Legislative Initiatives Impacting Florida School Districts

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Federal Tax Reform

Tax Reform is nothing new…..

Qualified Private Activities

IRS section	Type of Private Activity (italicized activities must be owned by the issuing government to qualify)	Subject to volume cap?	Year established
142	Exempt facility bonds		
142(c)	*Airports*	No	1968
142(c)	*Docks and wharves*	No	1968
142(c)	*Mass commuting facilities*	Yes	1981
142(e)	Water furnishing facilities	Yes	1968
142(a)(5)	Sewage facilities	Yes	1968
142(a)(6)	Solid waste disposal facilities	Yes/No[1]	1968
142(d)	Qualified residential rental projects	Yes	1968
142(f)	Local electric energy or gas furnishing facility	Yes	1968
142(g)	Local district heating and cooling facilities	Yes	1982
142(h)	Qualified hazardous waste facilities	Yes	1986
142(i)	High-speed intercity rail facilities	Yes[2]	1988
142(j)	*Environmental enhancements of hydroelectric generating facilities*	No	1992
142(k)	Qualified public educational facilities	No[3]	2001
142(l)	Qualified green building and sustainable design projects	No[3]	2005
142(m)	Qualified highway and surface freight transfer facilities	No[3]	2005
143	Mortgage revenue bonds		
143(a)	Qualified mortgage bond	Yes	1968
143(b)	Qualified veterans' mortgage bond	No	1968
144(a)	Qualified small issue bond	Yes	1968
144(b)	Qualified student loan bond	Yes	1976
144(c)	Qualified redevelopment bond	Yes	1968
145	Qualified 501(c)(3) bond	No	1968

Source: Congressional Research Service

Tax Cuts and Jobs Act (H.R. 1) – U.S. House of Representatives

On November 2, the House Ways and Means Committee released a tax reform bill with significant implications for the municipal market

Personal and Business Tax Reform

Individual Tax Rates (Section 1001)
Individual tax scheme would be collapsed to four brackets: 12%, 25%, 35%, and 39.6%

Enhancement of Standard Deduction (Section 1002)
Households would get a larger standard deduction of $24,000 for families and $12,000 for individuals

Mortgage Interest (Section 1302)
Would be capped for future mortgage loans of $500,000, down from $1,000,000. Current mortgages would be grandfathered

Source: U.S. House of Representatives, H.R. 1; Committee on Ways and Means – Tax Cuts and Jobs Act Bill

Repeal of Deduction for State and Local Government Taxes

Income and Property Taxes Paid (Section 1303)
Eliminate itemized deduction for state and local income or sales taxes (continue to allow itemized claim deduction for real property taxes paid up to $10,000)

Repeal of Alternative Minimum Tax (Section 2001)
The individual and corporate AMTs would be repealed

Business Tax Rates (Section 3001)
The tax rate for “C” corporations would be reduced to 20%, while the tax rate for pass-through businesses like “S” corporations and others would be 25%

Tax Cuts and Jobs Act (H.R. 1) – U.S. House of Representatives

Municipal Specific Implications

Termination of Private Activity Bonds (Section 3601)

- *Currently make up between 15 % to 20% of the municipal market*

The authority to issue (PABs) after year-end 2017 would be repealed; eliminating the ability to issue tax-exempt bonds in:

- PAB sectors currently subject to the AMT (i.e. airport special facilities, privately owned solid waste disposal, housing, etc.);
- 501(c)(3) sectors *NOT* currently subject to the AMT (i.e. not-for-profit health care, private higher education, etc.)

