Proponent Testimony of the Jack Schron, Jr., 6th District County Council, for Cuyahoga County

Regarding House Bill 251

I am pleased to present my testimony grading HB 215. My name is Jack Schron. I am currently serving my third term as 6th District Cuyahoga County Councilman where I represent approximately 130,000 people on the East and South sides of Cuyahoga County   I chair the Council's Economic Development Committee and serve on the county's Investment Advisory Committee.   I have served in these roles for about six years.

In my capacity on the three member Investment Advisory Committee it is our responsivity to set the investment policy for county funds and to seek out, through our oversight responsivity, to balance risk and returns on behalf of the county. The return on investments with the interest rates being at all-time lows has made it difficult to achieve favorable returns at the required risk levels. In an effort to seek higher returns while still seeking low levels of risk the Investment Advisory Committee adopted The **CUYAHOGA COUNTY Municipal Infrastructure Program.**

The **CUYAHOGA COUNTY Municipal Infrastructure Program** is a program that allows for the investment of a portion of the county's funds currently invested in our approved investment to now be invested by purchasing the bonds and other obligations of Cities, villages, townships, school districts and special districts whose boundaries are fully or partially within the County. The Program (see attached) is designed to assist the various types of governmental bodies by providing them a lower interest rate while returning to the county, payments at higher rates than we can achieve through traditional investments. This policy is designed to be a win/win for all involved,

The **CUYAHOGA COUNTY Municipal Infrastructure Program** has been in effect since 2014. During this time there has not been a single City, village, township, school district or special district to use the program. The reason mentioned is that the time and costs associated with processing under this program is not warranted due to The State of Ohio's current limitation of five years. We are being told that the time and origination fees cannot be justified to refinance or create original financing for only five years.

Today I speak in support of HB 251 to extend the period from five years to ten years. Counties having the funds would be able to earn their taxpayers, within their counties, higher returns while providing a valuable services to Cities, villages, townships, school districts and special districts whose boundaries. This would provide these governmental bodies with cost savings to borrow funds at better than market rates, recall higher priced borrowing instruments and do it over a longer period of time. This will provided a new tool which would provide certainly for both the county in its investment portfolio and the borrower and I encourage the passage of HB 251.

Thank you

Jack H. Schron, Jr.
6th District Councilman
Cuyahoga County

Attachment #1
In support of Proponent Testimony of the Jack Schron, Jr., 6th District County Council, for Cuyahoga County, Regarding House Bill 251

CUYAHOGA COUNTY Municipal Infrastructure Program Policies and Procedures Approved by Investment Advisory Committee February 3, 2014

Overview and Purpose

Cuyahoga County (the "County") has determined that it is in the best interest of the County and the political subdivisions that are located within the County to establish a program whereby the County purchases debt (bonds and notes) directly from political subdivisions within the County in the event that those entities do not have direct access to the markets that have been traditionally available to them in raising money for capital projects.

Specifically, most political entities have typically accessed the capital markets through the issuance of Limited Tax General Obligation Notes and Bonds ("LTGO Debt") in the public market. Some communities have been precluded from issuing new LTGO Debt since the most recent reappraisal of property in the County. With a reduction of assessed valuation, these communities are unable (or have limited capacity) to issue additional LTGO Debt under Ohio's constitutional ten-mill limitation. This constitutional debt limit sets a cap on maximum annual debt service on LTGO debt for all overlapping political subdivisions at 10 mills of property taxation. Consequently, as assessed valuation falls, the capacity to issue new LTGO Debt also falls.

The goal of the program is to assist the various local governments throughout the County in accessing capital in an efficient and cost effective manner. The County intends to invest in bonds and notes issued by local government entities. The County intends to invest only in securities that it deems to be secure. It will analyze each bond or note purchased to determine if the security features being offered by the borrower are adequate to provide the County with the protection it needs. The County intends for this program to be consistent with the risk limitations that apply to other investments that are eligible to be purchased in its portfolio.

Eligibility

Type of Government: Cities, villages, townships, school districts and special districts whose boundaries are fully or partially within the County.

Need of Local Government:

✓ Ability to Issue GO debt: An applicant must demonstrate that (i) it does not currently have capacity to issue additional LTGO Debt or (ii) that the issuance of the new debt that is the subject of the application would result in less than 1 mill of remaining capacity under the 10 mill limitation if it were issued as LTGO Debt.

Cuyahoga County Municipal Infrastructure Program Policy Statement page 2

✓ Project Size: The County will consider applications for projects of $3,000,000 or less and will limit its total exposure to any entity to $3,000,000.

