential campaign and since his election that U.S. airports are “like third-world countries.”

“We had the most beautiful airports,” Trump said during a June 21 rally in Cedar Rapids, Iowa. “Now we’re more like a third-world country. LaGuardia, Newark, LAX, Kennedy. They’re like third-world airports.”

While there are concerns about what eliminating the bonds would mean for infrastructure work, the U.S. Chamber of Commerce also is taking a holistic view of the tax overhaul and the potential for economic growth and benefits to companies, said Neil Bradley, the chamber’s chief policy officer.

Even so, reductions in the corporate tax rate won’t help businesses if they don’t have adequate roads and other infrastructure, said James, the Kansas City mayor.

“If they limit our ability to do anything with infrastructure, then this country will literally fall apart,” James said.

Bloomberg Politics

By Mark Niquette

November 17, 2017, 1:00 AM PST

— With assistance by Martin Z Braun

Let’s Talk Municipal Finance - Tax Anticipation Notes and Bond Anticipation Notes.

In this installment of the Let’s Talk Municipal Finance series, I will discuss two short-term alternatives to the issuance of long-term bonds for municipalities to access needed funds. These alternatives have a shorter maturity period and are either anticipated to be repaid by long-term bonds or other municipal revenue.

Tax Anticipation Notes
Tax anticipation notes, commonly referred to as TANs, are a form of municipal borrowing with a maturity date often less than one year from the date of issuance, payable from anticipated tax revenues of the municipality. In Maine, the issuance of a TAN is authorized by 30-A M.R.S.A. § 5771. In addition to authorizing the issuance of a TAN, Section 5771 puts certain restrictions on both the amount and the maturity date – the amount of the TAN is limited in relation to the total tax levy of the municipality in previous years and the maturity date is generally limited to one month after the end of the municipal year in which the note was issued.

The interest on payments on TANs is excludable from gross income under section 103 of the Internal Revenue Code. Unlike bonds, most TANs are typically issued directly through a bank to which the payments of principal and interest will eventually be made. As the name suggests, the funds used to make those payments are limited by statute to those raised out of taxes paid to the municipality; however, unlike some bonds, the funds can be used for general municipal purposes and need not be tied to a specific purpose. Therefore, the process required for a municipality to issue a TAN is much simpler than that required of a long-term bond, although certain documents, including a legal opinion on matters such as the tax exempt nature of the interest paid on the TAN, are usually required by the bank.

Bond Anticipation Notes
Bond anticipation notes, commonly referred to as BANs, are also a form of municipal borrowing, but share more characteristics with long-term bonds than a TAN. The key difference between a BAN and a TAN is that the municipality usually cites a specific purpose for issuing the BAN, which must be the same purpose as the anticipated long-term bond that the municipality intends to eventually issue to repay the BAN. BANs are subject to statutory requirements under 30-A M.R.S.A. § 5772, including a maximum face amount of the BAN not exceeding the authorized amount of the anticipated bond and a maximum period of borrowing of three years. Some municipal charters may also contain additional requirements or limitations for the issuance of BANs.

Northern New England Municipal Law Blog

by PretiFlaherty

November 21, 2017

Neighborly Launches Effort Aimed at Big Bond Investors, Tinkers with AI and Blockchain.

To lead the new Neighborly Investments effort, the company has brought in financial-

sector veteran Christine Todd.

Neighborly has always been idealistic. It was founded, in so many words, to help citizens invest in municipal bonds that help the communities they live in.

But now the platform wants to go after the big fish too — with artificial intelligence, future plans for blockchain and other changes to the way it does business.

The company has launched a new effort called Neighborly Investments, which for the time being is focusing on people and organizations with lots of money — multi-family offices, ultra-high net worth individuals, community banks and the like. Coming in to lead the effort is Christine Todd, who spent 22 years at the asset management firm Standish Mellon, serving as the company's president for about four years and managing $30 billion in municipal bonds.

"The thing that we realized midway in is the vast majority of the capital is managed by really smart people who have entrusted their money to professional money managers," said Jase Wilson, chief executive officer of the company.

They're people with lots of money to invest, which means that they need to be able to make large buys at once. The problem with the way Neighborly was built was that it's focused on individual municipal bond projects.

For now, Neighborly Investments functions pretty similarly to the regular Neighborly experience, except that its users will interact with it from a dashboard without going directly to the platform itself. In that way, they will be able to use the platform for vetting bonds according to Neighborly's standards, which emphasize impact. Neighborly's listings include both municipal bonds from the larger market and those that local governments have generated directly using the company's platform.

"They have a read-only view of what goes into their portfolio and they can follow the story of the impact they're having," Wilson said.

Because Investments' target users are people who invest large pools of money, it will offer some functionality meant to help those people more quickly process information about bonds.

"For them to go in and do even a $5 million buy on a single municipal bond offering is tough, because the way the market looks today is every project has 300 pages of documents to read," he said.

So the company has developed machine reading functionality, incorporating machine learning algorithms, to help users identify the most important points in those documents. Artificial intelligence will also help the company learn more about correlations between different aspects of bonds, creditworthiness and the impact that those bonds end up having.

The technology and user experience will be a competitive advantage for Neighborly against similar services for investment managers, Todd said.

"There will be surprising elements in fundamentals and impact that AI will surface that humans might not otherwise know," she said. "We will be able to scan the official statements and the documents to quickly get an understanding of the impact of each project rather than having human beings spend countless hours turning pages digging through that lengthy document."

The platform also offers the ability to apply several filters — geographic, project type, bond type, etc.

So a community bank could search for municipal bonds in its state, and could then narrow it down to bonds for park projects and then set terms for the types of bonds it wanted to see. The idea is to deliver bonds that meet the investor's definition of positive impact.

Todd said she thinks the platform can make a big change in a couple of ways. One is in changing the way people think about making an impact with their money. Many, she said, turn to philanthropy in an attempt to make the world better — but the world of savings and investment, she said, can have positive impacts too. A municipal bond might build a library, or a park, or help improve transportation for the people who need it the most.

Second, she hopes to influence how people think about infrastructure. The vast majority of public infrastructure projects in the country in the past two centuries have been funded by bonds, she said. And if President Donald Trump wants to spend $1 trillion on infrastructure in 10 years, a promise he campaigned on, he would do well to look at the $400 billion-per-year municipal bond market.

"What we'd like to see is the municipal market be not only part of the plan, but the cornerstone of that plan," Todd said.

In the future, Wilson said the company wants to offer bond packaging through Investments as well. Just like in the larger securities markets, where large lots of assets get bundled together into packages for investors to buy, Neighborly wants to bring together bonds that have been vetted according to its criteria and offer them en masse to big investors.

"That's on the road map," he said.

The company is also planning to eventually work blockchain into its system — "cloudsourcing," as Todd said, transactional data and other information so as to better create an environment of transparency and speed up internal processes.

Todd said she's excited about the prospect of jumping in with the company early on.

"I would say that my transition from Standish to Neighborly is very fortunate," she said. "Opportunities like these don't come along very often, where one's own experience and mission aligns so well with an opportunity to grow a younger firm and make a sign impact in doing so."

Neighborly wrapped up a $25 million Series A round in May. According to Wilson, the company has facilitated $100 million in bond investments this year, which was its first full year of offering investment capabilities to users.

GOVERNMENT TECHNOLOGY

BY BEN MILLER / NOVEMBER 22, 2017

Ben Miller is the business beat staff writer for *Government Technology*. His reporting experience includes breaking news, business, community features and technical subjects. He holds a Bachelor's degree in journalism from the Reynolds School of Journalism at the University of Nevada, Reno, and lives in Sacramento, Calif.

[Fitch: U.S. Airport Credits Experiencing Little To No Turbulence.]

Fitch Ratings-New York-13 November 2017: Strong passenger traffic along with stable airport finances will keep U.S. airport ratings well rooted in 'A' territory, according to Fitch Ratings in its latest peer review of U.S. airports.

Rating actions over the last year by and large mirrored movement seen last year with Fitch taking 12 positive rating actions on general airport debt across eight airports. Fitch also revised the Rating Outlook on four airports to Positive (Denver, San Diego, Burlington and Pensacola). The lone Fitch-rated airport with a Negative Outlook (Dayton International) remained so this year.

Changes in 11 of Fitch's attribute scores over the past 12 months were instrumental in much of the rating movement for airports, with Revenue Risk seeing much of the change. 'Sustainable positive passenger trends at a number of U.S. airports coupled with updated airline agreements with enhanced pricing flexibility contributed to many of the adjustments,' said Seth Lehman, Senior Director in Fitch's Global Infrastructure Group.

Highest rated airports are typically those with a strong underlying market or franchise driving demand, overall stability of cash flows through contractual agreements with airlines and other commercial users and healthy financial metrics. Conversely, weakest rated airports include those serving small markets or secondary airports subject to competition for passengers, or thinner financial metrics and elevated leverage.

Fitch's latest 'Peer Review of U.S. Airports' is available at 'www.fitchratings.com' or by clicking on the link.

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Fitch Teleconference Replay: Chicago Sales Tax Securitization Corp, IL.

Arlene Bohner, Amy Laskey, and Laura Porter discussed Fitch's 'AAA' rating on the Sales Tax Securitization Corp, IL Series 2017 A&B bonds.

Bond proceeds will be used by the corporation to purchase the sales tax revenues that secure the bonds. Funds will be applied to refund the city's existing sales tax revenue bonds. The bonds are expected to sell via negotiation the week of December 4. The Rating Outlook is Stable.

[Listen to the teleconference.]

[Bloomberg Brief Weekly Video - 11/16]

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

[Watch video.]

Bloomberg

November 16th, 2017, 12:58 PM PST

[Muni-Bond Market Braces for Borrowing Rush Ahead of Tax Changes.]

- **November, December could be 'huge' for issuance, analyst says**
- **Republican overhaul would pull tax break from many bond types**

The municipal market is preparing for a potential onslaught of bond deals before the end of the year as U.S. lawmakers consider pulling the tax break from tens of billions of dollars of debt issued each year.

The House of Representatives bill would require investors to pay income taxes on so-called private activity bonds, or PABs, which finance projects like airports, water facilities and toll roads, and do away with a frequently used refinancing technique known as advanced refunding. While the Senate version leaves PABs intact, the risk may push borrowers to act before the law is changed, Municipal Market Analytics said in a research report.

"It could be a huge end of the year," Matt Fabian, a partner with MMA, said in an interview. "Issuers will probably begin to access the market shortly just on the risk. If they're going to borrow next year they might as well accelerate to borrow now."

A late-year rush — if significant enough — would offset the slowdown in the municipal market, where new debt sales have declined from last year's record pace. That contributed to this week's drop in state and local government bonds prices, paring the gains that came after the tax overhaul promised to slash sales in the years ahead by pulling the tax-exemption from a significant chunk of the market.

Citigroup Inc. analysts raised their municipal-bond sales forecast for 2017 by $15 billion to about $380 billion as governments move to refinance before the tax law is potentially changed. There was $428 billion of municipal debt sold last year, according to data compiled by Bloomberg.

The pace of issuance through the end of 2017 may be limited because there are few weeks left to do so. Given that it's already mid-November, there isn't enough time for a lot of issuers to come to market before the end of the year, according to Philip Fischer, head of municipal research at Bank of America Merrill Lynch.

The Illinois Finance Authority used PABs to finance more than $24 billion in "essential infrastructure projects," including more than $3.6 billion in fiscal year 2017, according to a draft of a memo to Congress from the agency. Ending the exemption means projects may not get built, be delayed or reduced in scale, said Chris Meister, the authority's executive director.

"The virtue of private activity bonds is that it provides a fairly small benefit, but in each individual transaction it's a material benefit to non-profits to do the sort of work that either the private, for-profit sector cannot or does not want to do, or that government cannot or cannot afford to do," Meister said in an interview.

The Illinois authority is ready to move quickly to help borrowers get private-activity deals done before the end of 2017, according to Meister, who said he's heard that some borrowers are interested in moving up planned sales.

If enacted, the rollbacks to municipal-bond subsidies will "disproportionately" hurt states with fiscal challenges, said Richard Ciccarone, Chicago-based president of Merritt Research Services, which analyzes municipal finance.

"In Illinois, we can't replace those kind of government incentives with tax-supported programs because our balance sheet is already loaded with debt and pensions liabilities," Ciccarone said. "So we can't easily replace the loss of the lower cost to do your financing."

Bloomberg

By Elizabeth Campbell

November 14, 2017, 8:53 AM PST

[The Week in Public Finance: Trump's Impact on Trade, a Predatory Lending Loophole and More.]()

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

GOVERNING.COM

BY LIZ FARMER | NOVEMBER 17, 2017

[Fitch: Trump's Impact on Trade.]()

Sticks and stones aside, it turns out words really can hurt: President Trump's protectionist rhetoric over the past year may be leading to lower tax revenue for border states.

The [findings](), laid out this week by Fitch Ratings, suggest that the president's foreign policy agenda is cutting cross-border travel. Trump in January pulled the U.S. out of the fledgling Trans-Pacific Partnership. He has also said he wants to renegotiate the North American Free Trade Agreement (NAFTA).

Passenger crossings at several ports-of-entry were down year-over-year, particularly in Alaska, Idaho, Texas and Washington state. Notably, vehicle passenger traffic either fell or stagnated at three of the four largest ports-of-entry — San Ysidro and Otay Mesa, Calif., and Laredo, Texas. Along the northern U.S. border, passenger vehicle traffic at Michigan's three major border crossings all showed signs of softness.

Lower cross-border traffic, says Fitch, impacts sales and excise tax revenues collected in border communities.

The Takeaway: The reduced border crossings could be a sign of things to come if Trump implements protectionist policies. "Although reduced border crossings themselves are not credit negative, these fluctuations are an indicator of what border traffic declines might look like — on a larger scale — if NAFTA negotiations break down," says Fitch's Michael D'Arcy. "A re-imposition of tariffs would depress border traffic and sales tax receipts, factors which represent a credit risk to border municipalities, particularly in Texas and New Mexico."

Green Bond Issuance Surpasses US$100 billion in 2017.

Green bond issuance in 2017 has surpassed the US$100 billion milestone, marking a new record, according to Climate Bonds Initiative (CBI) data.

Last year saw a previous record of US$81.6 billion issuances, but CBI forecasts an estimated US$130 billion to be reached by the end of this year.

The Top 10 countries for green bond issuance so far in 2017 are as follows:

1. China
2. France
3. US
4. Germany
5. Netherlands
6. Sweden
7. Mexico
8. Spain
9. India
10. Canada

CBI noted that European nations have maintained their representation in the top 10, while the emergence of Mexico and India reflected their the growth in their green finance markets.

During 2017, France became the second nation to issue a sovereign green bond and Fiji has become the first emerging economy, Pacific Island nation and first from the Southern Hemisphere to issue a sovereign green bond. Nigeria is expected to become the first African nation to issue a sovereign green bond in the coming weeks.

Christiana Figueres, former UN climate chief, convenor of Mission 2020, said: "Passing US$100 billion in green bond issuance shows we are moving capital flows in the right direction. The priority is to accelerate green finance and climate investment between now and 2020 at a scale never seen before.

"A systemic response from global finance is required. Asset owners and managers need to adjust their capital allocations. Banks and corporates need to commence large-scale green bond programs.

Funding clean energy and green infrastructure to meet NDC goals is the objective. US$1 trillion in green finance by 2020 is the performance measure."

Sean Kidney, CEO, Climate Bonds, said: "We are looking for other nations to follow the lead of Poland, France, and Fiji on the sovereign issuance path. […] Now is the time for G20 and OECD countries to act and signal their intentions into 2018."

By Tom Kenning Nov 16, 2017

Trump Wants More Big Infrastructure Projects. The Obstacles Can Be Big, Too.

President Trump says he is frustrated with the slow pace of major construction projects like highways, ports and pipelines. Last summer, he pledged to use the power of the presidency to jump start building when it became bogged down in administrative delays.

"No longer will we allow the infrastructure of our magnificent country to crumble and decay," Mr. Trump said in August.

In an executive order, the president directed federal agencies to coordinate environmental impact reviews for major projects with the goal of completing them within two years. Such reviews can often take four years and, in some cases, even longer.

Continue reading.

THE NEW YORK TIMES

By BARRY MEIER

NOV. 18, 2017

S&P: Securitization Plan Won't Affect Chicago GO Debt Rating.

Chicago's authorized $3 billion sales tax securitization issuance would channel pledged sales tax revenues to a lockbox structure, unavailable to fund city operations or general obligation (GO) debt service until debt service needs on the securitized bonds have been met.

Continue Reading

Nov. 14, 2017

Market Commentary: Lots of Noise in the Muni Market as Confusion, Concern Surround PABs, Refundings.

The muni market outperformed Treasuries over the past week. Or it underperformed. Or it remained constant. It was a mixed bag for munis this week with yields rising slightly. However, finding a consistent theme is difficult because there is so much noise in the data right now, that it's difficult to tell where the market stands.

This Market Commentary is part of *Court Street Group's Perspective*. For a full copy of the report, click here.

The Court Street Group

by George Friedlander

Posted 11/17/2017

Leveraging CA SB1 Funding: Orrick

Considerations for California Public Entities Entitled to Receive SB1 Revenues and their Financial Advisors and Underwriters

In April 2017, the Road Repair and Accountability Act of 2017 was enacted in California (also known as California Senate Bill "SB1"). Key facts about SB1 are as follows:

- SB1 is the landmark transportation funding package which generates new revenues from several transportation-related taxes and fees.
- $5.2 billion a year is the new estimated revenue expected to be generated for use by the State, cities, counties and certain other governmental entities on transportation infrastructure in California.

