ICCCFO Spring Conference

Issuing Debt and Investing the Proceeds

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Today's Topics

- Issuing Debt
  - Overview of Borrowing Types
  - Working Cash Bonds
  - Bond Market Conditions
  - Method of Sale
- Investing Proceeds
  - IRS Reasonable Expectation Tests
  - Draw Schedule
  - Arbitrage Rebate Exceptions
  - Yield Restriction

Overview of Borrowing Types

Borrowing Options for Capital Projects – Illinois Community Colleges

Non-Referendum Bonds

Working Cash, Funding Bonds, PHS Bonds

Referendum Bonds

Alternate Revenue Bonds

Debt Certificates

Paid from tax levy

Paid from operating funds

Working Cash Bonds

Working Cash Fund Bonds

- Authorized by Section 3-33.2 of the Public Community College Act
- Proceeds of Working Cash Bonds are deposited into the Working Cash Fund
- Subject to limitation as to the lesser of the amount of Working Cash Bonds outstanding and Working Cash Fund size
- May be issued in excess of debt limit but once issued count against debt limit

Public Act 103-0278

- Public Act 103-0278 gives community colleges similar authority to Illinois K-12 school districts with respect to the use and flexibility of their working cash funds and clarifies that working cash fund bond proceeds may be used for any purpose (including capital projects) rather than just cash flow management.

Public Act 103-0278

- Monies in the working cash fund may be used for any and all community college purposes

- Did not change the bonding provisions for working cash bonds
  - They do not require a direct or backdoor referendum
  - They are subject to a BINA hearing
  - They will be limited tax bonds if issued by a tax-capped community college (subject to the Debt Service Extension Base)

Public Act 103-0278

- Also permits the abatement of the working cash fund
  - Via a resolution a community college may abate the working cash fund – to make a partial, permanent transfer of working cash fund moneys to the generating funds of the College at any time during the fiscal year and the moneys will not need to be reimbursed

Working Cash Fund Bonds

- What’s your community college’s working cash bond limit?
- Can you avoid the two-step debt certificates-to-funding bonds process?
- How might working cash bonds fit into the College’s longer term financing plan?