Credit Considerations

Types of Credit: The County will consider bonds and notes secured by the following types of revenue streams:

✓ Income Tax Pledge

✓ Non-tax Revenue Pledge

✓ Utility (Water and Sewer) Revenue Pledge

The County will not consider purchasing LTGO Debt because the primary purpose of the program is to assist entities nearing their LTGO debt limit. The County is also explicitly excluding bonds backed solely by a TIF revenue pledge or special assessment revenue pledge due to the perceived higher level of risk associated with such bonds and notes.

Maturity: Consistent with its current investment policy, the maximum maturity of any issue will not exceed 5 years from its date of issuance. Due to the illiquid nature of these investments, the County will not commit its resources for a longer duration.

Amortization: The County prefers to purchase bonds/notes from issuers participating in this program that will be fully amortized over the initial term of the loan. Nevertheless, the County recognizes that not all participating entities will have the desire or financial wherewithal to fully amortize the loan during the period that the securities are initially held by the County.

✓ Minimum Amortization: For those entities that do not fully amortize the loan during the initial term, the County is exposed, by definition, to risk associated with the ability of the borrower to refinance the balloon at the end of the initial term (presumably 5 years). In order to partially mitigate this risk, the County will require 40% amortization during the period it holds the bonds/notes and amortization will commence no later than the first anniversary of the loan and such amortization will result in approximately level total debt service payments in years 1 – 4 with a balloon for the balance in year 5. Bonds that are not fully amortized (without a balloon payment) will bear a higher interest rate than fully amortizing bonds (See "Interest Rates" below).

Coverage: For bonds/notes that are secured by either an income tax or non-tax revenue pledge, the issuer will be required to demonstrate minimum coverage of 300% of maximum annual debt service (excluding the balloon payment) The coverage will be calculated using the actual revenue stream from the pledged source from the year immediately preceding the issuance of the bonds. *Cuyahoga County Municipal Infrastructure Program Policy Statement page 3*

It is important to demonstrate strong coverage so that the issuer has the demonstrated capacity to refinance the bonds at the end of the initial 5 year period. If coverage is not strong, the issuer may not have an alternative outlet, and the County could be placed in a position of refinancing the loan for an indefinite period of time after the initial 5 year term. This potential constraint on the County's liquidity is not acceptable. Minimum coverage requirements for water or sewer utility debt will be set at lower levels (150%).

Lien Status: The County will require a pledge from the issuer that it has not issued and will not issue any debt that has a lien on the revenue stream that is superior to the lien received by the County. In other words, the County should not be subordinated to any other debt of the issuer that employs the same revenue stream as the bonds/notes held by the County. The County shall allow the issuance of additional bonds of the issuer pledging the same revenue stream on a parity or subordinated basis under the condition that the additional bonds do not jeopardize the minimum coverage requirement pledged to the County held bonds.

Debt Service Reserve: There will be no formal requirement for a debt service reserve fund, but the County reserves the right to insist upon a reserve up to 10% of the issue if it deems the credit quality of the applicant to be weak.

Payment Schedule: The County will require deposits into principal and interest accounts on a monthly basis and will further require that the accounts be fully funded at least 30 days prior to the principal or interest payment date which it is intended to fund. This funding system provides the County with an "early warning system" in the event that the issuer does not make timely deposits into the appropriate principal or interest account. Principal and interest payments will be payable semi-annually.

Call Feature: The County will permit issuers to call all or a portion of any note/bond issue at par on or after the second anniversary date of the issue by providing 30 days' notice to the County. The County seeks to provide the participants in the program with maximum flexibility in managing their individual debt portfolios. The County will not permit bonds/notes to be called prior to maturity if the called securities are to be refinanced with an additional loan from the program.

Revenue Intercept: The County will expect each participating jurisdiction to enter into an agreement with the County that will enable the County to intercept Local Government Fund payments due to the participating jurisdiction from the County in the event that the participating jurisdiction is delinquent in making required deposits of principal and interest in a timely manner. The County will consider purchasing bonds/notes without the intercept feature, but such issues will carry a higher rate of interest than those incorporating the intercept feature (See "Interest Rates" below). *Cuyahoga County Municipal Infrastructure Program Policy Statement page 4*

Application and Review Process
The County strives to create an application and review process that is thorough yet simple and streamlined. Each participant application should include the following information:

✓ Name of Issuer

✓ Primary Contact Information

✓ Bond Counsel Contact Information

✓ Project Description

✓ 2 Most Recent Audited Financial Reports

✓ Description of Revenue Stream Pledged

✓ 5 Year History of Pledged Revenue Stream

✓ Schedule of Outstanding Debt of the Issuer with an identification of any outstanding debt secured by the pledged revenue stream

✓ Future Capital Plans

✓ Authorizing Legislation

✓ Most recent rating reports (if available)

✓ Budget projections for next 5 years (if available)

✓ Other supporting documentation as required by the County to make an informed decision.