Governmental entities entitled to receive the new SB1 revenues may be evaluating whether there is a need for accelerating the SB1 funding by leveraging the revenue stream(s). This will depend in large part on the amount of eligible transportation projects that are construction ready.

Read Article

by Jenna Magan

November.14.2017

Orrick

U.S. Muni Supply Tops $4 bln Next Week, as Focus Stays on Tax Reform.

Nov 17 (Reuters) – New York's Metropolitan Transportation Authority will lead next week's U.S. municipal debt load, which includes $4.2 billion of total bonds and $69 million in notes.

The MTA will issue about $2 billion in bonds to refinance outstanding transportation revenue bonds, so-called green bonds that support financing for projects that reduce the impact of climate change.

In another large negotiated deal, Virginia's Commonwealth Transportation Board will issue $479 million to refund outstanding notes and help pay for a slew of repairs and work on Virginia state-owned roads.

That deal, set to price on Tuesday, is being underwritten by Wells Fargo.

The biggest competitive bond next week will come from New York'sOrange County, which plans to issue some $55.5 million in public improvement serial bonds.

Georgia will provide the largest note issuance, a negotiated, $35 million deal from the Atkinson-Coffee County Joint Development Authority, underwritten by Raymond James.

The U.S. muni bond world will continue to watch tax reform efforts next week, as President Donald Trump and Republicans in U.S. Congress push tax legislation that could have an impact on municipal investing.

The so-called Tax Cuts and Jobs Act, which passed in the House of Representatives on Thursday, still must pass muster in the Senate before making it to Trump's desk.

The bill would terminate private activity bonds (PABs), and repeal advance refundings, which municipal issuers use to refund bonds ahead of their call dates to take advantage of lower interest rates.

While the bill preserves the tax-exempt status of some municipal bonds, PABs and refunding bonds account for some 40 percent of all tax-exempt bonds, PNC Managing Director and municipal strategist Thomas Kozlik said in a note on Wednesday.

"There are scenarios we envision where no tax-exempt advance refunding or private activity bonds are sold for the first three to four months, or perhaps maybe not at all in 2018, if there is no conclusion about tax reform," Kozlik wrote.

By Nick Brown

Mixed Results in Pre-Trade Market Highlight Continued Caution Among Issuers.

"There is an alchemy to new security issuance that involves equal parts macroeconomics, politics, and routine funding needs of corporations and municipalities," said Richard Peterson, Senior Director, S&P Global Market Intelligence. " As those three variables continue to fluctuate over the course of the year, we're seeing those same undulations in the pre-trade market where issuers are readying new instruments to bring to market. We expect that general sense of cautiousness to pervade new issuance activity for the near-term."

READ PRESS RELEASE

CUSIP Request Volume Signals Sluggish Pace of Corporate and Muni Bond Issuance.

NEW YORK, NY, NOVEMBER 13, 2017 – CUSIP Global Services (CGS) today announced the release of its CUSIP Issuance Trends Report for October 2017. The report, which tracks the issuance of new security identifiers as an early indicator of debt and capital markets activity, found mixed results this month. Pre-trade requests for new corporate debt identifiers decreased in October, while requests for new corporate equity and municipal bond identifiers saw some increases. This is suggestive of a continued sluggish pace of new security issuance in the fourth quarter of 2017.

READ REPORT

S&P: Local Government Pension and Other Postemployment Benefits Analysis: A Closer Look

Since the turn of the century, most U.S. public sector pension plans have experienced a sharp increase in unfunded liabilities due to several factors including demographic shifts primarily associated with the baby boomers, significant increases in life expectancy, and investment returns…

Continue Reading

Nov. 8, 2017

How Lawrence Used Regenerative Public Finance to Fund a Single Fire Truck.

One bond. One project. One fire truck.

Firefighters are part of the backbone of our communities. They're the ones running into a burning building when everyone else is running out, they're first on the scene to provide medical care, and they'll even help rescue your family cat from that sugar maple. Firefighters save lives, protect property and help educate the public about fire safety. Ensuring that they have the equipment they need to do their jobs is crucial.

But raising funds for fire equipment isn't always easy. The traditional transacting costs associated with issuing bonds are high, so cities often bundle projects into larger bond issuances – the average bond issuance in the year to date was $35.7 million, according to the MSRB. This "bundling effect" can sometimes delay the acquisition of important equipment, such as the purchasing of fire trucks.

Continue reading.

Neighborly

by Garrett Brinker

Posted 11/05/2017

The Week in Public Finance: The Senate's Tax Reform Plan, Election 2017's

Impact on Spending and More

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

GOVERNING.COM

BY LIZ FARMER | NOVEMBER 10, 2017

Struggling Suburb? Merge It With the Big City Next Door.

It wouldn't be a panacea, but it's an option that needs to be on the table.

Consolidation of city and county governments has long been in vogue with good-government advocates. But while the cost/benefit of these kinds of "big box" mergers is questionable, one kind of smaller-scale jurisdictional union makes a lot of sense: the merger of struggling inner-ring suburbs with adjacent central cities.

The problems facing inner-ring suburbs, which contain as much as 20 percent of the American population, have been getting increasing attention. While many of these communities are doing well or even thriving, others have encountered serious challenges with population loss, increasing poverty, declining household incomes, retail vacancies and dead shopping malls. As their tax bases shrink, these communities run into serious financial challenges, leaving them struggling to provide basic services to their residents.

Troubles in an inner-ring suburb can be more difficult, in a sense, than in a bigger city. These smaller communities are often off the public's radar, so problems there seldom get media or state-level attention until a crisis occurs, as with the turmoil following the police shooting in Ferguson, Mo., or the pay scandal in Bell, Calif.

Compared to cities, inner-ring suburbs have a limited range of housing and retail building types. Some of these, such as small ranch homes or simple strip malls, are now out of favor in the market. If a more monolithic suburb has these off-trend buildings, attracting residents and businesses can be challenging. What's more, many suburbs were built as bedroom communities. They lack the regional assets of big cities, such as powerful office-based central business districts, seats of government, cultural institutions, universities or hospitals. They have fewer assets to redevelop around.

These challenges often overlap with racial ones. In many regions, black city residents, along with members of other minority or ethnic groups, have been moving to the suburbs in search of the American dream of home ownership. While this often goes well, some of these inner-ring suburbs have proven to be similar to the troubled city neighborhoods that people have fled. When public pension costs, bond debt and other bills from the past come due in such declining places, suburban residents are unable to draw on the tax base of a larger, asset-rich central city.

A merger is not a panacea. Nobody should expect one to magically address poverty or segregation, for example. But when fiscal conditions make it impossible to fund basic public services, merging with an economically stronger municipality can help address that problem. The other options for struggling municipalities all come with their own sets of downsides. A financial control board or even a bankruptcy can potentially address debt or pension problems, but they won't help with a declining tax base. Neglect or simply providing life support through subsidies might be viable politically in the short term — until a crisis strikes. But temporary subsidies ignore underlying problems and allow them to continue to fester. And finally, a state takeover comes with its own risks. Just ask Flint, Mich.

I examined suburbs contiguous to several Midwestern and Northeastern post-industrial cities for my recent Manhattan Institute study, “Mergers May Rescue Declining Suburbs.” I found that a large number of these suburbs face negative indicators like falling populations and rising poverty. Many are potential candidates for a merger, and I highlight 10 of them as examples.

We haven’t seen this type of merger in the recent era, but there have been a few proposals. One case is East Cleveland, Ohio. The Cleveland suburb has lost 37 percent of its population since 2000 and has a poverty rate of almost 43 percent. Fiscal problems forced it to cut its budget by 38 percent and lay off almost half of the municipal workforce. It had to borrow salt trucks from the state and an ambulance from a neighboring town. Merging with Cleveland could help to ensure that good-quality basic public services can be delivered there.

But let’s not kid ourselves: Mergers are extremely challenging politically. East Cleveland is again the example. After starting the process of exploring a merger, the mayor and city council president were recalled by narrow vote margins in a special election in December, killing the merger proposal for now.

Nevertheless, local and state leaders should keep mergers in mind as a policy tool. Then they can look for opportunities where need and political reality align to use it. They can also start drawing lessons from annexation battles. Annexations typically require a carrot of some sort to sell the proposal, such as getting utility service or investments in other infrastructure. For mergers to happen, states will likely need to step up to fund transition costs, potentially absorb excessive suburban fiscal liabilities and put a capital improvement plan on the table as a sweetener. Ohio’s state auditor had suggested a $10 million state infrastructure investment in East Cleveland contingent on a merger.

The challenges of helping economically declining and fiscally struggling inner-ring suburbs will not be easy ones to solve. There are no magic fixes, and the answers will vary by community. But merging with the adjacent central city is an option that needs to be on the table.

GOVERNING.COM

By Aaron M. Renn | Columnist
Senior Fellow at the Manhattan Institute

NOVEMBER 2017

[The Municipal Bond Trader Working the Phone Is Now a Dying Breed.]

- **Electronic networks account for majority of dealer trading**
- **Regulator says data provides first look at role of ATSs**

Even on staid municipal bond desks, the days of traders working the phones are rapidly fading.

Electronic-trading platforms, known as ATSs, for securities firms and big investors account for 59 percent of all state and local debt trades between dealers, according to data released by the Municipal Securities Rulemaking Board. Dealers can choose to trade one of three ways — through

ATS, broker's brokers or directly with each other.

"Our data provide the market's first view of the extent to which ATSs are used in the muni market," John Bagley, the Chief Market Structure Officer at the MSRB, said in a statement. "These platforms, which disseminate quotes and expand access to bond inventories, can help improve liquidity and market efficiency. They can also help dealers obtain the best pricing for investors."

The MSRB first began data collection on the amount of trading executed on ATSs in July of 2016. In the past twelve months, 29 percent of total inter-dealer par amounts traded were executed through an alternative trading system.

While a majority of inter-dealer trades used ATSs, 34 percent were still conducted directly between dealers and 7 percent through a broker's broker.

Bagley said that ATSs can provide a way for "dealers to access bids and offers from a wide range of market participants," given that securities firms have cut their bond inventories by about 50 percent over the past decade.

Bloomberg Markets

By Danielle Moran

November 9, 2017, 9:30 AM PST

Bloomberg Brief Weekly Video - 11/09

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

Watch video.

Bloomberg

November 10th, 2017

Public-Private Development: Aligning Interests Through a Ground Lease.

To facilitate real estate development projects, the public sector often seeks to structure its public-private transactions through a ground lease. For the public sector, a ground lease possesses a number of important features, including: (i) an enforceable mechanism to structure both the development and operational relationship with its private sector partner; (ii) the opportunity to realize longer-term economic value in the property once improved; and (iii) the means to ensure that particular public objectives are achieved. For the private sector, while a ground lease presents challenges that must be addressed, the structure allows for a number of benefits, including: (i) the opportunity to develop a project without carrying a significant upfront acquisition cost for the land; (ii) a means to access tax benefits; and (iii) a flexible structure that can adapt as a project moves from the construction phase to the operational phase.

Given the parties' varying objectives and the long-term nature of the relationship, public-private ground lease negotiations are complex and lengthy in nature. These negotiations typically focus on the following key provisions:

- rent, revenue participation and resets; tax benefits;
- capital work and public sector oversight; use and operations;
- term and purchase option;
- transfer restrictions;
- casualty events; and
- reporting requirements and audit rights.

By undertaking a ground lease transaction with a sound understanding of each party's key objectives and by using the negotiation process to align the parties' interests, the ground lease provides a means to optimally allocate risks and benefits to each of the parties, which can lead to transformative real estate development projects.

Rent, Revenue Participation, and Resets: Maximizing Public Sector Long-term Value

Although the public sector often has significant nonmonetary objectives when negotiating a ground lease, the public sector also seeks to maximize the value of its real estate interest. Since governmental entities are not equipped to enter into formal joint venture agreements with developers, a ground lease represents a suitable alternative form to memorialize these arrangements. Consequentially, the public sec-tor attempts to negotiate a rental stream that in the aggregate reflects its contribution to the project. Typically, negotiation of the rent provisions focus on: (i) a base rent that escalates over time; (ii) a participation component; and (iii) periodic resets. By structuring these revenue streams in a manner that provides the private sector with a level of certainty regarding its annual payments while also offering the public sector the opportunity to participate in the project's success, the parties can align their respective interests.

Base Rent

While base rents can vary, the parties tend to negotiate a rent that is between five percent and seven percent of the agreed-upon value of the land subject to the ground lease. The agreed-upon value presents the real challenge in this negotiation. While the public sector may anchor itself to an appraisal based on highest and best use, the developer wants to make sure that the appraisal accounts for any development limitations set by the lease. For example, even though an all residential project may represent highest and best use, if the developer is limited in the amount of residential space allowed in the project, the appraisal should account for such limitation.

Escalations

The escalation of ground rent payments represents a significant concern for both parties. Often times, the public sector negotiates to tie the escalations to an objective mea-sure such as the Consumer Price Index ("CPI"). The challenge with using CPI though is that land values and CPI increases do not necessarily correlate. In a strong real estate market, land values may rise significantly while CPI remains relatively flat. Over the past few years in New York City, for example, land prices have increased significantly while inflation has remained low. Although the relative steady nature of CPI in recent history would appear to benefit a developer, a developer often looks to have even greater certainty with respect to what its future rental payment stream will be given that ground leases can extend for upwards of 99 years. As a result, a developer either seeks to have a fixed annual percentage rental increase or looks to tie the increase to CPI subject to a cap on annual increases. Within this basic framework, there are numerous variations. For example, instead of increasing annually, the parties may agree to ground rent payments that step up periodically (e.g., once every three years).

Given that periodic increases may not appropriately reflect changes in property values, periodic reset provisions often are negotiated in ground leases. These provisions require that an appraiser undertake an appraisal, and as noted above in the context of base rent, the parties' negotiations focus on the scope of the appraisal. While the public sector tends to propose a highest and best use scope, the developer again needs to negotiate to ensure the valuation takes into account the limitations established by the ground lease as well as the age of the facility then on the property. The developer wants to ensure the valuation is of what the property is and not of what the property could be.

Participation

Since in many respects the ground lease acts like the public sector version of a joint venture, a participation rent provides the public sector with the opportunity to realize additional value for its property contribution, particularly in the event of a highly successful project. Given the unknowns associated with the project at the time the parties negotiate the participation provision, these negotiations can be particularly challenging. In addition to the percentage itself, the parties must agree on the base number to use in the calculation. While the public sector prefers to have the participation calculated off a gross revenue number, the developer understandably is resistant to such a calculation because a net number is more reflective of the true success of the project. For the public sector, a net number presents a challenge because the public sector is not well positioned to assess the appropriateness of certain expenses incorporated into the calculation. For instance, the developer may allocate certain overhead costs to the property's operation, which can be difficult for the public sector to verify. Consequentially, the public sector needs to have appropriate audit rights to confirm the participation payments.

As with rent escalations, there are numerous variations to the rent participation framework. For example, the parties typically discuss whether to use a tiered structure for the participation. In this instance, the parties agree to adjust the percentage rent applied to revenues as those revenues grow in a given year. To the extent a project is more successful, the public sector receives compensation for a greater share of that success.

While the parties may see each component of the rent stream in a binary light, when viewed in terms of a structure that over time (i) provides the developer with some level of certainty regarding payments, (ii) fairly compensates the public sector for its initial investment through the contribution of its property and (iii) further benefits the public sector party in a manner that tracks the success of the project, the rent stream represents one significant tool to align the interests of the two parties.

Tax Benefits: Other Forms of Public Sector "Investment"

Although tax benefits represent another deal term viewed in a zero-sum fashion, when war-ranted these benefits are an additional form of public sector investment in a project. This is particularly true given that the public sector is increasingly less likely to make direct capital contributions as budgets tighten. Through the targeted use of tax benefit tools, the parties can work together to develop an optimal plan that further ensures the project comes to fruition.

Tax Exemptions

Maximizing the long-term value of its property represents one public sector objective, but the ground lease also is often the means through which the public sector can further invest in the project by providing a real estate tax exemption. Typically, property owned by a public sector entity is not subject to real estate tax under applicable state law. For example, Section 404 of the New York Real Property Tax Law exempts real property owned by the State of New York from real estate taxes while Section 406 exempts real property owned by the City of New York from real estate taxes. Therefore, by having a public sector entity retain the fee interest, the entity can make an-other longer-term investment in the project through the real estate tax exemption.

If the parties have not agreed to preserve the real estate tax exemption, the public sec-tor typically negotiates a provision requiring that the developer make payments-in-lieu of taxes, or PILOTs, which the parties can structure to mirror the amount that the developer would otherwise pay annually or can structure as a fixed-payment schedule. In addition to real estate taxes, in certain instances the public sector can provide other tax benefits through the ground lease. For example, in New York City, the public sector may provide a sales tax exemption through the ground lease.

Tax-Exempt Financing

In addition to facilitating a tax exemption, ground leases commonly are used in tax-exempt financing transactions, which represents yet another manner in which the public sector can contribute to a project. The parties can structure this financing in a few different ways. The public sector and developer may undertake a tax-exempt bond financing in which PILOT payments made by the developer act as the source of repayment of the bonds. Per Internal Revenue Service regulations, the PILOTs must be "commensurate with the amount imposed by a statute for a generally applicable tax".

Another tax-exempt financing structure used for development projects involves 501(c)(3) bonds. This particular structure has become more prevalent in the student housing area as public universities turn to private developers to build new student housing. In this type of public-private partnership, the university ground leases its property to a not-for-profit conduit issuer who in turn issues 501(c)(3) bonds to finance the student housing development. The not-for-profit tenant also enters into development and management agreements with a private sector partner who proceeds to develop and operate the project. The ground lease has a term that extends for a period sufficiently beyond the term of the bonds. At the end of the lease term, the improved property returns to the university. Through this structure, the university has the ability to not only access tax-exempt financing but also to work with a developer with expertise in student housing development without fore-going its fee interest in a property.