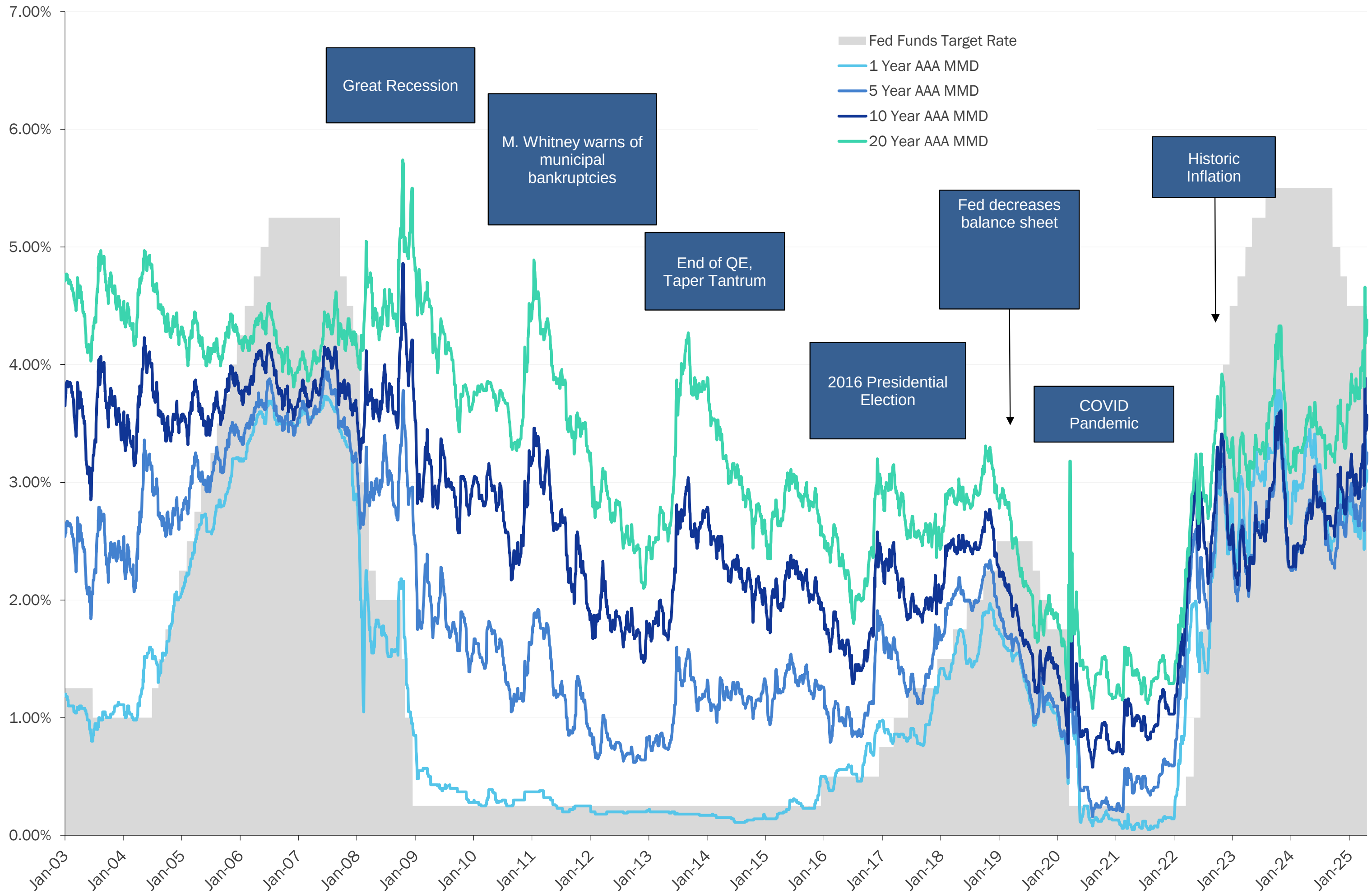
Bond Market Conditions

Bond Market Tone

- The tax-exempt bond market has been volatile given recent tariff announcements by President Trump
  - They have elevated concerns about a global trade war and a slowdown in economic growth, leading to increased expectations for rate cuts
    - Potentially at least four cuts anticipated this year, with the first one likely in June

- The tax-exempt bond market will continue to respond to both global and domestic economic data, including monthly CPI reports and employment data

