



IGFOA ANNUAL CONFERENCE

Moving into the Future with Purpose

Springfield, Illinois
September 9-11, 2024

Funding Capital Projects: Bonding vs. Spending Reserves

Presented By:

Kim Auchstetter, Finance Director, Village of New Lenox

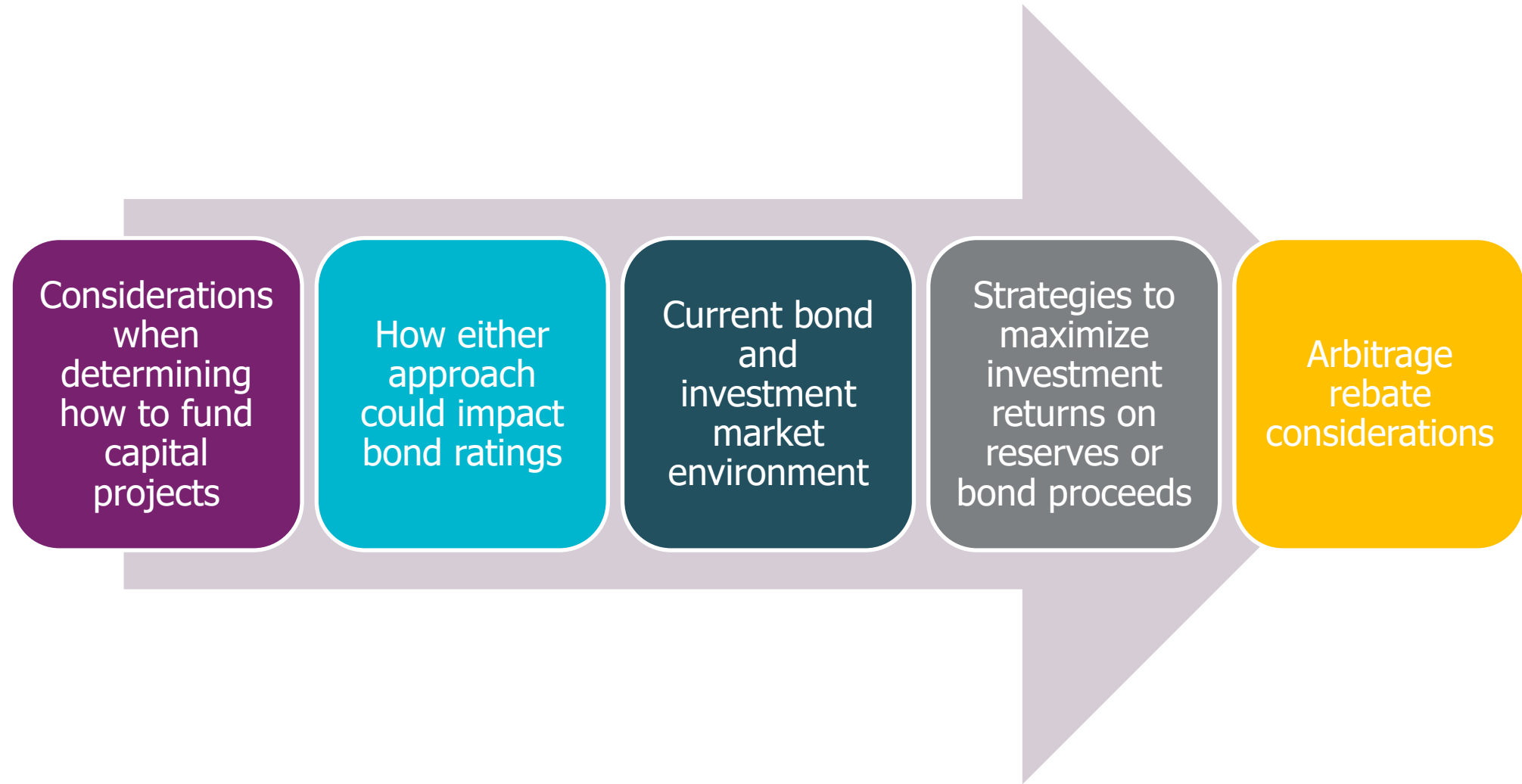
Michelle Binns, Director, PFM Asset Management

Sarah Sullivan, Managing Director, S&P Global Ratings

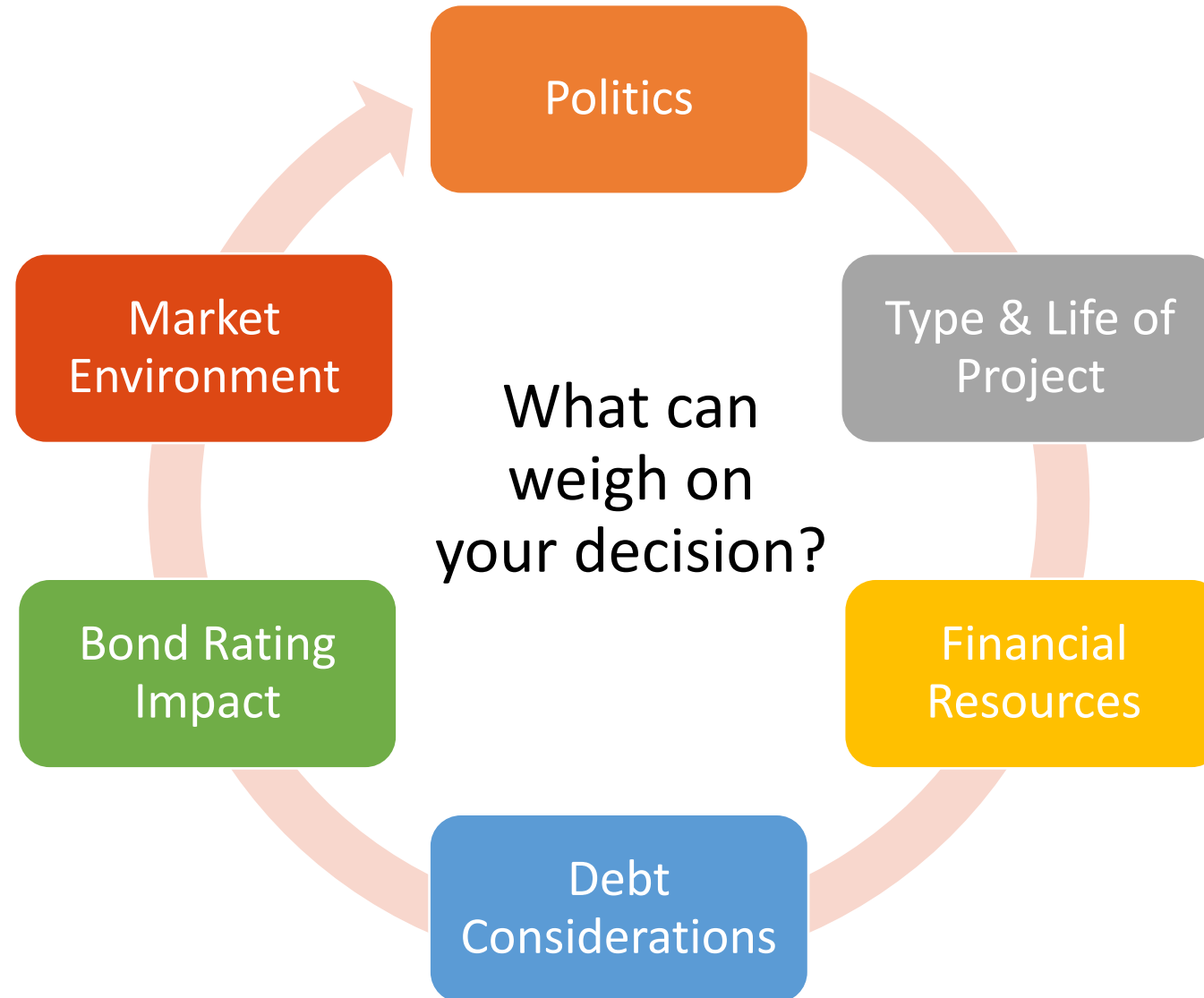
Dalena Welkomer, Director, Baird Public Finance

September 9, 2024

Overview



Considerations for Funding Capital Projects



Village of New Lenox Strategic Plan



2014-2016

Strategic Priority	Key Outcome Indicator (KOI)	Target	Strategic Initiatives
FISCAL STABILITY	General Fund reserve balance	90 days reserves	a) Create plan to restructure debt
	Bond rating	AA+	b) Develop LT financial outlook
	Property tax burden	Increase rebate from 60% to 75%	c) Analyze comp plan for implementing EAV targets d) Create financial plan-use of excess funds e) Systematic review of operations

Use of excess funds started here

2023-2026

Strategic Priority	Desired Outcome	Key Outcome Indicator	Target	Strategic Initiatives
FINANCIAL STABILITY <i>A financially responsible organization</i>	Strong financial system	- Reserve balances - Bond rating	- Maintain 25% fund balance reserve annually - Maintain AA+ bond rating	a) Assess current fee structure and sufficiency
	Moderate local tax rates	- % of tax rebate - Property tax rate	- Rebate 100% of residential property taxes annually	b) Develop a strategy to increase non-resident revenue
	Diverse revenue sources	- C/I- Residential EAV ratio - Non-tax revenue	- Less than 20% of General Fund Revenue from tax sources (excluding sales tax) by 2028 - C/I-Residential EAV ratio increased by \$25,000,000 by 2028	c) Update plan to demonstrate strong Village financial conditions d) Establish strategy for revenue diversity and stabilization

