Community College League of California

March Legislative Webinar

2017 Tax Cuts & Jobs Act Summary & Implementing Legislation Impacting Facilities Financing for Community Colleges

Today's Webinar

- *Facilities Projects - Budget Update*
- *2017 Tax Cuts & Jobs Act Summary*
- *Implementing Legislation Impacting Facilities Financing for California Community Colleges*
- *Q & A*

Presenters

Introduction to Presenters

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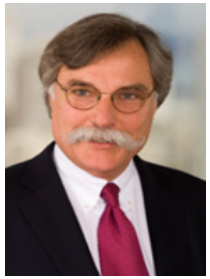

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Facilities Projects

Honoring the Will of Voters

Fund Capital Outlay Projects

- In 2016, California voters approved a facilities bond providing a $2 billion infrastructure investment in California's community colleges.

- For the 2018-19 budget, the Governor proposed funding for only five of 14 capital outlay projects.

- Our community colleges have $29.9 billion in unmet facility needs identified in the current Capital Outlay Plan.

Projects Left Out of the Budget

1. Los Rios, Natomas Education Center Phase 2 and 3
2. Mt. San Jacinto, Menifee Valley Center Math and Science Building
3. Cabrillo College, Modernization of Buildings 500, 600, 1600
4. Imperial Valley College, Academic Buildings Modernization
5. College of San Mateo, Building 9 Library Modernization
6. Skyline College, Workforce and Economic Development Prosperity Center
7. College of the Sequoias, Basic Skills Center
8. Monterey Peninsula, Fort Ord Center Ft Ord Public Safety Center
9. Woodland College Performing Arts Facility

Total $8,365 $137,850

The Right Economic Decision

- Waiting to approve worthy projects will increase the costs of these projects.
- Approving the nine unfunded projects would only add about $7.4 million in annual interest costs over the next 30 years.
- Funding all 14 projects is only 20% of the total bond authority granted by Prop 51.

2017 Tax Cuts and Jobs Act Bill Summary and other 2017 California Legislation (AB 195)

Tax Reform's Potential Impact on Municipal Market

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- **Both House and Senate passed different versions of the bill in early December, budget conferences made revisions in mid-December, and President Trump signed on December 22, 2017. These changes take effect January 1, 2018:**

Provision	Description	Impact on Municipal Issuers and Market
Individual Income Tax Rates	Modifies seven brackets (10% - 37%)	May reduce attractiveness of tax-exempt bonds
State and Local Tax Deduction (SALT)	$10,000 cap for combination of state property tax, income and sales tax deduction	May induce investors in high-tax states to seek more tax-exempt bonds
Corporate Tax Rate	Reduce to 21%	May lower attractiveness of tax-exempt bonds for corporations and insurance companies
Tax Credit Bonds	Eliminates ability to issue QZABs, CREBs, QSCBs, BABs, and other tax credit bonds	No changes to subsidy payments for bonds issued before December 31, 2017; may reduce incentive to fund energy efficiency projects
Advance Refundings	Eliminates tax-exempt advance refundings	Limits issuers to current refundings; may reduce feasibility of refundings and encourage use of taxable bonds or forward delivery structures
Fiscal Impact	Estimated to generate $1.5 trillion deficit over the next decade	Deficit of more than $150 billion in any year may trigger additional sequestration of Federal Subsidies for BABs and similar products; may increase Treasury borrowing needs which may increase bond interest rates