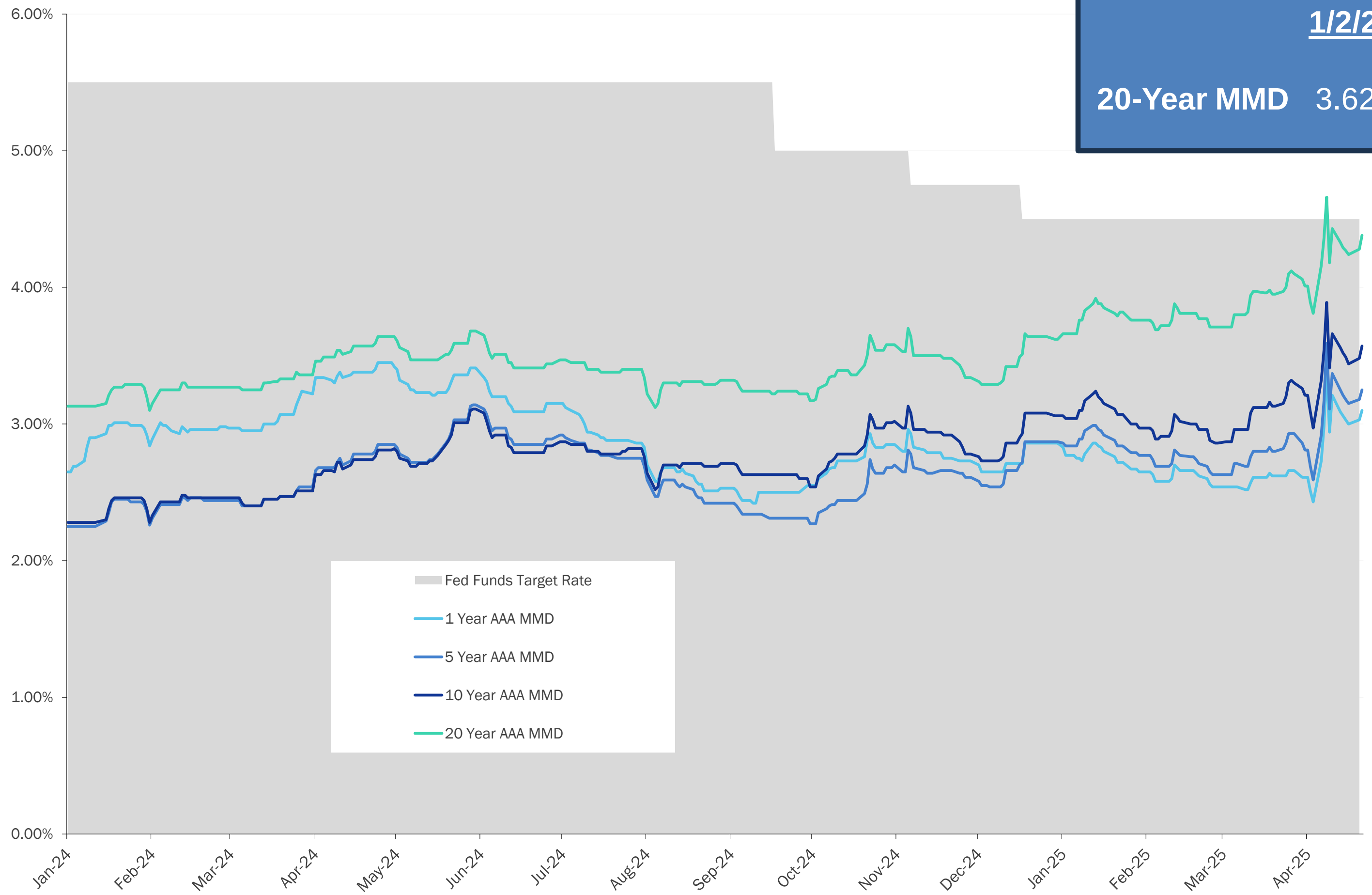
Historical Tax-Exempt Rates



*The Municipal Market Data "MMD" is a AAA municipal bond market index produced by TM3. As of April 22, 2025.

Tax Exempt Rates since January 1, 2024

	1/2/25	4/10/25	4/22/25
20-Year MMD	3.62%	4.66%	4.38%



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20-Year MMD Changes (Basis Points)

4/8	+35
4/9	+20
4/10	+30
4/11	-48
4/14	+25
4/15	-10
4/16	-04

- Next Fed meetings: May 6/7, June 17/18, July 29/30
- CPI and employment reports will be released monthly

Method of Sale

Sale Type

PUBLIC OFFERING

- The Issuer and financial advisor prepare an official statement
- Underwriter that will resell the bonds to investors is selected via a competitive or negotiated sale
- Issuer obtains a bond rating
- Requires disclosure counsel to review the official statement
- Will likely have a lower interest rate, but will have higher costs of issuance

DIRECT PLACEMENT

- No official statement, rating, underwriter or disclosure counsel is required
- A term sheet is sent out to banks and other local units of government that will provide a proposal to purchase the bonds directly
- The interest rate is typically higher than a public offering but may result in a lower overall financing cost since some costs of issuance are avoided
- This process has typically proven to be effective for relatively smaller bond issues paid off with a shorter amortization

Types of Public Offerings

NEGOTIATED SALE

- The Issuer preselects a broker-dealer as underwriter
- This firm sells the bonds to investors

COMPETITIVE SALE

- The Issuer engages a municipal advisor to manage the bond issuance process
- Underwriter selected via a competitive sale in which multiple bids are received to purchase the bonds
- The winning bidder sells the bonds to investors
- The bidder with the lowest true interest cost is selected

Choosing the Method of Sale

A competitive sale is appropriate when:

- Issuer has a strong underlying credit rating at least in the "A" category
- General obligation bonds or full faith obligations (e.g. alternate revenue bonds or debt certificates)
- Structure does not include special features that would require extensive explanation to the market
- Issuer is frequently in the market and/or issue size is conducive to attracting investors

