

ONE CITY'S DEBT STRATEGY – DEBT ISSUANCE AND COST SAVINGS FOR THE CITY OF DENTON

Presented to the Texas City Attorneys Association on
November 15, 2012

City of Denton Overview

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- Founded in 1857 and incorporated in 1866.
- City continues to grow in terms of size and population.
 - ▣ Completed annexation proceedings for approximately 7,500 acres in 2010.
 - 3,400 acres annexed immediately, and 4,100 acres were given five-year non-annexation agreements.
- With annexation, City of Denton is approximately 94.9 square miles.
 - ▣ Strategically located 35 miles northeast of Fort Worth and 37 miles northwest of Dallas (Intersection of I-35E and I-35W).
 - ▣ 18 miles from DFW Airport.
- Home of two major universities and approximately 51,000 students.
 - ▣ Texas Woman's University (TWU).
 - ▣ University of North Texas (UNT).
- Regional center for medical services with two major hospitals.
 - ▣ Denton Regional Medical Center.
 - ▣ Presbyterian Hospital of Denton.
 - ▣ Wide range of specialty surgery and treatment centers.

City of Denton Overview (cont'd)

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- Estimated population of approximately 116,000 in 2012.
 - ▣ Population was 66,270 in 1990 and 82,976 in 2000.
- In 2011, Denton named as 7th fastest growing city in the country with a population over 100,000.
 - ▣ Growth continues to move north on both I-35E and I-35W.
 - I-35E expansion will begin in Spring 2013.
 - ▣ City will likely continue to have a rapid growth rate in the future due to available land in these corridors.
 - ▣ Center for Economic Development and Research at UNT estimates that the City of Denton's population will approach 210,000 by 2030.
- Growth will necessitate the issuance of debt to build required infrastructure for city services.

Service Profile

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- City of Denton is considered to be a “full service” municipal operation.
- The City provides general government services including:
 - ▣ Police and Fire
 - ▣ Parks and Recreation
 - ▣ Library
 - ▣ Planning
 - ▣ Code Enforcement, etc.
- Ongoing general government activities are typically driven by personnel costs associated with the services provided.
 - ▣ In the General Fund, for example, approximately 73% of the cost is related to salaries and associated benefits.
 - ▣ As such, cost drivers and decision points are dramatically different from other activities.

Service Profile (cont'd)

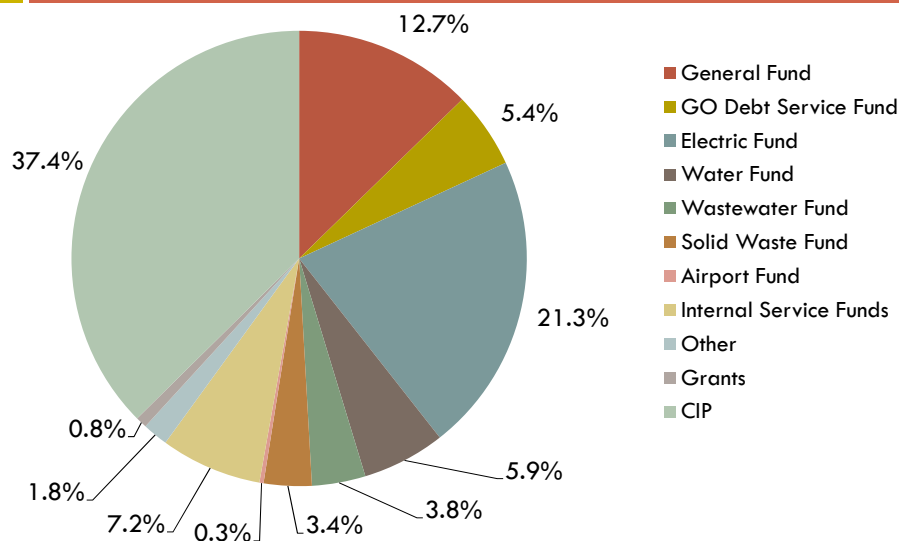
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- The City of Denton also operates several other self-supporting (or enterprise) operations.
 - ▣ Electric utility (Distribution and Transmission services).
 - ▣ Water utility (Water Treatment Plant).
 - ▣ Wastewater utility (Wastewater Treatment Plant).
 - ▣ Solid Waste services (Landfill).
- These services are capital intensive operations.
 - ▣ In the Electric Fund, for example, only 6% of the costs are related to personnel.
 - ▣ Majority of expenses tied to capital program.
- Approximately \$312 million in debt is expected to be issued over the next five years for the services described above.
 - Does not include any general government activities!!

