Bonds and Post-Issuance Compliance

2024 BOOKKEEPERS CONFERENCE

March 15, 2024 | Rolling Meadows, Illinois

Introductions

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Agenda

- (1) Illinois School District Borrowing Options and Alternatives
- (2) Process of Issuing Bonds
- (3) Post-Issuance Compliance
  - (a) Arbitrage Rebate and Spending Bond Proceeds
  - (b) Private Use and Record Retention
- (4) Continuing Disclosure

(1) Illinois School District
Borrowing Options and Alternatives

What is a Municipal Bond?

- Municipal Bonds are issued to provide funds to state and local governmental units to build public projects and infrastructure
- Represents a promise to repay investors an amount of money borrowed (principal) along with interest (“debt service”), according to a fixed schedule
- Typically, an investor receives tax-free interest payments so it offers to buy Municipal Bonds at a lower interest rate
- Municipal Bonds usually mature between 1-20 years from issuance date (maximum 20 years per State statute)
- **Debt Service Levy:** Amount of property taxes requested to pay principal and interest on outstanding general obligation (GO) Municipal Bonds

School Borrowing Options

- The Illinois School Code prescribes very specific methods for school districts to issue municipal bonds which are as follows:
- Types of General Obligation (GO) School Bonds
  - GO School Building Bonds ***(paid from a separate bond levy)***
    - Authorized via referendum
  - Non-referendum GO Bonds ***(paid from a separate bond levy)***
    - Described in more detail on the next two slides
- Other borrowing options mechanisms ***(payable from operating dollars)***
  - Alternate revenue bonds
  - Debt or lease certificates
  - Capital leases
- Tax Anticipation Warrants (TAWs) for short-term cash flow needs