The County will create a review committee to approve/deny each application. This Committee will consist of the County Treasurer (or designee), the County's investment advisor, the County's financial advisor and legal counsel to the County. There will be a modest fee charged by the advisor(s) and legal counsel, and such fee will be incorporated into the costs of issuance of the borrower's bond/note issue. Fees imposed by the County will be available to the borrower at the time of application.

As part of the review process, a "due diligence call" will be held with the issuer at which time the review team members can pose questions directly to the issuer.

Loan Documentation
At the closing of each bond/note issue, the County will receive a transcript of proceedings from the issuer that includes all of the typical closing documents except that the County will not require:

✓ Preliminary or Final Official Statement

✓ Ratings

✓ Opinion attesting to the tax-exempt status of the bonds being purchased.

Program Parameters
Program Size: The program size will be capped at 10% of the average par amount of the County's investment pool for the preceding three years.

Maximum Bonds Maturing Per Year: The County will strive to have the total amount of bonds maturing in any year to be no more than 25% of the maximum pool size. This provision will be phased in over the first 5 years of the program.

Interest Rates

The County intends to provide the issuer with a fair and attractive interest rate while at the same time earning an attractive yield on its portfolio. Since the County does not benefit from tax-exempt interest rates, the rates will be set based upon a “spread” to treasuries, which is the most common method of pricing taxable municipal bonds.

The spread to treasuries will change over time in the market. The County will publish its interest rate setting mechanism on a quarterly basis for bonds purchased by the County during that quarter. The yield on the 5 year treasury bond will be utilized as the benchmark rate and the credit spread will be set by the County with input from its investment advisor. The base rate will be for issues that participate in the intercept program and also are fully amortized (no balloon) during the initial term of the issue. Additional spread will be added for loans that do not participate in the intercept program and for loans that are not fully amortized (balloon at final maturity). The actual rate for each bond issue will be set on the date that the County purchases the bonds based upon the 5 year treasury rate on that date plus (or minus) the approved “spread” for the then current quarterly period. Credit spreads for issuers not taking advantage of the intercept feature and for those not structuring a fully amortizing loan will be set by the County with input from its investment advisor at the same time that the base interest rate spread is set each quarter.

The County understands that the program will not always produce the optimal result for some issuers. It is the County’s goal to offer an alternative to other available financing tools, but the County encourages issuers to examine all of the financing options available to them.

Miscellaneous

The following items (not previously discussed) are hereby addressed in this policy:

✓ Bond Counsel: Bond Counsel will be selected by the issuer.

✓ Paying Agent/Registrar: The County will hire a single paying agent/registrar for the program whose primary responsibility will be to hold (i) any debt service reserve funds, (ii) monthly deposits of principal and interest, and (iii) pay principal and interest to the County when due.

✓ Program Fees: The County intends to recover its expenses for administering the program (investment advisor/financial advisor/legal counsel). A master fee schedule will be available to issuers at the time of application.

✓ Ratings: Not required

✓ Credit Enhancement: Not required

✓ Notice to County Prior to Maturity: Each issuer must provide notice to the County of its plans to refinance the bonds/notes held by the County on their final maturity date at least 1 year prior to such date. If the entity plans to refinance the original bonds/notes with an additional sale to the County, it must submit a new application at the time that the notice is given. The County will approve or reject the application within 60 days of its receipt. This process is intended to provide each issuer with ample time to seek alternative financing plans in the event that the County elects to not purchase the refunding notes/bonds. If a renewal bond or note is purchased by the County, the interest rate will be set at the maturity of the initial bond or note being refinanced.

Attachment #2
In support of Proponent Testimony of the Jack Schron, Jr., 6th District County Council, for Cuyahoga County, Regarding House Bill 251

CUYAHOGA COUNTY Municipal Infrastructure Program Frequently Asked Questions –

Who can participate in the program?

Virtually all local governments in the County can participate in the program. We are not restricting participation by type of government. However, a participant must be able to demonstrate that they have no capacity or very limited capacity to borrow on an unvoted general obligation basis under Ohio's 10-mill limitation.

Why must a participant demonstrate limited capacity under the 10-mill limit?

