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Tax Reform Impacts on State and Local Government Agencies – A Comprehensive Discussion

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Tax Cuts and Jobs Act – Impacts on State and Local Government Agencies

- Tax bill signed into law on Friday, December 22, 2017
- Majority of the bill's provisions have an effective date of January 1, 2018

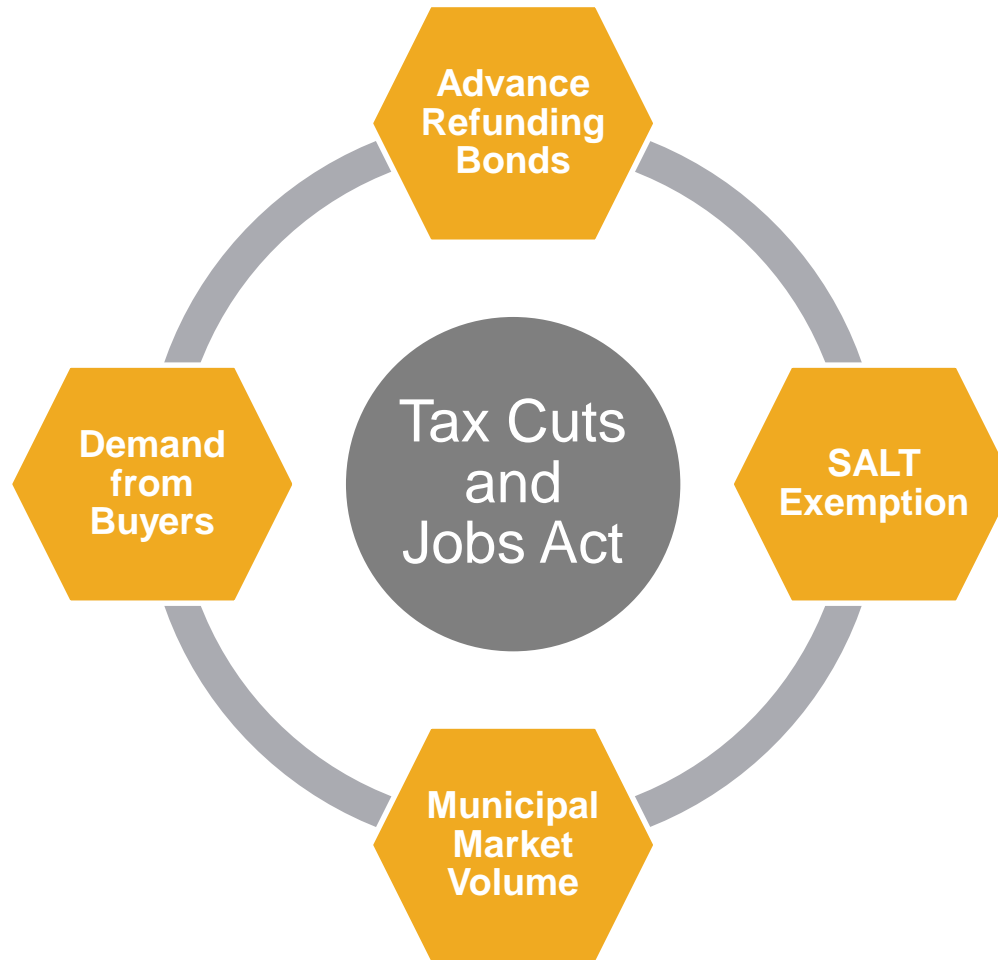
Positives for municipal bond issuers

- Eligible new money projects can still be funded with tax-exempt bonds
- Current refunding bonds can still be issued tax-exempt
- Private Activity Bonds (PABs) kept their tax-exemption, including stadium bonds
- Changes to the Alternative Minimum Tax (AMT) have decreased the penalty associated with issuing bonds subject to the AMT