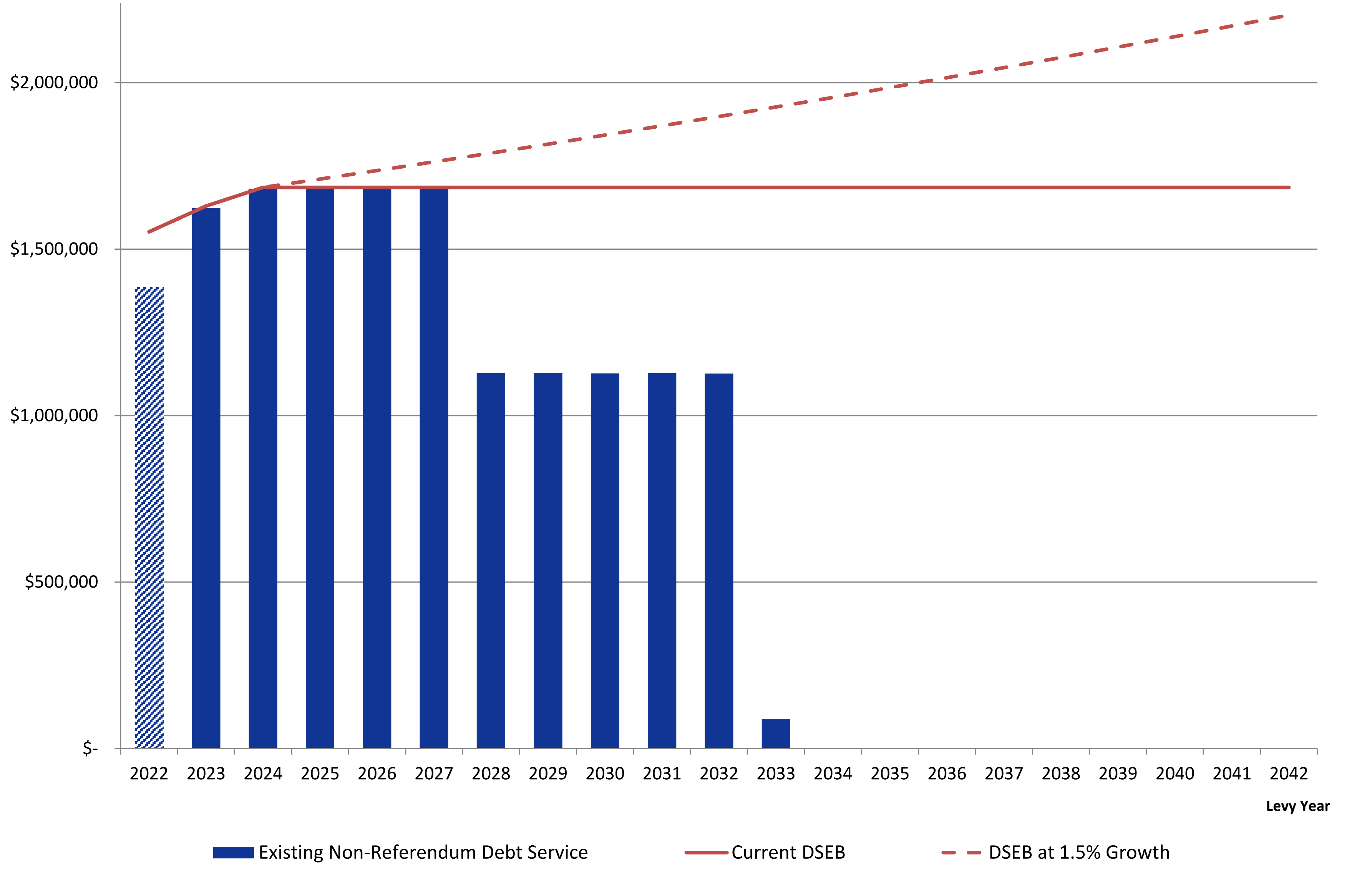
Non-Referendum GO Bonds

- School districts subject to the tax cap have a levy limit on the annual debt service payments for non-referendum GO bonds called the Debt Service Extension Base (DSEB)
- A district's DSEB is equal to the amount of non-referendum debt service levied in the year tax caps went into effect
  - Public Act 96-0501, enacted in 2009, increases a district's DSEB annually by lesser of the Consumer Price Index (CPI) or 5%
  - Example:

Original DSEB established in 1994: ***$1,191,364***

Current DSEB for levy year 2024: ***$1,685,263***

DSEB Example



Non-Referendum GO Bonds

- The following types of non-referendum GO bonds are available to school districts:
  - **Working Cash** (for capital projects or operating capital)
    - If for capital, funds are abated (permanent transfer) to the O&M fund and then transferred to the capital projects fund
  - **Life Safety** (issued in evidence of life safety approvals)
  - **Funding** (pays off a claim or liability like a land contract)
  - **Tort**
- However, in a tax capped county, a district must have a DSEB to issue the bonds listed above or have the bonds approved at a referendum
- Unless approved at referendum, all of these require a Bond Issue Notification Act (BINA) hearing
- Unless approved at referendum, Working Cash Bonds and Funding Bonds also require a back door referendum which is a 30-day petition process (10% of registered voters)

Legal Debt Margin

- 6.9% of EAV for K-8 and 9-12 districts, 13.8% of EAV for unit districts
- Less: outstanding principal

Levy Year	2022	2023	2024	2025	2026
Collection Year	2023	2024	2025	2026	2027
Fiscal Year Ending 6/30	2024	2025	2026	2027	2028
Direct Debt, Beginning of Period (1)	$ 16,030,000	$ 15,275,000	$ 12,890,000	$ 10,530,000	$ 8,130,000
Principal Paydown, Series 2021A (2)	(755,000)	-	-	-	-
Principal Paydown, Series 2021B (2)	-	(1,965,000)	(1,980,000)	(2,000,000)	(445,000)
Principal Paydown, Series 2024 (2)	-	(420,000)	(380,000)	(400,000)	(1,310,000)
Direct Debt, End of Period (1)	$ 15,275,000	$ 12,890,000	$ 10,530,000	$ 8,130,000	$ 6,375,000
Equalized Assessed Valuation	$ 239,623,433	$ 244,415,902	$ 249,304,220	$ 254,290,304	$ 259,376,110
Assumed EAV Increase		2.00%	2.00%	2.00%	2.00%
Statutory Debt Limit @ 13.80%	$ 33,068,034	$ 33,729,394	$ 34,403,982	$ 35,092,062	$ 35,793,903
Direct Debt, End of Period as % of EAV	6.37%	5.27%	4.22%	3.20%	2.46%
Statutory Debt Margin at End of Period (1)	$ 17,793,034	$ 20,839,394	$ 23,873,982	$ 26,962,062	$ 29,418,903