General Fund Balance is in Excess of 25%



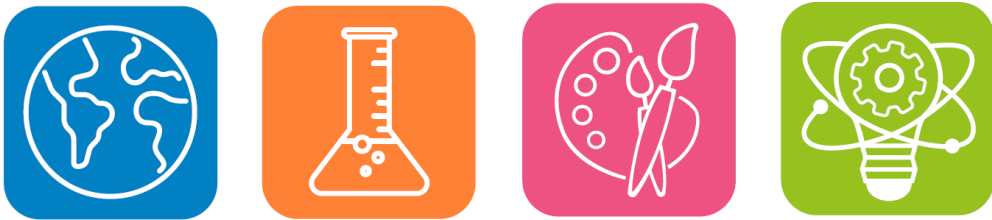
- Update Capital Improvement Plan (CIP) to identify financial commitments that includes General Fund obligations (debt)
 - G.O. debt levies are abated annually
 - Alternative General Fund revenue used to fund debt obligations
 - Sales Tax-45% of General Fund revenue
 - Utility Tax-4.2% of General Fund revenue
- List use of funds priorities as directed by the Strategic Plan
 - One-time use of funds vs. ongoing operating expenditures

- Village purchases underutilized vacant buildings/land for future development by outside party
- In order to control what is developed on prime real estate, the Village purchased 103 acres of property near Silver Cross Hospital
- Village was approached by not-for-profit children's museum needing to expand from their current Frankfort location

Two Mayor Legacy Projects Announced in Spring 2023



KidsWork Children's Museum

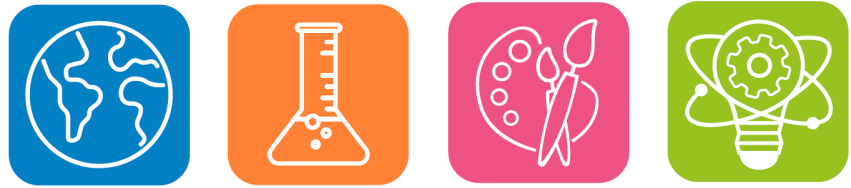


KidsWork
children's museum

Crossroads Sports Complex



Identifying the Legacy Project Costs



KidsWork
children's museum

- Land cost paid with cash
- Hired architect to determine needs/cost
- Determined project can be funded with cash on hand

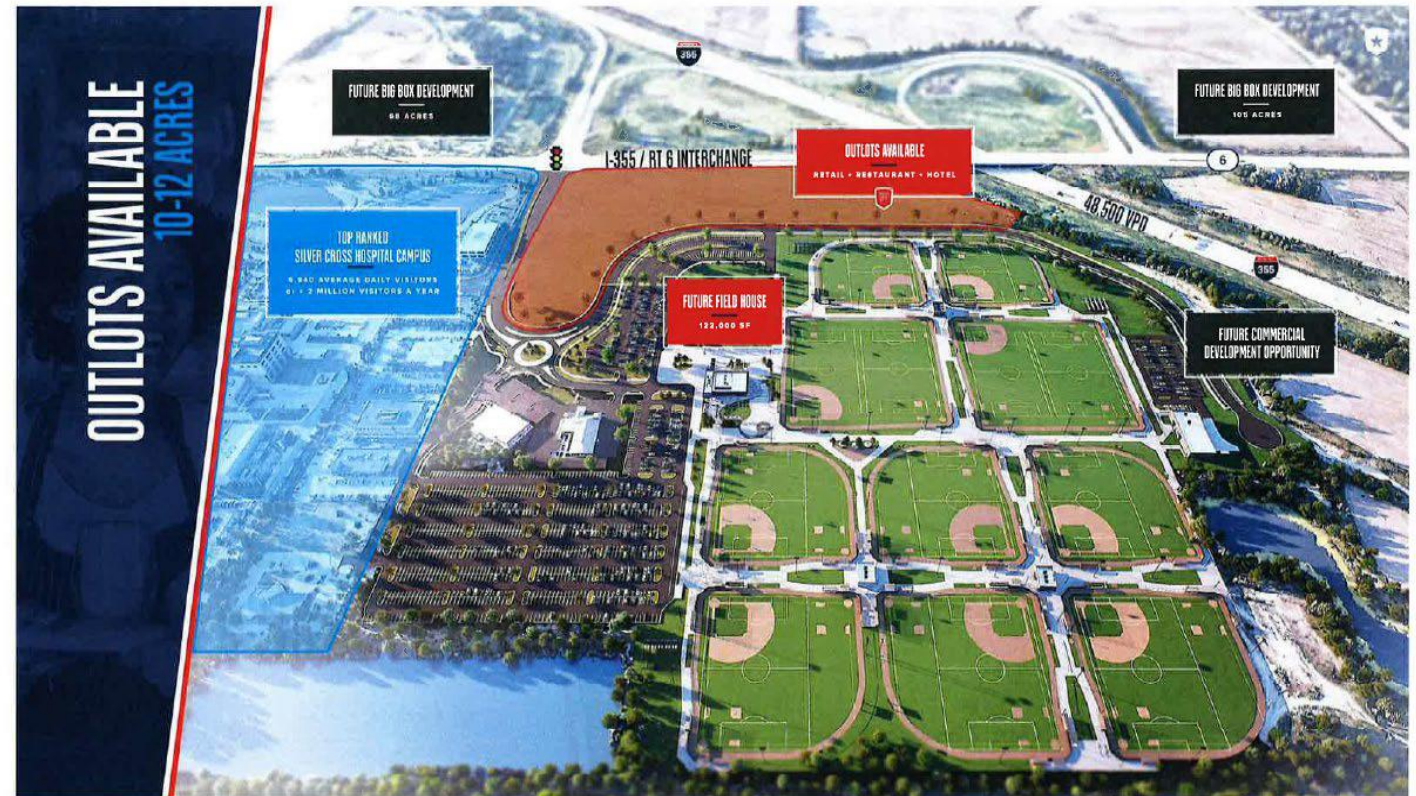


- Land cost paid with cash
- Hired Sports Facilities Advisory to complete a 5-year operating pro-forma for indoor & outdoor sports complexes



- Goal: Opening Season 2025
- Construction began immediately utilizing General Funds on hand
- Reimbursement Resolution approved March 2024
- Bond Proceeds Timeline Set with Financial Advisor and Bond Counsel; May 2024 with closing July 31, 2024

Moving forward with \$70M Sports Complex Phase 1-outdoor complex



What is the Type of Project that Requires Financing?

Examples From Local Illinois Debt Policies

- Do you have policies in place that establish parameters for funding such projects?
- Does the life or size of the need warrant debt?
- Have you planned for the need and what are your financial resources?

From Reserves on Pay-As-You-Go Basis:

- Capital projects < \$500,000.
- Projects that can be adequately funded from existing revenues/reserves.
- Project phasing - financing incrementally over a longer timeframe.
- Projected useful life of project < 10 years.

Through Issuance of Debt:

- Capital projects > \$500,000.
- Projects that cannot be adequately funded from existing revenues/reserves.
- Distribute cost of project over period in which residents and visitors benefit from it.
- Projected useful life of project > 10 years.
- May issue short-term debt if life of item > 1 year.

Do You Have the Financial Resources?

Financial Resources Sufficient?

Fund Balance Policy/Practice

Long-Term Capital Plan

- ✓ Identify capital needs, funding options and operating budget impacts.
- ✓ Building reserves for clear purposes can help reduce or eliminate the need for debt.

- ✓ Would funding capital projects deplete reserves below required funding level?
- ✓ Does the policy allocate sufficient reserves for funding capital equipment replacement or construction of capital improvements?

- ✓ YES - Consider potential rating pressures and market environment.
- ✓ NO - May require debt to cover the shortfall.

Examples of When Debt May be Needed

Insufficient reserves to fund utility infrastructure upgrades. Future rate increases are necessary to support the project and the repayment of debt. Puts the burden on future users of the system.

Utility Project



Need for new building with insufficient reserves or an annual revenue stream to finance it. Requires bond referendum to authorize bond issue and establish a levy for repayment.

Fire Station Project

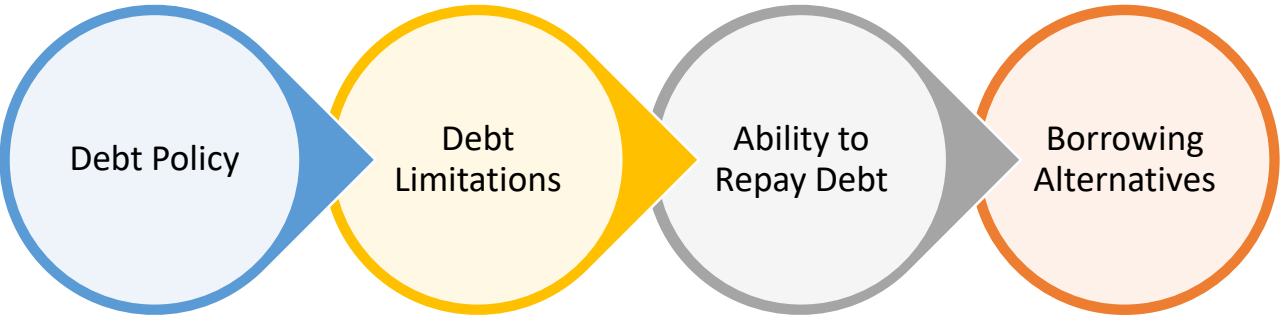


Insufficient reserves in the TIF Fund to support a development project. TIF increment from the new development is projected to be sufficient to cover annual debt service. Allows for the development to occur and increment to grow.