Estimated to raise $38.9bn in revenues over 10 years

Repeal of Advance Refunding Bonds (Section 3602)

- Not permitted after December 31, 2017
- Current refundings would still be permitted for governmental issuers

Estimated to raise $17.5bn in revenues over 10 years

Repeal of Tax Credit Bonds (Section 3603)

- Not permitted after December 31, 2017
- Continue receiving tax credits and payments for tax credit bonds already issued

Estimated to raise $500mm in revenues over 10 years

No Tax-Exempt Bonds for Professional Stadiums (Section 3604)

- Effective for bonds issued after the date of introduction (November 2, 2017)

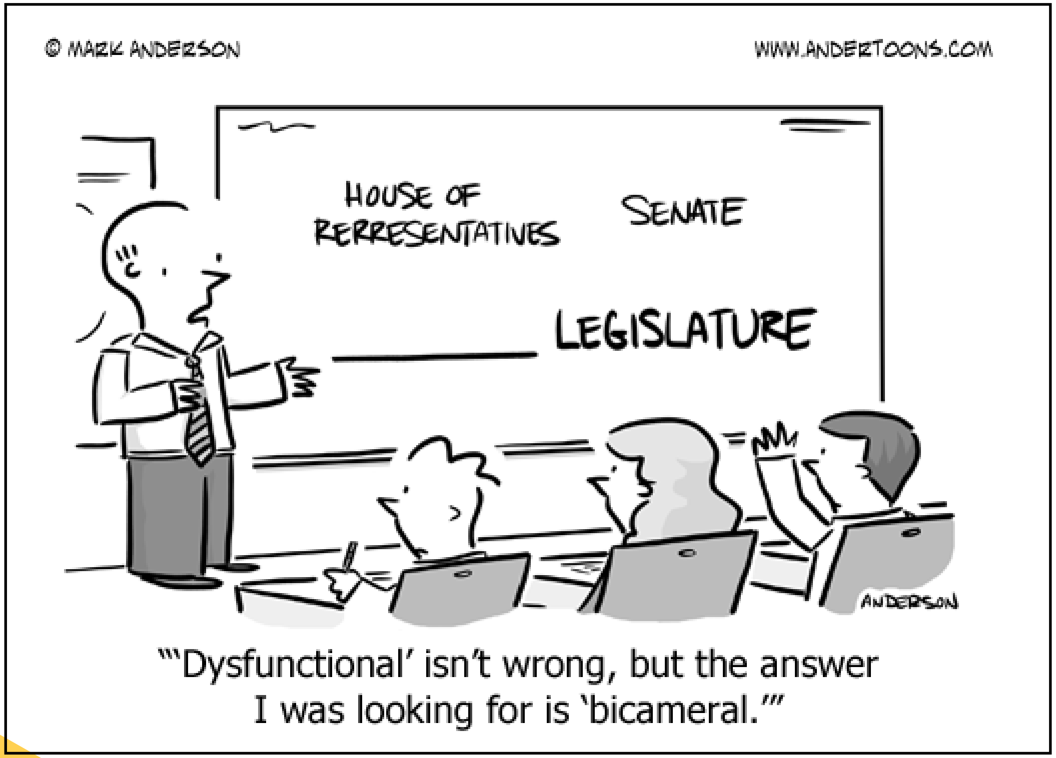
Estimated to raise $200mm in revenues over 10 years

Tax Reform Timeline

- House Ways and Means Committee will begin deliberations on the bill on Monday, November 6, with final House approval targeted by Thanksgiving
- Senate Finance Committee released bill November 10
- Congressional Republicans are targeting passing a final bill by year-end

Senate Bill

- Senate Bill released on November 9
- Significant differences with House must be worked out before final passage of tax bill



Comparison of House & Senate Bills

Issue	House Bill	Senate Bill
Individual Tax Brackets	Four brackets ranging from 12% to 39.6%	Seven brackets ranging from 10% to 38.5%
State and Local Tax Deduction	Partial repeal with property tax cap	Total repeal
Corporate Tax Rate Cut	Cut to 20% in 2018	Cut to 20% in 2019
Mortgage Interest Tax Deduction	Cap at $500k and one home	Maintain $1M cap
Estate Tax	Eliminates estate tax in 2024, until then would double $5.49M exemption	Doubles $5.49M exemption but maintains tax
Medical Expense Deduction	Repeal	Maintain
Child Tax Credit	$1,600k per child + $300 parent credit	$1,650 for those earning under $500k
Private Activity Bonds	No longer tax exempt	Maintain tax exemption
Advanced Refunding	No longer tax exempt	No longer tax exempt

