

# Debt Financing Options and Processes: Overview and Updates

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# Overview

- Financing Options for Utilities
  - Revenue Bonds
  - GO Bonds
  - Installment Financing
  - Bond Anticipation Notes (“BANs”) & USDA
- The Financing Process
  - Realistic timeline
  - Financing **Team**
    - Members and Roles
    - LGC Approval Process
- Market Considerations

# Revenue Bonds

- Security – Net Revenues
- Legal Authority – No voter approval required
- Covenants
  - Rate Covenant
  - Additional Bonds Test
  - Debt Service Reserve Fund
- Structure – Typically 25-year term
- Rating Factors
- Publicly-offered or privately placed depending on size; can be negotiated

# General Obligation Bonds

- Security – General taxing power
- Legal Authority – Voter approval required
  - Exception: Two-Thirds
- No Special Covenants
- Structure – Typical 20-year term
- Rating Factors
- Publicly-offered; Generally competitively bid, can be negotiated

# Installment Financing

- Security
  - Pledge to appropriate for Debt Service
  - Lien on financed asset
- Legal Authority – No voter approval required
- No Special Covenants
- Consideration of putting lien on utility assets
- Structure – Typically 10-15 year term (amortizations have fluctuated)
- Rating Factors
- Public or Private offerings (COPs vs. IPCs)

# BANs

- Two-Step Process Governed by USDA
  - Interim BAN to be taken out with USDA Loan at maturity
    - Structure - Typical 18-24 month term
    - Authorized and Issued like a GO or Revenue Bond
    - Must abide by USDA requirements for bidding, project funding, documentation
  - Long-term Note provided by USDA
    - Structure – Typical 40-year term
    - Usually unrated
    - Limited availability
    - Privately offered to USDA

# The Structure Does Make a Difference: Example Repayment

**Loan - \$1,200,000 for a 10 year term for W&S improvements,  
Rate is 3.50% Bank Qualified, payments made annually**

## Level Principal

### ➤ Year 1:

**\$120,000 principal**

**\$42,000 interest**

**\$162,000 total payment**

➤ To reach 1.2X coverage,  
need revenues of \$194,400

## Level P&I

### ➤ Year 1:

**\$102,290 principal**

**\$42,000 interest**

**\$144,290 total payment**

➤ To reach 1.2X coverage, need  
revenues of \$173,148

**Higher debt service in early years of level principal structure (+12.3% in year 1), but less interest over the life of the loan (5.1% = \$11,896).**

# Going from Idea to Funding

- Identify financing team
- Prepare calendar – approx 3 mos on public deal
- Document preparation - bond docs, disclosure docs, feasibility study
- Rating Agency visits
- Meetings/Calls to finalize docs/Post disclosure document
- Sale
- Closing





# Members of a Financing Team

- Issuer – Finance Director, Utility Manager, Attorney
- Local Government Commission
- Underwriter – More than one if over \$20 million
- Attorneys – Bond Counsel, Underwriter's Counsel
- Feasibility Consultant (Revenue Bonds)
- Bond Insurer
- Rating Analyst
- Financial Advisor (if desired)
- Trustee (Revenue Bonds, COPs)

# Role of the LGC

- Created after The Great Depression to promote sound financial management by North Carolina local governments
- Approves almost all debt for local government units
- Prepares offering material and competitively sells GO Bonds

# LGC Approval Process

- Meets first Tuesday of each month
- Application deadline at most one month prior to each meeting (varies by security)
- Bond documents drafted by attorneys and reviewed by working group prior to LGC approval
- Regular contact with LGC re: upcoming bond projects always a good idea

# General LGC Guidelines

- Typically need over 70% of project to have been bid to get approved
- All major permitting must be in-hand
- Looking for all project funding sources to be identified (SRF, grant funds, contractual payments in-hand or expected by closing)

# On the Horizon....

- Tax-Exempt Bonds increasingly seen as tax “loophole”
- Increasing likelihood that tax-exemption will be modified significantly
  - Reduction of benefit?
  - Elimination of treatment?
- Local government community has been slow to action
- Market conditions still not optimal
- Seeing a little new money come back but mostly refundings hitting their “sweet spot”; mostly combined deals thus far in 2013
- Refunding of USDA obligations 2012’s “new product” – expect to see more of that if rates stay low

# Questions?

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# SUPPLEMENTAL SLIDES



# Role of Financing Team Members

- Issuer
  - Finance Director and Utility Manager to develop project plan, cost estimates, financing plan
  - Attorney to review documents, coordinate approvals, provide opinion as to proper authorization
- Local Government Commission
  - Oversight of financing process
- Underwriter
  - Work with Issuer to develop financing plan
  - Quarterback the deal - coordinating schedule, meetings, contact with bond insurer/rating agencies, development of financing team
  - Responsible for sale of bonds



# Role of Financing Team Members

- Bond Counsel
  - Work with Issuer to develop financing plan and identify best financing structure
  - Draft bond documents and necessary approvals
  - Conduct tax due diligence and assure compliance with tax laws
  - Coordinate closing
- Underwriter's Counsel
  - Draft disclosure documentation and bond purchase agreement
  - Assure underwriter complies with securities regulations
- Feasibility Consultant
  - Prepare feasibility study for inclusion in disclosure document
  - Develop rate model for future rate adjustments

# Role of Financing Team Members

- Bond Insurer
  - Provide municipal bond insurance policy for DS payments
  - Provide surety policy for DSR
  - Often have consent rights in bond documents
- Rating Analyst
  - Review transaction and provide credit rating
- Financial Advisor
  - Work with Issuer to develop financing plan
  - Often coordinates with rating agencies and bond insurers
- Trustee
  - Serve as depository and paying agent under bond documents
  - Require documentation for disbursement from bond funds