

# Bonds 101

**ICCCFO Conference**

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**STIFEL** | Public Finance

## Bond Basics - Overview

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- Bonds are loans, like mortgages or car loans.
- They are paid back with property tax or other district revenue.
- The tax rates used to repay most bonds are limited by law and set by the County Clerk.
- Issuing bonds (getting the loan) may need the approval of the voters, may be subject to petition or may be permissible under law by Board authority.

## Bond Basics – Overview Continued

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- Today, the tax-exempt bond market is a **\$4.1 trillion dollar marketplace** where issues are bought, sold and traded much like stocks.
- A tax-exempt bond represents borrowed money which the borrower is then legally obligated to repay to investors at a certain time and with, in most cases, a fixed rate of interest.
- Tax-exempt bonds are issued to finance a variety of capital improvements that benefit the citizens of a particular area.
- Illinois Community College Act and the Local Government Debt Reform Act provide the legal basis for districts to borrow money. (Can't just take out a “loan” at local bank)

## Bond Basics – Investing in Bonds

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- Bonds represent a debt obligation of the District. The District promises to pay the investor a specified interest rate over a certain period of time. Upon maturity of the bond, the investor receives back all of the original principal.
- Generally issued in \$1,000 or \$5,000 denominations with annual principal and semi-annual interest payments
- Generally rated by one or more of the industry's respected rating agencies (Moody's, Standard & Poor's, Fitch).

## Bond Basics – Investing in Bonds Continued

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- Municipal bonds tend to carry credit ratings of AAA, AA, A or BBB. Bonds rated below these levels are considered speculative (junk bonds).
- Bond prices fluctuate with the rise and fall of interest rates. You can lose money in bonds if interest rates rise and you sell before maturity or if the issuer defaults.
- Treasury bonds are considered the safest. Other categories of bonds include U.S. government agency bonds, corporate bonds and municipal bonds.

# Bond Basics – Credit Ratings

Credit Rating Scales by Agency, Long-Term

Moody's	S&P	Fitch	
Aaa	AAA	AAA	Prime
Aa1	AA+	AA+	High grade
Aa2	AA	AA	
Aa3	AA-	AA-	
A1	A+	A+	Upper medium grade
A2	A	A	
A3	A-	A-	
Baa1	BBB+	BBB+	Lower medium grade
Baa2	BBB	BBB	
Baa3	BBB-	BBB-	
Ba1	BB+	BB+	Non-investment grade speculative
Ba2	BB	BB	
Ba3	BB-	BB-	
B1	B+	B+	Highly speculative
B2	B	B	
B3	B-	B-	
Caa1	CCC+	CCC	Substantial risk
Caa2	CCC		Extremely speculative
Caa3	CCC-		Default imminent with little prospect for recovery
Ca	CC	CC	
	C	C	
C	D	D	In default
/			
/			

"Junk"



## Bond Basics – Value of Tax-Exempt

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- Investors willing to give or accept lower interest rates, because interest earnings are not subject to federal income tax.

$$\text{Taxable Equivalent Yield} = \frac{\text{Tax-Free Yield}}{100\% - \text{Tax Bracket}}$$

**Example:**

$$7.94\% = \frac{5.00\%}{100\% - 37.0\%*}$$

\*2023 Federal Income Max Tax Rate (37.0%)

## **Bond Basics – Tax-Exempt or Taxable Interest**

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- IRS Regulations determine the tax status of Municipal Bond interest payments
- Bonds issued for capital purposes are generally tax-exempt
- Bonds issued for working capital (operating) purposes are generally taxable.



# Community College Bond Basics – Repayment Sources

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- The following are examples of the revenue stream and bond type associated with each:

## Revenue Pledged

## Type of Bond

Property Tax (ad valorem  
property tax unlimited as to rate  
and amount)



General Obligation  
Unlimited Tax

General Operating Revenues



Non-GO  
Limited Tax Bond / Debt  
Certificate

General Operating Revenues



Alternate Revenue Bond

# Community College Bond Basics – Debt Limit

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- Statutory debt limit is **2.875% of EAV**
  - EAV including TIF and EZ
- Do not count:
  - Tax Anticipation Warrants/Notes
  - Revenue Anticipation Notes
  - Personal Property Replacement Tax Notes
  - Alternate Revenue Bonds (unless back-up property taxes were levied)

# Community College Bond Basics - Debt Capacity

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## Community College District No. 5XX (Hometown Community College) Many Counties, Illinois Debt Statistics