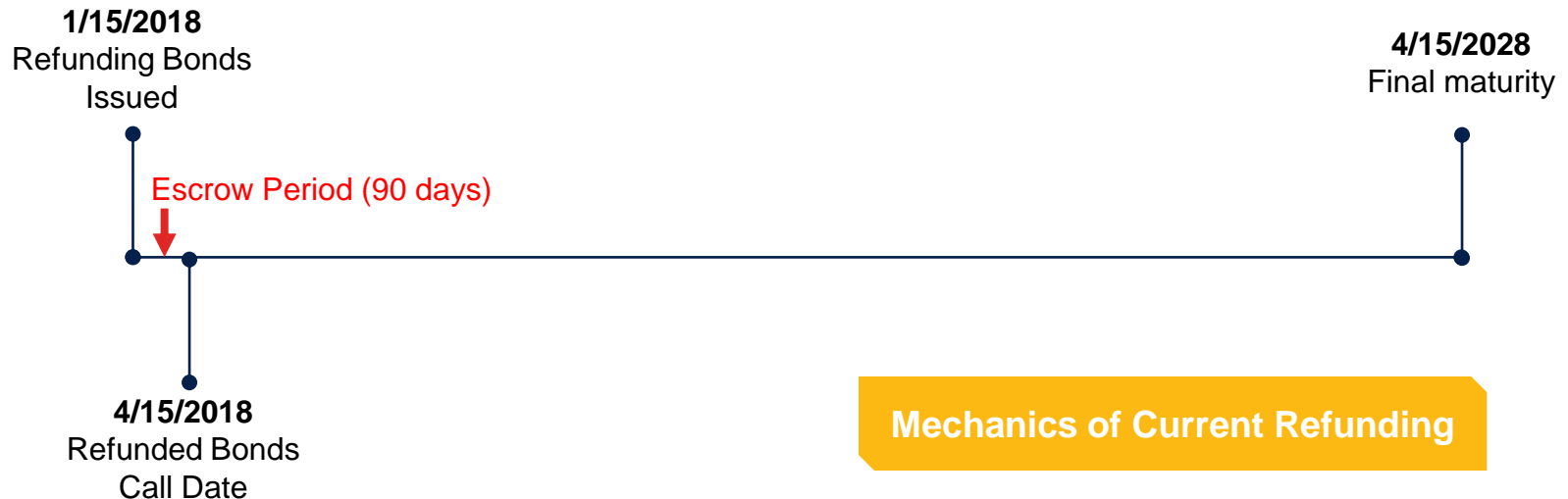
Negatives for municipal bond issuers

- Tax Credit bond programs eliminated going forward
- Private college endowments over \$500 million will have earnings taxed at 1.4%
- Interest on advance refunding bonds is taxable
- Cap on State And Local Taxes (SALT) Exemption
- Lower federal income tax rates for both individual and corporate filers

Tax Cuts and Jobs Act – Impacts on State and Local Government Agencies



Refunding Basics – Current Refunding (Example)