(1) Assumes that the principal due in the current year is paid or that the funds are set aside for payment. Does not include leases.
(2) Principal paid on January 1 of the fiscal year.

- Exemptions exist for some bonds
  - Working cash bonds and funding bonds are exempted at the time of issuance but count after issuance
  - Alternate Bonds do not count against a district's legal debt margin unless a tax is extended to pay debt service

School Borrowing Options Summary

Payable from a separate tax levy: Working Cash Bonds, Funding Bonds, Tort Funding Bonds, Life Safety Bonds, Building Bonds.
Payable from operating funds: Debt/Lease Certificates, Alternate Revenue Bonds.

	Working Cash Bonds	Funding Bonds	Tort Funding Bonds	Life Safety Bonds	Building Bonds	Debt/Lease Certificates	Alternate Revenue Bonds
Purpose	- Capital projects - Cashflow	- Capital projects - Pay claims	- Pay tort judgments or settlements	- Life safety projects	- School construction & renovation	- Capital projects	- Capital projects
Referendum Requirement	30-day notice period	30-day notice period	No	No	Yes	No	30-day notice period
Separate Tax Levy Available	Yes	Yes	Yes	Yes	Yes	No; paid from Operations	Yes; paid from Operations or other source
Subject to Debt Service Extension Base	Only if capped	Only if capped	Only if capped	Only if capped	No	No	No
Public Hearing Required (BINA)	Yes	Yes	Yes	Yes		No	Yes
Final Maturity Limit	20 years	20 years	20 years	20 years	20 years	20 years	40 years
Subject to Debt Limit	No	No	Yes	Yes	Yes	Yes	No (as long as levy is not accessed)
Other Restrictions	Principal limited by a working cash formula	Often a 2-step process involving initial issuance of debt certificates				Lease required for new building	Revenue coverage tests may apply

(2) Process of Issuing Bonds

How Are Bonds Sold to Investors?

BOND SALE

- PUBLIC OFFERING
- DIRECT PLACEMENT

COMPETITIVE SALE

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

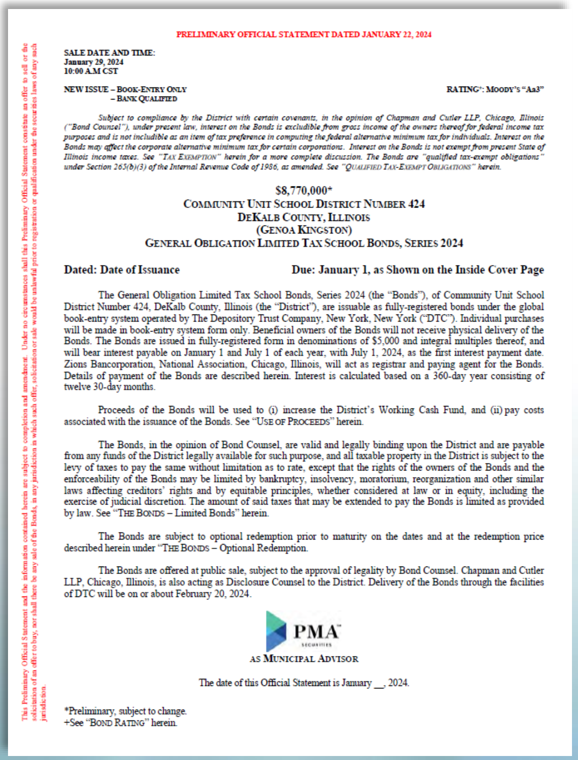
NEGOTIATED SALE

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

Participants in a Publicly Offered Bond Issue

Official Statement

- The official statement is the primary market disclosure document prepared by, or on behalf of, the Issuer in connection with a public offering of its bonds