### EAV History

<u>Levy Year</u>	<u>EAV</u>	<u>% Change</u>
2007	3,406,640,993	
2008	3,529,828,912	3.62%
2009	3,594,517,566	1.83%
2010	3,589,355,702	-0.14%
2011	3,871,378,534	7.86%
2012	3,869,565,219	-0.05%

### Debt Capacity

2012 EAV	3,869,565,219
	x
	<u>2.875%</u>
Debt Limit	111,250,000
	-
Outstanding Debt	<u>\$57,000,000</u>
Remaining Debt Capacity	<b>\$54,250,000</b>

# Community College Bond Basics – Working Cash Limit

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## Community College District No. 5XX (Hometown Community College) Many Counties, Illinois Working Cash Fund Calculations

<u>Levy Year</u>	<u>EAV</u>
2012	3,869,565,219

### Part I Working Cash Fund Bond Limit

20__ Equalized Assessed Value:		\$3,869,565,219
Maximum Education Fund and O&M Fund Tax Rate:		0.2500
		\$9,673,913
	<b>PLUS</b>	
CPPRT (FY 20__ Est. per IDOR website)		\$575,651
	Subtotal	\$10,249,564
<hr/>		
x 75%		\$7,687,173
Outstanding Working Cash Bonds (Assumes all of 2001 WCF bonds have been ret		\$0
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<b>Maximum Working Cash Fund Bonds Outstanding</b>		<b>\$7,687,173</b>

# Community College Bond Basics – Working Cash Limit Cont.

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## Part II Working Cash Fund Balance Limit

	Maximum Education and Operations and Maintenance Tax Extension	\$9,673,913	
Plus	CPPRT Lesser of FY 20__ actual or Est. FY 20__	\$575,651	
Equals		\$10,249,564	
Times	ninety percent	\$9,224,608	
	Monies to be received by the District in the current FY for educational or operations and maintenance purposes from the State or Federal government or other sources (except CPPRT) from FY 20__ Audit pg. 83	\$47,858,900	
Plus			
Equals	Maximum Working Cash Fund balance	\$57,083,508	
	the amount presently to the credit of the Working Cash Fund (including amounts loaned to the Education and O&M Funds) from FY 12 Audit	\$15,000,000	
Less			
Net	<b>Working Cash Fun Balance Limit</b>		<b>\$42,083,508</b>
	<b>Lesser of Part I or Part II is Net Working Cash Fund Bond Limit</b>		<b><u>\$7,687,173</u></b>

# Illinois Bond Basics

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## ***Protection, Health and Safety Bonds***

- For alterations and repairs to facilities for health, safety, environmental protection, accessibility or energy conservation
- Not subject to backdoor referendum
- Bond Issue Notification Act (“BINA”) hearing required
- Maximum amount outstanding \$4,500,000 (\$20,000,000 for CCD #522 and CCD #536)
- Maximum Financing Term = 20 years
- Repaid from bond and interest levy (subject to Debt Service Extension Base)

## ***Building Bonds***

- Must be approved by voters at general election (3 elections every 2 years)
- Maximum amount determined by voted authorization
- Maximum financing term = 20 years
- Repaid from bond and interest levy

# Illinois Bond Basics

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## ***Working Cash Bonds***

- Bond Issue Notification Act (“BINA”) hearing required
- Maximum amount determined by State formula
- Maximum financing term = 20 years
- Unless sold as federally taxable, must comply with cash-flow borrowing need calculations and repayment restrictions
- Repaid from bond and interest levy (subject to Debt Service Extension Base)

## ***Funding Bonds***

- Subject to Backdoor Referendum – 30-day Petition Period
- Bond Issue Notification Act (“BINA”) hearing required
- Can only be issued to pay an existing “claims” of the District
- Maximum financing term = 20 years
- Repaid from bond and interest levy
- Subject to Debt Service Extension Base

# Illinois Bond Basics

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## *Alternate Revenue Bonds*

- No voter approval required
- Backed by proven revenue stream, such as student tuition or fees, state grant/aid, etc.
- Secondarily backed by general obligation property tax pledge of the District should the pledged revenue source be insufficient at any time
- Does not count against debt limit unless G.O. levy is used, then all outstanding bonds are counted towards the debt limit
- Must demonstrate that the dedicated revenue covers 125% of annual debt service (Audit or Feasibility Report)
- 30 day back door referendum period – 7 ½% of Registered Voters
- Does not count toward debt service extension base
- BINA hearing required



# Illinois Bond Basics

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## *Debt Certificates*

- No voter approval required
- Must have sufficient revenue stream to support debt service
- More difficult credit rating process, compared to G.O. Bonds or Alternate Revenue Bonds
- Generally rated one notch lower than G.O. Bonds which means higher insurance costs and interest rates
- Debt counts against debt limit
- Does not count toward debt service extension base
- Title to property remains with the District

# Illinois Legislation Update: Public Act 103-0278

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On June 28<sup>th</sup>, 2023, the Governor signed legislation which, among other things, made changes to the Working Cash Fund Law for community college districts:

**First, the law allows a District to Abolish their Working Cash fund without a referendum.**

- This allows the district to increase or recreate a working cash fund at anytime without voter approval.