TIF Project



Varies if Home Rule or
Non-Home Rule Unit
of Government



Debt Limitation (% of EAV) by Type of Non-Home Rule Issuer*

Type of Non Home Rule Issuer	Overall Debt Limitation	Non Referendum Debt Limitation**
City/Village	2.875%	0.500%
County	8.625%	0.500%
Park Districts	2.875%	0.575%
Forest Preserve Districts	2.300%	0.300%
Fire Districts	5.750%	-
Library Districts	2.875%	-

*Certain types of issuances and certain project types could be excluded from these debt limitations.

** Applicable to those entities subject to the Property Tax Extension Limitation Law (PTELL).

**20 Year General Obligation Bond
Hypothetical Debt Service Cost***

Project Proceeds	Hypothetical Annual Debt Service	Hypothetical Total Debt Service
\$5 Million	\$375,000	\$7,500,000
\$10 Million	\$745,000	\$14,900,000
\$15 Million	\$1,115,000	\$22,300,000
\$20 Million	\$1,485,000	\$29,700,000
Hypothetical True Interest Cost		3.90%

*Assumes current market interest rates for general obligation bonds rated "AA-" as of August 1, 2024. Assumes 20 year term level annual debt service.

General Characteristics of Illinois Borrowing Alternatives

Option	Security	Applicable to Non-Home Rule		Notes
		Referendum Required	Subject to Debt Limit*	
Unlimited Tax General Obligation ("UTGO") Bonds	Ad valorem property tax unlimited as to rate or amount.	Yes	Yes	Strongest security and lowest cost option.
Limited Tax General Obligation Bonds ("LTGO")	Debt service extension base ("DSEB"). Ad valorem property tax unlimited as to rate but limited as to amount.	No	Yes, non-referendum debt limit.	- Only for entities subject to PTELL. - Similar cost to UTGO bonds. - DSEB grows at lesser of change in CPI or 5%.
General Obligation Alternate Revenue Bonds	Dedicated revenue stream that will generate a minimum of 1.25x debt service coverage. Additional security provided by ad valorem property taxes unlimited as to rate or amount.	No, but subject to 30-day backdoor referendum period.	No, unless property tax levy is not abated.	- Similar cost to UTGO bonds. - Most common revenue sources pledged: - Utility revenues - Sales, income or hotel/motel taxes - Tax increment revenues - General Fund - Annual issuance of LTGO Bonds (DSEB) - Levy is abated each year provided the pledged revenue is sufficient.
Debt Certificates	Payable from any legally available revenue source. No dedicated property tax levy.	No	Yes	- Weaker security than GO bonds due to lack of property tax pledge, therefore higher borrowing cost. - First budget obligation with a pledge of the issuer's general obligation. - Generally rated the same as UTGO bonds.
Revenue Bonds	Payable solely from the revenues pledged. May pledge one or a number of revenue sources.	No	No	- Could be a weaker security than GO bonds due to lack of property tax pledge, therefore higher borrowing cost. - Investors like to see sufficient debt service coverage. - Typically requires a reserve fund to provide additional security to bondholders and enhance the rating. - Rating outcome driven by revenue source, debt service coverage, reserve fund and other factors. - Generally lower than UTGO bond rating.

* Debt limitations vary by type of non-home rule entity. See prior slide.

Agenda

- Current criteria overview, debt and reserves
- Proposed criteria* overview, debt and reserves
- Examples

- *Pursuant to our proposed criteria described in Request For Comment: Methodology For Rating U.S. Governments, published Jan. 11, 2024

- **Budgetary Flexibility/Reserves:** measures the degree to which the government can look to additional financial flexibility in times of stress
- **Debt:** The analysis of debt focuses on the nature of the pledged security, the debt repayment structure, the debt-service burden, and the future capital needs of an issuer.
- **Current Criteria & Percent of Indicative Score:**
 - ✓ Budgetary Flexibility: 10%
 - ✓ Debt & Contingent Liabilities: 10%
 - ✓ Other factors considered: institutional framework (10%), economy (30%), management (20%), Liquidity (10%), and budgetary performance (10%)
- **Proposed Criteria & Percent of Initial Assessment:**
 - ✓ Reserves and Liquidity: 20% of initial assessment
 - ✓ Debt and Liabilities: 20% of initial assessment
 - ✓ Other factors considered: economy (20%), financial performance (20%), management (20%)

Current Criteria

Budgetary Flexibility for Municipalities & Counties

Table 10
Assessing The Budgetary Flexibility Score (see paragraphs 59-64)

	Available Fund Balance As A % Of Expenditures				
%	>15	8-15	4-8	1-4	≤1
Score	1	2	3	4	5
A score of '1', '2', '3', '4', and '5' means very strong, strong, adequate, weak, and very weak, respectively.					
Qualitative factors with a positive impact on the initial score:			Qualitative factors with a negative impact on the initial score:		
If projections for the current year and the following year suggest a better initial score.			If projections for the current year and the following year suggest a worse initial score.		
Ability to avoid financial imbalances with demonstrated capacity and willingness to cut operational spending (by more than 2%), resulting from a flexible cost structure, flexible legislation, and/or widespread political support.			High levels of questionable receivables or amounts due from other funds with deficit balances.		
Existing state tax caps do not apply to the government, or the government retains substantial flexibility under the caps.			Limited capacity to cut expenditures due to infrastructure or operational needs or political resistance.		
Demonstrated ability and willingness to raise taxes when needed (and voter support is usually obtained when such approval is required).			Limited capacity to raise revenues due to consistent and ongoing political resistance which can include self-imposed restrictions through charter or local initiative processes.		
Timing of fiscal year and tax billing dates result in high cash with abnormally low fund balance levels.			Where cash accounting is used, the criteria use cash balances instead of fund balances and the score is worsened by one point.		
Maintenance of an available fund balance exceeding 30% of general fund expenditures for the most recently reported year, the current year and next year.					

- Measures fund balance as a % of expenditures
- “Available fund balance” reflects all funds legally available for operations
- Adjustment examples:
 - ✓ Available fund balance under \$500,000 (worsen)
 - ✓ Available fund balance greater than 75% (improve)
 - ✓ Use of cash accounting (worsen)
 - ✓ Maintenance of consistently high fund balance that we expect to continue (improve)

Debt Ratios for Municipalities and Counties

- Debt service as a % of expenditures measures annual fixed-cost debt burden.
- Net direct debt as % of revenues measures total debt burden on the government's revenue.
- Adjustment examples:
 - ✓ Entity planning to issue substantial debt to address infrastructure needs (worsen)
 - ✓ Above-average amortization inflates debt service, masking future flexibility (improve)
 - ✓ Overall net debt as percentage of market value below 3% (improve)
 - ✓ Overall net debt as percentage of market value above 10% (worsen)

Table 14 Assessing The Debt And Contingent Liabilities Score (see paragraphs 78-84)					
	Net Direct Debt As % Of Total Governmental Funds Revenue				
Total Governmental Funds Debt Service As A % of Total Governmental Funds Expenditures	<30	30 to 60	60 to 120	120 to 180	≥180
< 8	1	2	3	4	5
8 to 15	2	3	4	4	5
15 to 25	3	4	5	5	5
25 to 35	4	4	5	5	5
≥35	4	5	5	5	5
A score of 1, 2, 3, 4 and 5 are very strong, strong, adequate, weak and very weak, respectively.					
Qualitative factors with a positive impact on the initial score:			Qualitative factors with a negative impact on the initial score:		
Overall net debt as a percentage of market value below 3%.			Significant medium-term debt plans produce a higher initial score when included.		
Overall rapid annual debt amortization, with more than 65% coming due in 10 years.			Exposure to interest-rate risk or instrument provisions that could increase annual payment requirements by at least 20%.		
			Overall net debt as a percentage of market value exceeding 10%.		
			Unaddressed exposure to large unfunded pension or OPEB obligations leading to accelerating payment obligations over the medium term that represent significant budget pressure (see paragraph 82). If there is a plan to address the obligations, the final score worsens by one point; otherwise the score worsens by two points.		
			Speculative contingent liabilities or those otherwise likely to be funded on an ongoing basis by the government representing more than 10% of total governmental revenue.		