Tax Reform's Potential Impact on Municipal Market

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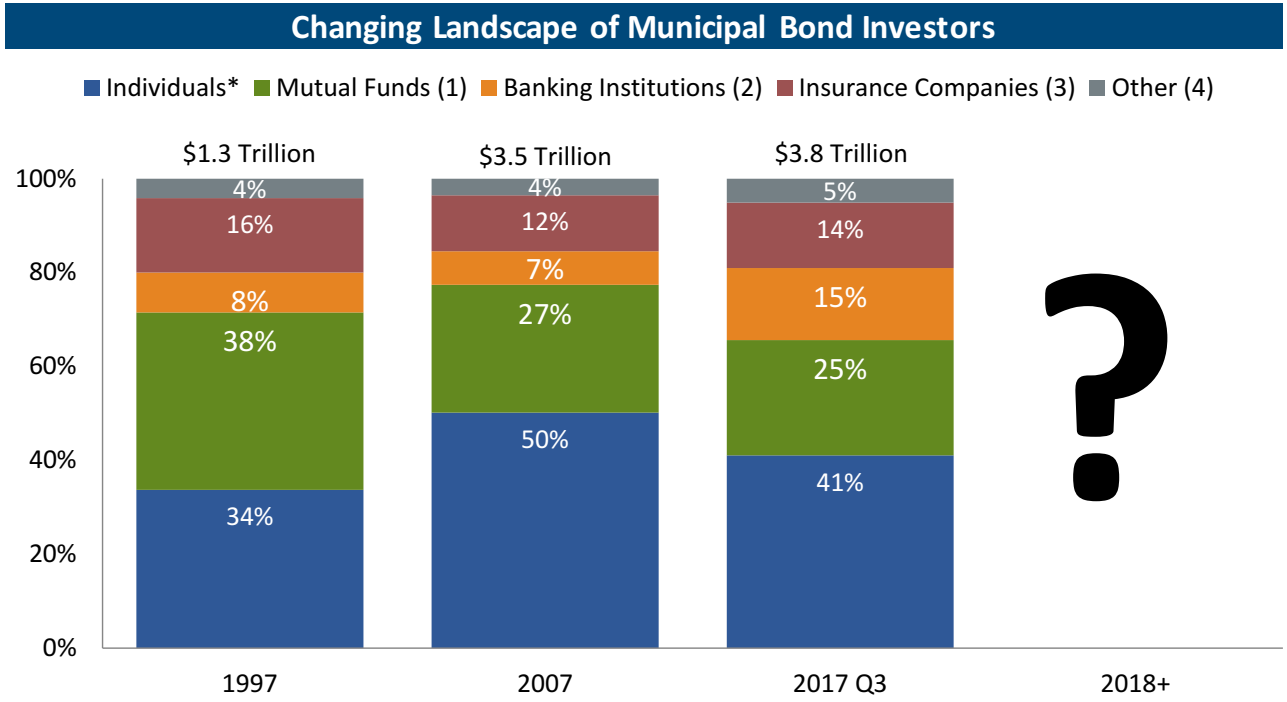
- **2018 bond issuance volume is expected to be 20% - 25% lower in the aftermath of significant Q4 2017 issuance coupled with elimination of advance refundings and tax credit bonds**
- **The bill does not cap or repeal municipal bond exemption, remaining one of the few tax-advantaged vehicles available for taxpayers**
- **The reduction of corporate tax rate to 21% will likely reduce the appetite of bank portfolios and property/casualty insurance companies for tax-exempt municipals**



Source: SIFMA and the Federal Reserve System

(1) Includes mutual funds, money market funds, closed-end funds and exchange traded funds.

(2) Includes U.S. chartered depository institutions, foreign banking offices in the U.S., banks in U.S. affiliated areas, credit unions, and broker dealers.

(3) Includes property-casualty and life insurance companies.

(4) Includes nonfinancial corporate business, nonfinancial non-corporate business, state and local governments and retirement funds, government-sponsored enterprises and foreign holders.

* Household holdings is revised up by about $840 billion, on average, from 2004 forward.