**Second, it allows a District to Abate (partially transfer) their Working Cash fund to any other fund.**

- This allows the district to transfer funds from their working cash fund to other funds more in need.
- Transferred funds no longer need to be paid back to the working cash fund.
- Must maintain at least 0.05% of the then-current value of the District's EAV when abating funds.

**Finally, this essentially reduces the need for issuing debt certificates into funding bonds (unless there's insufficient working cash capacity).**

# Illinois Bond Basics – Community College Borrowing Summary

Bond Type	General Obligation Building Bonds	Working Cash Fund Bonds	Funding Bonds	Protection, Health, and Safety Bonds	Debt Certificates	Alternate Revenue Source Bonds
Voter Approval Required	Yes	No	No	No	No	No
Repaid from Separate Levy	Yes	Yes	Yes	Yes	No	(As Backup)
Issued Under DSEB if Subject to PTELL	No	Yes	Yes	Yes	No	No
Subject to Backdoor Referendum / ROI Required	No	Yes	Yes	No	No	Yes
BINA Hearing	No	Yes	Yes	Yes	No	Yes
ICCB Approval Required	No	No	No	No	No	No
Count Toward Debt Limit	Yes	Yes*	Yes*	Yes	Yes	No (Generally)
Maximum Term (Years)	20	20	20	20	20	40

*The matrix above includes some of the most typical long-term borrowing options but please note that other options exist and this summary covers only certain important information.*

*\* Working Cash Fund Bonds and Funding Bonds count towards the statutory (2.875%) debt limit, but may be issued in excess of such limit.*

# Illinois Bond Basics – Other Special Types of Bonds

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## ***Refunding Bonds***

- Issued to refinance/restructure existing bonds
- Done for savings or tax rate management

## ***Insurance Reserve Bonds***

- Issued to refinance/restructure existing bonds
- Done for savings or tax rate management

## ***Tort/Judgment Funding Bonds***

- Issued to pay for Tort judgment or settlement
- Not subject to referendum, petition or debt limit

# Property Tax Extension Limitation Law (PTELL)

- *As known as “Tax Caps”*
- PTELL was created to slow the growth of property tax. County voters have to vote PTELL in.
- Currently 39 (out of 102) counties currently are under PTELL, with DuPage, Kane, Lake, McHenry and Will included with the original 1991 legislation, and Cook added in 1994.
- Ten counties voted and defeated the issue.

# Property Tax Extension Limitation Law (PTELL)

*Here are the basic limitations of PTELL:*

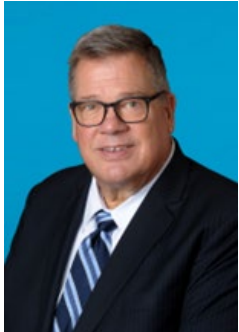
- A district's property tax extension can increase no more than the lower of 5% or the current CPI from one year to the next.
- Exceptions: “New Growth” . New property or improvements can be added at full value the first year they are assessed.
- There are LOTS of quirks and restrictions under PTELL.

# Property Tax Extension Limitation Law (PTELL)

- PTELL CONFUSES THE GAME AGAIN- Long Term Borrowing opportunities differ for PTELL districts.
- PTELL districts are blessed/cursed with something called the **Debt Service Extension Base (DSEB)**.
- This is a number based on the non-referendum Bond and Interest Tax Extension the year prior to PTELL taking effect. DSEB is the amount of money a PTELL district may levy to repay **all non-voted** bonds and hence limits the amount of borrowings.
- If the district had no debt - they have no DSEB. If they had lots of debt, they have a high DSEB. Luck of the draw or good planning.

# Contacts - Resource – Questions?

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**Kevin Heid**  
*Managing Director*  
[heidk@stifel.com](mailto:heidk@stifel.com)  
(309) 661-0004



**Tom Crabtree**  
*Managing Director*  
[crabtree@stifel.com](mailto:crabtree@stifel.com)  
(314) 342-8457



**Nate Fretz**  
*Director*  
[fretzn@stifel.com](mailto:fretzn@stifel.com)  
(309) 661-0028

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