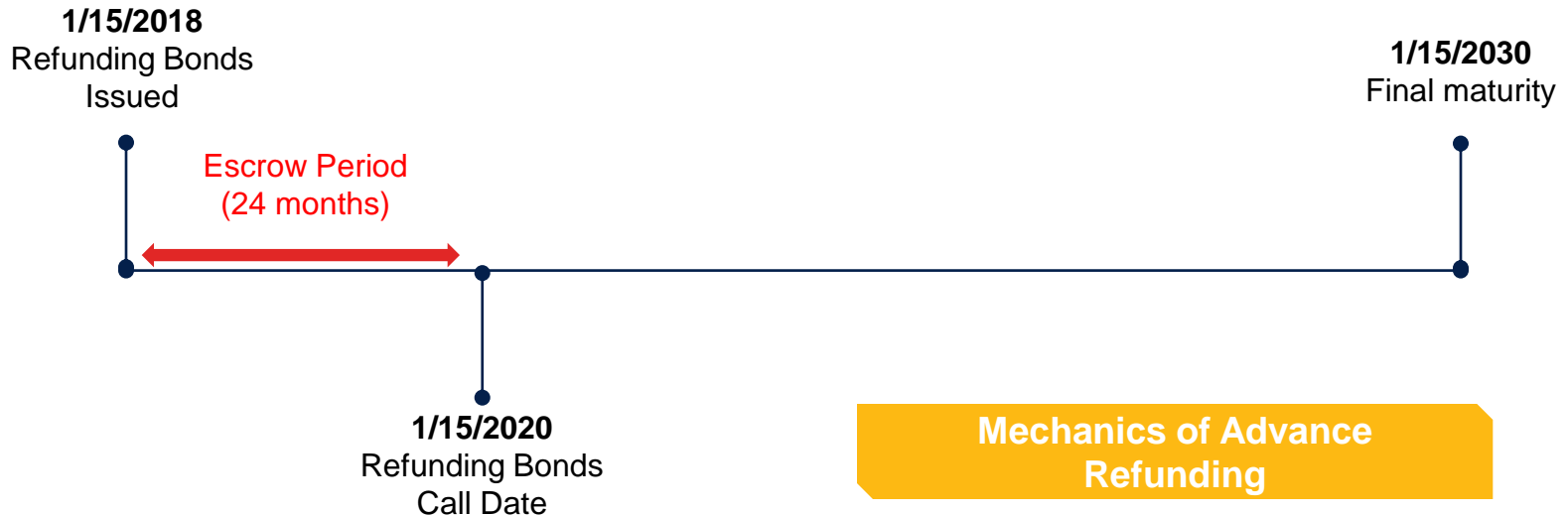
Refunded Bonds

- Series 2008
- Issued 4/15/2008
- Final Maturity 4/15/2028
- Call Date 4/15/2018

Mechanics of Current Refunding

- Refunding Bonds are issued on 1/15/2018
- Proceeds from Refunding Bonds pay
 - Series 2008 principal and interest due 4/15/2018
 - Redemption of remaining 2008 principal on 4/15/2018
- Escrow period of 90 days or less = Current Refunding

Refunding Basics – Advance Refunding (Example)



Refunded Bonds

- Series 2010
- Issued 1/15/2010
- Final Maturity 1/15/2030
- Call Date 1/15/2020

Mechanics of Advance Refunding

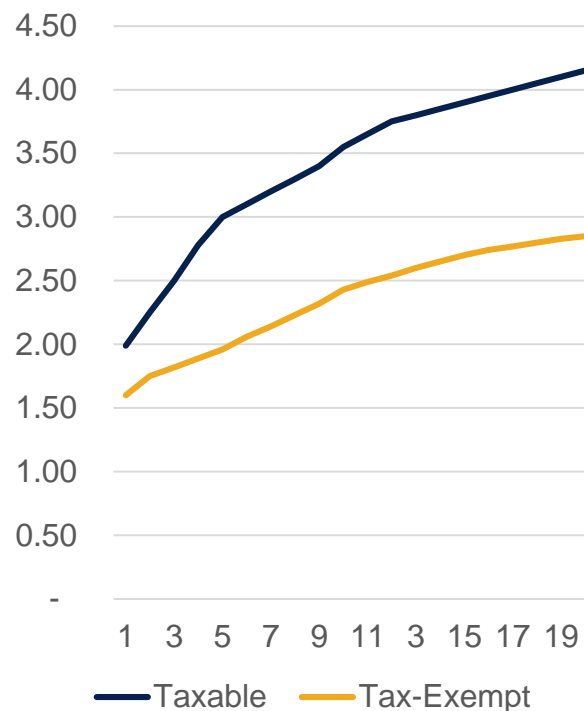
- Refunding Bonds are issued on 1/15/2018
- Proceeds from Refunding Bonds pay
 - Series 2010 principal and interest due from 7/15/2018 to 1/15/2020
 - Redemption of remaining 2010 principal on 1/15/2020
- Escrow period greater than 90 days = Advance Refunding

Taxable Advance Refunding (Example)