Construction and Public Sector Oversight: Ensuring the Project Comes to Fruition

With respect to the project's construction period, the parties need to focus on establishing a process that provides the public sector with sufficient comfort that construction progresses on schedule while at the same time not limiting the developer's ability to use its expertise to efficiently manage construction. The extensive negotiations that typically take place over the level of the public sector entity's involvement in monitoring a project's construction phase is particular to the public-private context. When viewed in the context of the ground lease being analogous to the public sector's version of a joint venture, this focus makes a good deal of sense. The public sec-tor usually undertakes an extensive diligence process to ensure that its private sector partner is proposing a feasible project and that the developer has the resources and ability to successfully deliver the project on time and on budget. The resulting ground lease safeguards relating to project delivery are particularly critical to the public sector because all too often the public sector has experienced situations in which its property winds up being saddled with a ground lease and where the developer can-not deliver a project.

As noted above, the public sector often makes significant contributions to the development project through its land contribution as well as tax benefits and should negotiate the construction period provisions as a joint venture partner would. In fact, the public sec-tor may structure the transaction so that the ground lease only becomes effective upon the developer fulfilling certain conditions, including a final set of plans and specifications, a fully negotiated construction contract and construction financing in place. The parties may negotiate an agreement to lease or development agreement to govern the period prior to the ground lease becoming effective. The public sector also seeks to have the developer provide a completion guaranty and/or provide security in the event of default where the developer leaves the property with a partially completed project that the public sector must remove. As is the case in a traditional construction financing, a key item with respect to the completion guaranty is the identity of party who will provide the guaranty. Since the developer likely has formed a special purpose entity with no other assets to act as tenant under the ground lease, the public sector needs to ensure the sponsor entity steps in to provide the guaranty.

To make sure construction proceeds in accordance with the final project budget and schedule, the public sector wants to negotiate into the ground lease rights to monitor construction through regular updates and inspections. For the developer, it seeks to make certain that these rights do not delay the project's development. During negotiations, the parties will likely discuss the appropriateness of having a deemed approval provision with respect to items for which the public sec-tor has an approval right. While a reasonable request, the public sector must make sure it is equipped to respond in a timely fashion.

Although the public sector strives for certainty in this process, there often is significant uncertainty associated with development projects. Hence, a developer looks to build enough flexibility into ground lease provisions so that the developer does not risk an event of default if and when construction does not proceed according to plan. This is particularly important because the ground lease will need to include typical provisions that make it financeable, including provisions regarding recognized leasehold mortgagees, notice and cure rights for mortgagees and new lease rights in the case of a termination. Given that the construction lender shares the public sec-tor entity's interest in project certainty, the public sector may take comfort in the construction lender having the necessary rights and protections typical in a construction loan provided by an institutional lender. To ensure that the lending party is an institutional-type lender with sound underwriting standards and the ability to insist on customary lender protective provisions in the loan, the public sector typically negotiates recognized mortgagee provisions requiring the lenders to be of a certain financial standing.

Not surprisingly, one of the biggest points of negotiation in the construction context is the completion date. Obviously, a developer seeks to have as much cushion as possible on this term. Additionally, its construction lender wants to make sure that there is sufficient time so that in the event the lender must foreclose on the developer's interest and bring in a replacement developer there is time for this to occur without facing a default and potential termination of the ground lease. Since the completion date may trigger the commencement of rent payments, the public sector may have a basis for negotiating a liquidated damages provision for lengthy delays in completion. As the delay grows, the public sector has grounds to expect a higher damage payment.

Use and Operations: Ensuring Success is Not Fleeting

Through the combination of a prescriptive use provision with defined parameters for granting relief, the parties can establish a structure that protects the public sector's interest in seeing its property activated in a particular way while also allowing the developer to make adjustments if market conditions warrant. Since the public sector often enters into a ground lease expecting a particular end use that satisfies certain public objectives, the public sector typically negotiates prescriptive use and operation provisions that go beyond standard provisions prohibiting noxious uses. For example in a retail development, the use provisions may specify the type and quality of tenants as well as minimum operating hours. The public sector typically also includes limitations on "going dark" to prevent extended periods of inactivity on the property. Collectively, these use provisions are particularly important because job creation often is a key project objective. Furthermore, in the event that the public sector expects to derive a significant component of the project's economic value from percentage rent, the public sector wants to ensure the property remains active.

In addition to the economic component, the use provisions may also act as another overlay of zoning with certain uses being prescribed for different components of the project. For example, the use provisions may prescribe streetscape retail on the ground level with commercial office space residing on upper level floors. The public sector may also negotiate to have a portion of the developed project retained for its own use or the use of groups in the surrounding community. As a result, the public sector seeks to ensure that the various uses are compatible.

While the public sector, as is the case during construction, seeks certainty, the developer again seeks the flexibility to allow the project to adapt over time. The developer may needs this flexibility because the market for the project does not materialize as expected or be-cause market preferences change over time. The developer typically makes the case that it is incentivized to maximize activity on the property since profit maximization is its primary motivation. To the extent one use does not maximize profits, the developer will ultimately choose another use that does over having the property remain dark.

To address these competing concerns and to implement a structure that provides some level of flexibility, the parties can agree to include a set of parameters, which if met would provide the developer with a basis to request relief from the prescriptive use provision. For example, in the event the ground lease re-quires a particular type of tenant as occupant for a minimum amount of space, the agreement could provide that if the developer can demonstrate it has diligently marketed the space for a minimum period of time but has not attracted a tenant the developer would have the ability to offer the space to a wider range of tenants.

Term and Purchase Option: Determining How Long is Long-Term Part I

Given the significant investment that a developer makes to develop a project, a ground lease tends to be a minimum of 25 years and often runs 49 years or more. Generally, a lease of 25 years does not provide sufficient time to make a developer's investment of time and money worthwhile. It is not atypical to have a 49-year ground lease with tenant options extending the term to an aggregate of between 75 years and 99 years.

In the context of the ground lease term, negotiations tend to focus on whether or not the developer will have the option to purchase the property at some point during the term. While the public sector may want to preserve its reversionary interest in the property, if structured correctly, the public sector can realize the value of its property interest through the purchase option once the project has reached stabilization. As in the case of the base ground rent and rent reset calculation, the purchase option negotiation focuses on the scope for the appraisal that is typically undertaken to determine the developer's purchase price. The parties can look to the present value of the future rental payments to inform the discussion, but the fact that the public sector likely expects a portion of its return in the form of percentage rent means that the base rent stream does not fully reflect the value of the public sector's interest. While the parties can estimate future participation based on past experience, the public sector also must ensure that the valuation is not depressed because the developer opportunistically exercises the option at a low point in the market. As a result, the parties must work through a number of scenarios to appropriately address the potential issues raised by valuing the public sector's interest.

The developer's argument for a purchase option is stronger in the instance where the ground lease is simply undertaken to provide a tax benefit or facilitate a tax-exempt financing. In those instances, the parties can tie the purchase option to the point in time when the agreed-upon tax benefits have expired or when the tax-exempt financing has been repaid.

Transfer Restrictions: Determining How Long is Long-Term Part II

Although provisions restricting transfers apply to both the development stage and operations stage, the parties can craft these provisions to provide the public sector with the comfort of knowing that the developer will not exit before project completion and with knowing that over the long term a party with the necessary property management expertise will oversee its operations. Developers generally understand that the public sector is looking to the developer to deliver the project so the ground lease significantly limits the developer's ability to transfer its interest in the project during construction. While the developer needs sufficient flexibility to bring in additional equity partners, the public sector wants to ensure that the developer retains control over management of the project given the reliance on the developer's expertise. The public sector also wants to make sure the developer continues to have "skin in the game." As a result, during the construction phase, the ground lease may include a minimum equity stake for the developer as well as a requirement that the developer remain in control of the project.

Once the developer completes the project and the project reaches stabilization, the developer has a basis to negotiate less restrictive transfer provisions. The developer's business model may not focus on the continued management of a stabilized asset. As a result, provided that the developer has successfully delivered on its construction commitments, the ground lease may allow for less restrictive transfer provisions during the operational phase. For the public sector, the key component of a less restrictive provision is that a property manager with a sufficient level of expertise and quality manage the project moving forward. The parties may agree in advance on a group of entities from which to choose or may agree on a set of criteria, such as a certain amount of space under management, that a property manager would need to satisfy.

Casualty Event: To Restore or Not to Restore

Given the length of a ground lease's term, the parties need to address the potential that at some point a casualty occurs. By crafting provisions that take into account the extent of the damage and the timing of the event relative to the lease's remaining term, the ground lease can reflect the public sector's interest in having the project restored while not overly burdening the developer with an absolute restoration obligation. For the public sector, it seeks to ensure that the private sector party is carrying sufficient insurance so that proceeds cover restoration of the project. The public sector looks require that the developer restore the project to at least the same condition as prior to the casualty event. In contrast, the private sector party wants to preserve the flexibility to determine how best to proceed based on the extent of the damage and when during the term the casualty takes place. Typically, a developer agrees to the restoration requirement provided the extent of the damage caused by the casualty does not exceed an agreed-upon threshold amount. The parties may base this threshold amount on the value of the property or on the square footage of the property. For example, a developer may agree to restore provided the damage does not exceed 50 percent of the value of the property or instead 50 percent of the square footage of property. During the final years of the ground lease, neither party may have an interest in restoring the project given the project's age and the ground lease's remaining term. As a result, the parties typically agree to lower the material casualty threshold in the final years of term so that the developer's restoration requirement is limited to minor casualty events.

In the casualty provisions, the parties also need to account for the potential requirements of the developer's lender who will seek to control the use of any insurance proceeds in the event of a casualty. For the public sector, the lender's right does not present an issue provided the lender agrees to have the proceeds used first for restoration. Repayment of any loan amounts should occur only in the event that the developer has the right to terminate without restoring the property. In the event that a casualty triggers a termination of the ground lease and pay out of proceeds, the parties need to work through the waterfall for these proceeds. The developer will seek to have proceeds first paid to it for the value of the improvements while the public sector will seek to have at least a portion of the proceeds paid to it for the value of its land. This tension again leads to the parties seeking an appraisal to determine the relative value of their interests in the property.

Reporting and Auditing: Providing for Transparency

By incorporating transparency measures into the ground lease, the parties are more likely to receive the necessary buy-in from public stakeholders and are more likely to achieve their collective objective of developing a successful project. When negotiating a ground lease with the public sector, a developer needs to understand that the public sec-tor must ensure that a transparent process occurs both for its own interests and the interests of its constituents. Since the public sector entity undertaking the ground lease likely has reporting obligations to public bodies and the public at-large, the public sector typically includes a robust set of reporting obligations on the part of the developer as well as significant auditing rights. With respect to reporting, the public sector has an interest in ensuring the project delivers on the commitments made in the ground lease and any ancillary agreements. In an economic development project, for example, the public sector wants to receive updates with respect to the number and types of jobs being created as well as average wages being paid. The public sector may also require a local hiring effort as part of the project, which requires additional compliance monitoring.

It also is worth noting that as the public sec-tor increasingly becomes subject to stronger transparency measures, the public sector in turn must ensure that it receives the information necessary to keep constituents apprised of project developments and whether the project is delivering the benefits promised. To ensure that the public sector receives the in-formation that it needs in a format that it can readily digest, the parties should agree at the time of ground lease execution on the appropriate format for periodic reporting. Additionally, the public sector is likely subject to the oversight of other public sector parties, so audit rights represent an important provision to work through. For example, in New York City, the city comptroller's office conducts audits of city agencies so these agencies must have the means to respond by having an appropriate level of audit rights.

In addition to compliance and audit, the developer must report on the project's financial operation to the extent that a participation rent comprises a component of the rental stream. Since the public sector from time to time may disagree with the calculations used for participation rent, the public sector needs the ability to more closely review the books and records of the project to make sure the calculations are fair and accurate. This is particularly important when participation rents are based on net income figures. To the extent that general overhead costs, for example, are being allocated to the project, the public sector wants to ensure that these costs are appropriately attributable to the project.

Conclusion

Although ground lease negotiations present challenges for both private sector and public sector parties, the nature of the process can allow the parties to work through these challenges to develop an agreement that aligns their respective interests and optimally al-locates risk over the length of the ground lease. For the public sector, the ground lease acts as means to invest in a project through the contribution of its property and potentially other public sector support and allows for a level of protections for the public sector that appropriately reflects the stage in which the project exists. For the private sector, the ground lease is a means to receive that public sector support while at the same time providing flexibility over time to adapt the project and its role in the project within parameters agreed upon at the outset of the term. Taken together, the ground lease provides the basis for a structuring a mutually beneficial long-term relationship between the public and private sectors.

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by Patrick J. O'Sullivan, Jr.

Herrick, Feinstein LLP

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.

[Bond Buyer Announces Finalists for 16th Annual Deal of the Year Awards.]

The Bond Buyer Tuesday announced the finalists for its 16th annual Deal of the Year awards.

Issuers were honored in eight categories, and all the award winners are also finalists for the national Deal of the Year Award, which will be announced at a Dec. 6 ceremony held at 583 Park Avenue in New York City. The winner will also be revealed online at BondBuyer.com later that evening.

For more than a decade and a half, the editors of The Bond Buyer have selected outstanding municipal bond transactions for special recognition. The 2017 awards, which considered deals that closed between Oct. 1, 2016 and Sept. 30, 2017, drew nominations that represent the full diversity of the communities and public purposes that are served by the municipal finance market.

“The nominees faced stiff competition from many eminently qualified deals,” said Michael Scarchilli, Editor in Chief of The Bond Buyer. “We chose the finalists for innovation, the ability to pull complex transactions together under challenging conditions, the ability to serve as a model for other financings, and the public purpose for which a deal’s proceeds were used.”

For the seventh year, the Deal of the Year gala will also include the presentation of the Freda Johnson Award for Trailblazing Women in Public Finance. This year marks the third in which the organization is honoring two public finance professionals; one from the public sector and one from the private. The 2017 honorees are Chicago chief financial officer Carole Brown and Julie Morrone, a principal at Rosemawr Management.

The finalists are:

NORTHEAST REGION
The Massachusetts Bay Transportation Authority’s $370 million issuance of sustainability bonds and bond anticipation notes. Proceeds of the offering, the first tax-exempt sustainability bonds ever issued in the United States, will go exclusively toward projects that benefit the environment or society more broadly.

SOUTHWEST REGION
The Fort Worth Transportation Authority’s first-ever transaction, a $325 million private placement to fund a commuter rail line that will alleviate traffic, provide much-needed rail service to Dallas-Fort Worth airport, connectivity to Dallas Area Rapid Transit’s rail system, as well as improving air quality.

MIDWEST REGION
The $1.3 billion inaugural financing from the newly-created Great Lakes Water Authority, among the most sizable water and sewer systems in North America. The sale unlocked substantial debt service savings for ratepayers and provided necessary funds for water system capital projects at an attractive borrowing rate.

SOUTHEAST REGION
The Kentucky Economic Development Financing Authority’s $472 million deal to benefit Owensboro Health. The sale represents the first new use of commercial bond insurance and first use of a surety in place of a Debt Service Reserve Fund in non-profit healthcare finance since the credit crisis a decade ago.

FAR WEST REGION
The Bay Area Toll Authority’s $1.9 billion sale as part of its San Francisco Bay Area Toll Bridge Seismic Retrofit Program. Over the past decade, BATA has completed more than $13.7 billion of bond financings and refinancings as part of the program, which has provided critical funding for retrofitting seven bay area bridges including the San Francisco-Oakland Bay Bridge.

NON-TRADITIONAL FINANCING
The City of Cambridge, Mass.’ $2 million sale of minibonds, with minimum denominations of $1,000, to fund city-wide municipal and school projects. The minibond structure allowed Cambridge to respond to an unmet need of its residents, who regularly expressed interest in actively investing in capital projects throughout the city.

HEALTHCARE FINANCING

Kaiser Permanente's $4.2 billion sale which represented the largest aggregate financing by a 501(c)3 healthcare institution, the largest taxable issuance by a 501(c)3 healthcare institution, and the largest Green Bond issuance by any healthcare organization. The California Health Facilities Financing Authority was the conduit issuer on the $2.1 billion tax-exempt component.

SMALL ISSUER FINANCING
The City of Missoula, Mont.'s $138 million sale of bond anticipation notes to purchase its water system from a private company. This was the inaugural financing for the city's newly formed water enterprise and the culmination of over six years of legal battles to purchase the water system through Montana's eminent domain statutes.

November 07 2017

Bondholders Fret as Alchemy Turns Chicago's Junk to Gold.

- **Chicago sales-tax securitization may herald trend for cities**
- **With money siphoned away, other bondholders left less secure**

Chicago's public pension debt is $36 billion and growing, it's facing $550 million in budget deficits over the next three years and this summer the state had to bail out a school system that was flirting with insolvency.

Yet next month, the nation's third-largest city — whose bonds were downgraded to junk by Moody's Investors Service two years ago — will start selling as much as $3 billion of debt that another rating company considers as safe as U.S. Treasuries.

That's because Chicago is selling off its right to receive sales-tax revenue from Illinois to a separate public corporation, which will issue new bonds backed by those funds, a structure called securitization. Because bondholders will be insulated from the city's finances and have a legal claim to the sales-tax money, Fitch Ratings deems the bonds AAA.