A negotiated sale is appropriate when:

- Issuer has a credit rating lower than "A"
- Bond insurance is unavailable
- Debt structure is complicated
- Issuer wants input in how bonds are allocated among underwriting firms and/or the types of investors to be reached
- Other factors exist that the issuer, in consultation with its municipal advisor, believes favor the use of a negotiated sale process

Source: Selecting and Managing the Method of Sale of Bonds (February 2014), Government Finance Officers Association (Best Practice).
See the following webpage: http://www.gfoa.org/selecting-and-managing-method-sale-bonds

Method of Sale

- Consult with the College's municipal advisor about which method of sale should be selected for your bond issue
- Be flexible about each transaction, particularly in times of market volatility

IRS Reasonable Expectation Tests

IRS Reasonable Expectation Tests

- When issuing tax exempt bonds, the College should consider the following IRS requirements:
  - The College must reasonably expect to spend or contractually obligate 5% of a bond issue within six months of issuance
  - The College must reasonably expect to spend 85% of the bond proceeds in three years
  - The College must diligently spend the bond proceeds

- During the aforementioned 3-Year "Temporary Period," bond proceeds may be invested at materially higher yields than the bond yield

Construction Draw Schedule

- A community college should work with its architect and/or construction manager to establish an estimated monthly draw schedule as soon as possible
  - Doing so will enable your municipal advisor to determine whether the bonds may be sold all at once per IRS rules, and whether the College can qualify for one or more exceptions from arbitrage rebate (see next section)
  - Seek assistance to project potential arbitrage rebate