Interest Rate Table¹

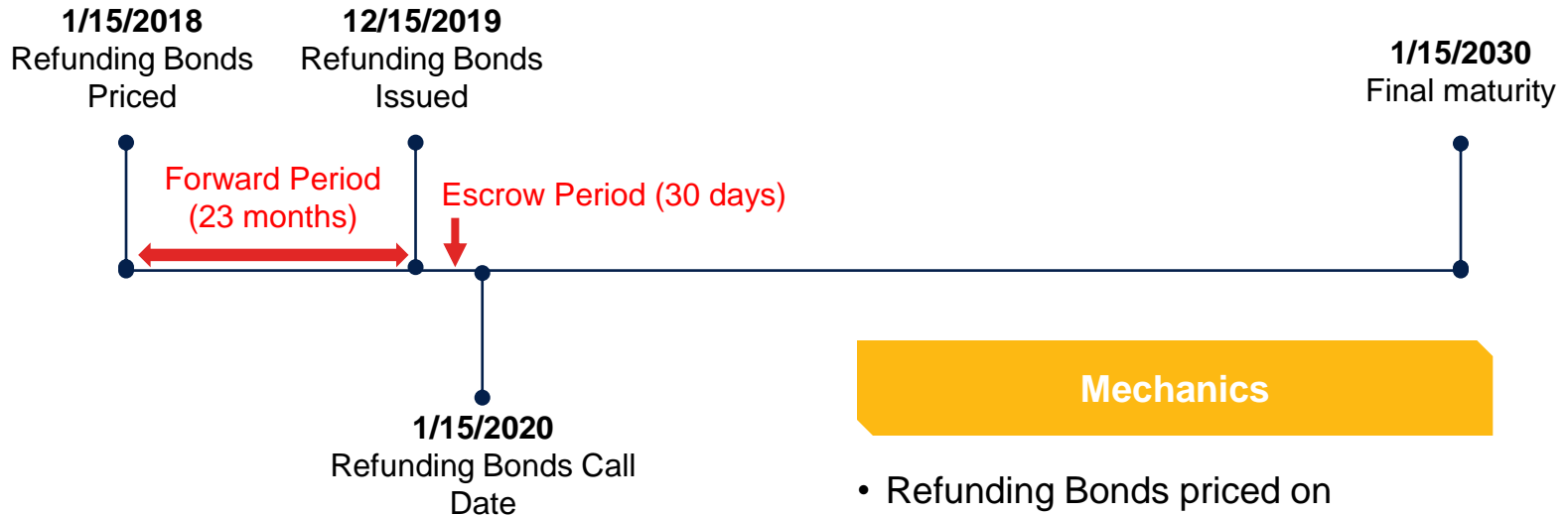
Maturity	Taxable	Tax-Exempt	Increase
1	1.99	1.60	0.39
2	2.25	1.75	0.50
3	2.50	1.82	0.68
4	2.78	1.89	0.89
5	3.00	1.96	1.04
6	3.10	2.06	1.04
7	3.20	2.14	1.06
8	3.30	2.23	1.07
9	3.40	2.32	1.08
10	3.55	2.43	1.12
11	3.65	2.49	1.16
12	3.75	2.54	1.21
13	3.80	2.60	1.20
14	3.85	2.65	1.20
15	3.90	2.70	1.20
16	3.95	2.74	1.21
17	4.00	2.77	1.23
18	4.05	2.80	1.25
19	4.10	2.83	1.27
20	4.15	2.85	1.30

Interest Rate Curves¹



(1) Rates are indicative only and based on market conditions as of 1/4/18 for a hypothetical bond issue by a K-12 public school issuer in the state of Indiana for a \$20 million, level debt service issue rated "AA+".