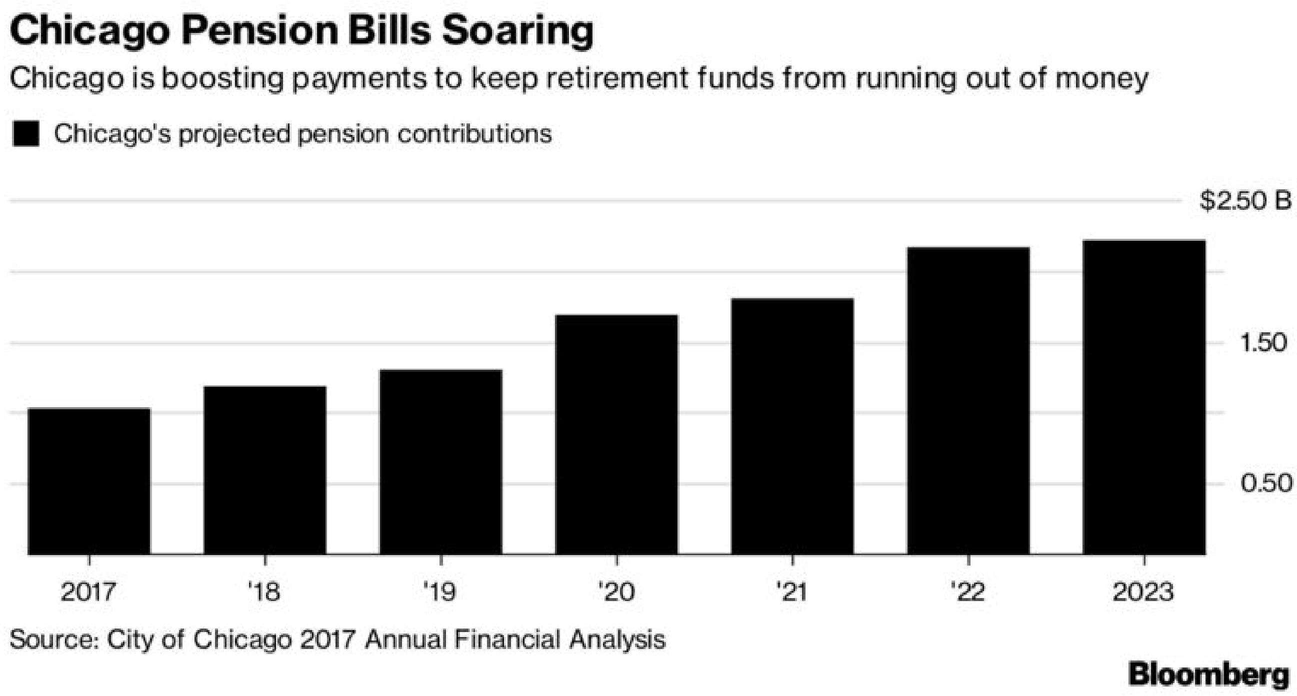
Some investors fear Chicago's approach may kick off a wave of securitizations by fiscally stressed municipalities that would increase their risk by siphoning away cash that backs bonds secured only by a promise to repay. Last month, Connecticut, which had a $3.5 billion two-year deficit, approved a budget that authorizes new debt backed by state income tax so it could receive a higher rating than the state's A+ general-obligation bonds.

"You are, through a process of alchemy creating AAA rated debt," said Christopher Dillon, a municipal bond portfolio specialist at T. Rowe Price Group Inc. "They've lowered their borrowing cost in the near term, but long term, it's just a continued degradation of the full faith and credit at the general-obligation level."

Detroit Casts Shadow

Since Detroit's bankruptcy four years ago, investors in the $3.8 trillion municipal market have given greater scrutiny to securities backed by a government's good word instead of a secure revenue stream. When that city emerged from court, holders of "limited" general-obligation bonds received 42 cents on the dollar for their investments, compared with 100 cents for owners of Detroit's water and sewer debt.

Institutional Investors from Pacific Investment Management Co. to Standish Mellon Asset Management Co. have said they favor revenue bonds, which don't compete for resources with public pensions, over general-obligation debt.



Creating separate entities to issue higher-rated debt isn't a new phenomenon. New York City, Philadelphia, Washington, Nassau County and Buffalo, New York, have all issued higher-rated dedicated-tax bonds to save money. But Chicago's sale comes as many cities face pressure from deeply underfunded pensions and opting for bankruptcy has lost some of its taint after a handful of governments did so after last decade's recession, though Illinois municipalities aren't allowed to take that step.

Chicago was extended the power to securitize its sales-tax payment by Illinois lawmakers this year. Paying off higher cost debt by issuing the new bonds will save Chicago almost $100 million in 2018.

Chicago's new bondholders will have a first claim to more than 90 percent of the approximately $715 million of sales-tax revenue collected each year, according to a presentation to Chicago's aldermen. The state, which collects sales taxes, will send the revenue directly to the bond trustee. Any excess revenue will go to the city.

“It just reeks of having your cake and eating it too,” said Triet Nguyen, managing director at NewOak Capital. “You can prioritize certain revenue but the general obligation-bonds are actually fine.”

The lower rating on Chicago's general-obligation bonds reflects all its debt, including securitizations and dedicated-tax bonds, and the government's ability to repay it, said Amy Laskey, a managing director at Fitch. The new bond issue hasn't affected that rating because the city is refinancing at a lower cost, not increasing its overall debt.

“The real sea change would be if they decided for some reason to issue a whole ton of debt that they hadn't planned to before,” Laskey said. “I haven't heard any indication from them that's the case.”

S&P Global Ratings grades the sales-tax securities slightly lower than Fitch at AA, the third-highest grade. They aren’t rated by Moody’s.

Puerto Rico Fight

Some investors say the legal battle now being waged in federal court between Puerto Rico’s general-obligation debt owners and sales-tax bondholders shows that legal structures like the one set up in Chicago are no guaranty when a borrower goes bankrupt or encounters severe financial distress.

In 2006, Puerto Rico passed a law creating a separate entity to issue sales-tax backed bonds with a legal structure similar to Chicago. The commonwealth approved a 5.5 percent sales tax and sent a portion to an entity known as Cofina. The new tax-backed bonds issued by the agency had a bigger margin of safety to pay debt service and garnered A+ ratings, five levels higher than Puerto Rico’s general-obligation bonds at the time.

This year, Puerto Rico entered into a form of bankruptcy and Cofina bondholders discovered the debt might not be so secure.

In June, the island said it may need more than $400 million in sales-tax revenue held by Cofina’s bond trustee for government operations. Cofina bondholders are fighting the move in bankruptcy court. General-obligation bondholders assert the money belongs to them, arguing that the territory’s constitution guarantees them a first claim on the government’s resources.

“We’re seeing these structures don’t always stand up the way they were designed to in bankruptcy,” said Tamara Lowin, director of research at Belle Haven Investments. “The market’s not putting as much faith in them as they have in the past.”

Bloomberg Markets

By Martin Z Braun

November 10, 2017, 4:30 AM PST Updated on November 10, 2017, 9:04 AM PST

— With assistance by Elizabeth Campbell

Chicago School Bonds Top Next Week's $9.84 bln Muni Bond Sales.

CHICAGO, Nov 10 (Reuters) – The junk-rated Chicago Board of Education will sell $922 million of bonds next week in the wake of a new Illinois education funding formula that allocates more money to the cash-strapped district.

The two-part bond sale, pricing through J.P. Morgan on Wednesday and Thursday, tops the $9.84 billion of bonds and notes selling in the municipal market in the coming week, according to Thomson Reuters estimates on Friday.

Escalating pension payments have led to drained reserves and debt dependency for Chicago Public Schools (CPS), the nation’s third-largest public school system.

The state funding formula enacted in August allocates an additional $450 million to CPS in the current fiscal year from new state money for operations and pensions and a local property tax increase.

“CPS is a different credit than it was just a few months ago,” Ronald DeNard, the district’s senior vice president of finance, said in an investor presentation.

But the district’s general obligation ratings remain in junk with major credit rating agencies. Ahead of the deal, Fitch Ratings upgraded the district to BB-minus with a stable outlook from B-plus, citing the additional state aid. It also noted a continued high dependence on cash-flow borrowing. CPS has said it will decrease its reliance on tax anticipation notes to $1.3 billion in fiscal 2018 from $1.55 billion the prior year.

S&P rated the GO bonds B with a stable outlook, noting the district’s “extremely weak liquidity and its vulnerability to unexpected variances in its cash-flow forecast.”

CPS will sell $632.5 million of GO refunding bonds and nearly $225 million of new GO bonds, as well as $64.9 million of dedicated capital improvement tax bonds that are rated at the investment-grade level of A by Fitch.

The biggest chunk of the GO bond deal, $441.7 million, will restructure 9 percent floating-rate debt that CPS sold in 2011, 2013, and 2015 into a fixed-rate mode.

Another low-rated Illinois issuer, the Metropolitan Pier and Exposition Authority, which owns Chicago’s McCormick Place convention center, will sell $475 million of new and refunding expansion project bonds through Citigroup on Tuesday. The bonds are rated BB-plus by S&P and BBB-minus by Fitch.

Meanwhile, U.S. municipal bond fund flows turned positive in the latest week, according to Lipper, a Thomson Reuters unit. Funds reported net inflows of $463 million in the week ended Nov. 8 compared to net outflows of $655 million in the prior week.

(Reporting By Karen Pierog; Editing by Chizu Nomiyama)

Republican Tax Bill Seeks Elimination of Some Municipal Debt.

CHICAGO — The U.S. House Republican tax bill released on Thursday would put an end to tax-exempt debt issuance by state and local governments for an array of health care, education, and economic development financing, which took municipal market participants by surprise.

The proposed elimination of low-cost funding through private activity bonds, which many in the $3.8 trillion U.S. municipal market were not expecting, would raise nearly $39 billion for the federal government over the next nine years, according to a summary of the legislation.

“This came as quite a shock,” said Barbara Thompson, executive director of the National Council of State Housing Agencies, noting that there had been assurances from Congress that private activity bond issuance would be retained.

Thompson said it would be devastating for the country’s production of affordable housing.

“The bill will increase borrowing costs and harm the ability of state and local governments to build and to maintain the infrastructure,” needed for critical health, education, ports, airports, and low-income housing, Sandy MacLennan, president of the National Association of Bond Lawyers, said in a statement.

Non-profit hospitals, which are major issuers of tax-free bonds to fund capital projects, would also be hit.

“For many communities, tax-exempt financing, such as private activity bonds, has been a key to maintaining vital hospital services,” Tom Nickels, executive vice president of the American Hospital Association, said in a statement.

“If hospital access to tax-exempt financing is limited or eliminated, hospitals’ ability to make investments in new technologies and renovations in the future will be challenged.”

Also on the chopping block are advance refunding bonds, which issuers in the U.S. municipal bond market use to take advantage of lower interest rates before outstanding bonds can be called.

“Current-law advance refunding bonds provide state and local governments with incentives to issue two sets of federally subsidized debt to finance the same activity,” the House bill’s summary stated.

Tax-credit bonds, which never really caught on with investors, would be repealed but federal tax credits for existing bonds would remain in place. Bonds issued for professional sports facilities would be subject to federal taxation under the bill.

The Alternative Minimum Tax would end under the legislation. That tax is applied to earnings from a small percentage of muni bonds sold by issuers such as airports and housing authorities that have substantial private-activity components in their deals.

The proposals are not a sure thing. The bill has a long legislative process ahead with changes expected before it could be voted into law.

Bill Gale, co-director of the Urban-Brookings Tax Policy Center, said the likelihood of the final bill including the elimination of private activity bonds was “not high.”

“It is hard to get support. There are an enormous number of revenue raisers in here and every one of them is politically going to be hard,” Gale said.

By REUTERS

NOV. 2, 2017, 9:30 P.M. E.D.T.

(Reporting By Karen Pierog; Editing by Daniel Bases)

[Denver Supportive Housing Social Impact Bond Initiative: Housing Stability Outcomes Report to the Governance Committee.]

Abstract

In February 2016, the city of Denver and eight private investors closed on the city’s first social impact bond (SIB), an $8.6 million investment to fund a supportive housing program for 250 of the city’s most frequent users of the criminal justice system. The city will make outcome payments over five years based on the initiative’s goals of housing stability and decreased jail days. This report details the first assessment of housing stability payment outcomes.

[Read the full report.]

The Urban Institute

Sarah Gillespie, Devlin Hanson, Mary K. Cunningham & Mike Pergamit

October 30, 2017

Fitch: U.S. Public Finance Upgrades Match Downgrades, Ending 13 Quarter Streak.

Fitch Ratings-New York-01 November 2017: The third quarter of 2017 marked the end of a 13 consecutive quarter streak in which U.S. public finance upgrades outnumbered downgrades, according to a new Fitch Ratings report.

Affirmations accounted for 78% of total rating actions in 3Q17, on par with 2Q17 result. "There were 35 upgrades and 35 downgrades in 3Q17, a decline from 94 and 37, respectively, in the prior quarter," said Jessalynn Moro, Managing Director and head of Fitch's U.S. Public Finance group. "Downgrades were driven largely by the healthcare and public power sector. Higher activity from the prior quarter was driven by completion of the tax-supported portfolio review under new criteria."

The downgrade of Puerto Rico's Sales Tax Financing Corporation (COFINA) senior and subordinate lien sales tax revenue bonds and the Employees Retirement System of the Commonwealth of Puerto Rico (ERS) pension funding bonds accounted for approximately 45% of all downgraded par. The number of Negative Rating Outlooks in 3Q17 declined to 96, marking the first time that Negative Rating Outlooks have fallen below 100 since 1Q08.

Also noteworthy, the healthcare sector experienced a marked increase in both Positive and Negative Rating Watches in 3Q17 compared to 2Q17 following the release of Fitch's 'Exposure Draft: U.S. Not-for-Profit Hospitals and Health Systems Rating Criteria' on Sept. 6, 2017. The U.S. nonprofit and healthcare systems sector is currently the only sector that holds a Negative Sector Outlook for the year.

For more information, a special report titled "U.S. Public Finance Rating Actions Third-Quarter 2017" is available on the Fitch Ratings web site at www.fitchratings.com.

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Bloomberg Brief Weekly Video - 11/02

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

Watch video.

November 2nd, 2017

Bloomberg

The Week in Public Finance: The Cost of the Opioid Epidemic, Connecticut's Budget and a Disaster Relief Bond.

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

GOVERNING.COM

BY LIZ FARMER | NOVEMBER 3, 2017

CDFI Fund Opens Application Period for Bond Guarantee Program.

Learn more.

CDFI Fund | Nov. 1

U.S. Municipal Debt Trading Drops in 3rd quarter of 2017.

Oct 31 (Reuters) – U.S. municipal bonds trading in 2017's third quarter dropped by 21 percent to $661 billion compared to the same period in 2016 and was the lowest par volume since 2016's first quarter, the Municipal Securities Rulemaking Board (MSRB) reported on Tuesday.

The number of trades in the latest quarter rose by 7 percent to 2.29 million with customer purchases accounting for most of the transactions, according to MSRB, the self regulator of the $3.8 trillion market for debt sold by states, cities, schools and other governmental and non-profit issuers.

Customer buying activity fell to an average daily par amount of $5.4 billion in the third quarter from $6.72 billion in the same quarter in 2016, the report said.

The heaviest trading was in Texas tax and revenue anticipation notes due in 2018 with a 4 percent coupon in both par amount and number of trades during the quarter. Other actively traded securities by par amount were Virginia's Tobacco Settlement Financing Corp bonds due in 2046 with a 6.71 percent coupon and state of Illinois bonds due in 2033 with a 5.10 percent coupon.

Issuers filed 30,869 disclosure documents with the MSRB during the quarter, with bankruptcy and default-related disclosures totaling 37. (Reporting By Karen Pierog; editing by Diane Craft)

S&P Credit Conditions: U.S. State And Local Governments Can't Rely On Robust Economic Growth To Solve Budget Imbalances.

Legislative gridlock in Washington appears to be taking the upper hand over proposed legislation designed to spur growth in the economy. This is keeping GDP growth low: S&P Global currently projects overall GDP growth of 2.1% in 2017, a tick downward from 2.2% in prior projections.

Continue reading.

Nov. 1, 2017

Should State and Local Governments Use Pay for Success Financing to Support Medication-Assisted Treatment (MAT) for Opioid-Use Disorder?

The increasing rate of opioid use disorder and overdose deaths has become a national opioid crisis, which has further increased pressure for policy-makers to "just do something." However, the opioid crisis is complicated, and it isn't always clear how state and local governments can improve the situations people are facing.

Pay for Success (PFS) is an innovative financing model that allows state and local governments to ensure their scarce resources are used for programs that actually improve people's lives. As one of the only evidence-based solutions available to help address the opioid crisis, implementing Medication-Assisted Treatment (MAT) through PFS financing may be an effective means for jurisdictions to "do something" that improves the situation. However, successful PFS projects also involve requirements that are not well-suited to every program.

This debate brings together policy researchers, medical practitioners, decision-makers, and PFS experts to discuss and debate whether state and/or local governments could (or should) use PFS to implement MAT as an approach to address the opioid crisis in their jurisdictions.

Continue reading.

The Urban Institute

Bloomberg Brief Weekly Video - 10/26

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

Watch video.

Bloomberg

October 26th, 2017

[The Number of Americans That Directly Own Bonds Fell to One Percent in 2016.]

The day when Americans bought and owned individual bonds are all but gone.

Direct household participation in the bond market has fallen to 1.3% in 2016, albeit from a relative low of 5% in 1989, according to a recent study by the St. Louis Federal Reserve.

But the falling cost of participation in financial markets should have smoothed over the path for more Americans to become investors. The expense of taking part in the markets' ups and downs have slipped thanks to the rise of passive investing and exchange-traded funds, which have pushed actively managed funds to cut their fees. This has made U.S. perhaps one of the best places to be an investor, according to a Morningstar report.

Continue reading.

MarketWatch

by Sunny Oh

Oct 25, 2017

Municipal Priorities: How To Avoid The Sinkholes.