Federal Tax Reform – Elimination of Advance Refundings

- Under current federal tax law, municipal issuers may refinance bonds prior to their call date using a technique known as an advance refunding:
    - Bonds issued more than 90 days prior to the call date of bonds to be refunded
    - Proceeds of refunding bonds placed into irrevocable escrow to pay principal, interest and redemption price on refunded bonds through and including the call date
    - Escrow proceeds invested in federal securities (typically SLGS and/or OMS)
    - Refunded bonds are deemed defeased and no longer an obligation of the issuer

- Proposed legislation would eliminate tax-exemption of refundings issued more than 90 days prior to the call date

- Still may issue advance refundings with taxable bonds

Federal Tax Reform – Elimination of Advance Refundings

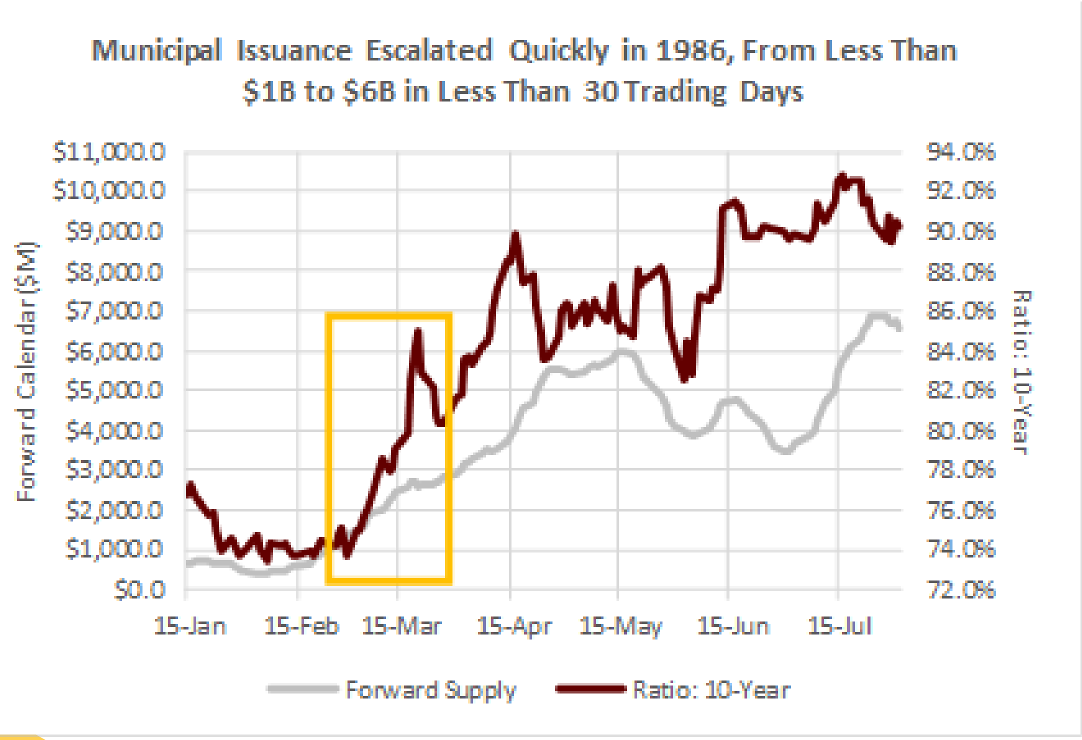
- Advance refundings have accounted for significant amount of municipal volume in recent years
- $109.2 billion refunding bonds sold YTD as of November 3, 2017[1]
  - $35.7 billion solely advance refunding
  - $30 billion either combination of advance & current refunding or unknown

Quarterly	Volume (US$ MM) 2017	No. of Issues 2017	Volume (US$ MM) 2016	No. of Issues 2016	Ptc.Chg
Q1	80,916.8	2,278	92,153.9	2,769	-12.2%
Q2	93,400.6	2,925	112,215.7	3,626	-16.8%
Q3	79,900.2	2,311	105,707.7	3,076	-24.4%
Refunding Status					
New financing	137,627.4	5,045	127,991.6	5,027	7.5%
Refunding	82,861.2	2,466	153,027.1	4,618	-45.9%
Refunding & new financing	67,737.6	774	79,462.8	966	-14.8%
Refinancing & new financing	0.0	0	234.0	2	0.0%

[1]Source: Bond Buyer

Federal Tax Reform - How will Market Respond?