Tax Reform's Potential Impact on CA CCDs

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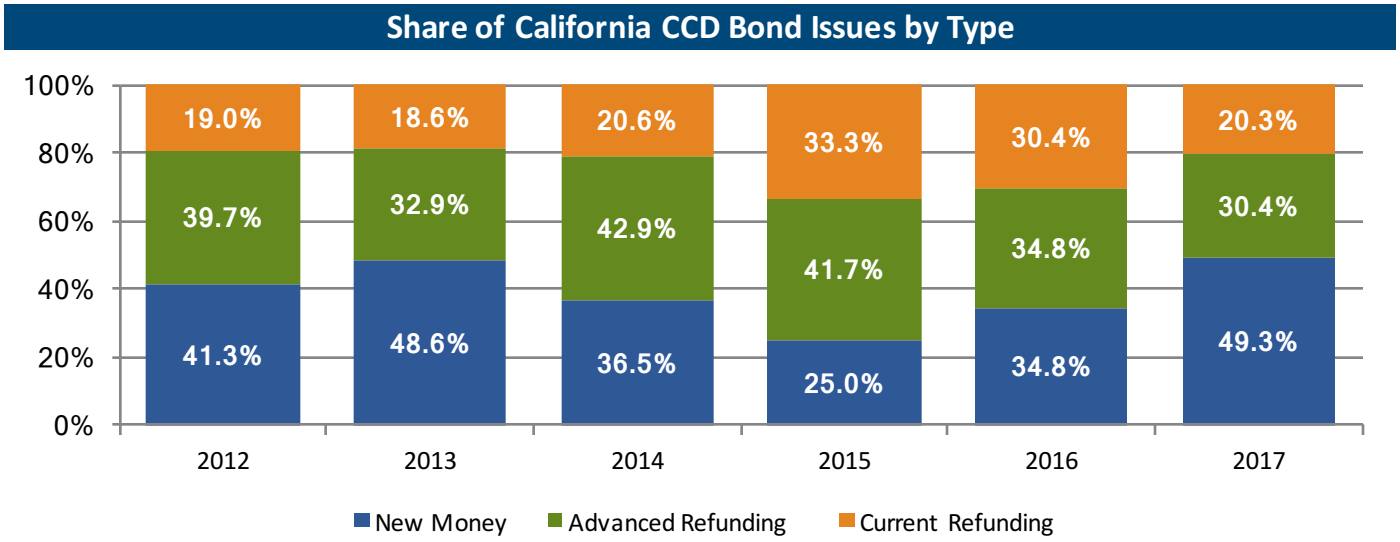
- **The limitation to $10,000 of the State and Local Government Tax Deduction and/or property tax deduction cap and the mortgage interest deduction cap ($750,000 max mortgage) could put negative pressure on California local taxpayers and impact CCDs' ability to pass local bond measures**
- **The elimination of the tax credit bond programs increase the cost of borrowing for California educational facilities (QZABs and CREBs have been a tool for solar & energy efficiency projects in recent years)**
- **The elimination of tax exempt advance refundings reduces the ability to restructure or refinance for savings on securities previously issued**
  - May create new call provision structure for selling new bond issues (i.e. going from 10 year call provisions to shorter call protection, 7, or 5 years)



Source: Thomson Reuters.

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Assembly Bill 1194 (Dababneh)

- **Tax Rate Statements must now include:**
  - The best estimate of the average annual tax rate that would be required to be levied to fund the bond issue over the entire duration of the bond debt service
  - **The final fiscal year in which the tax is anticipated to be collected**
  - The best estimate of the highest tax rate that would be required to be levied to fund the bond issue, and an estimate of the year in which that rate will apply
  - The best estimate of the total debt service, including the principal and interest, that would be required to be repaid if all the bonds are issued and sold

Assembly Bill 195 (Obernolte)

- **75-Word Ballot Statement :**
  - Must include the amount of money to be raised annually and the rate and duration of the tax to be levied for the bonds
  - Must be a true and impartial synopsis of the purpose of the proposed measure
  - Must be in language that is neither argumentative nor likely to create prejudice for or against the measure

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Unintended Consequences of AB 195

- **Confusion instead of transparency**
- **Possible emergency legislation**
- **Requirement consumes 16 of the 75 available ballot question words**

Sample Ballot Statement
"To _____, shall this measure of the _____ Community College District issuing $___ in bonds at legal rates be adopted, levy on average 2.5 cents per $100 assessed value, $___ annually for _____ [e.g. job training facilities], while bonds are outstanding, with annual audits, etc.?"

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Senate Bill 450 (Hertzberg)

- **Prior to authorization of the issuance of bonds with a term greater than 13 months the governing body of a public body shall obtain and disclose all of the following information in a meeting open to the public:**
  - The true interest cost of the bonds
  - The finance charges of the bonds (essentially costs of issuance)
  - The amount of proceeds received by the issuer less finance charges, reserves and capitalized interest
  - The total payment amount of the bonds (debt service + finance charges not paid with proceeds of the bonds), calculated to the final maturity date
- **Good faith estimates can be provided by the underwriter, financial adviser or private lender**
- **SB 450 determinations will be added to the bond issuance resolution**

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Senate Bill 1029 (Hertzberg)