Sometimes things go wrong with a corporation. It could be hugely disappointing quarterly revenues and earnings. Maybe low energy prices or competition annihilates the sector. It happens. Corporate bond prices of these disappointing companies also decline as their spreads to comparable maturing Treasurys widen.

Some examples of bad news we've seen are Under Armour, Macy's and other retailers getting 'Amazoned.' Hertz restating financials is another. You get the picture. A corporate bondholder can lose 5 to 10 points in a flash. The really bad news is announced and—BAM—it's instantly reflected in lower bond prices.

But the municipal bond market works differently from the corporate bond market. Munis respond to news in glacial time. There's no need to react to bad news in the next nanosecond. That's not the way munis trade. Investors have plenty of time to digest news, numbers and consequences before making a decision.

Continue reading.

Forbes

by Marilyn Cohen

October 24, 2017

Muni Bond Monday Update: 10-Year Yield Increases.

A look at the AP Municipal Bond Index for Monday, Oct. 23:

BIGGEST MOVER: One-year bonds. Yield climbed 5 basis points over the last week to 1.02 percent.

TWO-YEAR: Yield dropped less than a basis point to 1.09 percent. The two-year/10-year spread is 119 basis points, down from 121 basis points a week ago. The two-year/30-year spread is 176 basis points, down from 177 basis points a week ago.

10-YEAR: Yield increased 1 basis point to 2.28 percent, compared with 2.38 percent for a 10-year Treasury. The gap between 10-year municipal bonds and Treasurys has been widening over the last week. It was 2 basis points on Oct. 16. The 10-year/30-year spread for municipal bonds is 57 basis points.

30-YEAR: Yield rose by 2 basis points to 2.85 percent, compared with 2.89 percent for a 30-year Treasury.

The Week in Public Finance: Tax Reform Fast-Tracked, Puerto Rico's Cleanup Mishap and the Pension Penalty.

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

BY LIZ FARMER | OCTOBER 27, 2017

GOVERNING.COM

S&P: The Opioid Crisis Is Real, But Not Yet A Threat To State Credit Quality.

Does the current opioid drug epidemic pose a threat to state credit quality? The answer is probably not, although some states will be more affected than others, and the full costs are not clear. States have not precisely tallied the cost of the epidemic nor reported them in a comparable way.

Continue reading.

Oct. 31, 2017

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5 Good Reasons Why Local Governments Should Embrace Long-Term Budget Forecasting.

There are plenty of reasons why cities and counties focus on short-term fiscal needs. Here are some advantages for those who change that risky mindset.

SAN ANTONIO — In the world of city and county budgeting, the “balancing of the short term and long term is one of those inherent difficulties with local government."

That's according to Kurt Wilson, the city manager in Stockton, California. He should know. Wilson was appointed to his position in January 2014, just 10 weeks after the city of 300,000 residents located about 50 miles south of Sacramento had entered bankruptcy.

"A bankruptcy is the result of a series of bad decisions," Wilson said this week during an educational session on long-term budget forecasting at the International City / County Management Association's annual conference, which wrapped up Wednesday in San Antonio. "It's difficult for an elected official to make long-term decisions" when re-election and trying to please everyone are top of mind, he said.

Continue reading.

ROUTE FIFTY

BILL GRASS

OCTOBER 26, 2017

From P3s to 'Invisible Collection': How State and Local Agencies are Financing Fixes to US Infrastructure.

Infrastructure may not be high on the public's radar, at least until it fails or is preparing to do so.

If the Hudson River tunnel, which connects commuters between New Jersey and New York City's Pennsylvania Station had to shut down, the repercussions — and logjams — would reverberate all along the Northeast Corridor. The tunnel, which suffered severe damage from Superstorm Sandy in 2013, is now undergoing a $13 billion facelift as part of a $35 billion Amtrak-led program that will see improvements and upgrades to the region in an attempt to prevent the kind of disruption that would accompany tunnel closures.

When a fire under a bridge section along Interstate 85, one of Atlanta's busiest highways, caused it to crumble, state transportation officials pulled out all the stops to fast-track the project. The replacement work, which, under normal conditions, could have taken more than a year, took just 45 days — one month ahead of schedule — as a result of collaboration between the contractors, engineers and state agencies.

Though repairing the highly trafficked segment was a priority for stakeholders, cash incentives from the Georgia Department of Transportation for contractor C.W. Matthews undoubtedly helped the project team shave precious days off their schedule.

Still, the average infrastructure project wasn't making headlines until President Donald Trump made the issue of the nation's crumbling bridges, roads and other public assets, in addition to how to finance their repairs and replacements, a central tenet of his campaign. Trump and his advisers bet that the idea of private investment would take hold with American businesses and voters — and they were right.

P3s and their place in infrastructure

As was touted during his campaign, Trump until recently had been bullish on using the private sector to take on the task of a $1 trillion infrastructure agenda, including formalizing the campaign promise in his subsequent budget proposal. The president reneged on that proposal last month, saying public-private partnerships (P3s) would no longer play a significant role in his infrastructure agenda, though lawmakers and the construction industry still await details of his plans.

According to David Fernandez, a public finance attorney and shareholder at Buchanan Ingersoll & Rooney, it's going to be a long wait. That wait, however, could end if Congress is able to reach an agreement on tax reform. If all goes to plan for the Trump administration, the new program would see legislation that repatriates corporate earnings, perhaps creating new revenue streams to help finance such a massive program.

"You have to have the tax reform to make infrastructure work," Fernandez said.

But many states, whether unwilling or unable to wait for such a plan to be implemented, have begun turning to their own strategies to finance repair and modernization programs at home. Though the president has said he will no longer place his bets on the delivery method, many states are signing on to P3s to upgrade their infrastructure.

"The reason I like [P3s] is you're borrowing on the creditworthiness of the project," Fernandez said.

When government agencies borrow money for a capital project or for any other reason, the borrowing costs hinge on the public entity's credit rating. Private investors and the banks that private consortia tap to finance their part of these projects, however, look at the project's potential for success to determine risk and, ultimately, interest rates.

That is, of course, if the private part of the P3 is going to finance the project. More often than not, public entities use financing vehicles like municipal bonds or general obligation bonds to finance the work, John Brown Miller, president of the Winchester, MA–based nonprofit infrastructure consultancy the Barchan Foundation, said. Even P3s that finance public projects in exchange for compensation use a debt strategy of 80% to 85% of their total obligation, Fernandez said.

Invisible collection and the 'painless pain'

But state and local governments have other options for revenue streams, not just outside of bonds in P3 projects.

One method governments can turn to is imposing extra tolls or similar user fees like congestion pricing in order to pay for maintenance, repairs and new transportation projects. Some New York City officials are considering congestion pricing as a way to ease traffic by charging a premium for motorists traveling in and out of the area during certain high-traffic time periods.

Fernandez calls this method of collection "painless pain" because this invisible collection mechanism allows motorists to breeze through toll and other fee collection points without having to stop at a checkpoint and pay for the charge. The mechanism is the most obvious solution, he said, barring some type of on-the-spot collection system, which Fernandez said would likely lead to complaints about higher taxes and could potentially scuttle fee increases altogether.

Turning to the feds

Government agencies who may be short on funds may also try their luck applying for federal loans and grants.

If traditional lenders are involved, as in the case of a P3, Miller said, those lenders like to see loans like Transportation Infrastructure Finance and Innovation Act (TIFIA) low-interest loans used for extra financing. That's because the TIFIA loan obligation does not interfere with lenders' first position on projects in case of a bankruptcy or other financial setback.

The system, however, isn't perfect. In July, a Senate panel heard testimony on a potential expansion of the TIFIA program, as well as how to improve the loan process for future borrowers. A shortened timeline for responding to TIFIA letters of interest, better outreach to rural areas and revamping the existing credit-rating system were all cited as ways to improve the program.

Grants, Fernandez said, are contingent on the revenue stream backing them, and taxpayer pockets only run so deep. Relying on grants long-term, he said is not viable.

Still, they have made some projects possible, like the Minnesota Southwest light-rail, the Maryland Purple Line light-rail project and the CalTrain rail line electrification project.

Energy savings performance contracts (ESPCs) can also finance certain infrastructure projects today based on the projected savings those improvements will bring for decades to come.

For example, Johnson Controls is updating the state of Hawaii's port lighting to LED systems. The ports will save approximately $2.5 million a year on energy costs when the project is complete. The state calculated those savings over a 20-year time period, allowing the Hawaii Department of Transportation to use the $2.5 million to finance the LED project.

Those projects that can generate the most savings — those with the highest energy costs — are usually the ones that see the most benefit.

According to Russell Garcia, Johnson Controls' director of higher education for North America, public universities are using ESPCs to finance repairs and capital projects based on energy savings and, sometimes, operational savings. Depending on the type of agreement these universities strike with Johnson Controls, Garcia said, can sometimes transfer the risk of financing their projects on future savings through a guarantee that would see the company cover any shortfalls.

The University of California at Merced, Garcia said, is using an ESPC to finance a portion of its $1.3 billion campus expansion as part of its Merced 2020 Project.

As far as federal funding for infrastructure? Fernandez is optimistic but realistic.

"There are subtle ways the government is putting the structure into place."

Construction Dive

by Kim Slowey

Oct. 26, 2017

[Less Water, More Risk: Exploring National and Local Water Use Patterns in the U.S.]

Amidst a rising number of extreme weather events, service fluctuations, and other investment concerns, America’s water infrastructure is at a crossroads. Frequently overlooked and taken for granted, water is not just vital for life, but also provides an economic foundation for millions of businesses, farms, power plants, manufacturers, and households that depend on a reliable supply each day in the United States.

Despite seeing declining levels of water use in recent years, the U.S. still depends on nearly 355 billion gallons each day, an enormous total speaking to the breadth of uses nationally. Water use remains high in many cases, but it is also falling across the board as new conservation measures and technologies have been introduced. Utilities must confront several competing needs as a result: fixing aging, brittle infrastructure systems in service of a productive economy while generating less predictable revenues from lower levels of water use. Rising water bills, in turn, are helping to cover these costs and are often hitting lower-income households and other vulnerable users the hardest.

To provide reliable, cost-effective service, utilities—alongside local planners, economic development officials, and other leaders—need more detailed metrics and a better understanding of how regional water needs are shifting. By providing a comprehensive comparison of metropolitan and non-metropolitan water use, this report helps to meet this need. It not only highlights the scale and complexity of how users in different areas depend on water, but it also points to difficulties these users—and providers—face managing this scarce resource in an economically efficient and equitable way.

Continue reading.

The Brookings Institute

by Joseph Kane

Senior Research Analyst and Associate Fellow – Metropolitan Policy Program

October 20, 2017

Study Says New PABs for Public Buildings Would Add $8B in Economic Growth 1st Year.

WASHINGTON — Congressional passage of a bill that would allow private activity bonds to be used for public-private partnerships to finance public buildings would provide an economic boost of more than $8 billion in the first year, reports a study by the Beacon Hill Institute.

The Beacon Hill Institute, a free-market think tank based in Boston, analyzed the potential benefits of the Public Building Renewal Act, bipartisan bills (H.R. 960 in the House, S. 326 in the Senate) that the lead House sponsor will propose including in tax reform legislation.

Rep. Mike Kelly, R-Pa., who introduced the bill Feb. 7, plans to propose adding the Public Building Renewal Act to tax reform legislation when the House Ways and Means Committee votes on it in early November, his spokesman Tom Qualtere said Friday.

The bill would allow the issuance of up to $5 billion in new PABs for constructing government-owned buildings such as elementary and secondary schools, facilities used for educational purposes by state colleges and public libraries.

Kelly has 16 Republicans and 11 Democrats who are cosponsors in the House.

An identical version of the bill in the Senate has eight Republican and three Democratic sponsors.

The lead Senate sponsor is Sen. Dean Heller, R-Nev., who offered his bill at the same time and is a member of the Senate Finance Committee which will also vote on the details of tax reform.

The Kelly-Heller Public Building Renewal Act amends the Internal Revenue Code by expanding the definition of “exempt facility bond” to include bonds used for qualified government buildings.

Exempt facility bonds already are tax-exempt private activity bonds used for airports, highways, mass commuting facilities, sewage plants and other public purposes that may have some small private involvement.

The Beacon Hill study looked at 13 major public-private partnerships in the United States that have been undertaken using the existing laws ranging from the Port of Miami Tunnel in Florida to the Presido Parkway connecting the Golden Gate Bridge to the city of San Francisco.

Also on that list: the Denver FasTracks commuter rail and bus project and the new Goethels Bridge connecting New Jersey and the New York City borough of Staten Island.

“We estimate that, on average, P3s save 24.6% in project costs (design, construction, operation and maintenance),” the report said.

The Council of Development Finance Agencies, which annually tracks the issuance of PABs, supports the proposed legislation as a way of encouraging more cost-saving P3s.

“States and municipalities need more help if they’re going to rebuild their aging infrastructure, and passing legislation that encourages private investment in public facilities would go a long way toward solving that problem,” said Tim Fisher, legislative and federal affairs coordinator for the Council of Development Finance Agencies.

Beacon Hill said that passage of the proposed legislation “could provide a critical financing tool to speed the recovery effort” from the recent hurricanes that struck Texas, Florida and the U.S. Caribbean.

“According to the Houston Independent School District, 22 of its 245 schools had extensive damage that will keep them closed for months and about 53 have “major” damage,” , the think tank said.

Puerto Rico and the U.S. Virgin Islands sustained massive damage from Hurricane Maria that will require extensive rebuilding.

Beacon Hill estimated that the use of if P3s were used to finance 20% of all applicable state and local government buildings over time, this would result in $2.796 billion in building construction.

The Bond Buyer

By Brian Tumulty

October 30 2017, 6:00am EDT

Is the Trump Administration a Friend or Foe of America's Infrastructure?

As a candidate, Donald Trump deserved credit for identifying a policy that damages jobs, competitiveness, and economic growth: underinvestment in infrastructure.

Americans overwhelmingly agree. A poll this summer found that 89 percent of Americans believe infrastructure investment strengthens the economy, with 81 percent saying it would benefit them personally. More than half (56 percent) think U.S. infrastructure is in bad condition, compared to just 30 percent who say it is in good condition. Americans everyday confront the problems created by bad roads, broken public transit, ancient airports, and crumbling bridges, that are generations behind what is enjoyed in other parts of the world.

Unfortunately, Trump's plans as president could make the situation worse. Yes, he still promises a $1 trillion federal infrastructure package, but his proposed budget cuts to infrastructure are $55 billion more than the new federal dollars he included. Moreover, his tax plans and congressional politics suggest his overall impact on infrastructure likely will be substantially more negative.

Continue reading.

The Brookings Institute

by Blair Levin and Adie Tomer

Friday, October 27, 2017

Getting Shovel-Ready: Opportunities for Infrastructure Finance.

The Trump Administration identified infrastructure as one of its top priorities, yet legislation to boost private and public investments in infrastructure projects remains elusive. Leading a panel on *The $1 Trillion Question* at SIFMA's Capital Markets Conference in Washington D.C, Chris Hamel, Head of Municipal Finance at RBC Capital Markets, explored the state of infrastructure finance and how the policy debate on Capitol Hill may affect the ability of the public and private sectors to fund infrastructure projects.

"We track the P3 end of the market," said Stephen Howard at Barclays. Holding up a list of 43 projects across the country, Howard stated 25 have real potential for development. The same list five years ago was probably half this length. With gradual, incremental tweaks at the federal level, he expects the list to grow to 50-60 projects in the next five years with 30 likely candidates for development. Now, he said, "it boils down to how local jurisdictions can get shovel-ready projects."

"There is I believe plenty of capital," said Western Asset Management Company's Robert Amodeo. "I am bidding [on projects] every month whereas two years ago I was bidding every 12 months. There are more projects and they are more interesting, but there is still too much capital chasing too few investment opportunities."

U.S. infrastructure is so complex, noted the panelists, that a single policy option cannot address all existing concerns. Tax credits for instance, said Robert Andres, tax and economic policy advisor for the U.S. Senate Committee on Finance, are "a targeted tool but not a panacea."

The Administration has a role to play, and it doesn't necessarily need to be top-down, said Robyn Boerstling of the National Association of Manufacturers. Projects aren't getting built in some places and that is for a reason. "Multi-jurisdictional states are a headache – the Administration can and should find a way to break those logjams. Eliminate showdowns and slow downs."

At the close of the discussion, Hamel asked the panelists to envision they were invited to Mar--Lago. "What ideas would you pitch to the President on infrastructure?"

Amodeo called for better government coordination, optimization of vehicles used to get capital to communities, and seeking ways for the public sector to earn better returns on their portfolio. Andres urged a focus on funding. Boerstling said we should identify specific projects and lean on the strong support from the business community. Howard wants to expand the exemptions for private activity bonds and the Transportation Infrastructure Finance and Innovation Act (TIFIA) to support funding for greenfield projects.

SIFMA believes we can close the infrastructure gap by preserving the tax exemption of municipal bonds, expanding the use of private activity bonds, promoting design-build as a procurement mechanism for state and local governments, providing a tax credit for equity investors in infrastructure projects, expanding alternative federal financing programs, and permitting the use of new financial instruments for infrastructure finance. For more on our positions, see:

- SIFMA Statement on ASCE 2017 Infrastructure Report Card
- Financing Infrastructure: Why Public-Private Partnerships Matter

So, are we shovel-ready? Capital is ready and waiting. What we need now are the projects and the legislation to encourage them.

SIFMA

By Michael Decker
Michael Decker is Managing Director and Co-Head of Municipal Securities at SIFMA

October 25, 2017

Don't Expect Congress to Follow a Tax Reform Bill with Infrastructure Legislation.