- New issue calendar building as issuers accelerate bond issues to close before December 31
- Anticipate greater surge in PAB issuance than advance refundings
  - Issuers have refunded most bonds eligible for advance refunding
  - New money transactions down significantly over last 10 years



Federal Tax Reform – How will Market Respond?

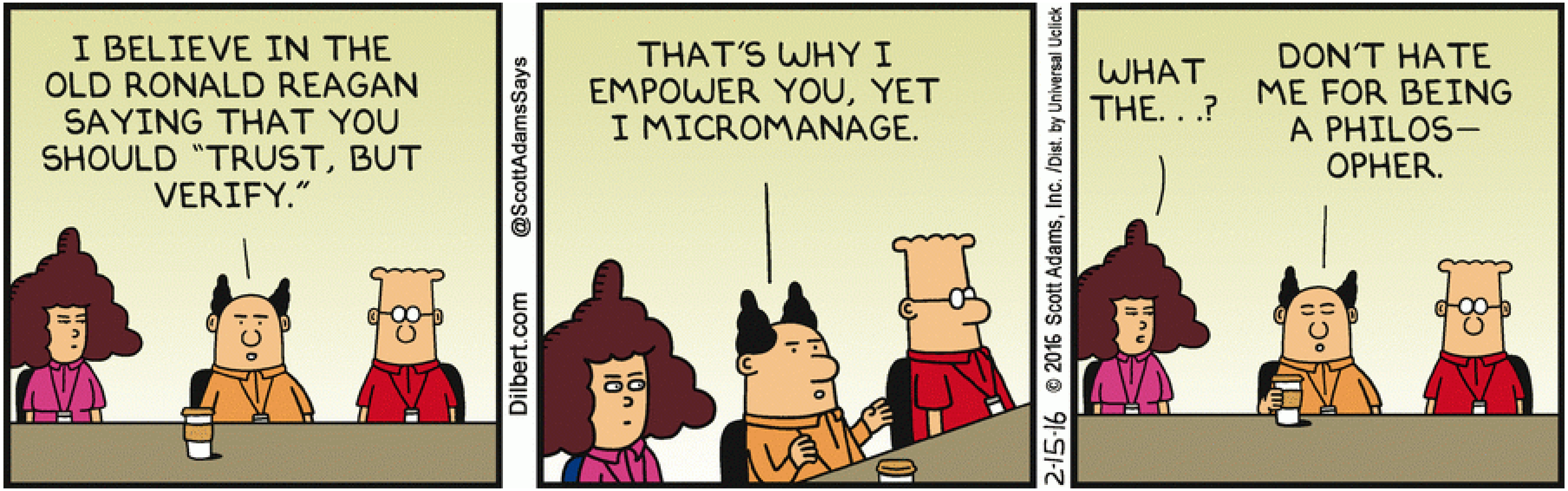
Issuer Strategies if Advance Refundings eliminated

- Forward Delivery Bonds/Loans
  - Interest rates/yields locked in current market
  - Transactions does not close until < 90 days of call date (i.e. current refunding)
  - Forward period typically 12-18 months

- Forward Starting Interest Rate Swaps
  - Interest rate locked in current market
  - Transactions does not close until < 90 days of call date (current refunding)
  - Option to:
    - terminate swap and issue fixed rate debt or
    - maintain swap and issue variable rate debt
  - Typically longer forward period available compared to forward delivery bonds