Forward Delivery Tax-Exempt Bonds



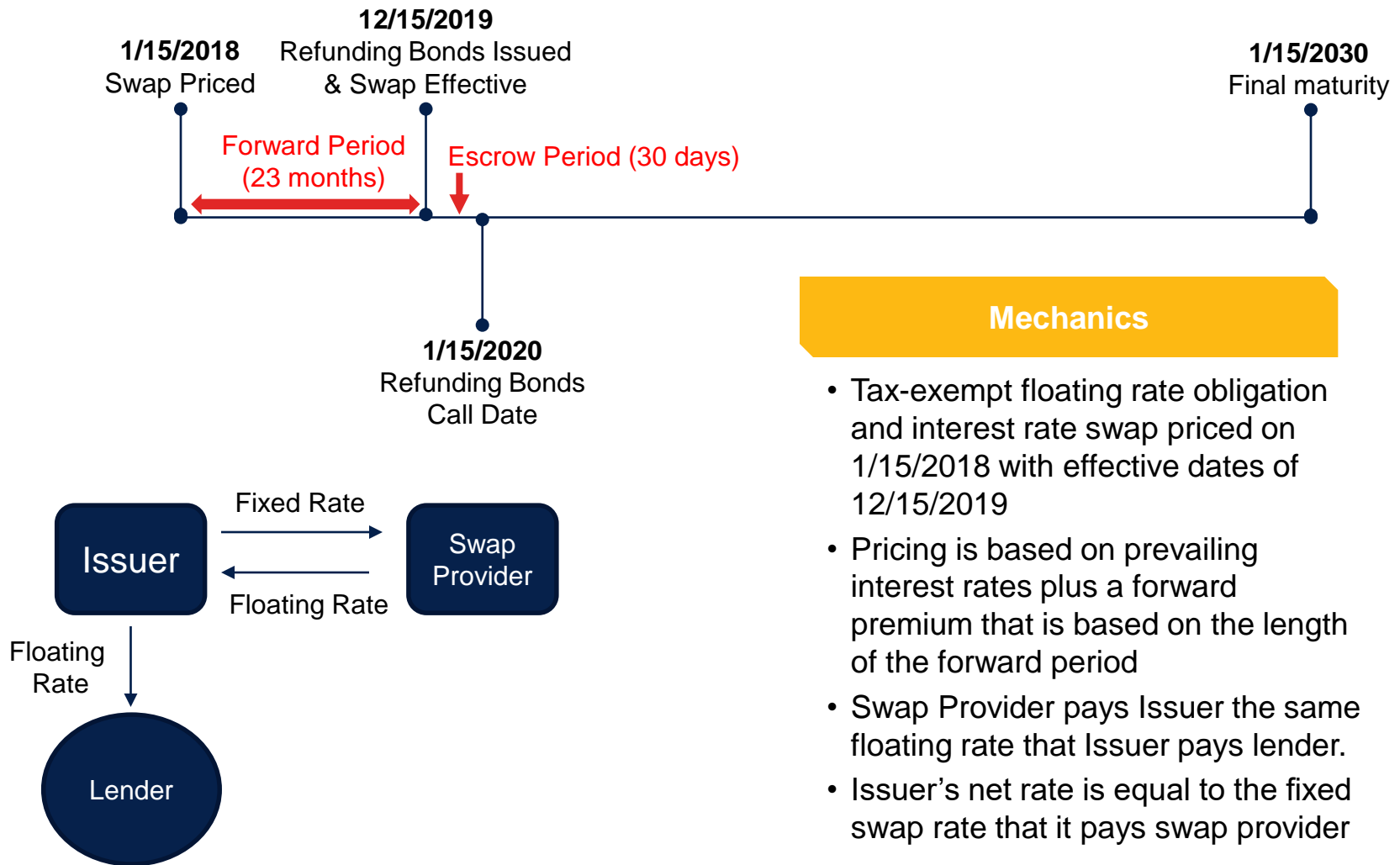
Refunded Bonds

- Series 2010
- Issued 1/15/2010
- Final Maturity 1/15/2030
- Call Date 1/15/2020

Mechanics

- Refunding Bonds priced on 1/15/2018 for delivery on 12/15/19
- Pricing is based on prevailing interest rates plus a forward premium that is based on the length of the forward period
- The refunding escrow is funded on 12/15/19, 30 days prior to the call date and within the 90 day maximum current refunding window