PRELIMINARY OFFICIAL STATEMENT DATED JANUARY 22, 2024

This Preliminary Official Statement and the information contained herein are subject to completion and amendment. Under no circumstances shall this Preliminary Official Statement constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Bonds, in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction.

SALE DATE AND TIME:
January 29, 2024
10:00 A.M CST

NEW ISSUE – BOOK-ENTRY ONLY
– BANK QUALIFIED

RATING+: MOODY'S "Aa3"

Subject to compliance by the District with certain covenants, in the opinion of Chapman and Cutler LLP, Chicago, Illinois ("Bond Counsel"), under present law, interest on the Bonds is excludible from gross income of the owners thereof for federal income tax purposes and is not includible as an item of tax preference in computing the federal alternative minimum tax for individuals. Interest on the Bonds may affect the corporate alternative minimum tax for certain corporations. Interest on the Bonds is not exempt from present State of Illinois income taxes. See "TAX EXEMPTION" herein for a more complete discussion. The Bonds are "qualified tax-exempt obligations" under Section 265(b)(3) of the Internal Revenue Code of 1986, as amended. See "QUALIFIED TAX-EXEMPT OBLIGATIONS" herein.

$8,770,000*
COMMUNITY UNIT SCHOOL DISTRICT NUMBER 424
DEKALB COUNTY, ILLINOIS
(GENOA KINGSTON)
GENERAL OBLIGATION LIMITED TAX SCHOOL BONDS, SERIES 2024

Dated: Date of Issuance **Due: January 1, as Shown on the Inside Cover Page**

The General Obligation Limited Tax School Bonds, Series 2024 (the "Bonds"), of Community Unit School District Number 424, DeKalb County, Illinois (the "District"), are issuable as fully-registered bonds under the global book-entry system operated by The Depository Trust Company, New York, New York ("DTC"). Individual purchases will be made in book-entry system form only. Beneficial owners of the Bonds will not receive physical delivery of the Bonds. The Bonds are issued in fully-registered form in denominations of $5,000 and integral multiples thereof, and will bear interest payable on January 1 and July 1 of each year, with July 1, 2024, as the first interest payment date. Zions Bancorporation, National Association, Chicago, Illinois, will act as registrar and paying agent for the Bonds. Details of payment of the Bonds are described herein. Interest is calculated based on a 360-day year consisting of twelve 30-day months.

Proceeds of the Bonds will be used to (i) increase the District's Working Cash Fund, and (ii) pay costs associated with the issuance of the Bonds. See "USE OF PROCEEDS" herein.

The Bonds, in the opinion of Bond Counsel, are valid and legally binding upon the District and are payable from any funds of the District legally available for such purpose, and all taxable property in the District is subject to the levy of taxes to pay the same without limitation as to rate, except that the rights of the owners of the Bonds and the enforceability of the Bonds may be limited by bankruptcy, insolvency, moratorium, reorganization and other similar laws affecting creditors' rights and by equitable principles, whether considered at law or in equity, including the exercise of judicial discretion. The amount of said taxes that may be extended to pay the Bonds is limited as provided by law. See "THE BONDS – Limited Bonds" herein.

The Bonds are subject to optional redemption prior to maturity on the dates and at the redemption price described herein under "THE BONDS – Optional Redemption.

The Bonds are offered at public sale, subject to the approval of legality by Bond Counsel. Chapman and Cutler LLP, Chicago, Illinois, is also acting as Disclosure Counsel to the District. Delivery of the Bonds through the facilities of DTC will be on or about February 20, 2024.