WASHINGTON – Congress won't follow tax reform legislation with a big infrastructure bill, members of the Securities Industry and Financial Markets Association meeting here were told on Monday.

During a session called, "Infrastructure Finance: The $1 Trillion Question" at SIFMA's annual meeting, Michael Decker, a managing director and co-head of munis for SIFMA who was in the audience, asked panelists about the prospects for an infrastructure funding bill or whether infrastructure might be part of tax reform legislation.

The panel's moderator, Chris Hamel, a managing director and head of public finance at RBC Capital Markets as well as head of SIFMA's infrastructure policy committee, put his own spin on the question, asking, "A year from now will we be in this room discussing and celebrating the implementation of an infrastructure bill" or talking about whether there will be such a bill and what should be in it?

“No, we won’t,” said Bobby Andres, a tax and economic policy advisor to the Senate Finance Committee who stressed he was speaking personally and not on behalf of any committee or any member of Congress.

“If you want to get a bill done, you’re going to need money to do that bill,” he said. “As of right now, there is zero conversation happening about linking tax reform and infrastructure.”

“If you think that [Congress] is going to do a $5 trillion tax cut bill and then turn around in January and do an infrastructure bill of any substance … that’s just not going to happen,” he said. “And then what’s left is sort of the other regulatory changes, which would probably struggle in the Senate to get 60 votes.”Stephen Howard, a director and head of infrastructure at Barclays Capital, agreed, saying, “I don’t see a massive, transformative infrastructure bill on its own.”

“I don’t know how you pay for it,” said Robert Amodeo, head of municipals at Western Asset Management Co. “Because if we have tax reform that’s supposed to be revenue neutral and it’s not, how do you embark on another spending program without immediate returns?”

Amodeo explained that typically it takes three to five years to see returns from infrastructure spending and that there’s not an immediate boost in productivity.

However, if tax reform happens piecemeal, maybe that will increase the probability of infrastructure legislation, Amodeo said, adding, “I really think tax reform will drive whether we have infrastructure legislation or not.”

Andres said that it will be important for Congress, in debating tax reform legislation, to “do no harm to the current set-up” such as eliminating or restricting private activity bonds. “Let’s not screw up what we’re already doing right now, and then, [we can look at] what can we add on to that to make things look a little bit better.”

Amodeo and Howard said state and local governments and some private consortia are moving forward with infrastructure projects and are not waiting for federal dollars.

There was consensus among the panelists that plenty of capital exists for infrastructure projects.

Howard said that $200 billion per year is currently being invested in infrastructure projects today, if one looks at both tax-exempt and taxable bonds, bank loans and grants. “Let’s not mess it up, let’s add incrementally to it,” he said.

Howard and other panelists said there is a lot that administration officials are doing and can do to help infrastructure projects, such as Trump’s Executive Orders to streamline the permitting and the environmental process for projects.

Howard predicted the federal government will make incremental changes in grant programs such as the Transportation Infrastructure Finance and Innovation Act (TIFIA) or Water Infrastructure Finance and Innovation Act (WIFIA) to “incentivize innovation at the state and local level” for infrastructure projects.

He also predicted the federal government will take steps to expand the use of tax-exempt private activity bonds so they can help finance projects in which private parties participate.

Howard said tax regulators should not require the redemption or defeasance of outstanding tax-exempt bonds when those bonds have financed an existing publicly-owned asset that has been privatized.

Hamel asked the panelists if public-private partnerships will be part of the mix for whatever infrastructure policy initiative is advanced next year and whether some kind of infrastructure tax credit might provide revenue.

Despite President Trump's recent comments that he doesn't like P3s, Robyn Boerstling, vice president of infrastructure, innovation and human resources policy for the National Manufacturers Association, said, "I don't think public-private partnerships are going away."

Amodeo said, "We're going to build an American version of what we see globally, one where you can transfer the economic risk of a public asset while maintaining ownership by the public."

In the past munis have played the key role in infrastructure projects with the public taking on all the risk, he said. Now we have to invite private capital in to help share the risk without privatizing the asset. He said munis will continue to play "a very important role."

Howard said his firm tracks P3 infrastructure projects. It currently has a list of 43 such projects around the country. Half of those are transportation-related and half are split between social, environmental and other projects. Probably only half of the total 43 will move forward, he said, but the list is double what it was five years ago.

"I think we're going to see a gradual increase in the number of deals that under development with a bunch of small tweaks that are going to take place at the federal level," he said, adding that he sees his list of P3 projects growing from 43 to 50 or 60 in another few years, of which 30 will move forward.

Amodeo said he has "strong views" on tax credits. "I think they can blunt the incentive to control economic risks. I think it's a disaster, frankly."

He pointed to a project that involves the gasification of municipal waste. The product is to be added to jet fuel.

"The only reason this project is being built is because of the tax credits," he said.

"It does not work economically. So you have to be judicious in how you allocate tax credits."

Andres said tax credits have been very successful for some projects involving renewable energy and housing.

"But they are a targeted tool" and they can't be used as a panacea, he said.

Andres talked about the Move America Act (S.1229) that was introduced by Sens. Ron Wyden, D-Ore. And John Hoeven, R-N.D., in May. The bill would offer more financial options for P3s through a combination of a new class of private activity bonds and expanded tax credits.

The Bond Buyer

By Lynn Hume

October 24 2017, 12:57pm EDT

[Why Isn’t the Bond Market More Worried About Climate Change?]

Coastal towns destroyed by Sandy still have perfect credit scores. Why?

Early this month, when the annual king tide swept ocean water into the streets of Miami, the city’s Republican mayor, Tomás Regalado, used the occasion to stump for a vote. He’d like Miami residents to pass the “Miami Forever” bond issue, a $400-million property tax increase to fund seawalls and drainage pumps (they’ll vote on it on Election Day). “We cannot control nature,” Regalado says in a recent television ad, “but we can prepare the city.”

Miami is considered among the most exposed big cities in the U.S. to climate change. One study predicts the region could lose 2.5 million residents to climate migration by the end of the century. As on much of the Eastern Seaboard, the flooding is no longer hypothetical. Low-lying properties already get submerged during the year’s highest tides. So-called “nuisance flooding” has surged 400 percent since 2006.

Business leaders are excited about the timing of the vote in part because Miami currently has its best credit ratings in 30 years, meaning that the city can borrow money at low rates.* Amid the dire predictions and the full moon floods, that rating is a bulwark. It signifies that the financial industry doesn’t think sea level rise and storm risk will prevent Miami from paying off its debts. In December, a report issued by President Obama’s budget office outlined a potential virtuous cycle: Borrow money to build seawalls and the like while your credit is good, and your credit will still be good when you need to borrow in the future.

The alternative: Flood-prone jurisdictions go into the financial tailspin we recognize from cities like Detroit, unable to borrow enough to protect the assets whose declining value makes it harder to borrow.

The long ribbon of vulnerable coastal homes from Brownsville to Acadia has managed to stave off that cycle in part thanks to a familiar, federally backed consensus between homebuyers and politicians. Homebuyers continue to place high values on homes, even when they’ve suffered repeated flood damage. That’s because the federal government is generous with disaster aid and its subsidy of the National Flood Insurance Program, which helps coastal homeowners buy new washing machines when theirs get wrecked. Banks require coastal homeowners with FHA-backed mortgages to purchase flood insurance, and in turn, coastal homes are rebuilt again and again and again—even when it might no longer be prudent.

But there’s another element that helps cement the bargain: investors’ confidence that coastal towns will pay back the money they borrow. Homebuyers are irrational. Politicians are self-interested. But lenders—and the ratings agencies that help direct their investments—ought to have a more clinical view. Evaluating long-term risk is exactly their business model. If they thought environmental conditions threatened investments, they would sound the alarm—or just vote with their wallets. They’ve done it before—cities like New Orleans, Galveston, Texas, and Seaside Heights, New Jersey were all downgraded by rating agencies after damage from Hurricanes Katrina, Ike, and Sandy. But all have since rebounded. There does not appear to be a single jurisdiction in the United States that has suffered a credit downgrade related to sea level rise or storm risk. Yet.

* * *

To understand why, it helps to look at communities like Seaside Heights, the boardwalk enclave along the Jersey Shore whose marooned roller coaster provided the definitive image of the 2012 storm.

Seaside Heights was given an A3 rating from Moody's in 2013, meaning "low credit risk."* Ocean County, New Jersey—the county in which Seaside Heights sits—has a AAA rating. In the summer of 2016, before Ocean County sold $31 million in 20-year bonds, neither Moody's Investor Services nor S&P Global Ratings asked about how climate change might affect its finances, the county's negotiator told Bloomberg this summer. "It didn't come up, which says to me they're not concerned about it."

The credit rating agencies would deny that characterization—to a point. They do know about sea level rise. They just don't think it matters yet. In 2015, analysts from Fitch concluded, "sea level rise has not played a material role" in assessing creditworthiness, despite "real threats." Hurricane Sandy had no discernible effect on the median home prices in Monmouth, Ocean, and Atlantic Counties, which make up New Jersey's Atlantic Coast. The effect on tourism spending was also negligible.

"We take a lot from history, and historically what's happened is that these places are desirable to be in," explains Amy Laskey, a managing director at Fitch Ratings. "People continue to want to be there and will rebuild properties, usually with significant help from federal and state governments, so we haven't felt it affects the credit of the places we rate."

There are three reasons for that. The first is that disasters tend to be good for credit, thanks to cash infusions from FEMA's generous Disaster Relief Fund. "The tax base of New Orleans now is about twice what it was prior to Katrina," Laskey says, despite a population that remains 60,000 persons shy of its 2005 peak. "Longer term what tends to happen is there's rebuilding, a tremendous influx of funds from the federal and state governments and private insurers." Local Home Depots are busy. Rental apartments fill up with construction workers. Contractors have to schedule work months in advance. Look at Homestead, Florida, Laskey advised, a sprawling city south of Miami that was nearly destroyed by Hurricane Andrew. Today it is bigger than ever. "If there was going to be a place that wasn't going to come back, that would have been it."

What emerges from the destruction, for the most part, are communities full of properties that are more valuable than they were before, because they're both newer and better prepared for the next storm. Or as a Moody's report on environmental risk puts it, "generally disasters have been positive for state finances." But this is entirely dependent on federal largesse: After Massachusetts brutal winter of 2015, FEMA granted only a quarter of the state's request for aid. Moody's determined that could negatively impact the credit ratings of local governments that had to shoulder the cost of snow and ice removal.

Second is that people still want to live on the shore. "The amenity value of the beach is something you can enjoy every day of the summer," says Robert Muir-Wood, the chief research officer at Risk Management Solutions. "People may say, 'The benefits of living on the beach to my health and wellbeing outweigh the impact of the flood.'" That calculus is strongly influenced by affordable flood insurance policies, but it has not changed. In a way, despite the risks, the sea is a more dependable economic engine for a community than, say, a factory that could shut its doors and move away any minute.

Most bonds get paid off from property taxes. If property values remain high, bondholders have little to worry about. If, on the other hand, property values fall, tax rates must rise. If buildings go into foreclosure, or neighborhoods undergo "buy-outs" to restore wetlands or dunes, more of the burden to pay off that new seawall falls on everyone else.

Third: Most jurisdictions are large. New Jersey's coastal counties also contain thousands of inland homes whose risk exposure is much, much lower. Adam Stern, a co-head of research at Boston's

Breckinridge Capital Advisors, argues that the first credit problems will come for small communities devastated by major storms.

Still, Stern said, his firm looks at these issues. “One of the things we try to get at when we look at an issuer of bonds that’s on the coast: Do you take climate change seriously? Are you planning for that?” Still, he said, bond buyers—like everyone else—discount the value of future money, and hence future risk. When could the breaking point for the muni market come? Stern predicts that will happen when property values start to discernibly change in reaction to climate risk. It’s a game of chicken between infrastructure investors and homeowners.

“I think we’re in territory that’s changing right now,” says John Miller, an engineer studying climate change and credit risks at Wharton’s Risk Center. He pointed to Sea Bright, a barrier-island borough of New Jersey just south of New York Harbor. A municipal analysis concluded that by 2050, one in five of the borough’s parcels will be underwater—amounting to 17 percent of the total value of all Sea Bright real estate. Under 2050 SLR predictions, a 100-year flood would put 99 percent of parcels underwater. That year, 2050, is just beyond the 30-year frame used to sell both homes and bonds.

Generally, though, if you are looking for financial markets to start enforcing the risks of climate change, don’t look at towns on the rebound. Those places—whether they’re building seawalls or simply enforcing building codes on reconstructed properties—are better prepared. “The places you’re going to see the biggest disasters,” Muir-Wood predicts, “are the ones that haven’t been hit.”

Slate.com

By Henry Grabar

Henry Grabar is a staff writer for Slate’s Moneybox.

How Cities Are Defending Themselves Against Sea Level Rise.

HOBOKEN, N.J. — Superstorm Sandy and a series of lesser coastal storms since that 2012 disaster compelled some coastal communities to defend themselves by elevating homes and critical infrastructure, building sand dunes, widening beaches and erecting or raising sea walls.

But as sea levels continue to rise around the world, that’s not an option in large cities, where skyscrapers can’t be elevated and subway and train tunnels act as turbocharged flumes when millions of gallons of stormwater rush through them.

The answer, some cities have decided, is a mixture of hard and soft barriers; green infrastructure to capture rain and absorb storm water; temporary storage space for runoff; and drastically increased pumping measures.

Here’s a look at some steps being taken by cities around the world to address the issue:

LOS ANGELES

In addition to physical barriers and widened beaches, Los Angeles is planting trees and paving some roads with cooler surface material so that less heat is reflected. They and other cities have also baked sustainability and resiliency concerns into municipal polices on development.

“It’s a challenge and an opportunity at the same time,” said Matt Petersen, who served as the city’s chief sustainability officer until earlier this year. “Infrastructure and buildings are vulnerable to sea level rise. We can’t solely build our way out this this, but we can take steps to mitigate it long term. There are 150 million Americans that are vulnerable to sea level rise, and cities need to address that.”

The Port of Los Angeles recently added 6 inches (152mm) to the height of its proposed Wilmington Waterfront Promenade to compensate for anticipated sea level rise.

BALTIMORE

Baltimore requires new construction to have an additional two feet of elevation, and some existing buildings have been raised. The city uses bulkheads, and is integrating parks into green space flood-absorption areas. It is considering protective walls for certain vulnerable parts of the city.

LONDON

London is protected in part by a flood gate on the Thames River that can block exceptionally high tides or storm surges from the North Sea. Storm defenses were elevated for 11 miles (17.7 km) of the riverfront.

SHANGHAI and WUHAN

Flood gates and levees help protect the Chinese city of Shanghai. Elsewhere in China, the city of Wuhan is undergoing a test project to make it a “sponge city” capable of absorbing rain through a variety of green methods, including capturing stormwater and using it for its own water needs.

By THE ASSOCIATED PRESS

OCT. 27, 2017, 1:06 A.M. E.D.T.

KBRA Releases U.S. Not-For-Profit Healthcare Rating Methodology.

Kroll Bond Rating Agency (KBRA) announces the release of the methodology for rating U.S. not-fo--profit healthcare issuers. The methodology describes the major factors that KBRA considers when assigning a rating to not-for-profit hospitals and health systems.

Please click on the link below to access the methodology:

U.S. Not-For-Profit Healthcare Rating Methodology

If you have any difficulties accessing the methodology, please contact info@kbra.com or visit www.kbra.com.

Bloomberg Brief Weekly Video - 10/19

Taylor Riggs, a contributor to Bloomberg Briefs, talks with Amanda Albright about this week’s municipal market news.

Watch video.

October 19th, 2017

Bloomberg

Wells Fargo, Banned by California, Finds Way to Still Land Bonds.

- **Bank wins bidding for $554 million of state's debt sale**
- **As scandal takes toll, bank becomes bigger player in auctions**

Wells Fargo & Co. has been barred from being hired to underwrite California bond sales, but that hasn't kept it entirely on the sidelines.

The San Francisco-based bank won the bidding for $554 million of California bonds that were sold in an auction Tuesday, according to data compiled by Bloomberg. That sale came just one day after Treasurer John Chiang said Wells Fargo wouldn't be picked for state investment work for at least another year, a result of the nationwide backlash against the bank following revelations employees opened bogus accounts in customers' names to meet sales quotas.

The ban applies only to sales managed by an underwriter hired in advance, a method used for about three quarters of municipal-bond offerings. Wells Fargo hasn't been barred from auctions.

The "purchase clearly shows that we will continue Wells Fargo's strong, decades-long commitment to the State of California in order to support its issuers and state residents," Phil Smith, who runs the lender's government and institutional banking unit, said in a statement Wednesday.

With public officials in New York, Washington and Illinois also moving to sever ties to the bank, Wells Fargo's municipal-bond business has lost ground, slipping two ranks to the seventh largest this year, according to data compiled by Bloomberg. It appears to be bidding more aggressively in auctions to offset some of the impact: This year, it's the third largest underwriter of debt sold by competitive bidding, up from sixth in 2016.

Bloomberg Markets

By Laura J Keller and Danielle Moran

October 18, 2017, 9:13 AM PDT

Facing Sanctions, Wells Fargo Aggressively Pursuing Competitive Muni Bond Deals.

LOS ANGELES — Wells Fargo appears to be countering restrictions on its ability to act as senior manager on negotiated bond deals by going after competitive deals more aggressively.

When the news broke last year that the bank's employees had secretly created accounts without clients' approval, public officials in California, Illinois, Washington, Massachusetts and New York implemented restrictions limiting business with the bank on negotiated bond sales and institutional investments.

The bank has risen in the rankings both nationally and in California for competitive municipal bond deals, while its volume on the negotiated side has fallen dramatically.