- Financial results – historic and budgeted/projected
 - ✓ Operating results in general fund and total governmental funds
 - ✓ Revenues and expenditures over time
 - ✓ Available fund balance over time
 - ✓ Planned spenddowns of fund balance that align with fund balance policy
- Financial Management:
 - ✓ Existence of formal policies or informal targets that establish minimum reserve levels, and adherence to such policies/targets
 - ✓ Development of and regular updates to capital improvement plans
 - ✓ Development of and regular updates to financial plan detailing future funding needs
 - ✓ Ability to adapt budget as needed and stay within budget goals

Proposed Criteria

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments"

Jan. 11, 2024

Proposed Criteria: Reserves And Liquidity

Local government	1	2	3	4	5
Available reserves % of revenues	>15	8-15	4-8	1-4	<1

Qualitative adjustments

Adjustment for under or overstated reserves

Considers if reserves are over or understated and would align with a different initial assessment

Adjustment for projections that suggest a different assessment

Considers whether prospective changes to reserves would result in a better or worse initial assessment

Liquidity and contingent liability risks adjustment

Considers whether liquidity pressures could worsen initial assessment

- Available reserves as a % of revenues
- Qualitative adjustment examples:
 - ✓ Significant additional reserves that are available for general operations (improve)
 - ✓ Significant increase or decrease in projected reserves (improve or worsen)
 - ✓ Reserves are nominally low (worsen)

Proposed Criteria: Debt And Liabilities

	1	2	3	4	5	6
Local government						
Current cost for debt and liabilities % of revenues	<8	8-14	14-20	20-25	25-30	>30
Net direct debt per capita	<500	500-1,500	1,500-2,500	2,500-3,500	3,000-4,500	>4,500
Net pension liabilities per capita	<500	500-1,500	1,500-2,500	2,500-3,500	3,000-4,500	>4,500

Qualitative adjustments

Adjustment for under or overstated current costs

Considers if initial assessment should be adjusted because current costs for debt and liabilities are over or understated and would align with a different initial assessment

Adjustment for under or overstated long-term debt and liabilities

Considers if initial assessment should be adjusted because long-term debt and liabilities are over or understated and would align with a different initial assessment

Adjustment for projections that suggest different assessment

Considers whether prospective changes to current costs and long-term debt and liabilities would result in a different initial assessment

- Current cost includes annual debt service, pension, and OPEB expenditures.
- Qualitative adjustment examples:
 - ✓ Debt amortization is slow (<20% over 10 years) or rapid (>80%)
 - ✓ Tax-supported debt receiving consistent enterprise “self-support” (improve)
 - ✓ Significant medium-term debt plans (worsen)

Examples – Current Criteria

Example 1: \$5 Million Capital Project Reserve Funded

- IL Municipality with very strong fund balance and very weak debt. The city has had strong budgetary performance in recent years, and they have a fund balance policy of 50% of expenditures
- Current Rating: A+

	Example		2023	2022	2021
Operating Expenditures (\$000)	49,500		48,000	46,500	45,000
Available reserves % of operating expenditures	67%		80%	75%	70%
Total available reserves (\$000)	33,400		38,400	34,875	31,500
Debt service % of governmental fund expenditures	21		21	24	37
Net direct debt % of governmental fund revenue	94		94		

*IL Municipality Median Fund Balance at A+: 65.9%

Example 2: \$5 Million Capital Project Bond Funded

- IL Municipality with a very strong fund balance and adequate debt. The city has had strong budgetary performance in recent years and has existing debt.
- Current Rating: A+

	Example		2023	2022	2021
TGF Revenues	22,947		22,279	21,630	21,000
TGF Expenditures	21,855		21,218	20,600	20,000
Available Reserves as % of Expenditures	69%		66%	63%	60%
TGF Debt Service as % of Expenditures	11%		10%	11%	12%
Net Direct Debt as % of TGF Revenue	52%		31%	33%	35%
Debt Description	Adequate		Adequate	Adequate	Adequate

*IL Municipality Median Fund Balance at A+: 65.9%

Example 3: \$5 Million Capital Project Reserve Funded - Smaller Budget

- IL Municipality with a very strong fund balance and very weak debt. The city has had strong budgetary performance in recent years and has a minimum reserve policy of 15% of expenditures.
- Current Rating: A+

	Example		2023	2022	2021
Operating Expenditures (\$000)	8,742		8,487	8,240	8,000
Available reserves % of operating expenditures	6%		65%	64%	63%
Total available reserves (\$000)	517		5,517	5,274	5,040
Debt service % of governmental fund expenditures	21%		21%	24%	37%
Net direct debt % of governmental fund revenue	94%		94%		

*IL Municipality Median Fund Balance at A+: 65.9%

*IL Municipality Median Fund Balance at A: 57.1%

Example 4: \$5 Million Capital Project Bond Funded - Smaller Budget

- IL Municipality with a very strong fund balance and adequate debt. The city has had strong budgetary performance in recent years.
- Current Rating: A+

	Example		2023	2022	2021
TGF Revenues	6,556		6,365	6,180	6,000
TGF Expenditures	6,338		6,153	5,974	5,800
Available Reserves as % of Expenditures	65%		64%	62%	60%
TGF Debt Service as % of Expenditures	14%		10%	11%	12%
Net Direct Debt as % of TGF Revenue	106%		31%	33%	35%
Debt Description	Weak		Adequate	Adequate	Adequate

*IL Municipality Median Fund Balance at A+: 65.9%

Example 5: \$5 Million Capital Project Bond Funded – no existing debt

- IL Municipality with a very strong fund balance, no existing debt, and strong budgetary performance in recent years. They have a fund balance policy of 25% of expenditures.
- Current rating: A+

	Example		2023	2022	2021
TGF Revenues	8,195		7,957	7,725	7,500
TGF Expenditures	8,086		7,851	7,622	7,400
Available Reserves as % of Expenditures	29%		28%	28%	27%
TGF Debt Service as % of Expenditures	3.09%		0%	0%	0%
Net Direct Debt as % of TGF Revenue	61%		0%	0%	0%
Debt Description	Adequate		Very Strong	Very Strong	Very Strong

*IL Municipality Median Fund Balance at A+: 65.9%

Examples – Proposed Criteria

Example 1: \$5 Million Capital Project Reserve Funded

- Scenario: IL Municipality with a population of 30,000, a very strong fund balance and moderate debt. The city has had strong budgetary performance in recent years, and they have existing debt.
- Current Rating: A+

	Scenario		2023	2022	2021
Operating Revenues (\$000)	51,500		50,000	48,500	47,000
Available reserves % of operating revenues	68%		80%	75%	70%
Total available reserves (\$000)	35,000		40,000	36,375	32,900
Initial Reserves Score	1		1	1	1
Current cost for debt and liabilities % of revenues	15%		16%	15%	17%
Net direct debt per capita (\$)	1,100		1,200	1,300	1,400
Net pension liabilities per capita (\$)	1,200		1,200	1,300	1,400
Initial Debt Score	3		3	3	3

IL Municipality Median Fund Balance at A+: 65.9%

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments" Jan. 11, 2024

Example 2: \$5 Million Capital Project Bond Funded

- Scenario: IL Municipality with a very strong fund balance and low debt. The city has had strong budgetary performance in recent years, and they have existing debt.
- Current Rating: A+

	Scenario		2023	2022	2021
Operating Revenues (\$000)	51,500		50,000	48,500	47,000
Available reserves % of operating revenues	82%		80%	75%	70%
Initial Reserves Score	1		1	1	1
Current cost for debt and liabilities % of revenues	16%		10%	11%	12%
Net direct debt per capita (\$)	1,600		933	967	1,000
Net pension liabilities per capita (\$)	567		600	633	667
Initial Debt Score	3		2	2	2

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments" Jan. 11, 2024

Example 3: \$5 Million Capital Project Reserve Funded - Smaller Budget

- Scenario: IL Municipality with a population of 30,000, very strong fund balance and moderate debt. The city has had positive budgetary performance in recent years, and they have existing debt.
- Current Rating: A+

	Scenario		2023	2022	2021
Operating Revenues (\$000)	7,649		7,426	7,210	7,000
Available reserves % of operating revenues	12%		80%	75%	70%
Total available reserves (\$000)	941		5,941	5,408	4,900
Initial Reserves Score	2		1	1	1
Current cost for debt and liabilities % of revenues	23%		23%	23%	23%
Net direct debt per capita (\$)	900		933	967	1,000
Net pension liabilities per capita (\$)	1,550		1,550	1,550	1,550
Initial Debt Score	3		3	3	3

IL Municipality Median Fund Balance at A+: 65.9%

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments" Jan. 11, 2024

Example 4: \$5 Million Capital Project Bond Funded - Smaller Budget

- Scenario: Smaller IL Municipality with a very strong fund balance and weak debt. The city has had strong budgetary performance in recent years, and they have existing debt.
- Current Rating: A+

	Scenario		2023	2022	2021
Operating Revenues (\$000)	22,947		22,279	21,630	21,000
Available reserves % of operating revenues	60%		60%	60%	60%
Initial Reserves Score	1		1	1	1
Current cost for debt and liabilities % of revenues	23%		17%	18%	18%
Net direct debt per capita (\$)	3,600		2,800	2,900	3,000
Net pension liabilities per capita (\$)	1,700		1,800	1,900	2,000
Initial Debt Score	4		3	3	3

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments" Jan. 11, 2024

Example 5: \$5 Million Capital Project Bond Funded - No Existing Debt

- Scenario: Smaller IL Municipality with a with a very strong fund balance and no existing debt.
- Current Rating: A+