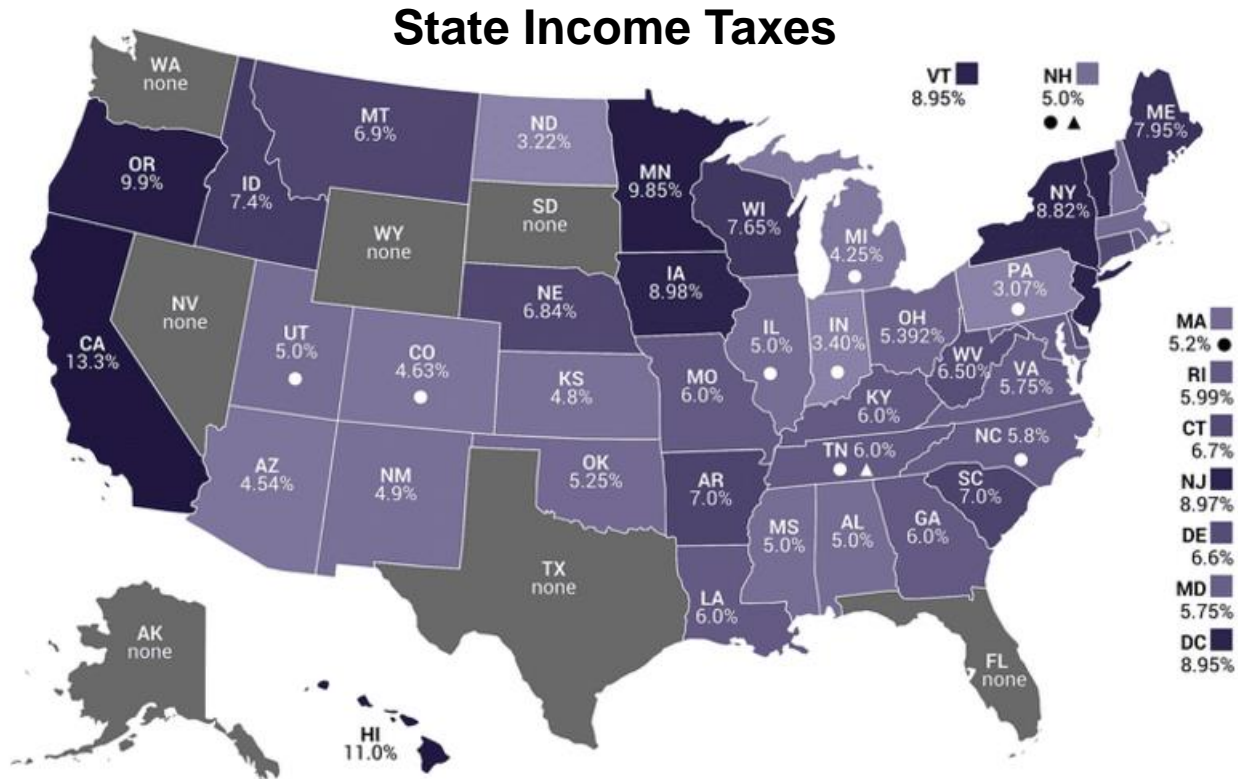
Forward Starting Interest Rate Swap



- Tax-exempt floating rate obligation and interest rate swap priced on 1/15/2018 with effective dates of 12/15/2019
- Pricing is based on prevailing interest rates plus a forward premium that is based on the length of the forward period
- Swap Provider pays Issuer the same floating rate that Issuer pays lender.
- Issuer's net rate is equal to the fixed swap rate that it pays swap provider

Impact of SALT Provisions

- In the past, State and Local Taxes (SALT) have been an eligible exemption when filing federal income taxes
- Tax Bill caps that exemption at \$10,000



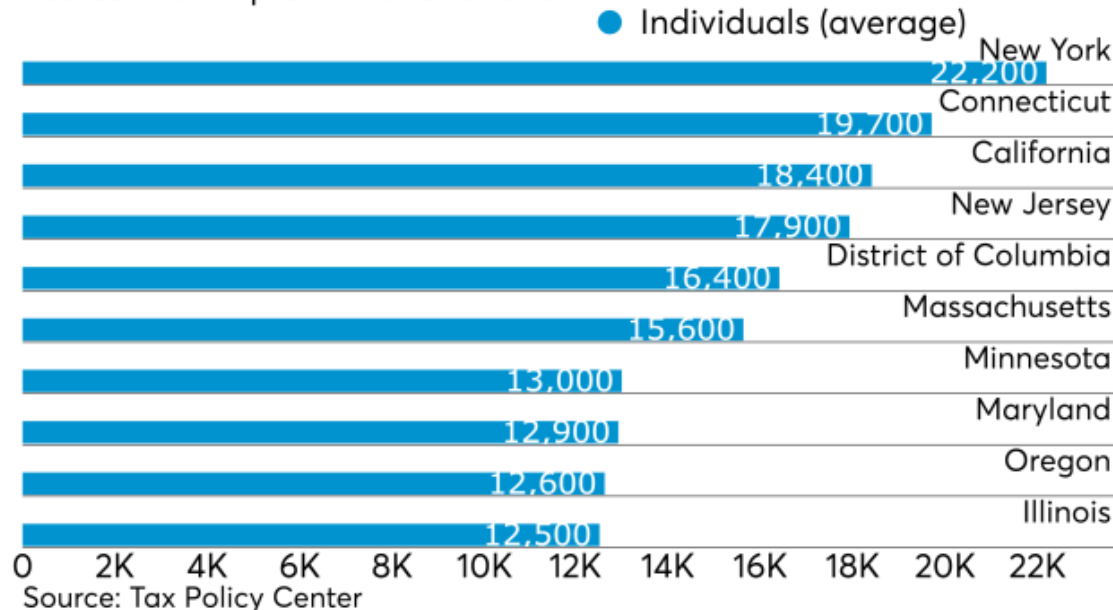
Source: TaxFoundation.org (rates as of 1/1/2018)