PMA SECURITIES
AS MUNICIPAL ADVISOR

The date of this Official Statement is January __, 2024.

*Preliminary, subject to change.
+See "BOND RATING" herein.

- The official statement discloses all material information on the offering
- The official statement is the main source of anti-fraud liability in a municipal transaction
- The obligation for the accuracy and completeness of the disclosure lies with the Issuer
  - Experts may assist, but cannot completely discharge, the Issuer's obligation
  - Issuer, Underwriter, Municipal Advisor, Attorneys (Underwriter's Counsel/Disclosure Counsel/Issuer's Counsel) all have potential anti-fraud liability for material misstatements and omissions in an official statement

(3) (a) Post Issuance Compliance -- Arbitrage Rebate and Spending Bond Proceeds

Allowable Investments

What Can a School District Invest in?

- Defined by Illinois Statute - (30 ILCS 235)
  - Registered Money Market Fund Pools
  - US Treasury and Agency Securities
  - Certificates of Deposit
    - Federally insured up to $250k
  - Demand/Checking Accounts
  - Corporate Obligations
  - Municipal Securities
  - Repurchase Agreements
- Further defined by district Investment Policy
  - District investment policies can be more limiting that statute, not less.

Determining Investment Strategy

Investment Strategy

- The investment strategy should be focused on the district cash flow plan
  - Identifying an adequate liquidity level
  - Ensuring all liabilities are funded
    - **Matching assets to liabilities** and just in time funding
  - Identifying the low point in fund balance
    - Help pinpoint the amount of long-term investment potential
    - Laddering out the long-term portfolio
  - Think strategically about how you are budgeting interest income
    - Because of the variability of interest from year to year districts need to be careful relying on interest income to balance the budget

Investing Bond Proceeds
Arbitrage Considerations

What is Arbitrage?

Arbitrage Rebate

- Arbitrage: Difference between (i) what would have been earned if tax-exempt bond proceeds were invested at bond yield and (ii) the earnings on the investment of such tax-exempt bond proceeds in higher yielding securities.

- Rebate: Issuer must pay (or rebate) arbitrage profits to federal government.

- Anything above bond yield gets paid to the US Treasury, unless you meet one or more exceptions
  - See next page

Arbitrage Exceptions

- Small issuer exception for schools
  - Issue less than $15 million of tax-exempt bonds in a calendar year

- Spend down exceptions
  - 6-month exception – Spend all proceeds within six months
  - 18-month exception – Spend all proceeds according to the following schedule:
    - 15% of proceeds within six months
    - 60% of proceeds within 12 months
    - 100% of proceeds within 18 months
  - 24-month construction exception
    - 10% of proceeds within six months
    - 45% of proceeds within 12 months
    - 75% of proceeds within 18 months
    - 100% of proceeds within 24 months

What is Arbitrage?

- Yield Restriction
  - Borrowers receive a 3 year “temporary period” of unrestricted investments if the issuer reasonably expects to:
    - Within 6 months, incur a binding obligation to a third party to expend at least 5% of the net sale proceeds on capital projects
    - Spend at least 85% of the net sale proceeds on capital projects within three years
  - If issuer meets these requirements, the issuer may invest its proceeds in any investment that adheres to their investment policy

Tracking Bond Proceeds

- Make sure the bond proceeds are deposited in a separate account
- Interest earned and expenses need to be tracked monthly to know how the district is trending towards a potential rebate and if the spend down exception can be met
- Tracking on a monthly basis will also help the district identify the amount that should be left in the account to make the necessary rebate payment
- <u>Arbitrage is not a bad thing!</u> It means the district maximized how much could be earned. Not knowing how much is owed and making the payment is where problems would begin.