- Use of shorter optional call features

State of Florida Legislation



State Legislation - HB 7069

- HB 7069 became law on July 1, 2017

- Controversial in terms of both content and manner in which it passed

- Summary of certain key provisions
  - Redirects Title I funds
  - Creates Schools of Hope program for underperforming schools
  - Expands the Best and Brightest Teacher program and creates the Best and Brightest Principal program
  - Requires School Districts to share capital outlay millage levy (COML) with qualifying charter schools on a per student basis

State Legislation - HB 7069

- HB 7069 may significantly impact Capital Funding

- Requires School Districts to share capital outlay millage levy (COML) with qualifying charter schools on a per student basis.
  - Deducts funds needed for payments related to debt issued prior to 3/1/2017
  - The number of eligible charters as well as the students can change from year to year - not predictable
  - Deducts State dollars allocated to charter schools
    - Set annually by the legislature

- Districts do not have to share:
  - Local Option Sales Surtax
  - Proceeds of General Obligation Bonds

State Legislation - HB 7069

- Sharing of capital outlay funding from discretionary millage to eligible schools
  - Two forms of student membership to become eligible: 75% or more FRL or more than 25% ESE students.
  - If neither threshold is met, charters receive 1 FTE equivalent.
    - Receive 1.25 FTE if they meet one requirement
    - Receive 1.5 FTE if they meet both requirements

- Formula for Local Millage Distribution:
  1. Reduce the total capital millage levied by each District's debt service issued prior to March 1, 2017 as of March 1^{st} of the previous year (2017 for 2018 calculation)
  2. x = Adjusted millage
  3. Divided by District Capital Outlay FTE + Charter Unweighted FTE
  4. Multiplied by (each charter's FTE)

- **Transfer of COLM will take priority over lease payments (i.e. COPs) entered into after March 1, 2017**

State Legislation - HB 7069

- Top 10 Districts most affected by COLM sharing requirement (after payment of debt service)

1. **Sumter County**: $4.6 million of $13.8 million available (33.4%)
2. **Franklin County**: $435,800 of $1.8 million available (24.1%)
3. **Sarasota County**: $8.9 million of $65.6 million available (13.5%)
4. **Miami-Dade County**: $23.2 million of $196 million available (11.9%)
5. **Monroe County**: $1.1 million of $9.8 million available (10.8%)
6. **Glades County**: $92,100 of $885,000 available (10.4%)
7. **Lee County**: $7.3 million of $71.2 million available (10.2%)
8. **Broward County**: $12 million of $120.4 million available (10%)
9. **Indian River County**: $1.3 million of $13.5 million available (9.8%)
10. **Madison County**: $98,900 of $1 million available (9.5%)

Source: Miami Herald; Florida House

State Legislation - 2018

- Keeping an eye on proposed bills that failed in 2017 as well as new proposals

- HB 317 – Local Tax Referenda
  - *At a primary election and requires the approval of 60% of the qualified electors voting on the ballot question for passage; or*
  - *At a general election and requires the approval of a majority of the qualified electors voting on the ballot question for passage*

- SB 354 – Government Accountability

"I just feel paranoid all the time."

Impact of Legislation on Credit Ratings

Impact of Legislative and Other Matters on District Credit Ratings

Michael Rinaldi

Senior Director and Manager East Region. U.S. Public Finance

FSFOA November 16, 2017

FitchRatings

Fitch on Florida Schools

- Fitch maintains a public Issuer Default Rating (IDR) on 30 Florida school districts that collectively have more than $10 billion of par outstanding as of FY 2016

- High overall credit quality
  - 4 school districts rated 'AA+'
  - 6 school districts rated 'AA'
  - 14 school districts rated 'AA-'
  - 5 school districts rated 'A+'
  - 1 school district rated 'A-'

- IDR Outlooks
  - 28 are Stable
  - 2 are Positive

Fitch Criteria – Revenue Framework

- Two key criteria points - revenue growth prospects and independent legal ability to increase revenue
- Not uncommon of U.S. school districts generally, Florida school districts have limited, if any, independent ability to raise revenues materially without external approval
- Voter-approved revenue streams for capital and operating purposes are typically considered in the context of long-term liabilities and operating performance