States Impacted the Most by SALT Provisions

- Several states are investigating methods of eliminating or reducing impact of this provision
 - Reclassifying SALT as payroll taxes or charitable donations
 - State of California proposal

The biggest losers

States with top SALT deductions



Changes to Individual Tax Brackets

2017 Tax Brackets

Single	Married Filing Jointly	Marginal Tax Rate
\$0 - \$9,325	\$0 – \$18,650	10.00%
\$9,326 - \$37,950	\$18,651 - \$75,900	15.00%
\$37,951 - \$91,900	\$75,901 - \$153,900	25.00%
\$91,901 - \$191,650	\$153,901 - \$233,350	28.00%
\$191,651 - \$416,700	\$233,350 – \$416,750	33.00%
\$416,701 - \$418,000	\$416,751 - \$470,700	35.00%
\$418,001 +	\$470,700 +	39.60%

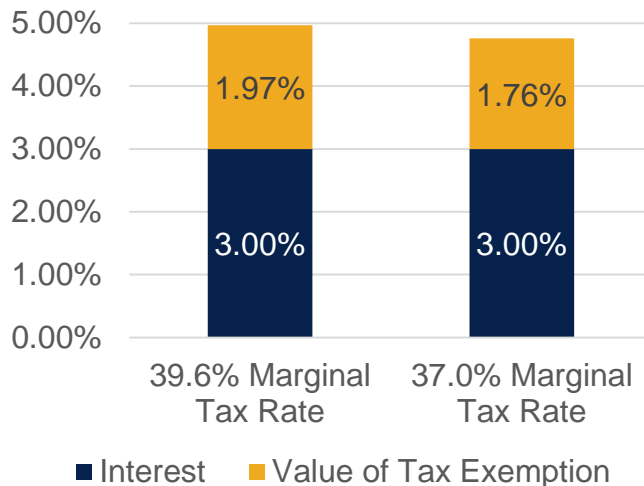
2018 Tax Brackets

Single	Married Filing Jointly	Marginal Tax Rate
\$0 – 9,525	\$0 – \$19,050	10.00%
\$9,526 - \$38,700	\$19,051 - \$77,400	12.00%
\$38,701 - \$82,500	\$77,401 - \$165,000	22.00%
\$82,501 - \$157,500	\$165,001 – \$315,000	24.00%
\$157,501 - \$200,000	\$315,001 - \$400,000	32.00%
\$200,001 - \$500,000	\$400,001 - \$600,000	35.00%
\$500,000+	\$600,001 +	37.00%