- **Establishes local debt policies and reporting requirements for California local government agencies**
- **Effective for all debt sold on or after January 21, 2017**
- **A report must be provided no later than 30 days prior to issuance to California Debt and Investment Advisory Commission (CDIAC) that the issuer has adopted a debt policy and that the bond issue complies with those debt policies**
- **Local debt policies should include the following**
  - The purposes for which debt proceeds may be used
  - The types of debt that may be used
  - The relationship of the debt to, and integration with, the issuer's capital improvement program or budget
  - Policy goals related to the issuer's planning goals and objectives
  - The internal control procedures that the issuer has implemented, or will implement, to ensure that the proceeds of the proposed debt issuance will be directed to the intended use
- **Annual report submitted to CDIAC no longer than 7 months after fiscal year reporting period is over (July 1-June 30)**
  - First reports due this year in January

Financial Markets Overview

Financial Markets Overview

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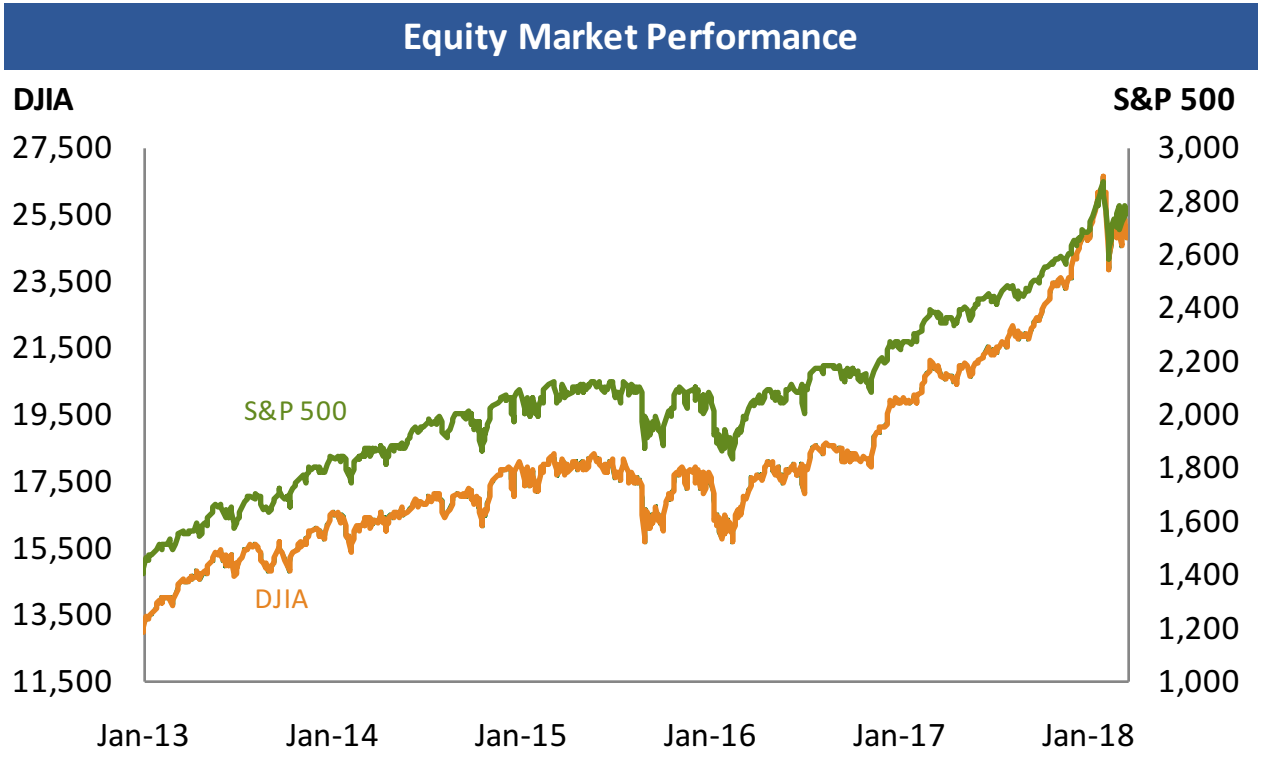
- **Strong equity markets through Q4 2017**
  - Dow, S&P 500 and NASDAQ have consistently hit new records



