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Volusia / Flagler FGFOA

Learning Objectives

- Understand the requirements associated with the new Municipal Advisor Rules and how it affects you
- Basic understanding of the issues associated with why determining if a bank direct placement is a security or a loan
- Basic understanding about some of the issues related to Continuing Disclosures on Bond Issues
- Impact of Tax Reform on Municipal Debt

Table of Contents

- Hilltop Securities Inc. formerly FirstSouthwest Tab 1
- Dodd Frank and MSRB Rules relating to Municipal Advisors Tab 2
- Bank Direct Purchases – Loan or Security? Tab 3
- Continuing Disclosure – (SEC Rule 15c2-12) Tab 4
- Impact of Proposed Tax Reform on Municipal Issuers Tab 5

Overview of Hilltop Securities Inc.

Tab 1

Overview of Hilltop Securities

Trusted Leader in Public Finance

- First Southwest Company merged with HilltopSecurities on January 22, 2016
- Wholly owned subsidiary of Hilltop Holdings Inc. (NYSE: HTH)
- FirstSouthwest, which was founded in 1946 continues to be one of the leading Financial Advisory / Investment Banking firms in the nation
- More than 112 years of combined industry experience
- Over 47 office locations in 19 states including offices in Orlando, Ft. Lauderdale, Miami and Palm Beach Gardens
- Approximately 945 employees including 175 public finance professionals
- \$17.2 billion in retail assets under management
- \$22 billion in Clearing Services client assets
- \$10.7 billion in Municipal Cash Management assets under management

Primary Business Lines

- Public Finance
- Capital Markets
- Retail
- Clearing Services
- Structured Finance
- Securities Lending

HilltopSecurities Office Locations



Comprehensive Services and Solutions for Municipal Clients

HilltopSecurities is a diversified investment bank specializing in public finance, capital markets, correspondent clearing and asset management. We set ourselves apart by putting our clients first.

HilltopSecurities Offers a Comprehensive Municipal Product and Service Platform

Product/Service Expertise
Financial Advisory
Investment Banking
Municipal Underwriting
Structured Finance
Continuing Disclosure
Investment Pools
Asset / Investment Management
Pension / OPEB Advisory
Arbitrage Rebate
Mortgage Origination Programs

Sector Expertise	
Airports	Ports
Benefit Plan Services	Public Power
City/County/State	School Districts
Convention Center / Hotel	Special Districts
General Obligation	Stadiums/Public Facilities
Healthcare	State Revolving Funds
Higher Education	Student Loans
Housing	Toll Roads Rapid Transit
Public-Private Partnership	Water and Sewer

A Leader in Public Finance

- From January 1, 2012 through December 31, 2016, the firm provided services on 7,390 transactions totaling more than \$364 billion as financial advisor or underwriter (*Source: Ipreo MuniAnalytics*)
- Our combined work as financial advisor or underwriter averages to approximately 28 issues and more than \$1.4 billion per week

	Number of Issues (bonds and notes)	Par Amount (\$ million)
Financial Advisor	5,183	\$181,966
Underwriter	2,207	182,328
TOTAL	7,390	\$364,294

Hilltop Securities- Financial Advisor		
Year	Number of Issues	Par Amount (\$ million)
2012	1,093	\$35,003
2013	1,025	29,951
2014	1,013	37,563
2015	1,016	39,155
2016	1,036	40,294
TOTAL	5,183	\$181,966

Hilltop Securities – Senior or Co-Managing Underwriter		
Year	Number of Issues	Par Amount (\$ million)
2012	648	\$53,479
2013	464	42,879
2014	384	28,580
2015	393	28,182
2016	318	29,403
TOTAL	2,207	\$182,328

NOTE: The data in the tables above include transactions in which First Southwest Company, LLC, served as financial advisor and Southwest Securities, Inc. served as senior or co-managing underwriter (or vice-versa) on the same issue, all prior to the two firm's merger effective on January 22, 2016.

