

CITY OF MINNEAPOLIS

Introduction to City Debt Obligations

Ways & Means Committee

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Minneapolis
City of Lakes

Introduction to City Debt Obligations

- **What is a Debt Obligation, or a “Bond”?**
 - In return for receiving cash now, a promise to repay lender, with interest, over time.
- **“Bonds” versus “Loans”**
 - Generally, loans are made by a specific lender, and have terms and conditions negotiated between the lender and the borrower, usually including a specific maturity date and interest rate;
 - Bonds are securities, with varying maturity dates and interest rates, sold into the capital markets, with a given “issue” of bonds having similar characteristics except for maturity and interest rate
- **Why does City issue debt?**
 - Provide cash for large capital projects;
 - In certain circumstances, provide cash for a 1-time infusion to fund a multi-year operational matter (e.g., fleet, pensions, facilities, technology, etc.);
 - Source of cash to lend to private/non-profit partners to *finance* their projects

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- **Types of City Bonds (and principal outstanding as of 3/31/14)**
 - General Obligation – tax-backed: Annual levy of property taxes provides revenue to repay principal and interest; outstanding principal = **approximately \$160M**
 - General Obligation – revenue-backed: While promising to levy property taxes if necessary, source of repayment is a dedicated revenue stream (e.g., parking revenue, utility rate revenue, property assessments, etc.); outstanding principal = **approximately \$630M**
 - Revenue-backed: direct revenue pledge only, no general tax pledge; only City debt currently of this type is certain Tax Increment-backed bonds; outstanding principal = **approximately \$25M**
 - Common Bond Fund: specialized, structured financing vehicle for economic development projects; bonds secured by lease payments from borrowers, with additional reserve requirements and limited City tax pledge; outstanding principal = **approximately \$95M**
 - **Total City Debt outstanding = approximately \$910M**
- **Other City Issuance**
 - Conduit borrowings: City issues bonds, lends proceeds to non-profit entity (including large health-care enterprises) or housing developer. Repayment solely responsibility of borrower; City has no repayment obligation; outstanding principal = **approximately \$2.4B**

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- **Tax-Exempt versus Taxable**

- Subject to IRS regulations, interest earned on municipal bonds is tax-exempt when issued and used for a *public purpose*; lowers governmental borrowing cost
- In certain situations, when bond proceeds are used for benefit of a *private purpose*, interest is taxable

- **Public versus Private Purpose**

- Public Purpose: Streets, Public Buildings, etc.
- Potential Private Purpose: Arenas, Development Financing

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- **Bond Issuance Process (Downtown East example)**
 - Bond Resolution (attachment A): provides legal framework and authorizes issuance; adopted by Council and sometimes BET as well
 - Underlying financing documentation and contracts (attachment B): specify rights and obligations of all parties to the transaction
 - Official Statement (attachment C)/bond pricing: describes transaction, characteristics of repayment mechanism, disclosures of relevant financial matters. Provides information leading to setting of interest rates
 - Closing (attachment B): final execution of all underlying contracts, certifications, and legal opinions. Cash exchanged.

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- **Rating Agencies:**

- Current General Obligation ratings:

- Fitch: AAA
- Moody's Aa1
- S&P AAA

- Current Common Bond Fund rating: A+ (S&P)

- Ratings importance: higher rating = lower interest costs; also independent indicator of overall financial strength; increases lender/market confidence in *ability to pay*

- Criteria: mix of quantitative (relative debt amount, fund balances, etc.) and qualitative (local economy, financial management, etc.)

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- **Key Considerations:**

- Bonds are long-term commitments; significant financial impact (2014 interest expense = approximately \$33M)
- Balancing act between use of existing cash resources vs. bonding; managing and planning for cash balance by activity
- Legal, compliance and regulatory environment evolving: both issuance process and post-issuance compliance (including continuing disclosure) more stringent
- Market “rewards” strong credits; differentiates within rating categories
- Remain aware of periodic federal initiatives to limit application of tax-exemption; raising borrowing costs



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Questions