Traditionally, local governments throughout Ohio have met their borrowing needs through the issuance of unvoted general obligation bonds and notes which are subject to Ohio's constitutional "10 mill limit". We the recent downturn in assessed valuation, borrowing capacity has been diminished or eliminated in many of our communities. The result is that many needed infrastructure projects have been delayed due to lack of access to the bond market. The County wants to provide our smaller communities with a vehicle to get these projects back on track.

Why has project size financed under the program been limited to $3,000,000?

There are a couple of reasons that we have placed a limit on project size. First, the County has limited capacity to invest in bonds and notes of local governments within its investment portfolio, and it does not want that capacity concentrated in just a few of our participating governments. Second, it is our contention that issuers of larger bond issues would have the ability to explore other means of accessing the capital markets through the issuance of revenue bonds, non-tax revenue bonds, etc. These may not be cost effective vehicles for smaller projects.

We would normally issue bonds for 20 or 25 years. Why have you limited the County's program to issues of 5 years or less?

The County simply does not have the ability to tie up assets in its investment portfolio for 20 to 25 years. Our investment policy calls for maximum maturity on all investments of 5 years, and we must build our program to operate within the prudent parameters set by that policy. We will be willing to consider buying future bonds/notes that refund a portion of those originally purchased by the County. However, we cannot make that firm commitment at this time.

We understand that the program would allow the County to intercept our local government fund payments. Why is this required and why would we agree to it?

Yes, the County is asking each participant to enter into an agreement that will allow the County to intercept local government fund payments due to the participating entity in the event that the participant is delinquent in paying its principal and interest obligations. The State of Ohio currently has intercept programs for school districts and community colleges where State aid can be intercepted if their participating districts are not current on their debt payments. It is our understanding that those intercepts have never been implemented. Likewise, we do not ever expect the need to intercept payments due to you, but this feature clearly provides us with a strong security feature. The County will consider purchasing bonds/notes from entities that do not enter into an intercept agreement, but the interest rate will be higher than for those participants who do enter into an intercept agreement. If a participant is confident in its ability to meet its obligations, we see no reason why it would not enter into the agreement.

What will determine if an application is approved or denied?

The County (with the assistance of their advisors) will completely review the information provided with each application. At the conclusion of the review, we will provide each application with a "thumbs up" or "thumbs down". We will, of course, first determine if the applicant meets the basic conditions of participation. Second, if an applicant is willing to participate in the revenue intercept feature, the odds of approval increase. Likewise, loans that are fully amortized over the initial loan period will have a higher likelihood of approval because the risk of refinancing at the end of the initial term has been eliminated. The most important factor after meeting the basic participation guidelines will undoubtedly be the strength and reliability of the revenue stream being pledged to repayment. The County will not be "grading" applications. We do not want to be in the business of creating a hierarchy of credits within the County. We are not a rating agency. All approved applications will be eligible for the same interest rate treatment. Consistent with this practice, applications will either be approved or denied without dissemination of any scoring scale or hierarchy. For those applications that the County considers "marginal", we will work with the applicant to improve the credit characteristics being offered. The goal of the program is to help the applicant finance the project while, at the same time, protecting the invested assets of the County.

Do we need to fully amortize our bonds/note over the 5 year term?

No. The County is requiring that 40% of each loan be amortized during its initial term. However, if a participant fully amortizes the loan without a balloon at final maturity, it will have the opportunity to receive a lower interest rate on its loan.

How are interest rates determined?

The bonds/notes purchased by the County will carry an interest rate spread to the 5 year treasury. This is not a tax-exempt rate. We are using a taxable scale because the County does not benefit from tax exempt income. The spread to the 5 year treasury will be set by the County with input from its investment advisor. The actual rate will be locked in on the date that the County purchases the bonds/notes. We will offer a base rate (bonds notes that fully amortize and participate in the intercept) and higher rates for those bonds/notes that do not incorporate these two features. The rate will be fixed for the term of the bond/note.

Are ratings required?

Our goal is to make this program as administratively simple and minimize issuance costs in the process. We are not requiring participants to seek a rating, and we are not requiring the preparation of a preliminary or final official statement. You are free to use your existing bond counsel.

What if I borrow under the County's program and want to refinance at a later date?

No problem. The County has no interest in requiring you to remain in the program if you find a better alternative. The bonds/notes purchased under this program will be callable at any time.

Does this program provide me with the best solution to our borrowing needs?

We don't know and we encourage you to explore all of your options. Our goal is not to offer a program that is the "be all and end all" program. Our goal is to provide you access to capital at a time when your traditional avenue is not available to you. We offer an efficient road to accessing capital for smaller projects within the constraints imposed upon us by the County's investment policy.