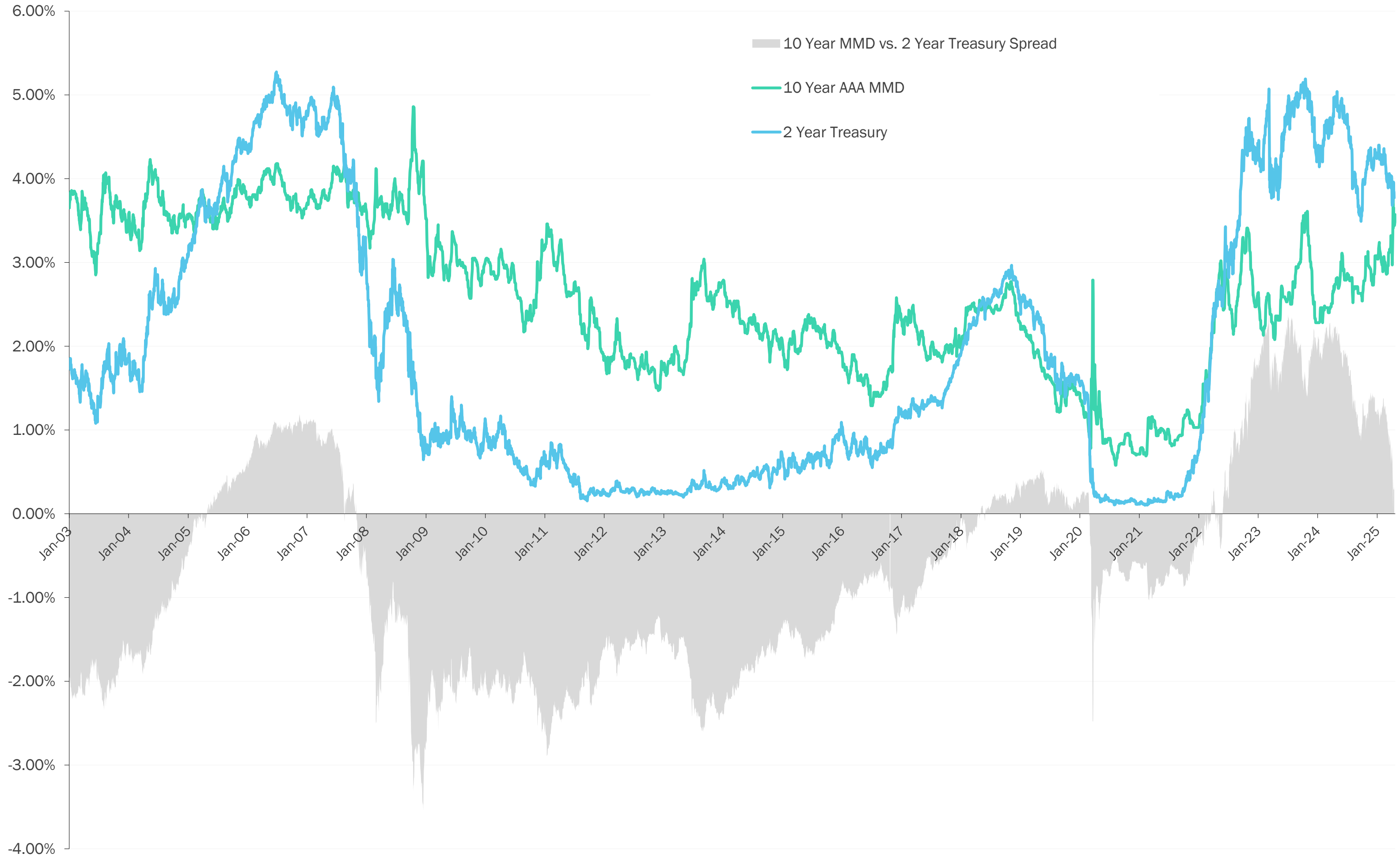
Arbitrage Rebate Exceptions

What Can a Community College Invest in?

- Defined by Illinois Statute - (ILCS 235)
  - Registered Money Market Fund Pools
  - US Treasury and Agency Securities
  - Certificates of Deposit
  - Demand/Checking Accounts
  - Corporate Obligations
  - Municipal Securities
  - Repurchase Agreements

- Further defined by the College's Investment Policy (Section 4:30)

Positive Arbitrage - 10yr MMD vs 2yr US Treasury



Arbitrage Rebate

- Arbitrage generally refers to investing tax-exempt proceeds in certain taxable investments that provide higher investment yields than the yield paid on the tax-exempt bonds
  - The Federal government is providing a subsidy through lower borrowing costs and forgoing tax revenues so the College should not get a double benefit through arbitrage
- Arbitrage profits
  - Generally, have to be paid to the Federal government
  - Payment of arbitrage profits to the Federal government is called “rebate”
  - Every five years and at the final retirement of all the Bonds, Issuer must pay (or rebate) arbitrage profits to the Federal government
- Certain exceptions
  - Small issuer exception
  - Spend-down exceptions

Arbitrage Exceptions

- Small issuer exception for community colleges
  - Generally, $5,000,000 in a calendar year
  - $15,000,000 of tax-exempt bonds in a calendar year if for construction

- Spend down exception if the issuer does not qualify for “Small Issuer”
  - “Reward” for spending bond proceeds quick enough
  - Allowed to keep positive arbitrage
  - Must meet each spending benchmark, no catch up allowed…

    See next slide for more detail

Spend Down Exceptions

6-Month	18-Month	2-Year (ACP)
All gross proceeds	**All new money (including land purchase)**	**Construction issues**
✓ 6 months 100%*	✓ 6 months 15%	✓ 6 months 10%
	✓ 12 months 60%	✓ 12 months 45%
	✓ 18 months 100%**	✓ 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*

Yield Restriction

Yield Restriction

- After 3 years from the closing date (upon expiration of the Temporary Period), tax-exempt bond proceeds:
  - Enter Yield Restriction Status
  - May not be invested in investments guaranteed by the federal government (i.e. FDIC CDs)
    - Exception: U.S. Treasury Securities

Arbitrage Considerations and Yield Restriction

Best Practices

- Understand the general rules regarding arbitrage rebate
- Engage your municipal and investment advisors to prepare an analysis that will help the College satisfy IRS requirements and maximize interest earnings while monitoring compliance with spending exceptions
- Arrange for timely computation of rebate liability and payment if necessary
- Arbitrage is not a negative, it simply means you've earned all the interest you are allowed to earn

Questions? Contact Us

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