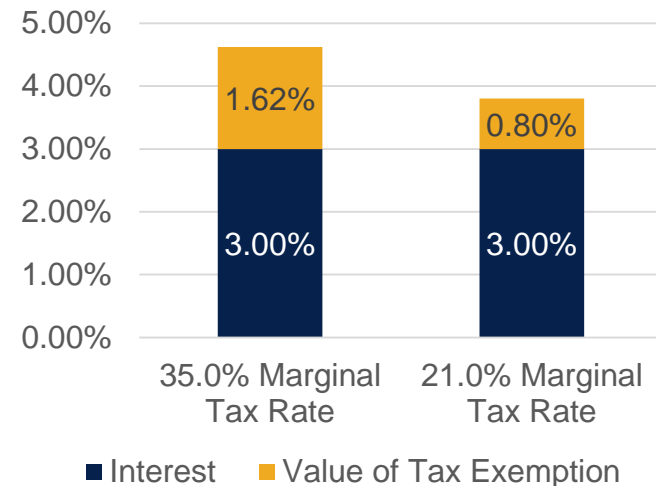
Source: IRS.gov

Impact of Income Tax Rates on Municipal Bond Buyer Segments

Retail Investors



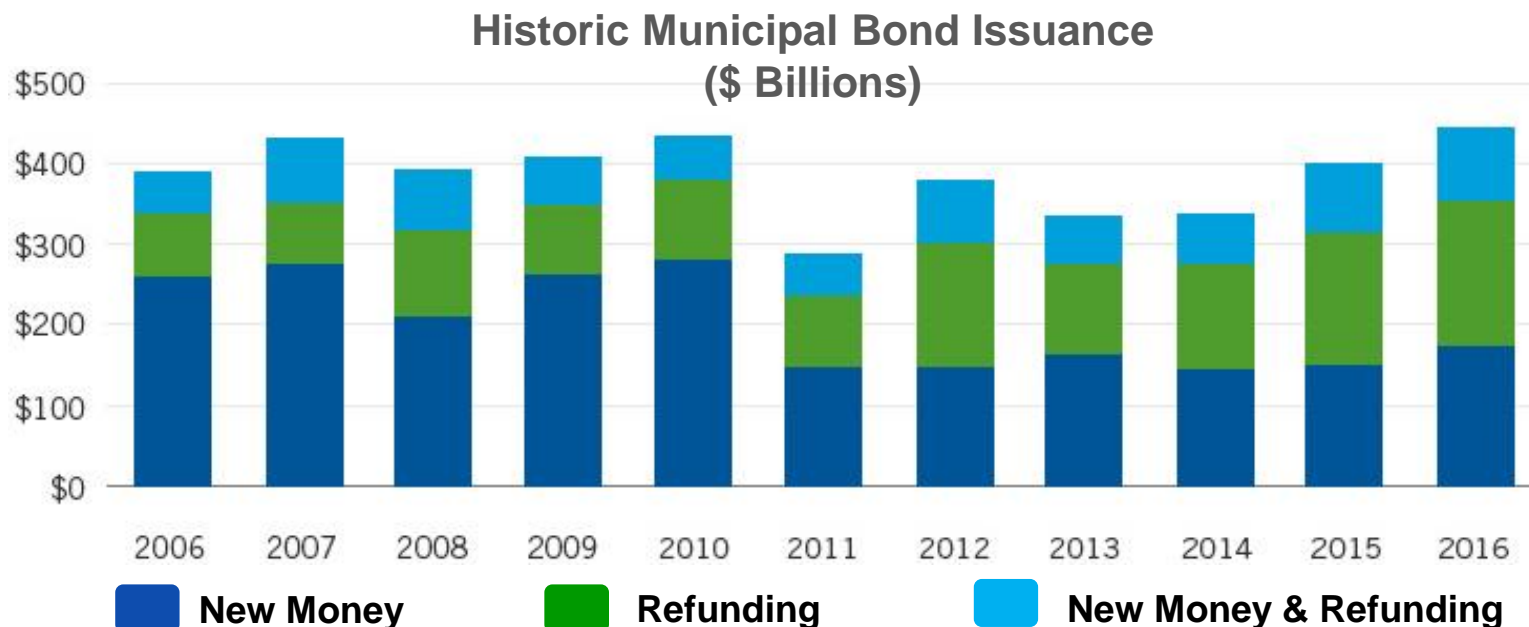
Institutional Investors



- The benefit of tax-exempt interest income has been impacted more for institutional investors than retail investors

Historical Market Volume – New Money vs. Refunding

- Municipal bond market analysts are forecasting lower market volume in 2018, due in part to the elimination of tax-exempt status for advance refunding bond issues
 - Municipal Market Data survey respondents predict a decline in 2018 of 8% to 34% with most expecting between \$305 to \$350 Billion



Source: Securities and Exchange Commission

Questions & Answers