	Scenario		2023	2022	2021
Operating Revenues (\$000)	8,195		7,957	7,725	7,500
Available reserves % of operating revenues	29%		28%	28%	27%
Initial Reserves Score	1		1	1	1
Current cost for debt and liabilities % of revenues	16%		9%	9%	9%
Net direct debt per capita (\$)	714		0	0	0
Net pension liabilities per capita (\$)	2,629		2,571	2,714	2,857
Initial Debt Score	3		2	2	2

Pursuant to "Request For Comment: Methodology For Rating U.S. Governments" Jan. 11, 2024

Related Research

[Request For Comment: Methodology For Rating U.S. Governments - Jan. 11, 2024](#)

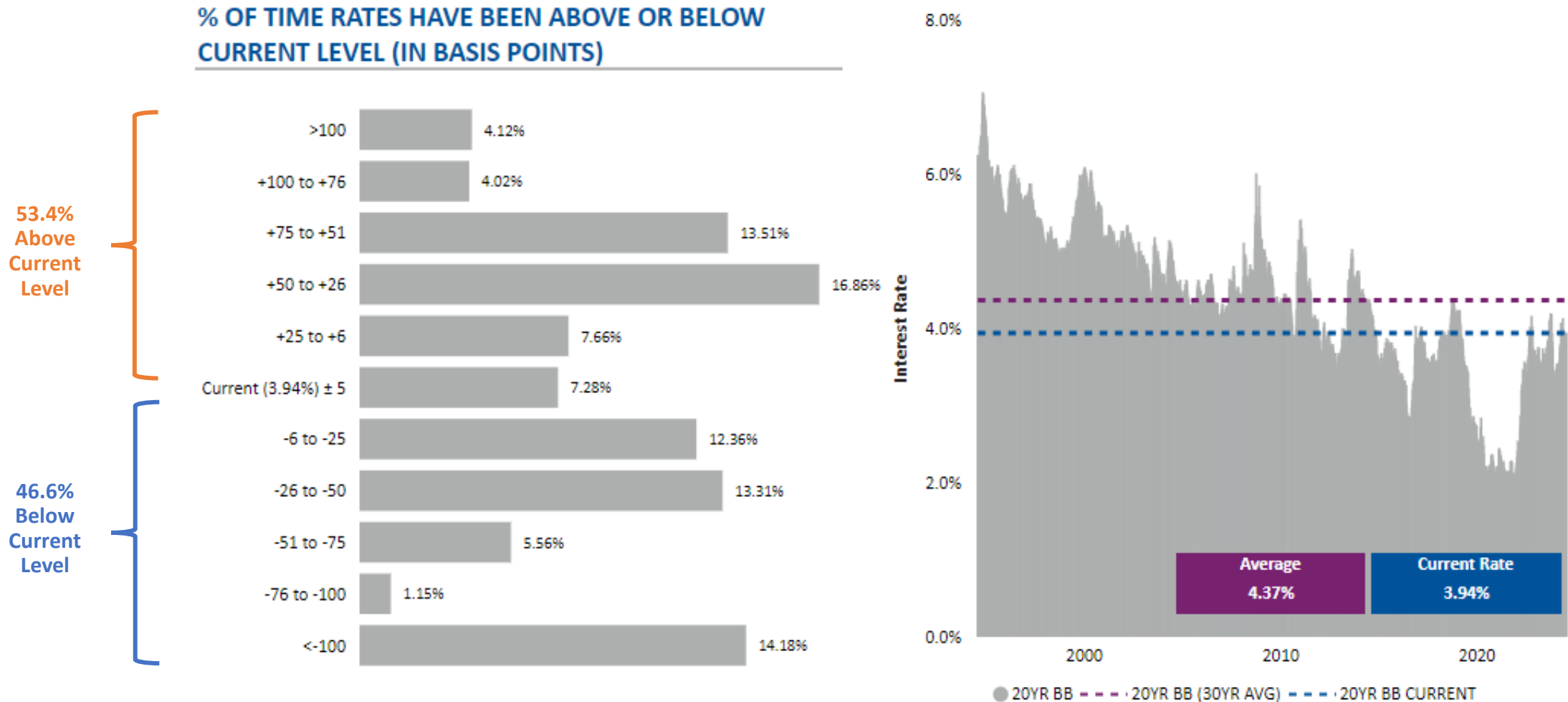
[U.S. Local Governments Credit Brief: Illinois Counties And Municipalities Means And Medians - Sept. 14, 2023](#)

[U.S. Local Governments General Obligation Ratings: Methodology And Assumptions - Sept. 12, 2013](#)

Bond Buyer General Obligation Bond Index – 30 Year History

What is the Bond Buyer 20-Bond Index?

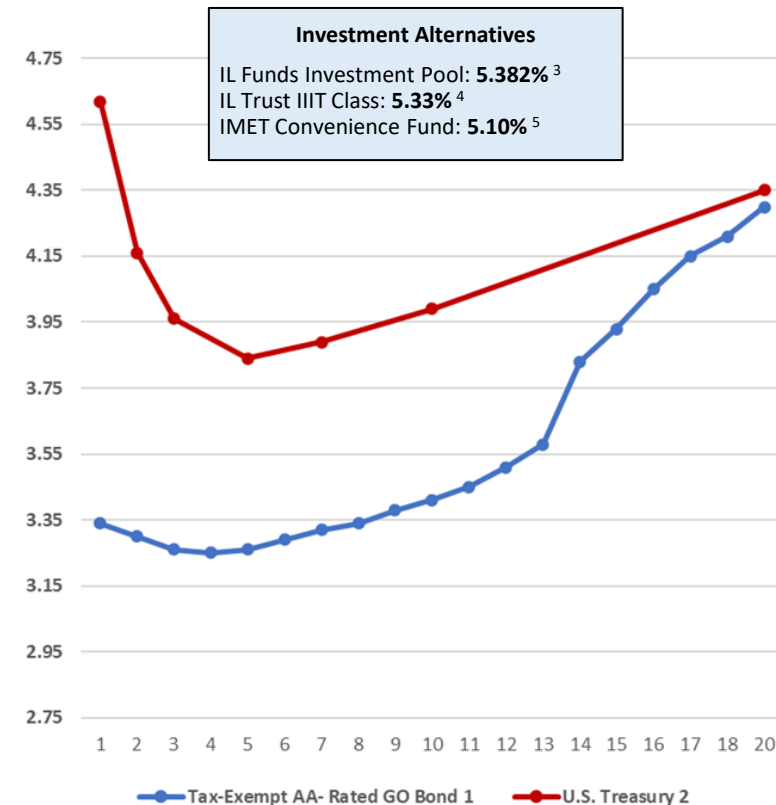
General Obligation Bonds maturing in 20 years are used in compiling this index. The 20-bond index has an average rating equivalent to Moody’s Aa2 and S&P’s AA.



Long-Term Bonds Rates vs. Short-Term Investment Returns

- Long-Term Bond Rates:
 - ✓ Estimate true interest cost of **4.09%** for “AA-” rated 20-year tax-exempt general obligation bond in Illinois (yields range from 3.25% to 4.30%). ¹
 - ✓ The Municipal-to-Treasury spread ranged from 60.0% on the short-end of the curve to 83.8% on the 30-year bond as of August 1, 2024.
- Short-Term Investment Returns (July 2024 Averages):
 - ✓ Illinois Funds Local Government Investment Pool = **5.382%**. ³
 - ✓ Illinois Trust IIIT Class = **5.33%**. ⁴
 - ✓ IMET’s Convenience Fund’s = **5.10%**. ⁵
- The current unique yield curve offers higher short-term investment returns vs. long-term bond rates.
 - ✓ No restrictions on the investment rate of return on reserves so long as it’s a qualified investment.
 - ✓ Investment earnings could be used to build reserves, put towards deferred capital projects or offset interest cost on a debt transaction.

AA- Rated GO Bond Yield Curve
vs. U.S. Treasuries



¹ Estimated interest rates for an Illinois tax-exempt general obligation bond rated AA- by S&P as of market conditions August 1, 2024.

² Source: U.S. Department of the Treasury. Rates as of August 1, 2024.

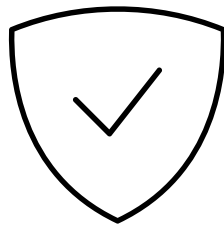
³ Source: Illinois State Treasurer website for Illinois Funds Daily Rates.

⁴ Source: Illinois Trust IIT Class.

⁵ Source: Illinois Metropolitan Investment Fund.