Revenue Growth Considerations

- Our assessment of a school district's revenue growth prospects generally incorporates expectations for the following:
  - State general revenue growth
  - Education funding policy – FEFP funding levels
  - School district enrollment trends and expectations
- State revenues are expected to rise at a healthy pace over the foreseeable future given a resumption of population growth and stronger economic expansion

FEFP Funding

- FEFP funding growth has slowed in recent years and is marginally above the level appropriated by the legislature a decade ago

Year	Base Student Allocation ($)	Annual Change	Total FEFP Funding ($)	Annual Change
2017-18	4,204	1.1%	7,297	1.4%
2016-17	4,160	0.1%	7,196	1.5%
2015-16	4,154	3.0%	7,089	2.9%
2014-15	4,032	7.5%	6,891	1.8%
2013-14	3,752	4.7%	6,769	6.1%
2012-13	3,583	3.0%	6,377	2.6%
2011-12	3,479	-4.0%	6,217	-9.9%
2010-11	3,624	-0.2%	6,897	0.7%
2009-10	3,631	-6.6%	6,847	0.0%
2008-09	3,886	-4.8%	6,847	-3.9%
2007-08	4,080	2.5%	7,126	4.1%
2006-07	3,982		6,848	

Source: Florida Department of Education

Enrollment Gains Modest for Most Traditional Public Schools

- Public school enrollment has not been particularly robust, increasing by less than 1% per year since 2007-08

- During this same period, charter school enrollment has increased by a CAGR of more than 10%
  - According to FL DOE during the 2016-17 school year, over 283,000 students were enrolled in 654 charter schools across the state

  - Charters now account for about 10% of public school enrollment compared to 4% in 2007-08

Revenue Framework Key Rating Factor Assessment

- Revenue framework key rating factor (KRF) assessments are currently ‘a’ or ‘bbb’-category
- Florida school district’s have very limited capacity to counteract cyclical revenue declines through independent revenue policy action
- Revenue growth for Fitch-rated Florida school districts has been fairly slow
  - The GF revenue CAGR for the 10-year period ending FY 2016 is 2.1% or just slightly ahead of the U.S. CPI

What Is the Credit Impact of HB 7069?

- In our view the law carries several provisions that may enhance the competitive position of charters relative to traditional public schools
- Among the most publicized provisions of HB 7069 is the allocation of traditional public school's capital outlay funds to eligible charters based on student enrollment
- Traditional public schools may take on more debt to replace capital outlay funds and pay-go investment
- Capital outlay resources previously reduced when the maximum millage rate was lowered from $2.00 per $1,000 AV

What Is the Credit Impact of HB 7069?

- Debt service incurred as of March 1, 2017 is deducted from the amount of shared local capital outlay funds but this 'exemption' will decline over time

- New construction demand may be manageable
  - Districts are currently meeting class size requirements
  - DOE projects enrollment growth of less than 1.0% thru 2022-23

- But what about investment to satisfy the 'maintenance creep' on existing facilities?

Rating Changes Not Anticipated

- Will continue to evaluate the impact of HB 7069 on an issuer-by-issuer basis, but we do not expect to take negative rating action in the near term

- Existing long-term liabilities are low which should allow for an increase in debt without meaningful pressure on credit quality

- All but 4 Fitch-rated FL school district's measure 6% or less debt and unfunded pension liability to personal income

  – Criteria metric guidance for a 'aaa' long-term liability KRF is <10%

Sound Management Practices

- Demonstrated ability to prepare for, and adjust to, shifts in operating environment

- Strong expenditure management
  - Personnel savings generally materialize from attrition and replacement of higher wage employees with less expensive hires.

  - Florida labor laws are not overly restrictive to budget management authority bestowed on elected and appointed school district officials

- Enhanced management tools (class size compliance, capital outlay use, etc.)

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FitchRatings