FY 2012-13 Adopted Budget by Fund

\$745.0 million for all funds

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City of Denton Debt Profile

As of September 30, 2012

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Type of Debt	Remaining Principal	Remaining Interest	Total
Revenue Supported GOs	\$59,955,300	\$15,287,272	\$75,242,572
Tax Supported GOs	79,359,700	23,882,118	103,241,818
Total General Obligation Bonds (GOs)	\$139,315,000	\$39,169,390	\$178,484,390
Revenue Supported COs	\$180,645,000	\$69,599,841	\$250,244,841
Tax Supported COs	34,580,000	9,210,475	43,790,475
Total Certificates of Obligation (COs)	\$215,225,000	\$78,810,316	\$294,035,316
Utility System Revenue Bonds	\$156,855,000	\$49,749,957	\$206,604,957
Total Revenue Supported Debt	\$397,455,300	\$134,637,070	\$532,092,370
Total Tax Supported Debt	113,939,700	33,092,592	147,032,292
Total Debt Outstanding	\$511,395,000	\$167,729,662	\$679,124,662

Municipal Bond Insurance

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- City of Denton General Obligation bond ratings:
 - ▣ 'AA' from Standard and Poor's.
 - ▣ 'AA+' from Fitch Ratings.
 - ▣ 'Aa2' from Moody's.
- City of Denton Utility System bond rating is 'AA-' from Standard and Poor's.
- In prior years, the City purchased municipal bond insurance to achieve a 'AAA' rating.
 - ▣ Bond insurance cost was significantly lower than projected interest cost savings associated with AAA rating.
 - ▣ Due to 2008 financial crisis, AAA bond insurance is no longer available.
 - As such, a different approach to issuing debt was considered.

Debt Strategy

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- Without bond insurance, the City would be required to utilize the 'AA-' rating for utility system revenue debt.
 - ▣ This rating results in a interest rate that is approximately 0.30% higher than AA rated bonds with a tax pledge.
 - ▣ On a \$50 million bond sale, this equates to approximately \$2 million in savings over a 20 year repayment term.
- As a result, the City of Denton began issuing Certificates of Obligation (COs) to fund utility system projects in 2010.
 - ▣ Counteracts absence of bond insurance and widening of credit spreads.
 - ▣ Lowers overall borrowing costs for the City.
 - ▣ Existing Revenue Bonds have also been refunded with General Obligation Refunding Bonds when economical.

Interest Cost Savings

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- Although it is planned that the utility ratepayer will pay the debt service, the taxpayer is ultimately responsible for the debt.
 - ▣ Accordingly, the taxpayer is acting as a guarantor of the debt, much like bond insurance.
 - ▣ Converts from "implicit" to "explicit" guarantee.
- Due to this fact, the City of Denton has elected to dedicate any interest cost savings associated with COs to Street Improvements.
 - ▣ Costs are reduced by using 'AA' versus 'AA-' bond rating.
 - ▣ Savings transferred from utility operations.
- For FY 2012-13, savings are \$270,000 per year.
 - ▣ Expected to approach \$900,000 annually by FY 2016-17.
 - \$18 million over a 20 year period!

Summary

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- Certificates of Obligation (COs) can be used to significantly lower borrowing costs when compared to Revenue Bonds.
 - ▣ Interest cost savings.
 - ▣ No need to have debt service reserve.
 - ▣ Current debt service reserve surplus can be applied to existing principal.
- Unlike Revenue Bonds, COs require that the City publish a Notice of Intent to issue debt.
 - ▣ Subjects the CO issuance to potential petition to call for an election on the sale of debt.
 - ▣ As a result, COs may not be the best method to acquire financing in all cases.