“We suspended them from being senior underwriter on negotiated sales where the Treasurer picks the underwriter,” said Marc Lifsher, a treasurer’s spokesman. “Wells didn’t have the ability to get that business.”

Wells Fargo’s winning bid Tuesday on a $557.2 million competitive, tax-exempt chunk of California general obligation bonds shows that the bank “will continue Wells Fargo’s strong, decades-long commitment to the State of California in order to support its issuers and state residents,” Phillip Smith, Wells Fargo’s head of government and institutional banking, said in a prepared statement. The auction was one of three pieces of $1.6 billion in bonds the state sold competitively Tuesday.

“By law we cannot stop them from being the lowest bidder on competitive sales,” Lifsher said. “There’s more than money here. The sanctions caused Wells Fargo much reputational damage; and still is doing so.”

Wells fell nationally from a fifth-place ranking crediting it with $26.1 billion of municipal bond underwriting in 2016 to seventh with $15.8 billion so far this year, according to Thomson Reuters data. On the competitive side, nationally it rose to a sixth-place ranking with $7.1 billion so far this year compared to fourth place with $7.6 billion in 2016.

In California, it’s soared to the top slot on competitive deals with $2.6 billion in 2017 from a fifth place rank with $674.1 billion last year. In Golden State negotiated deals, it fell from No. 6 with $3.8 billion in 2016 to seventh place with $3.3 billion.

Just Tuesday, Wells Fargo won $557.22 million of California general obligation bonds out of $1.6 billion sold in an auction by California.

This year alone, Wells Fargo has purchased $1.3 billion in competitive bond sales from the state of California, according to Wells Fargo. The bank currently holds a 56% market share of the state’s debt sold competitively in 2017.

The treasurer’s restrictions do not apply to auctioned competitive sales, so although it wasn’t able to act as a senior manager on the $15.9 billion in negotiated bond deals for fiscal 16-17, the bank has been able to participate in competitive deals.

One Midwest trader opined that Wells “really paid” to win Tuesday’s competitive deal to stay in the state’s “good graces” and preserve the relationship with the state while it works through its troubles.

“It’s hard to speculate that that would be their intention,” said Matt Fabian, a partner at Municipal Market Analytics.

“California bonds do have a fair bit of upside relative to a lot of things out there right now, and the market has a decent chance of tightening further,” Fabian said. “It could simply be a market call on their part.”

Fabian added that double-A-rated California debt is going for a steep price now — and the market in general is pricing higher.

"Unfortunately, the current market context favors having the bonds to sell versus buying the bonds at the right price, so things like this will happen even without Wells or California being involved," Fabian said of what Wells Fargo paid to be the winning bidder.

On Monday, Chiang, who is touting his toughness on Wells Fargo as he campaigns for governor, extended sanctions on the San Francisco-based bank another year.

"California is our headquarters state," said the statement in response from Wells Fargo's Smith. "It is where more than 43,000 of our team members work and call home. And it's where since 1852 we have invested billions of dollars to help millions of homeowners, automobile owners, and small, midsize and large businesses."

He failed to return calls seeking further comment on how the sanctions have impacted the bank's business.

Chiang has also asked federal regulators to look into the bank's institutional banking practices. The focus of federal investigations thus far has been on controversies surrounding the retail banking business.

Including the cities of Los Angeles, San Francisco and Santa Clara, Wells Fargo has purchased $2.6 billion year-to-date of California state and local debt, including more than $1.2 billion of debt offerings just since September 2017. That equals about 31% of total state and local debt sold competitively in 2017, according to the bank.

The Bond Buyer

By Keeley Webster

October 19 2017, 3:08pm EDT

Markets reporter Aaron Weitzman contributed to this report.

U.S. Municipal Disaster Plans Seen More Vital for Ratings: Report

NEW YORK (Reuters) – U.S. state and city governments' planning for natural disasters will become more critical to their credit quality as costs to deal with extreme weather events increase, S&P Global Ratings said in a report on Tuesday.

"What we do expect is the severity of. these storms – in terms of financial impacts and the human impact as population tends to move toward urban, coastal cities – will grow over time," Kurt Forsgren, public finance analyst at S&P, said in an interview.

Costs to build more resilient infrastructure will increase, while federal disaster relief could become less certain, according to the report on how climate change affects credit quality.

If extreme weather becomes more frequent, municipalities might be unable to count on the traditional level of federal disaster relief after an event, Forsgren said.

Climate change can hurt municipal issuers, for instance, if sea levels rise and damage properties and their values, or increase electricity loads because of higher average temperatures, the report said.

“Overall, we see some municipal issuers recognizing, measuring, and reporting their impact on the environment as well as documenting how operations and capital planning are changing in response, but this is not widespread,” the report said, adding that California is leading the pack.

While relatively few credit downgrades have been prompted by natural disasters or climate risks, S&P said that number could rise if climate risks increase and are not mitigated.

The report came after hurricanes Harvey, Irma and Maria inflicted widespread damage on areas including Texas, Florida and the Caribbean.

On Tuesday S&P revised its outlooks on five Texas municipal utility districts to negative due to impacts of Hurricane Harvey.

Moody’s Investors Service downgraded Puerto Rico’s General Obligation bonds on Oct. 11 to Ca from Caa3, citing in a report protracted economic and revenue disruptions caused by Hurricane Maria.

by Stephanie Kelly

October 17, 2017

Reporting by Stephanie Kelly; Editing by Daniel Bases and Richard Chang

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The Week in Public Finance: Hartford Nears Default, Columbus Soccer Threatens to Move and More.

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

GOVERNING.COM

BY LIZ FARMER | OCTOBER 20, 2017

Is Your State Ready for the Next Recession? Chances Are, It's Not.

A new report says one-third of states will face severe fiscal stress during the next economic downturn.

Nearly a decade since the last recession started, most states still aren’t prepared for the next one.

Fewer than half of states have the funds they need to weather the economic downturn, and nearly one-third would likely face significant fiscal stress, according to a report released today by Moody’s Analytics.

The report conducted the first-ever stress test on all 50 state budgets to assess their ability to absorb a fiscal shock. It found that 16 states have enough in reserves to get through the next recession somewhat comfortably. Another 19 states have some or most of the funds they would need, which means they would likely have to raise revenue and/or cut spending, as well as tap reserves, to balance their budgets during a downturn. And 15 states are so “substantially unprepared" for the next downturn, they would face major "economic repercussions."

The idea of stress testing state budgets, which was borrowed from the U.S. Federal Reserve, essentially throws different economic scenarios at a state budget to see how revenues would be impacted. While the idea is popular with economists and ratings firms, only a few states actually conduct their own stress tests.

In its analysis, Moody's Analytics ran two different scenarios: a moderate recession and a more severe downturn that mimics the losses experienced during the Great Recession. The models took into each state's tax structure, revenue volatility, expected spending on Medicaid, and existing reserves and fund balances, among other things.

Having the proper cushion allows lawmakers to keep making policy when times are tough, rather than simply just reacting, says Moody's senior economist Dan White, the report's author. "If you have the reserves put away and don't have to worry about making ends meet," he says, "that gives you more time to focus resources on things that are really plaguing you — like the cost of Medicaid."

White's modeling gives states at least one or two years before the next economic downturn. That means places like California, Kentucky and Wisconsin, which have about half of the savings Moody's estimates they need, potentially have time to improve their position. But for the states with slim-t--no savings set aside (such as Connecticut, New Jersey and Pennsylvania), White says it's likely too late to make the needed adjustment before the next recession.

Many of the states that fall into the unprepared category are there because they haven't addressed their structural budget burdens. Pennsylvania, for instance, has consistently struggled with balancing its budget over the last decade. Part of the reason is that its Medicaid spending is gobbling up nearly 40 percent of the budget and giving it less flexibility than any other state. "They just really haven't had the breathing room necessary to set aside any amount for reserves," says White.

While many state budgets were seemingly blindsided in 2008 by free-falling revenues, White says there was at least one person in every state who should have known the recession was coming: the state Medicaid director. That's because enrollment jumped significantly beginning in the first half of 2008, nearly a year before revenues began taking a nose dive.

Medicaid enrollment in states that have expanded their programs under the Affordable Care Act is still increasing for noneconomic reasons. But White expects that to level off before the next downturn.

GOVERNING.COM

BY LIZ FARMER | OCTOBER 18, 2017

S&P Credit FAQ: Understanding Climate Change Risk And U.S. Municipal Ratings.

The U.S. municipal market has always faced credit exposure to hurricanes, floods, drought, fires, tornados, earthquakes, and other catastrophes. In addition to episodic event risk from natural disasters, S&P Global Ratings believes it is important to consider the current long-term credit…

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Oct. 17, 2017

P3 Digest, October 17, 2017

Maryland Governor Announces Ambitious Three-Highway Expansion

Maryland Gov. Larry Hogan announced plans to widen three of the state's most congested roadways in what he…

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S&P U.S. State Pensions: Funded Ratios Declined Again In 2016.

In the ninth year of this historically slow economic recovery, many states are experiencing budget pressure as fixed costs rise and revenue growth remains stagnant. The current recovery from the Great Recession over the previous nine years has been relatively slow for state economies and tax revenues, which has posed challenges for rebuilding reserves and investing in infrastructure.

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Oct. 18, 2017

S&P: U.S. State Retiree Medical And Other Postemployment Benefit Liabilities Keep Rising As States Prioritize Other Obligations.

Total unfunded state other postemployment benefit (OPEB) liabilities have increased, according to S&P Global Ratings' latest survey of U.S. states. Many states have completed new OPEB actuarial studies since our last survey (which used 2015 or previous studies) and total unfunded liabilities across all states increased $22.7 billion or 3.9% in fiscal 2016.

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Oct. 18, 2017

Addressing the Growing Need for Senior Living Projects Through Tax-Exempt Bonds: Orrick

A Guide for Senior Living Facility Owners, Developers and Operators

As Baby Boomers begin to reach their seventies and life expectancy continues to increase, the U.S. senior population is expected to grow significantly in the coming years and decades. In fact, according to the U.S. Census Bureau:

- The population aged 65+ is projected to more than double in size between 2014 and 2060
- The biggest increase is expected to start in just a few years in the decade from 2020 to 2030, when those aged 65 and over are projected to increase by 18 million to a total of 74 million people, accounting for more than 20% of the total United States population

As the senior population continues to grow, so does the need for housing built specifically for seniors, such as multifamily senior apartments, continuing care retirement communities, independent living and assisted living facilities, skilled nursing facilities and memory care facilities ("senior living facilities").

Read the article.

October.13.2017

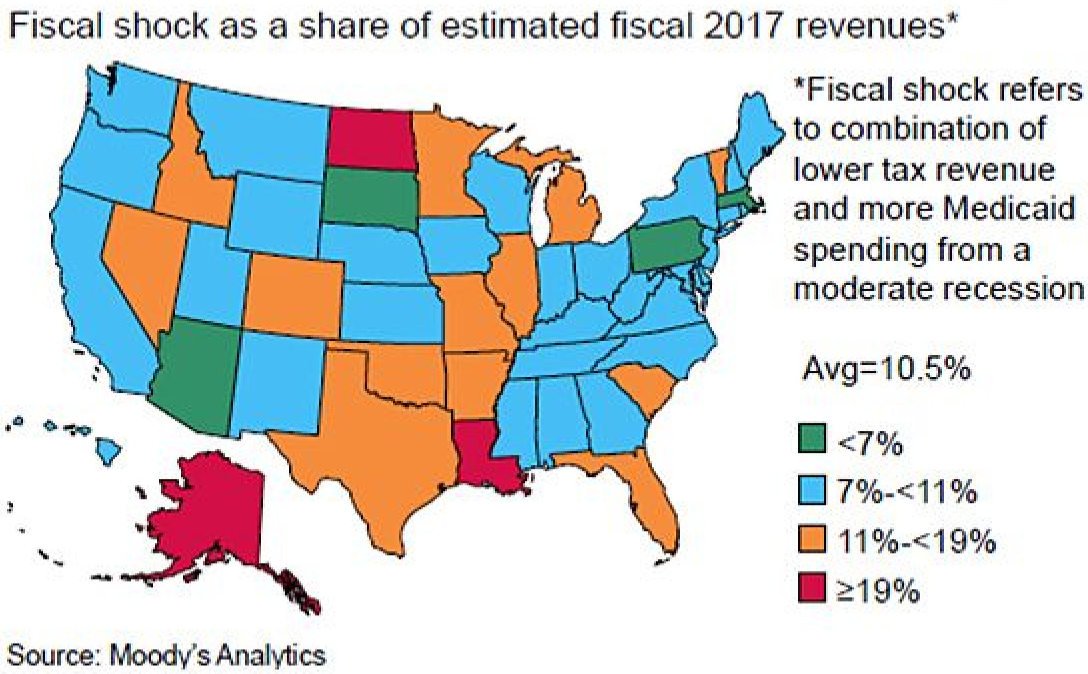
Orrick

These States Are the Least Ready for the Next Recession.

- **Moody's Analytics says 15 states not prepared for a downturn**
- **Louisiana, North Dakota, Oklahoma fare worst in stress test**

It's been more than eight years since the last recession, but nearly a third of America's states aren't ready for the next one.

Fifteen state governments don't have enough money saved to make up for the revenue that would disappear during a moderate recession, with Louisiana, North Dakota and Oklahoma the least prepared, according to stress tests conducted by Moody's Analytics. New Mexico, Illinois, Colorado, New Jersey, Pennsylvania, Missouri, Kansas, Virginia, Vermont, Arizona, Arkansas and Connecticut were also judged ill-equipped.



Moody’s Analytics isn’t forecasting a recession, though it said another one is only a matter of time.

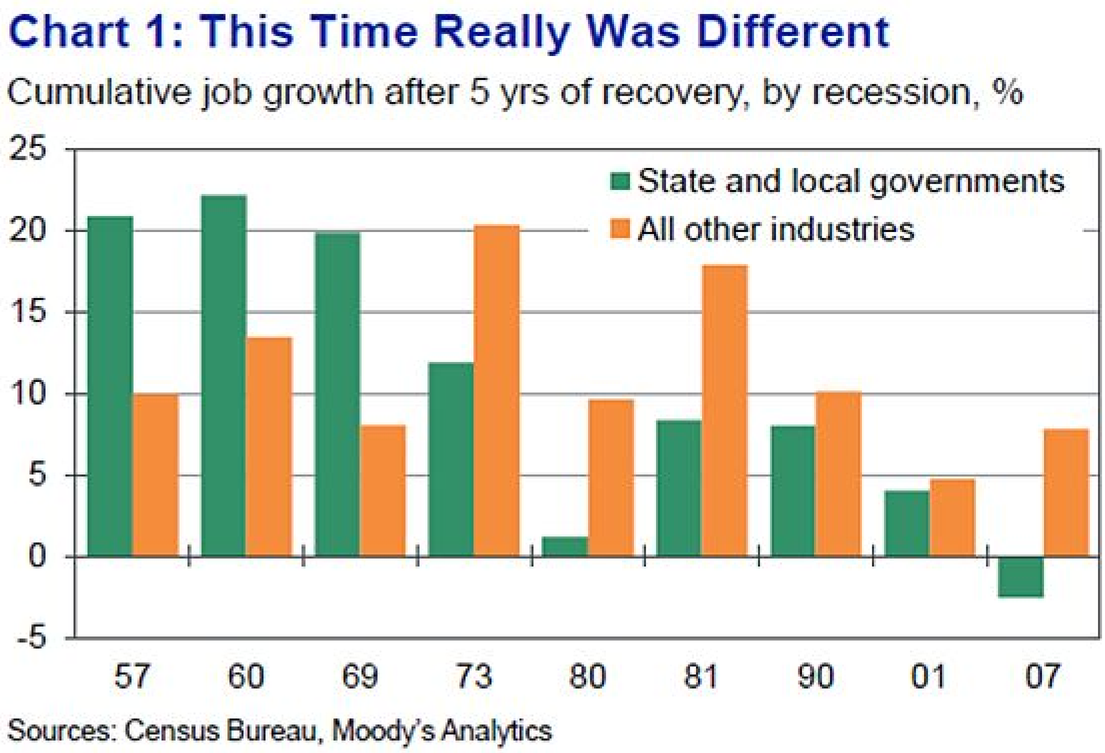
“A concerning number of states are still substantially unprepared for an economic downturn, and that level of unpreparedness will have economic repercussions if not addressed,” Moody’s Analytics economists led by Dan White wrote. “At the very least, states and local governments should be reviewing their reserve policies and checking on their adequacy following such a tumultuous fiscal period as the last decade.”

Despite the third-longest national economic expansion on record, soaring stock prices and an unemployment rate of less than 5 percent, many states are still having trouble balancing their budgets. Almost a dozen weren’t able to enact one by the time their new years started in July, and Connecticut still hasn’t. Pennsylvania did so, though lawmakers still haven’t figured out how to close the deficit that was left.

The median state rainy-day fund has enough to cover a little over 5 percent of the government’s general budget, according to Moody’s Analytics. That’s not too much more than what it was in 2008, which proved completely inadequate to offset the brunt of the Great Recession.

“This lack of preparation left some policymakers budgeting without a net at the worst possible time,” the analysts said in the report.

Once that recession struck, states and local governments shed almost 750,000 workers in the next five fiscal years, exerting further drag on the economy. Almost a decade later, municipal payrolls still haven’t returned to pre-recession heights, leveling off around 300,000 below the previous peak, according to Moody’s Analytics. State and local government employment is lower, on a per-capita basis, than at any time since the 1980s.



To come up with its list, Moody’s used state-by-state estimates of tax revenue shortfalls and Medicaid spending increases under a recession. The firm then compared that figure with the reserves held by each state as of fiscal year 2017. Moody’s Analytics regards states with a greater than 5 percentage point difference between actual and necessary reserves as unprepared.