Source: US Treasury Department, Bloomberg, Thomson Reuters. As of 3/22/18

Financial Markets Overview

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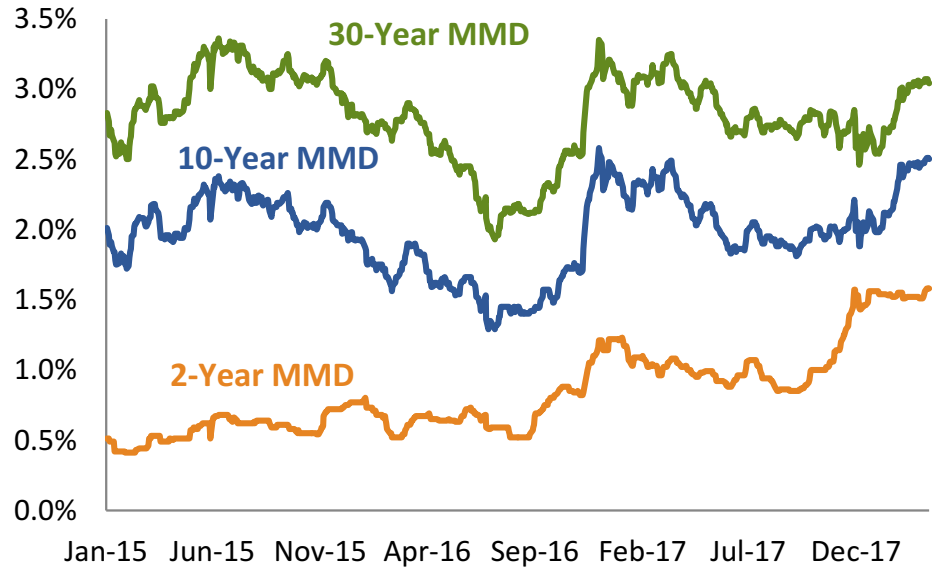
- **Gradual rate increases by FOMC**
  - Fed Funds Target Rate increased 5 times since December 2016, most recently from 1.50% to 1.75% at the March 20, 2018 meeting
  - Expectations for 2 additional rate hikes in 2018
  - Dovish members of the FOMC see headwinds to the economy subsiding

Treasury Market Yields



- **Fixed income yields drifting higher**
  - Over 2017, Treasury yields rose 70 bps on the 2 year, 28 bps on the 5 year, less than 3 bps on the 10 year, while the 30 year yield dropped by over 32 bps
  - Long end moving higher to start 2018; 10 year Treasury closed at 2.83% on March 22nd, up 37 basis points from start of 2018

Source: US Treasury Department, Bloomberg, Thomson Reuters. As of 3/22/18

Municipal Market Overview

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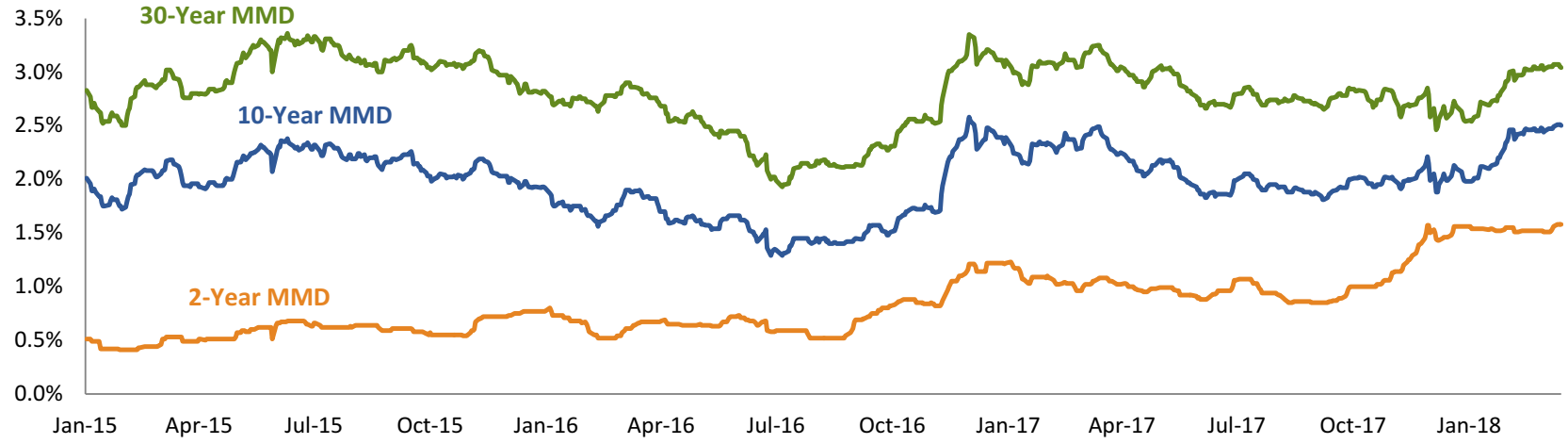
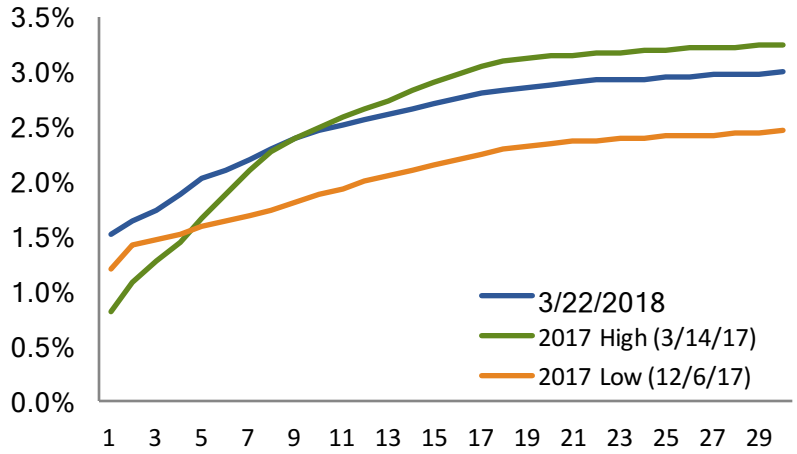
'AAA' Municipal Market Data Yields