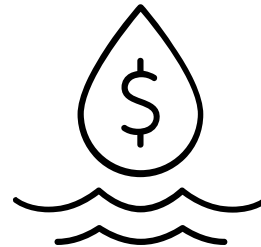
1

Safeguard
Principal



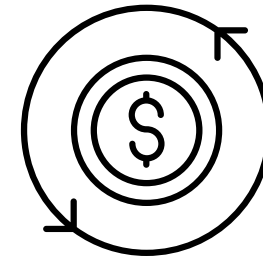
2

Meet Liquidity
Needs



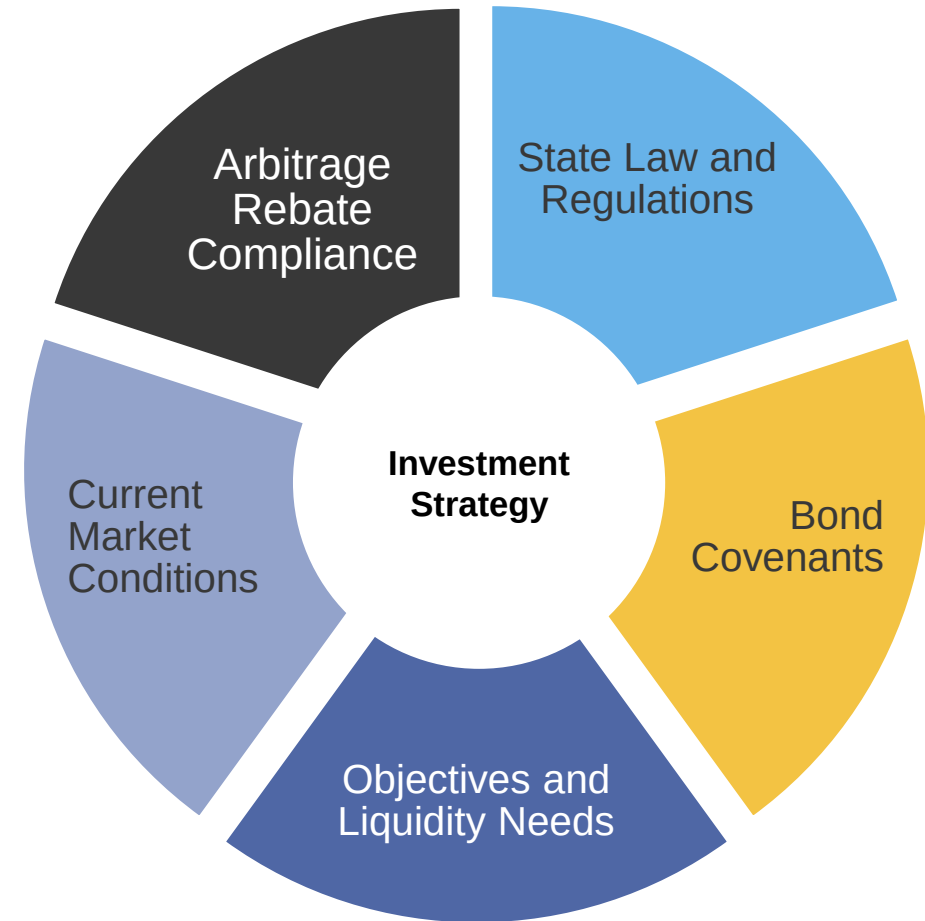
3

Achieve a Market
Return/Yield



Bond Proceeds Investment Strategy Considerations

- Seek safety of principal while providing adequate liquidity
- Current and future interest rate expectations
- Take into account any applicable arbitrage rebate regulations
- Provide a reasonable risk-adjusted return



For Institutional Investor or Investment Professional Use Only – This material is not for inspection by, distribution to, or quotation to the general public.

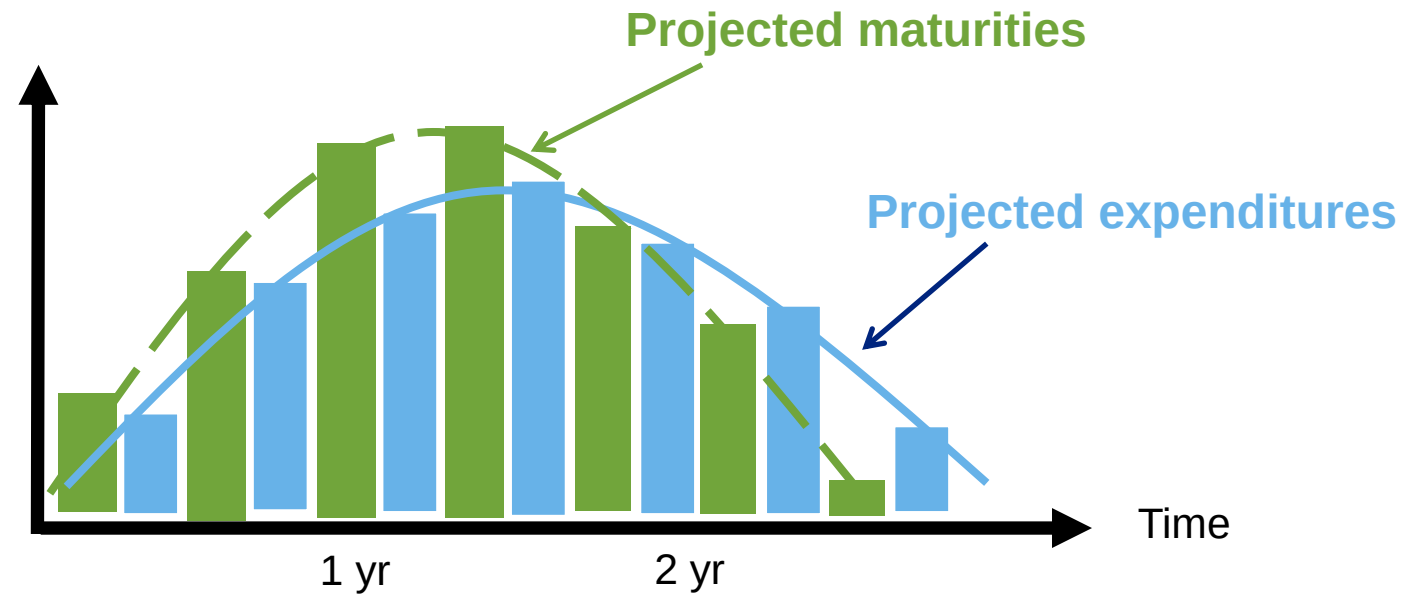
- Define in Investment Policy
- Complies with the Illinois Public Funds Investment Act (30 ILCS 235)
- Additional restrictions may be found in bond documents

Sector	Allowed
Bank Accounts	Yes
Local Government Investment Pools	Yes
Certificates of Deposit	Yes
U.S. Treasuries	Yes
U.S. Agencies	Yes
Instrumentalities (Supras)	Yes
Municipal Bonds	Yes
Commercial Paper	Yes
Corporate Notes	Yes
Negotiable CDs	Yes
Mutual Funds (Stocks)	NO

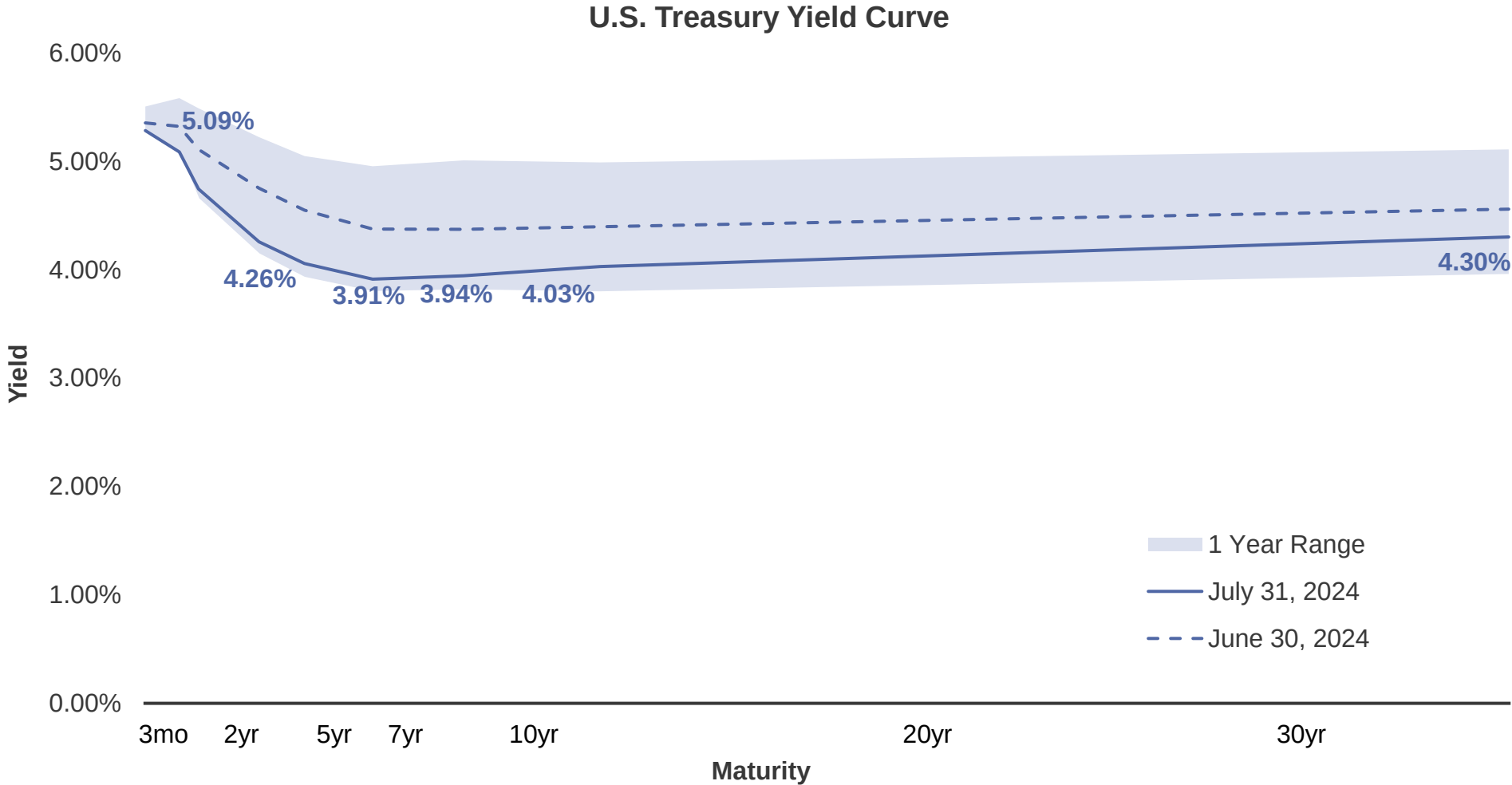
Source: Illinois Public Funds Investment Act. More detailed information can be found at: <https://www.ilga.gov/legislation/ilcs/ilcs3.asp?ActID=496>