Louisiana, the least prepared state, had a 24 percentage point difference between actual and necessary reserves. Alaska, the most prepared state, had 191 percentage points more in reserves than it would need under a moderate recession, according to Moody's Analytics.

States are more vulnerable to recession now than in the past, according to Moody's Analytics. Spending on Medicaid, the state-federal health-care program for the poor, is rising at a faster rate than revenue, becoming a much larger portion of budgets. Meantime, tax revenue collections have become volatile as states rely more heavily on progressive personal income taxes — and a smaller number of wealthy taxpayers — for revenue. Sales taxes are more stable but cover less of the service-oriented U.S. economy.

Energy and commodity states, like Alaska and Louisiana, and those that rely the most on progressive personal income taxes, such as California and New York, will experience more revenue volatility and should keep more in reserve, Moody's Analytics said. Meanwhile, Arkansas, with a much less volatile tax or economic structure, needs to save less, according to the report.

On average, a state would need to have more than 10 percent of its budget in reserve to weather a modest recession without having to resort to potentially drastic fiscal measures. It would take 16 percent to handle one akin to the last.

States should also develop better guidelines for using the funds, Moody's Analytics said. During the Great Recession, several states with "sizable reserves" used the money late or not at all as elected officials debated the true purpose of their reserves.

"As a result, several state rainy day funds were marginalized during one of the largest downpours in American history," according to the report. "This forced some states to take more severe fiscal actions than they otherwise might have, which subsequently weighed on the pace of economic recovery."

Bloomberg

By Martin Z Braun

October 17, 2017, 9:01 PM PDT

[Around the World, Private Capital is Solving Public Problems.]

The first ever Social Impact Bond ("SIB") was introduced in the United Kingdom when private investors funded an initiative aimed at reducing recidivism among inmates released from Peterborough prison.

Since its inception, it has achieved a rate of return of over 3 percent, while reducing recidivism rates by 9 percent. The financial return was contingent upon meeting a 7.5 percent reduction target set by the Ministry of Justice, which was exceeded. Today, there are approximately 89 SIBs in 19 countries addressing an increasing array of social issue.

SIBs are a financing tool in which governments contract with private entities to produce measurable results in areas such as criminal justice, substance abuse, early childhood development, homelessness, workforce development, and public health. Start-up capital is raised from investors, frequently with backing from foundations. But a financial return is only secured if a predetermined set of objectives are realized. In other words, if an initiative fails to meet its targets the loss is absorbed by investors not taxpayers. Under this “pay for success” model, governments only pay if and when certain goals are achieved.

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The Hill

BY DOUGLAS SINGLETERRY AND ZENON CHRISTODOULOU, OPINION CONTRIBUTORS

MSRB Investor Guide to Monitoring Muni Bonds.

Are muni bonds part of your retirement savings plan? Check out our investor guide on monitoring bonds.

How Optimistic Math Conceals Depth of America’s Public Pension Crisis.

Minnesota’s funded ratio fell more than 30%, leaving its state pension funded at 52.10%, according to S&P Global Ratings

Minnesota’s state pension funds became the seventh most underfunded in the country in 2016 after its largest fund lowered its expected rate of return to a more realistic level.

The move highlighted how optimistic return estimates for public pension funds have helped disguise the extent of America’s pension crisis and underscored how teachers, firefighters and other public employees may end up looking forward to a smaller safety net.

Minnesota’s actions were prompted by the Government Accounting Standards Board, which has pushed state pension funds to base their funding ratios on more conservative forecasts on their investments. In response, its largest pension fund for public-sector workers slashed its expected return from 7.90% to 4.17% for fiscal 2016.

Continue reading.

MarketWatch

by Sunny Oh

Published: Oct 23, 2017 8:19 a.m. ET

Planning For the End of LIBOR: Holland & Knight

By 2021, it is likely that LIBOR will no longer exist, and even more likely that it will no longer be the leading global benchmark interest rate. This news comes from the U.K. Financial Conduct Authority’s (FCA) announcement that after 2021, it will no longer make the reporting of interbank lending transactions on which LIBOR is based mandatory.1 That change, together with criticism that LIBOR rates are no longer supported by sufficient underlying market data and the rate fixing scandals in recent years suggest LIBOR's days are numbered.

The discontinuance of LIBOR would affect most financial markets, including the aviation finance industry. Many aviation finance transactions incorporate some form of a floating rate based on LIBOR whether it be in the form of a floating rate loan, floating rent rate, or default interest rate pegged to the benchmark. It is prudent to assess existing and future transactions that will remain in place past 2021 to ensure that they contain suitable provisions for selecting a replacement rate.

Lack of Data and Scandal

The London Interbank Offered Rate (LIBOR) was created almost 50 years ago to track the interest rate at which certain large institutional banks lend unsecured funds to each other in multiple currencies and for twelve different tenors on the London interbank market. LIBOR rates are created based on information supplied to the ICE Benchmark Administration by a panel of 20 banks that participate in the London interbank market. The panel is required to submit interest rate data from actual interbank loan transactions, and where no such transactions have taken place, the LIBOR rate is based on the submitting bank's traders' estimates of what the rate of an actual interbank loan on that date would have been. The published rates are the average of all submissions.

A dramatic decrease in interbank lending has left LIBOR as more a representation of expert opinion than a summary of actual market activity.2 According to Andrew Bailey, the head of the FCA, the number of certain interbank loan transactions has dropped down below 20 per year. For a rate that is set daily, this means that on most days the rate is set based on expert opinion alone. This lack of actual data, coupled with the recent LIBOR rate fixing scandals, are likely to spell the end of the benchmark. Since 2012, banks have been fined over USD$ 9 billion for fraud, collusion and manipulation of LIBOR rates.3

Alternatives to LIBOR

Belief that the end of LIBOR is near is strong enough that governments worldwide have started looking at replacement options. A few alternatives are starting to build momentum, but there is no consensus around which rate will replace LIBOR as the market standard benchmark. In fact, there is speculation that no single replacement will emerge and instead LIBOR could be replaced by multiple benchmarks, leading to a more fractured market and greater complexity for negotiating parties.

To address the end of LIBOR, the United States government created a panel of fifteen large U.S. banks called the Alternative Reference Rates Committee (ARRC). In June, the ARRC endorsed the use of what has come to be called the Broad Treasury Financing Rate (BTFR), which will be published by the Federal Reserve Bank of New York as the best practice for U.S. dollar derivatives and financial contracts.4 The intricacies of the BTFR are currently undergoing a public review and comment period, after which it is expected that the rate will be published beginning in the middle of 2018. Generally, the BTFR will represent the interest rate at which banks and others will fund overnight loans secured by U.S. government debt.

In the United Kingdom, the leading alternative appears to be the Sterling Overnight Index Average (SONIA), which reflects the rates for unsecured short-term transactions tied to the pound.5 SONIA's scope is more limited than LIBOR since it only covers sterling while LIBOR covers five different major currencies, and SONIA only measures the overnight rate while LIBOR covers seven maturities from overnight to 12 months.6 These limitations may hinder SONIA's adoption globally.

Existing Documentation

Aviation finance industry participants should review their existing documentation which incorporates LIBOR and may have a term or tenor through 2021 or beyond. LIBOR is used in loan documentation (secured and unsecured), all varieties of leases (with or without floating rent rates), MRO general terms agreements, and even guaranties or other credit support documentation. Even where the principal payment obligation is not a floating rate, documentation can have other types of floating rates that incorporate LIBOR such as default interest rates, or fixed to floating rate conversion options.

Documentation that incorporates LIBOR but lacks a mechanism for selecting a replacement when LIBOR is no longer available should be amended in the coming years if it is expected to remain in place past 2021.

However, documentation that incorporates LIBOR usually includes a mechanism for determining the applicable interest rate if LIBOR becomes unavailable. Here are some thoughts on assessing the adequacy of three of the most common varieties of replacement provisions:

- *Successor Provisions.* These provisions indicate that if another entity takes over the publishing of LIBOR from the ICE Benchmark Administration, or if the LIBOR rates are published in a different way in the future, that such successor publisher or means will be the new rate. These provisions won't be of much use if LIBOR ceases to exist.
- *Interpolation and Alternative Information Source Provisions.* Provisions that empower one party to interpolate between other available LIBOR rates if the LIBOR rate of the selected tenor is no longer available will not be of use if the benchmark itself no longer exists. Similarly, provisions that empower one party to select a different source for the screen rate will not be of use if the underlying benchmark is not available anywhere.
- *Unilateral Selection.* Another type permits the creditor party to unilaterally select a suitable replacement if the LIBOR rate is no longer available or no longer the market standard. Sometimes these provisions require consultation with the borrower, sometimes not. While we are likely to experience a period without a clear market standard alternative to LIBOR, generally speaking this type of a provision will still give the parties sufficient certainty that a suitable replacement will be selected when that time comes. In syndicated loan documentation, borrowers may wish to have the selection of a replacement rate require the approval of a majority of lenders, rather than requiring unanimous approval to expedite the selection of a new rate once a market consensus is reached.
- *Reference Bank.* Finally, so called "Reference Bank" provisions specify that a particular interest rate offer from a specified private bank or the average of rates supplied by a few banks will be the replacement rate if LIBOR is unavailable. This type of provision, which is found in standard LMA and LSTA documentation, is intended to resolve short-term LIBOR interruptions, but leaves considerable uncertainty if utilized indefinitely and should not be viewed as a practical permanent solution. For example, it is likely to result in a party paying different rates of interest under different deals that are on the same commercial terms but appoint different reference banks.

By the time LIBOR reporting is no longer mandatory, there ought to be greater consensus around the suitability of available replacements. For now, parties should be cautious about incorporating a LIBOR replacement they are not already familiar with. Until consensus grows in the financial sector, parties need to ensure that their existing documentation and new documentation contain adequate provisions for selecting a suitable replacement in the future.

Footnotes

1 https://www.fca.org.uk/news/speeches/the-future-of-libor

2 In 2015, about 70% of the bank submissions were experts guesses. http://www.businessinsider.com/demise-of-libor-part-of-massive-global-trend-many-overlook-2017-9

3 https://www.lexology.com/library/detail.aspx?g=342c165d-5c56-4cb5-a1cb-5a15696e91ca

4 https://www.newyorkfed.org/medialibrary/microsites/arrc/files/2017/ARRC-press-release-Ju--22-2017.pdf

5 https://www.lexology.com/library/detail.aspx?g=342c165d-5c56-4cb5-a1cb-5a15696e91ca

6 https://www.lexology.com/library/detail.aspx?g=342c165d-5c56-4cb5-a1cb-5a15696e91ca

Last Updated: October 17 2017

Article by Nathan Leavitt and Yue Qi

Holland & Knight

Nathan Leavitt is a Partner and Yue Qi is an Associate in the San Francisco office

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.

The Next Green Revolution: An Overview of the Rapidly Evolving Green Bond Market.

This article is from the Nonprofit Quarterly's fall 2017 edition, *"The Changing Skyline of U.S. Giving."*

Responsible investment means incorporating environmental, social, and governance (ESG) factors into investment decisions to generate sustainable returns and better manage risk. On a human level, it means incorporating the desire to make a difference in the world into the investment process. Green bonds, fixed income instruments that fund projects with environmental and/or climate benefit, are a type of responsible investment.1 More broadly, they are an example of leadership from the investment community in addressing the threat of climate change. In the wake of recent catastrophic hurricanes, this article provides an overview of the green bond market for potential investors and issuers seeking to do more to protect the planet.

Market Size and Trajectory

Green bonds have grown rapidly since they were invented by investors in 2007 to fund projects with climate or environmental benefits. Since then, two categories of green bonds (labeled and unlabeled) with four main structures (use of proceeds, revenue, project, and securitized) have emerged from a broadening range of issuers. Global green bond issuance is projected to double in 2017 from $93.4 billion of issuance in 2016,2 after doubling from $42 billion in 2015.3 With the Paris Climate Agreement and China's clean energy campaign as drivers of continuing growth, this deep dive into the emerging asset class is warranted. By way of background: under the Paris Climate Agreement, investors with an aggregate $11 trillion of assets under management (AUM) committed to build a green bond market,4 and the United States committed to reducing its greenhouse gas emissions 26 to 28 percent below the 2005 level by 2025.5

Continue reading.

NONPROFIT QUARTERLY

By BHAKTI MIRCHANDANI | October 10, 2017

Market Commentary: Muni Market Digests Large Supply With Much More to Come This Week.

This Market Commentary is part of *Court Street Group's Perspective*. A PDF of the full report is available here.

The first full week of October saw municipal bond interest rates move into lower ranges amid larger supply and continued anemic fund flow figures. The end of the third quarter saw high-grade bonds track about 20 basis points higher in the intermediate and longer-ranges of the yield curve.

Continue reading.

by Lynne Funk Posner

Posted 10/13/2017

Neighborly Insights

Credit Focus: State Revenue Scoreboard - CA, MA, MO, AR, GA, MS

This *Credit Focus* is part of *Court Street Group's Perspective*. A PDF of the full report is available here.

Disclosure of Revenues a Credit Positive

It seems that the states are realizing that more regular and timely disclosure of state revenues can have a beneficial impact in supporting their debt both during and after the marketing for their bonds. They seem to be realizing the municipal analysis is moving in a more quantitative direction all the time and that data is the key to this analysis. The demand for information — historically available to a limited number of inside government players — is bolstered by a more information savvy generation of analysts and investors as well as the ability of states to disseminate data through the internet that satisfies any regulatory concerns. As a result, the availability of such information expands constantly.

As as a result, we are able to comment on current state revenue results like the following:

Continue reading.

by Joseph Krist

Posted 10/13/2017

[S&P: Rising OPEB Liabilities For The 15 Largest U.S. Cities Could Strain Budgets And Pose Credit Risks.]

S&P Global Ratings' survey of the 15 largest (by population) U.S. cities' other postemployment benefits (OPEB) liabilities shows that these remain largely unfunded, face funding pressures, and pose a long-term credit risk. This is especially the case as health care costs continue to rise, the U.S. population continues to age, and uncertainty persists regarding the Affordable Care Act and Medicaid.

Continue reading.

Oct. 10, 2017

[Bloomberg Brief Weekly Video - 10/12]

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

Watch video.

October 12th, 2017

Bloomberg

[Pay for Success and the Savings Trap.]

Saving money isn't the point. The conversation should be about government effectiveness and positive outcomes.

"So, how does this *really* save our jurisdiction money?" I get this question about "pay for success" projects all the time, and I dread it — not because I can't answer it but because it's pernicious. It sounds practical and technocratic, but it's neither. It conceals an intricate web of misunderstanding about why and how to fund, manage and evaluate public programs.

What's more, this is largely a self-inflicted wound. From its inception nearly a decade ago, many of us involved with pay for success (PFS) have described it as a way to deliver "cashable savings." It's not. Framing it that way is both an over-simplification and a fundamental misreading of how the public sector works.

PFS projects are a way for governments to fund social programs on the basis of their performance. Parties agree on what outcomes constitute success and how to measure them, and then put a price tag on how valuable each outcome is. But most nonprofits that provide program services can't afford to wait to get paid until outcomes are achieved and can't bear the financial risks of a negative result.

That's why working capital for PFS programs is often provided by "impact investors," those who seek to generate social and environmental impact alongside a financial return.

Cost savings aren't the point — not for PFS projects and not for governments. The point is to create safe, just and prosperous communities at a reasonable cost to taxpayers. The idea that, for example, helping the homeless find stable housing has to save money is ludicrous; we support the homeless because the kind of society we want doesn't let the most vulnerable among us live, and too often die, on the streets. In plenty of areas this is obvious: K-12 education is incredibly expensive, doesn't show any fiscal return for decades and pays off over a lifetime — and is one of our most important public institutions.

Of course, some programs do drive down costs, and good cost-benefit analyses are valuable tools for making decisions. But we should be humble about our ability to predict the future. Sophisticated models can't tell us whether a new drug will stop a disease in its tracks, or whether treatment costs will plummet, or whether policies will change. Each of these dynamics changes the "savings" picture dramatically.

What is really misleading about the idea of cashable savings, though, is that "cashing" them is ultimately about effective governing. If, for example, a PFS program reduces days people spend in jail by 25 percent, it will mean fewer incremental costs, such as for inmates' food and clothing. But most of the real value will come from personnel. There will be less work for staff members — corrections officers, janitors — to do. A county can decide to "cash" those "savings" by downsizing jail staff, or it can decide to put these staffers to work on other tasks. Deciding to extract savings from the budget is a political question separate from programmatic success. It's the job of public leaders to decide what to do with the value created by good programs: extract and reallocate it, or reinvest it.

A better way to talk about programmatic success is in terms of effectiveness. Instead of focusing on the cost of services, we need to start focusing on the cost of getting good outcomes. Take the cost of high school. If our state spends $10,000 per student per year and graduates half of the class, we're paying $80,000 per graduate. If by spending another $1,250 per student per year we can boost graduation rates to 90 percent, we won't "save" any money, but we'll get a lot more bang for taxpayer's buck by paying only $50,000 per graduate.

This is what pay for success is about: not cashable savings but government effectiveness.

We need to start having a more sophisticated conversation about the value of programs and stop hiding behind the false simplicity of cashable savings. Governments need to redefine the terms of engagement to more thoughtfully make tough decisions about where to spend taxpayers' money. That's the only way we'll be able to accomplish something refreshingly bipartisan: getting more value out of our government spending.

GOVERNING.COM

By Jake Segal | Contributor
Director of advisory services for Social Finance

October 16, 2017

The Week in Public Finance: California's Wildfires, Illinois Going Into More Debt and Kentucky Embraces P3s.

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

GOVERNING.COM

BY LIZ FARMER | OCTOBER 13, 2017