Tracking Bond Proceeds

Investment Earnings Detail

$2,258,108.13	Current Portfolio Interest Income Estimate
$1,197,876.17	Potential Interest Income on Balances (4.75%)
$3,455,984.29	Estimated Interest Income (Not including Rebate)
4.268%	Total Return for Arbitrage Purposes
319	Weighted Avg Life of Future Projected Expenses

Investment Proceeds Information

	09/28/22	Closing Date - Investment Proceeds Received
	$60,002,244.65	Investment Proceeds Received
+	$2,951,470.78	Total Interest Income Net of Rebate
=	$62,953,715.43	Total Funding Available as of 04/07/23
-	$3,682,935.26	Cumulative Expenses Through 04/07/23
=	$59,270,780.16	Outstanding P & I Net of Rebate after 04/07/23

Portfolio Arbitrage Status

Yield Restriction: **The bond proceeds currently fall under the three year temporary period and are therefore not yield restricted.**

Arbitrage Rebate: **The proceeds are subject to arbitrage rebate. The district has not met the two year exception and does expect to pay arbitrage.**

$3,455,984.29	Estimated Interest Income (Not including Rebat	$3,455,984.29	4.268%	Current Interest Estimate for Arbitrage Purposes
$504,513.52	Anticipated Arbitrage Rebate Liability	$2,951,470.78	3.670%	Maximum Interest Limited by Arbitrage Yield
$2,951,470.78	Total Interest Income Net of Rebate	$504,513.52	0.597%	Potential Arbitrage Rebate Liability

Regulatory Requirement			Actual/Projected Portfolio Status			Regulatory Status as of 04/07/23
Estimated Spend-Down Requirements			Cumulative Expenses			$3,682,935.26 Expenses to Date: 5.80%
03/28/23	10%	$6,000,224.47	5.80%	$3,682,935.26	Actual Expense	Not met regulatory requirement
09/28/23	45%	$27,001,010.09	21.77%	$13,814,577.26	Projected Expense	Not met regulatory requirement
03/28/24	75%	$45,001,683.49	51.35%	$32,584,194.26	Projected Expense	Not met regulatory requirement
09/28/24	100%	$63,458,228.94	86.73%	$55,034,170.26	Projected Expense	Not met regulatory requirement

(3) (b) Post Issuance Compliance – Private Use and Record Retention

Use of Bond Proceeds / Financed Facilities — Private Business Use and Payments

- Tax exemption does not apply to any "private activity bond", with limited exceptions
- A private activity bond is a bond that has excessive private business use AND has excessive private payments/security
- De Minimis allowance
  - Private business use is limited to 10%, but
  - 5% limit for "unrelated" or "disproportionate" private business use (with little guidance from the IRS), so most tax counsel use the 5% limit as the baseline

Private Business Use and Payments

- Checklist for Post-issuance compliance:
  - Allocate bond proceeds and funds from other sources to ensure that bond proceeds are used for qualifying costs
  - Map out what outstanding bond issue financed which facilities and in what amounts; monitor private use of bond-financed facilities to ensure compliance with applicable percentage limitations
  - Identify <u>in advance</u> any new sale, lease or license, management contract, or other arrangement involving private use
  - Keep records of leases and management contracts even if expired

Record Retention

- Sufficient records must be retained to support the tax status over the term of the Bonds, plus 3 years after the final maturity date
  - For a refunding issue, material records relating to the original new money bonds and material records related to the refunding issue should be maintained until 3 years after the final redemption of both bond issues
- Consequences if adequate records are not maintained
  - Difficult to calculate private business use
  - Difficult to demonstrate tax compliance in the event of audit

Post-Issuance Tax Compliance Policy

- Adopt *written* procedures that can be understood and implemented over time even as officials responsible for compliance change
  - Having written post issuance compliance procedures may allow for more favorable settlement treatment from the IRS

1) Designate a Compliance Officer
   - Assign responsibility for monitoring
   - Include training with regard to tax and disclosure requirements
2) Retain accurate records

Post-Issuance Tax Compliance Policy

3) Implement procedures reasonably expected to timely identify and timely correct noncompliance
   - Integrate monitoring of tax law compliance with existing accounting systems (for example, use special coding on a ledger to review sales, leases or contracts involving bond financed property)
   - Use a compliance checklist
   - Due diligence at regular intervals
     - Principal and interest payment dates are good benchmarks
     - Self-help remedial actions may only be taken within specified time frames.