MMD Yield Curve



Market Indices Snapshot

	3/22/2018	3/22/2017	Change on Year (bps)	3-Year Average	10-Year Average
US Treasury					
2 Year	2.28%	1.27%	101	0.94%	0.87%
10 Year	2.83%	2.40%	43	2.10%	2.63%
30 Year	3.06%	3.02%	4	2.78%	3.50%
AAA MMD					
2 Year	1.64%	1.05%	59	0.86%	0.74%
10 Year	2.47%	2.30%	17	1.98%	2.42%
30 Year	3.00%	3.10%	(10)	2.81%	3.57%
SIFMA 7DAY	1.36%	1.23%	13	0.35%	0.53%
MIG 1 - 1YR	1.52%	0.93%	59	0.63%	0.54%

Sources: Thomson Reuters. As of 3/22/18

Municipal Market Supply and Demand

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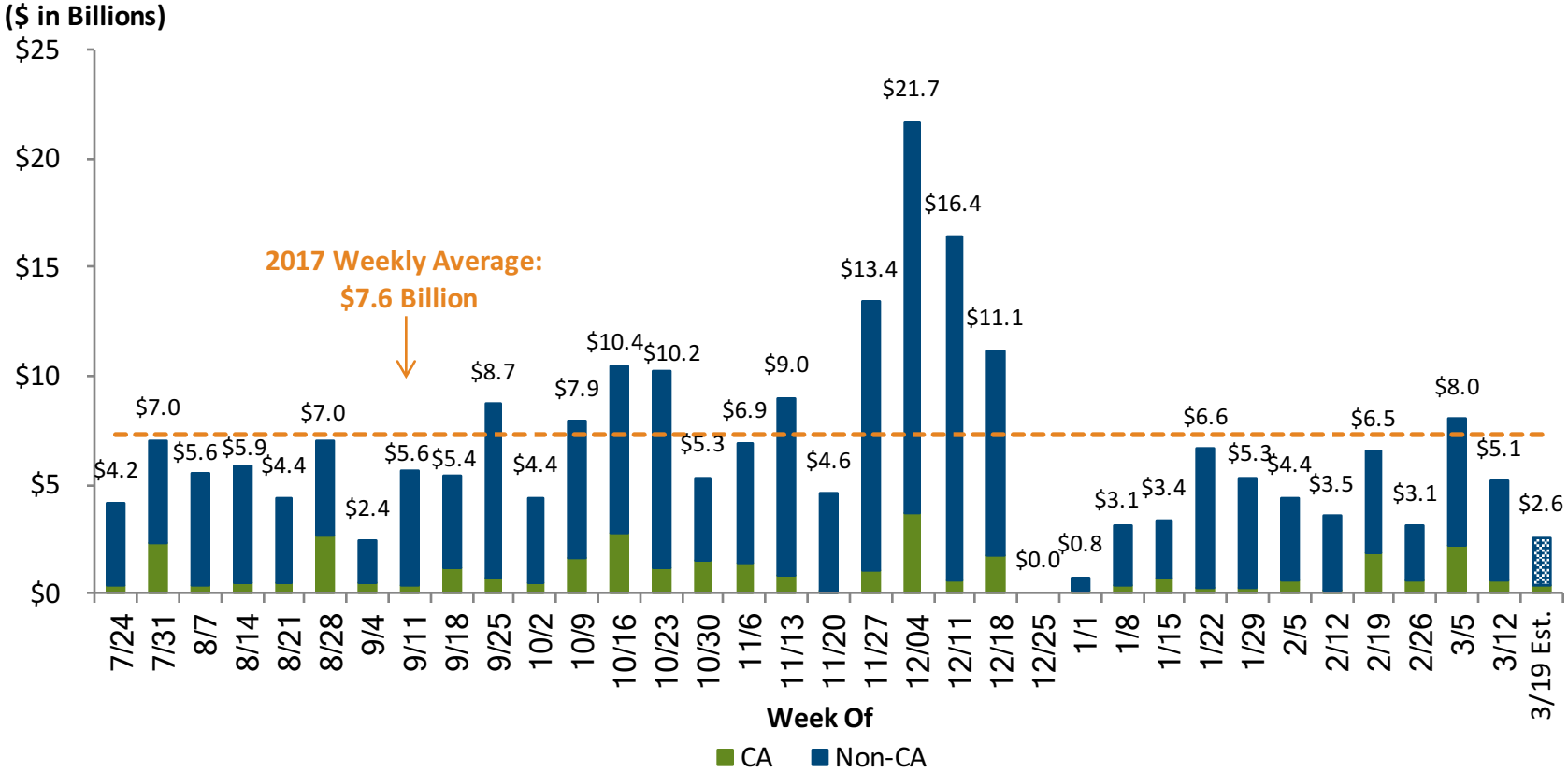
- **New negotiated calendar is expected to increase**
  - $2.6 billion supply estimated for the week of March 19th

