DEBT AND BOND FINANCING OF AIRPORT PROJECTS

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OVERVIEW – BRINGING BONDS TO MARKET

1. Bond Basics – The Straight and Skinny about Bonds
2. Legal principles
3. Structuring – how (and why) do we put this together?
4. Disclosure
5. Credit and marketing
6. Private placements vs. public offering
1 BOND BASICS

Everything you wanted to know, but were afraid to ask…
BOND BASICS

- Bonds are a loan – a promise to pay from identified revenues
  - Pledge of specified funds
  - Single borrower, generally multiple lenders
  - Trustee = lenders’ representative
- Airport bonds = revenue bonds
- State law governs bond issuance
- Federal law controls federal tax exemption
- Federal securities laws govern disclosure
WHY BONDS?

- Bonds allow for asset/liability matching
  - Repayment terms matched to the assets’ lives
  - Users pay the capital cost as they use them
- With tax exemption provides low cost of capital
- The market – including rating agencies, investors, SEC and IRS – monitors financial management and long-term focus
BOND INDENTURE

- A critical airport agreement – you need to know it!
- Pledge: specified revenues
  - What revenues are pledged or excluded?
  - Using PFCs
  - Interaction with Use and Lease Agreement
- Covenants, e.g.,
  - Coverage tests
  - Additional bond tests
  - Maintenance of assets
- Additional bonds test
- Restrictions on amendment
BOND PURCHASE AGREEMENT

- A “P&S” for bonds
- Conditions precedent to closing
  - “Roadmap” of required documents and conditions
  - Attached forms of opinions
  - “Outs” for underwriters
- Specifies primary terms
- Arm’s length transaction
- Letter of representations in conduit financing
TAX AGREEMENT

- Required for tax opinion
- Memorializes tax analysis
- Sets forth continuing and future obligations
- Finance and legal staff need to understand these requirements
  - Translate from the legalese
  - Template for annual compliance checklist
The trinity of regulation
AUTHORITY TO ISSUE BONDS

- State law question
- Typically interpreted narrowly
- Must demonstrate compliance with requirements
- Pledge requirements/limits
- Additional UCC requirements, if any
- Every state has its quirks!
FEDERAL SECURITIES LAWS

- What is a “security”?  
- SEC’s limited power to regulate municipal bonds  
- Rule 10b-5  
  - Materiality  
  - Responsibilities of issuers and others  
  - Applies to all statements to “the Market”  
- Rule 15c2-12  
  - Primary disclosure – the Official Statement  
  - Secondary disclosure  
    - Annual filings  
    - Event filings
FEDERAL TAX LAW

- Governmental bonds (Non-AMT)
- Private activity bonds (AMT)
  - Airport facilities – what qualifies?
  - TEFRA?
- Taxable bonds
  - Non-exempt facilities
- Ongoing compliance requirements
  - Rebate and spending
  - Private use and changes in use
  - Audits and retaining records
Addressing the issuer’s needs and investor concerns. What are the variables?
THE PLEDGE

- Clear, carefully drafted definition
- Airports typically pledge revenues, not unlimited taxes (“GOs”)
- Does pledge work with your Use and Lease Agreement?
- Revenues pledged
  - General airport revenue bonds (“GARBs”)
    - Exclusions often as important as pledge; e.g., PFCs or CFCs
  - Senior and subordinate liens
  - “Offsets” such as PFCs
  - Special facilities: limited source
    - Well suited for facility financing
INTEREST RATE

- Fixed rate is most prevalent
- Variable rates more flexible, but increase risk
  - Often require additional security
  - Interest rate reset periodically
  - May be tied to external index – beware the death of LIBOR!
  - Can be paired with swaps
- Taxable bonds becoming more popular
  - Less on-going compliance issues
  - Larger world-wide market
  - Higher rates?
OTHER CONSIDERATIONS

- Refunding vs. New Money
- Amortization and call options
- Derivatives
- Reinvestment of bonds proceeds and structured investment products
- Bond insurance
Impact of Federal Securities Laws – Speaking to The Market must be done with care
OFFICIAL STATEMENT

- Describes the issuer, the bonds, and security
- Issuer’s document
- No material misstatement or omission
- “Expertised” portions
  - Audited financial statements
  - Report of the Airport Consultant
  - Market study
- Risk factors
REPORT OF THE AIRPORT CONSULTANT

- Expert’s report
- Often required for additional bonds
- “Forward looking disclosure”
- Projects revenues and expenses into the future
CONTINUING DISCLOSURE

- Underwriter’s requirement under Rule 15c2-12
- Creates Issuer obligations:
  - Annual filing
    - Financial information
    - Operational data from OS
  - Event notices
    - Disclosure within 10 days
    - Internal reporting critical
    - New reportable events
      - Other material “debt-like” obligations and terms
      - Evidence of “financial difficulties”
Selling your debt to The Market
Credit ratings of Rating Agencies represent an “expert opinion” on the issuer’s ability to repay its debt
- Investors increasingly form their own credit assessments
- Credit ratings can have a substantial impact on pricing
- Changes in the credit rating can greatly shift investor sentiment
RATING PRESENTATIONS

- During a transaction, issuers generally get “one shot” to present their credit to the rating agencies.
- Rating agencies rely upon available information to formulate their opinion, but the rating presentation is a chance for the issuer to tell the story.
- A lead analyst and backup analysts are responsible for the review, but the rating is ultimately assigned by a Committee.
MARKETING BONDS TO INVESTORS

- Traditionally, most of the communication with investors is through the underwriter and the sales team
- Timing limited by the release of the POS
- Investors now seeking direct access to issuers:
  - Online investor presentations or “Net Road Shows”
  - Investor Luncheons
  - Physical Roadshows
  - One-on-one calls and meetings
  - Advertisements, radio spots
INVESTORS

- Ultimate buyers
- Individuals to large funds and banks
  - Bond (mutual) funds and asset managers
  - Insurance companies
  - Hedge funds and arbitrage investors
- They have the money, and lend it to the issuer
- They want their money back, with interest
  - Greater emphasis on credit quality than returns
  - Rely on ratings but do own credit analysis
- They want to know what’s going on – disclosure is key
  - Prompt
  - Accurate
PRIVATE PLACEMENT & DIRECT PURCHASES

What changes when you are not selling to The Market?
PUBLIC OFFERING vs. DIRECT PLACEMENT

- Public offering most typical
  - Requires Official Statement
  - Generally a sale through underwriter
  - Underwriters purchase bonds for resale

- Direct placements very popular after market crash
  - Often a single purchaser
  - No OS or ratings
  - Now regulated by 15c2-12
  - May be a loan or a security
  - Proposed amendment to muni advisor rules
KEY DIFFERENCES FROM PUBLIC OFFERING

- May be different issuance or sale requirements
- No OS; ad hoc disclosure
- Different securities law analysis
- Need for Investor’s Letter
- Tax law still applicable
- Flexible, customized structuring
  - Continuing covenants?
  - Draw down structure?
- Often RFP process for bids
WRAP UP & QUESTIONS

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