Sample Bond Proceeds Investment Approach

- Construction Fund Investment Approach:
 - ✓ Review draw schedule
 - ✓ Examine investment options in order to determine appropriate allocation to an individual portfolio
 - ✓ Purchase of an initial laddered portfolio of securities with maturities matching expected draws

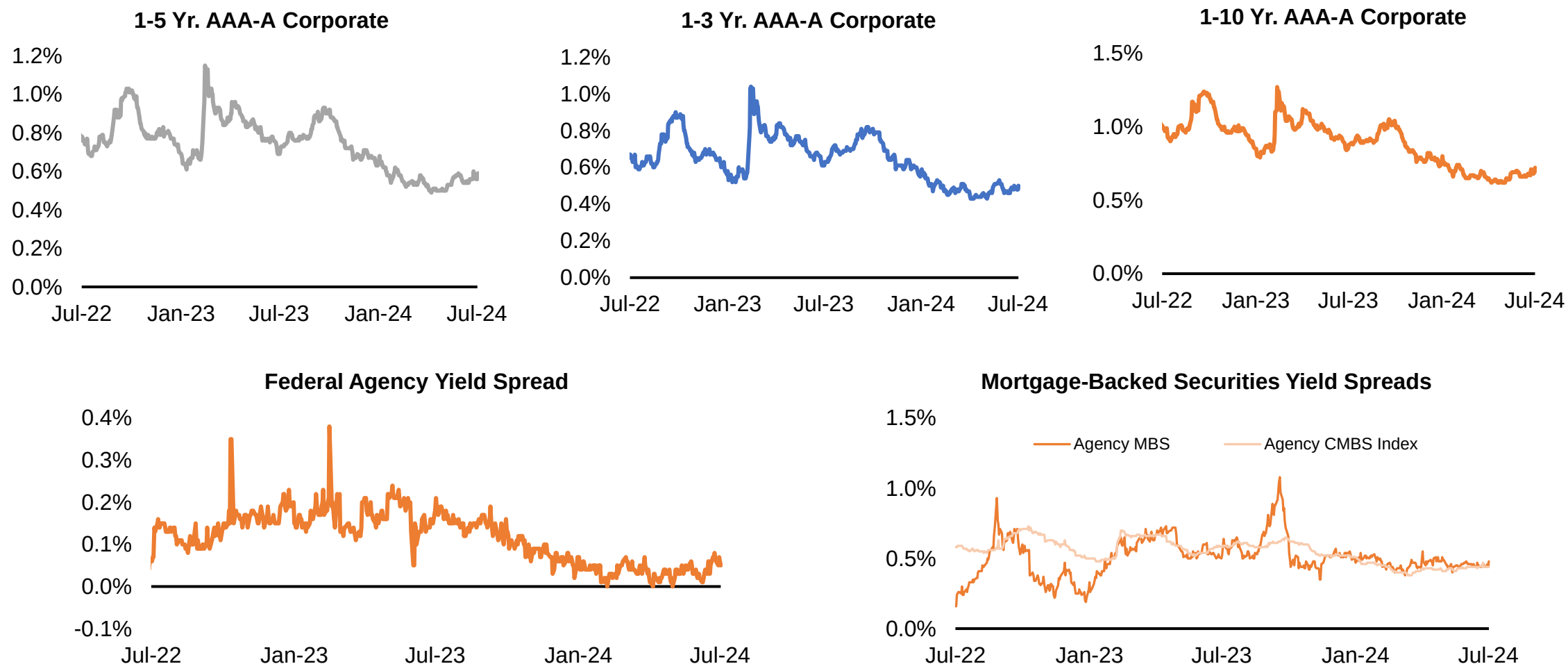


For illustrative purposes only.



Source: Bloomberg, as of 7/31/2024.

Sector Yield Spreads



Source: ICE BofA 1-5 year Indices via Bloomberg, MarketAxess and PFMAM as of 7/31/2024. Spreads on ABS and MBS are option-adjusted spreads of 0-5 year indices based on weighted average life; spreads on agencies are relative to comparable maturity Treasuries. CMBS is Commercial Mortgage-Backed Securities.

Hypothetical Analysis – Bonding vs. Using Reserves

Base Case - \$5 Million Draw on Reserves

Cash Reserves	\$5,000,000
Project Costs	(\$5,000,000)
Net (Cost)/Earnings	\$0

Assumes you forgo the opportunity to use these funds for other purposes.

Bond for \$5 Million - Through 10-Year Call Date

Estimated Available Funds:

Cash Reserves	\$5,000,000
Assumed Interest Earnings on \$5M to Call Date	\$1,787,552
Assumed Interest Earnings on Project Deposit	\$154,643
Total Estimated Available Funds	\$6,942,196

Estimated Costs:

Potential Debt Service to Call Date	(\$3,411,322)
Potential Cost to Redeem at Call Date	(\$3,290,241)
Total Estimated Costs	(\$6,701,563)

Potential Net (Cost)/Earnings Through Call Date **\$240,633**

Estimated Available Funds:

Assumed Interest Earnings from Call Date to Maturity	\$91,059
Potential Net (Cost)/Earnings Through Maturity	\$331,693

- Assumes 3.08% investment rate which is the 30-year average of Bank of America Merrill Lynch 1-3 year US Treasury Index.
- Project fund earns up to the arbitrage yield of 3.90% and makes 18-monthly equal draws.
- Assumes tax-exempt rates as of August 1, 2024 for \$5 million 20-year GO bond with S&P AA- rating.
- Assumes bonds are called in full in 10-years.

Assumes reinvestment of the \$240,633 at 3.08%.

Hypothetical Analysis – Bonding vs. Using Reserves (cont.)

Bond for \$5 Million - Through 20-Year Maturity

Estimated Available Funds:

Cash Reserves	\$5,000,000
Assumed Interest Earnings on \$5M	\$4,356,071
Assumed Interest Earnings on Project Deposit	\$154,643
Total Estimated Available Funds	<u>\$9,510,715</u>

Assumes \$5 million invested at 3.08% for full 20 years.

Estimated Costs:

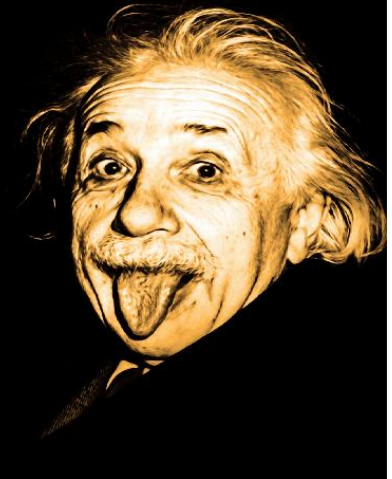
Potential Debt Service to Maturity	<u>(\$7,430,188)</u>
Total Estimated Costs	<u>(\$7,430,188)</u>

Assumes bonds are not called or refunded in 10 years.