National Weekly Municipal Bond Issuance



Sources: Thomson Reuters. As of 3/22/18

Municipal Market Supply and Demand

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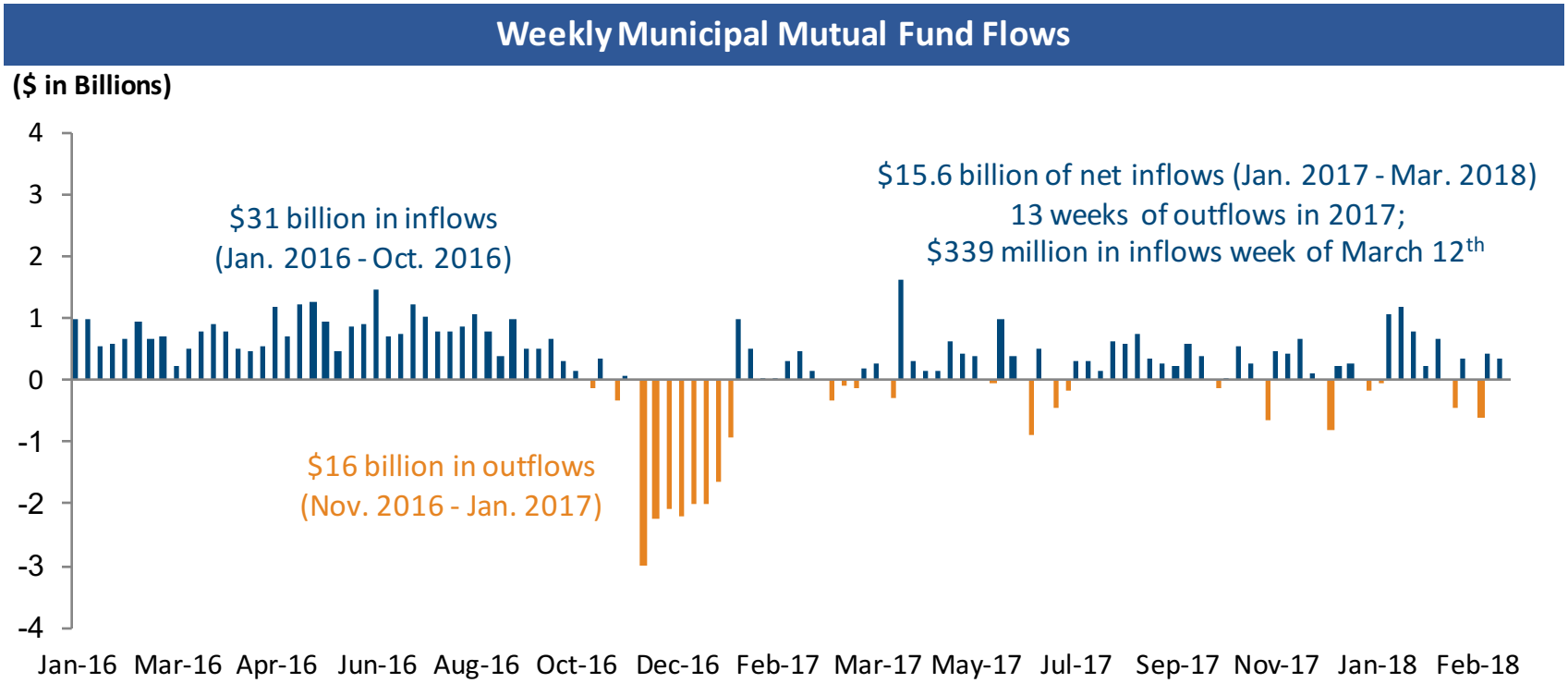
- Municipal bond funds have reported inflows totaling $339 million the week of March 12th
- Demand for municipal bonds is strong
  - Nearly constant inflows since the beginning of 2017 netting $15.6 billion