4) Report compliance efforts to elected officials (annually)

(4) Continuing Disclosure

Secondary Market Disclosure

- Continuing Disclosure Undertaking (CDU)
  - SEC Rule 15c2-12
  - Requires an underwriter to enter into an agreement with issuers to provide audited financial information, other financial information (possibly) and event disclosures to the market
  - SEC believes this information is important for market transparency and to promote a fair and efficient market
- Filings must be made electronically at the EMMA (Electronic Municipal Market Access) portal [www.emma.msrb.org]

CDU Filing Requirements

- If new issue is sold directly to an investor: No CDU (generally)
- If new issue is less than $1,000,000: No CDU
- If new issue is at least $1,000,000 and issuer has less than $10,000,000 of debt, issuer must agree to provide:
  - Audited financial statements
  - Reportable events
- If new issue is at least $1,000,000 and the issuer has over $10,000,000 of debt, issuer must agree to provide:
  - Annual financial information
  - Audited financial statements
  - Reportable events

CDU Filing Requirements (continued)

- "Annual Financial Information" (AFI)
  - Defined in reference to certain information and charts in the Official Statement, such as:
  - Debt Service Extension Base (DSEB)
  - Financial Information and Economic Characteristics: Trend of EAV, Tax Rates, Tax Extensions and Collections, Outstanding Debt, Debt Ratios
  - Summary of Operating Funds: Changes in Fund Balance, General Fund Revenue Sources, Budget

- Audit (and AFI, if applicable) must be filed with EMMA typically 210 days after fiscal year close, or in some cases within 30 days after availability, whichever is first

CDU Filing Requirements (continued)

- Reportable Events – must be filed within 10 business days after the <u>occurrence</u> of the event

- Prior to February 27, 2019, there were 14 Reportable Events

- Most common:
  - Rating changes
  - Bond calls
  - Payment delinquencies
  - Non-payment defaults

Two Newest Reportable Events

- School Districts subject to the new amendments will now be required to disclose:

  (1) (a) the incurrence of a financial obligation, if material, or
  (b) an agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation, any of which affect security holders, if material; and

  (2) a default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation, any of which reflect financial difficulties

- Examples: Bank loans and leases

Consequences for Failure to Comply with CDU Obligations

- Rule 15c2-12 requires issuers to disclose CDU non-compliance in official statements (five year look back)

- Districts that repeatedly fail to make CDU filings may not be able to access the public market

- Current Bondholders may sue for specific performance

- Districts that fail to make CDU filings may also face SEC action for other statements that reach the market, if materially misleading

Disclosure Policies and Procedures

- Main components: Designating a disclosure officer; adopting procedures for primary disclosure (official statements), for producing and filing annual financial information on EMMA and filing Reportable Events on EMMA.

- Incorporating robust disclosure practices/procedures and demonstrating a solid disclosure track record benefits an issuer by encouraging regulatory compliance and by enhancing credibility among investors, credit rating agencies and the public.

- All participants in the disclosure process should be encouraged to raise additional potential disclosure items at all times in the process.

- Disclosure questions should be discussed with appropriate management team members.

CDU Post-issuance Compliance Checklist

- Review your CDUs for deadlines and filing requirements
- Implement policies and procedures and training for bond issuance and post bond issuance, especially in light of the new continuing disclosure requirements
- Identify individuals responsible for CDU items and have a succession plan
- For annual filings consider including the required tables in your audit
- Subscribe to EMMA for email reminders
- Consider hiring a Third Party or Dissemination Agent

Questions and Answers

We thank you for your time!

Presenters:

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