To: School Board
William Gronseth, Superintendent

From: Douglas A. Hasler, CFO DH

Date: August 9, 2017

Subject: Update on LRFP Debt Restructuring Resolution

The Long Range Facilities Plan (LRFP) Debt Restructuring resolution approved by the Board at the June Board meeting expressed the Board's support for legislation permitting payment of specified certificates of participation (COPs) (2009B, 2010D, and 2012B) from sources other than the General Fund, and requested that the Administration and its advisors seek out alternatives to the existing debt repayment structure to conserve district resources.

Since the Board approved this LRFP resolution, I have been in communication with PFM, a financial advisor to school districts and other public entities on matters relating to bond financing. I have requested assistance from PFM on the two objectives established in the Board's resolution. I will summarize our progress on the resolution's two objectives below.

Goal – Payments for Specified COPs from source other than General Fund

The available funding sources for a Minnesota school district are limited, and each source of funding is generally subject to statutory (state or federal) restrictions. The only potential funding source (other than General Fund) for COP payments that we have been able to identify is the Debt Service Fund. Current law does not allow Duluth Public Schools to pay the COPs (which are paid out of the General Fund) out of the Debt Service Fund at our own initiative. A shift of these payments to the Debt Service Fund would require either (1) a successful referendum in which local taxpayers would approve such a shift; or (2) a change in state law authorizing such a shift without a referendum.

Both of these available options present significant challenges and/or risks. No referendum is a sure thing, especially one focused on a completed building project that would require taxpayers to absorb increased property tax costs. Further, it is not clear that there would be legislative support necessary to change Minnesota statute to allow for a shift of the COP payments to the Debt Service Fund without the referendum requirement. A final consideration that the Board needs to consider is whether either of these options would conflict with the School District's future needs for an operational levy referendum upon the expiration of the current operational levy in 2018.

<u>Goal – Alternatives to Existing Debt Repayment Structure to Conserve District Resources</u>

The primary means to restructure existing debt payments is through a refunding process. Such refundings are generally undertaken when current, prevailing market interest rates have fallen below those interest rates which are incorporated into existing debt issues. Duluth Public Schools has taken advantage of refunding opportunities in the past -- refunding bonds were issued to retire prior debt in 2015 and 2016 resulting in total debt payment savings of $8.6 million. Future refundings can/should be pursued, when market interest rates drop to levels that would generate sufficient savings through a refunding process.

One limitation associated with refundings is that existing debt issues have established "call dates" that prevent an issuer from paying off debt issues prior to a specified call date. At present, all existing debt issues have call dates that range from February 2019 to February 2027. Minnesota statute authorizes the refunding of a debt issue prior to a call date (an "advance refunding") only when the net present value of savings produced by a refunding is three percent or greater.

In an effort to provide the Board with the potential savings that could be generated through a refunding of all existing bond issues (as an earlier version of the resolution suggested), I requested that PMA prepare an analysis on this issue. The results of that analysis were shared with the Board in June. That analysis incorporated a number of simplifying assumptions including the following: the three percent net present value savings requirement did not exist, all debt issues could be refunded immediately unrestricted by call dates, and that the federal tax exemption for municipal interest payments would not be lost with the refunding of an existing refunding debt issue. These assumptions are not realistic, but did allow for a comprehensive analysis of all existing debt issues to be conducted. The result of such assumptions would be to understate the resulting debt payments resulting from the analysis. As you recall, the PMA analysis predicted that Debt Service payments would not go down as a result of a refunding, but would actually increase by over $20 million (for those debt issues currently paid out of the Debt Service Fund).

I have asked that PFM do an analysis similar to that done by PMA. At present, that analysis is not yet complete. I will share the results of this analysis with the Board when it is available.

I hope that the information included in this memorandum is helpful. I will continue to work with PFM on these issues. If any Board member knows of any individual or firm that they believe has ideas or proposals that would allow Duluth Public Schools to shift its COP payments out of the General Fund, and/or restructure our existing debt payments to create cost savings, please pass this information on to me so that I can evaluate these options.