Sources: Thomson Reuters, Investment Company Institute. As of 3/22/18

Conclusion:

Questions

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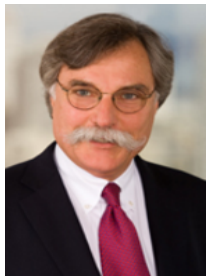

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Mr. Casnocha is the managing shareholder of Stradling's San Francisco office and a former member of the firm's board of directors. David has practiced in public finance for more than 40 years and serves as bond and disclosure counsel to public agencies and underwriter's counsel to both national and regional investment banking firms. He also has served as bond counsel to more than 600 school and community college districts in California. He has experience in primary and secondary school district financings, general obligation bonds, bond anticipation notes, certificates of participation, lease financings and tax and revenue anticipation notes. In addition, David has represented the California Education Facilities Authority on numerous private university financings and represents a range of nonprofit corporations that incur tax-exempt debt to finance their charitable purposes. As bond counsel to the California League of Community Colleges, he has helped design tax-exempt pool financings for tax and revenue anticipation notes, lease revenue bonds solar energy projects, and student housing. David also served as bond counsel on Other Post-Employment Benefit bond issues. He is experienced in a range of revenue bond financings for water, sewer and a variety of other enterprise systems.

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Robert Barna is a Managing Director in the Los Angeles public finance office of Stifel. Mr. Barna began his public finance career in 1993 and has experience in all facets of the municipal finance business. He specializes in the management, structuring and sale of California K-12 Education new money and refunding general obligation bonds, certificates of participation, tax credit bonds, Mello-Roos bonds and tax and revenue anticipation notes. Throughout his career, he has completed more than 200 financings totaling over $15.0 billion.

Mr. Barna graduated with a degree in Economics from University of California, Berkeley and a Masters of Business Administration from Columbia University. Mr. Barna maintains his Series 7, 50, 53 and 63 licenses with FINRA.

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John R. Baracy is a Managing Director in the Los Angeles public finance office of Stifel. Mr. Baracy began his public finance career in 1994 and has experience in all facets of the municipal finance business. He specializes in the management, structuring and sale of California K-12 Education and Community College District new money and refunding general obligation bonds, certificates of participation, tax credit bonds, Mello-Roos bonds and tax and revenue anticipation notes. In addition to managing the introduction of these financings into the market, Mr. Baracy performs debt capacity, general obligation bond tax rate and credit analyses, charter school finance analyses, California K-12 education finance legislation analyses, and evaluates the investment of bond proceeds. Throughout his career, he has completed more than 500 financings totaling over $9.25 billion.

Mr. Baracy graduated with a Bachelor of Science degree from Arizona State University with an emphasis in Finance. Mr. Baracy maintains his Series 7, 50 and 63 licenses with FINRA and frequently presents for California K-12 school district advocacy groups such as C.A.S.H., CASBO and CSBA. Mr. Baracy is currently on the C.A.S.H. Board of Directors.

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