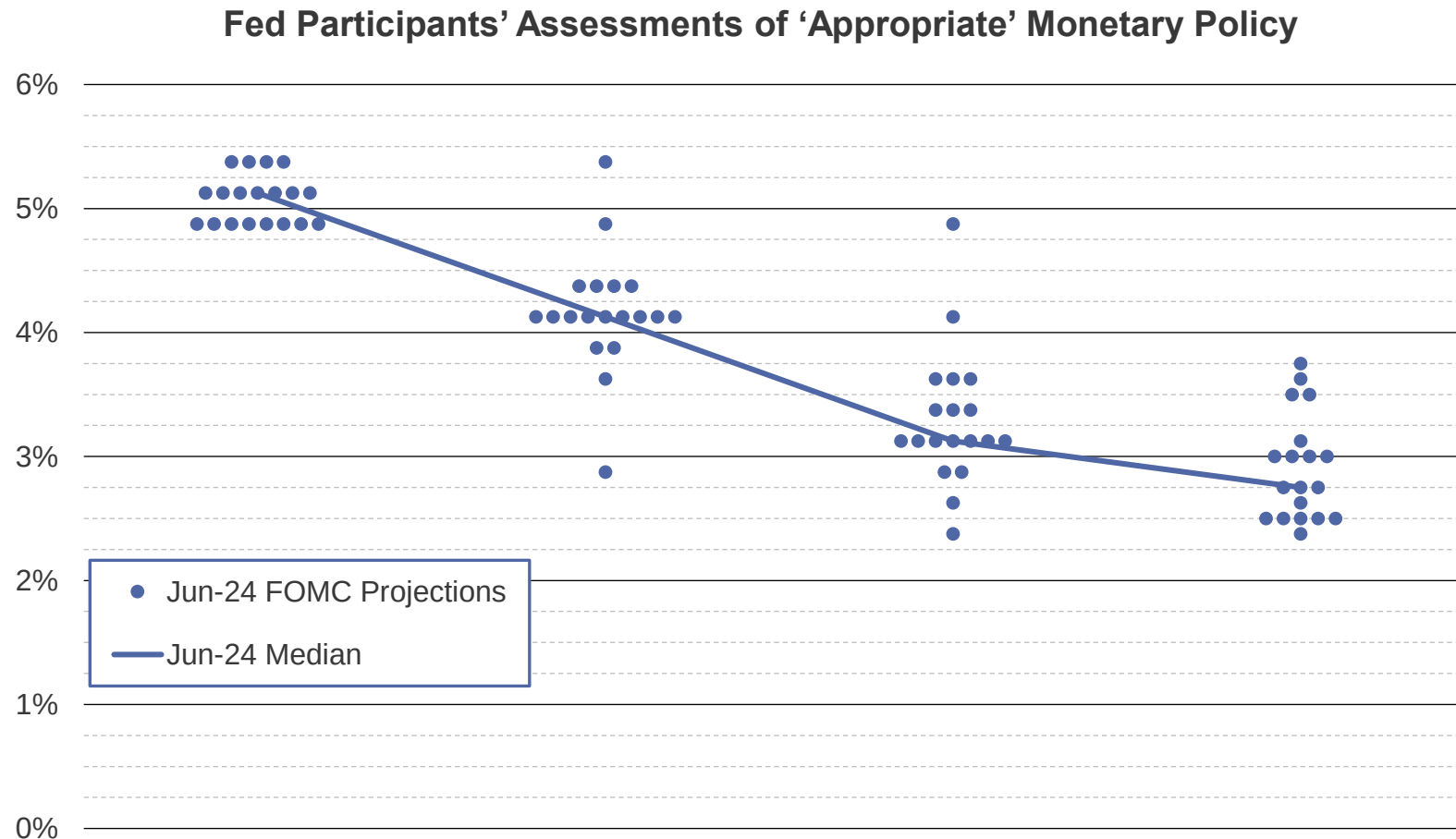
Net (Cost)/Earnings	\$2,080,527
----------------------------	--------------------

"Compound interest is the eighth Wonder of the World. He who understands it, earns it. He who doesn't, pays it."

- Albert Einstein



The Latest “Dot Plot” Shows One Rate Cut in 2024



Source: Federal Reserve and Bloomberg. Individual dots represent each Fed members' judgement of the midpoint of the appropriate target range for the federal funds rate at each year-end.

What is Arbitrage Rebate?

Arbitrage

- ▶ When the yield on taxable investments exceeds the tax-exempt restricted rate

Rebate

- ▶ Essentially a 100% tax
- ▶ Issuer's "rebate" or pay excess earnings to the IRS

Arbitrage Rebate

- ▶ Financial disincentive to violate the rules
- ▶ Non-compliance could result in taxable bonds

To prevent abuses, the tax code limits the permitted uses of tax-exempt bonds

Applies to every tax-exempt borrowing and some taxable subsidy obligations

Tax law and regulations create financial disincentives to prevent issuance of tax-exempt debt for profit-driven reasons

Prevents:

- ▶ Issuance of more bonds than are necessary
 - ▶ Issuance of bonds earlier than is necessary
 - ▶ Bonds from being outstanding longer than is necessary
 - ▶ In other words, borrow what you need, when you need it, for an appropriate duration based on what is being financed.
-
- ▶ Measured on an issue-by-issue basis
 - ▶ Arbitrate Rebate begins on the issue date
 - ▶ Yield Restriction begins at the expiration of a temporary period
-
- ▶ Yield restriction – IRC Section 148(b)
 - ▶ Arbitrage rebate – IRC Section 148(f)
 - ▶ Overlapping requirements – “Belt & Suspenders”

Exceptions to Arbitrage Rebate



- Small Issuer Exception
 - ✓ \$5 million of governmental bonds for municipalities
- Spending Exceptions
 - ✓ 6-month
 - ✓ 18-month
 - ✓ 2-year
- “Bona Fide” Debt Service Fund Exception
- Electing to pay the 1.5% penalty in lieu of rebate
- Investing in tax-exempt obligations (eliminating the “arbitrage”)

Spending Exceptions

- ▶ “Reward” for spending bond proceeds quickly
- ▶ Allowed to keep positive arbitrage
- ▶ Simple way to establish compliance (no future value, no yields)
- ▶ Must meet each benchmark, no catch-up allowed

Exception to
Arbitrage Rebate
Only

6-Month

All gross proceeds

✓ 6 months 100%*

18-Month

All new money

✓ 6 months 15%
✓ 12 months 60%
✓ 18 months 100%**

2-Year (ACP)

Construction issues

✓ 6 months 10%
✓ 12 months 45%
✓ 18 months 75%
✓ 24 months 100%**

* Exceptions for 5% of the proceeds of the issue if spent within one year

** De minimis (lesser of 3% or \$250K) and reasonable retainage (5% spent in 12 months) exceptions may apply for last benchmark

- **Arbitrage is not a bad thing!**

- ✓ It means the entity maximized how much could be earned. Not knowing how much is owed and making the payment is where problems would begin.
- ✓ Make sure the bond proceeds are deposited in a separate account and earnings are closely monitored.

- **Arbitrage – Tips for Compliance**

- ✓ Interest earned and expenses need to be tracked monthly to know how the local government is trending towards a potential rebate and if a spending exception can be met
- ✓ If small issuer exemption is not applicable, track investment return against bond yield
 - Tracking on a monthly basis will also help the local government identify the amount that should be left in the account to make the necessary rebate payment
- ✓ Monitor compliance with 6-month, 18-month or 2-year spending exceptions to rebate, if relevant
- ✓ Arrange for timely computation of rebate liability and, if rebate is payable, for timely filing of Form 8038-T and rebate payment
- ✓ Don't forget about yield restriction requirements that begin at the expiration of the 3-year temporary period

Questions?

Thank you for attending!



Kim Auchstetter

kauchstetter@newlenox.net

815-462-6430



Michelle Binns

binns@pfmam.com

872-240-6962



Sarah Sullivan

sarah.sullivan@spglobal.com

415-371-5051



Dalena Welkomer

dwelkomer@rwbaird.com

630-778-9857

Disclaimers



Investment advisory services are provided by PFM Asset Management LLC (“PFMAM”), an investment adviser registered with the U.S. Securities and Exchange Commission and a subsidiary of U.S. Bancorp Asset Management, Inc. (“USBAM”). USBAM is a subsidiary of U.S. Bank National Association (“U.S. Bank”). U.S. Bank is a separate entity and subsidiary of U.S. Bancorp. U.S. Bank is not responsible for and does not guarantee the products, services or performance of PFMAM. The information contained is not an offer to purchase or sell any securities. Additional applicable regulatory information is available upon request.

For more information regarding PFMAM’s services please visit www.pfmam.com.



Robert W. Baird & Co. Incorporated is providing this information to you for discussion purposes only. The information does not contemplate or relate to a future issuance of municipal securities. Baird is not recommending that you take any action, and this information is not intended to be regarded as “advice” within the meaning of Section 15B of the Securities Exchange Act of 1934 or the rules thereunder. In providing this information, Baird is not acting as an advisor to you and does not owe you a fiduciary duty pursuant to Section 15B of the Securities Exchange Act of 1934. You should discuss the information contained herein with any and all internal or external advisors and experts you deem appropriate before acting on the information.

S&P Global Ratings

Copyright © 2024 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

Australia: S&P Global Ratings Australia Pty Ltd holds Australian financial services license number 337565 under the Corporations Act 2001. S&P Global Ratings' credit ratings and related research are not intended for and must not be distributed to any person in Australia other than a wholesale client (as defined in Chapter 7 of the Corporations Act).

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.

spglobal.com/ratings

DISCLAIMERS AND COPYRIGHT NOTICE

The information and opinions conveyed at IGFOA conferences, institutes, and seminars are obtained from sources believed to be reliable, but IGFOA makes no guarantee of accuracy. Opinions, forecasts and recommendations are offered by individuals and do not represent official IGFOA policy positions. Nothing herein should be construed as a specific recommendation to buy or sell a financial security.

The IGFOA and speakers specifically disclaim any personal liability for loss or risk incurred as a consequence of the use and application, either directly or indirectly, of any advice or information presented herein. Unless otherwise indicated, all materials are copyrighted by the Illinois Government Finance Officers Association. The enclosed materials may not be reprinted, reproduced, or presented in any format without express written authorization. © 2024

Illinois Government Finance Officers Association
800 Roosevelt Road, Building C, Suite 312
Glen Ellyn, IL 60137
Phone: 630-942-6587
Email: info@igfoa.org
Visit <http://www.igfoa.org>