Florida Experience

Substantial Prior Experience with Florida Cities & Counties



- Bay County
- Broward County
- Charlotte County
- Citrus County
- DeSoto County
- Escambia County
- Indian River County
- Lake County
- Martin County
- Miami-Dade County
- Okaloosa County
- Okaloosa County Airport
- Osceola County
- Palm Beach County
- Sarasota County
- Seminole County
- Taylor County
- City of Apopka
- City of Bartow
- City of Crystal River
- City of Edgewater
- City of Fernandina Beach
- City of Fort Lauderdale
- City of Haines City
- City of Hollywood
- City of Kissimmee
- City of Lauderhill
- City of Leesburg
- City of Marco Island

- City of Mascotte
- City of New Smyrna Beach
- City of North Miami Beach
- City of North Port
- City of Ocoee
- City of Orlando
- City of Oviedo
- City of Palm Bay
- City of Palm Coast
- City of Panama City
- City of Pinellas Park
- City of Port St. Lucie
- City of Sanford
- City of South Daytona
- City of South Miami
- City of Tavares
- City of Umatilla
- City of Wauchula
- City of Winter Haven

- Florida Community Services Corporation of Walton County
- Florida Gas Utility
- Florida PACE Funding Agency
- Florida Ports Financing Commission
- Gasparilla Island Bridge Authority
- Miami Parking Authority
- Miami Dade Expressway Authority
- Okeechobee Utility Authority
- Orlando-Orange County Expressway Authority
- Orlando Sanford International Airport
- Pace Water Authority
- Peace River Manasota RWSA
- Riviera Beach CRA
- State of Florida
- Tampa Hillsborough Expressway Authority
- Town of Longboat Key
- Town of Orange Park
- University of Central Florida

Dodd-Frank and MSRB Rules relating to Municipal Advisors

Tab 2

Dodd-Frank Act and Municipal Advisors

- Passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010
 - Required the registration of municipal advisors with the SEC and provides for their regulation by the Municipal Securities Rulemaking Board (MSRB)
 - Includes a specific antifraud prohibition and imposes a fiduciary duty on municipal advisors
 - Defined what is a Municipal Advisor (MA)
- Final Municipal Advisor Rule is adopted in 2013 and it became effective in 2014

SEC's Municipal Advisor Rule

- The rule approved by the SEC requires a municipal advisor to permanently register with the SEC if it provides advice on the issuance of municipal securities or about certain “investment strategies” or municipal derivatives.
- The rule clarifies who is and isn't a “municipal advisor” and offers guidance on when a person is providing “advice” for purposes of the municipal advisor definition.
- A person is providing “advice” to a municipal entity or an “obligated person” based on “all of the relevant facts and circumstances,” including whether the advice:
 - Involves a “recommendation” to a municipal entity.
 - Is particularized to the specific needs of a municipal entity.
 - Relates to municipal financial products or the issuance of municipal securities.
- Provides the following exemptions from registration for Underwriters serving in an underwriting capacity:
 - Independent Registered Municipal Advisor (IRMA) Exemption
 - RFP Exemption
 - Underwriting Exemption

Municipal Securities Rulemaking Board (MSRB) & Municipal Advisors

- Established by Congress in 1975 as a self-regulatory organization with a mandate to regulate the activities of broker-dealers and banks that buy, sell and underwrite municipal securities
- In 2010, Congress expanded the MSRB's authority to include the regulation of municipal advisors – the firms (and their financial professionals) that provide advice to state and local governments and other municipal entities about the issuance of bonds and municipal financial products
- MSRB is under the oversight of Congress and the SEC, and its rules generally must be approved by the SEC before becoming effective
- Established rules governing municipal advisors, including but not limited to:
 - G-44: Supervisory and Compliance Obligations of Municipal Advisors
 - G-42: Duties of Non-Solicitor Municipal Advisors
 - G-37: Political Contributions and Prohibitions on Municipal Securities Business and Municipal Advisory Business
 - G-17: Conduct of Municipal Securities and Municipal Advisory Activities

MSRB Rule G-17

- **MSRB Rules G-17** In the conduct of its municipal securities or municipal advisory activities, each broker, dealer, municipal securities dealer, and municipal advisor shall deal fairly with all persons and shall not engage in any deceptive, dishonest, or unfair practice.
- Interpretive guidance on the rule includes, among other things:
 - Cannot use any deceptive, dishonest or unfair practices
 - Anti-fraud prohibition
 - Role of Underwriter/Conflict of Interest
 - Required Disclosures, including as it related to compensation
 - Underwriter duties

MSRB Rule G-42

- **MSRB Rules G-42** establishes core standard of conduct for Municipal Advisors including:
 - Duty of Care
 - Duty of Loyalty
 - Disclosure of Conflict of Interest and Other Information
 - Documentation of Municipal Advisory Relationships
 - MA must have a reasonable basis to believe recommendation is suitable
 - Prohibits certain activity such as excess compensation, false or misleading representations
- Issuer have been receiving written disclosure statements from their Municipal Advisors based upon requirements of the rule

Bank Direct Purchases – Loan or Security?

Tab 3

History – Bank involvement in the municipal debt

- **Prior to 1986** – Banks were among the largest buyers of tax exempt obligations (loans and bonds) – Purchased bonds in the Capital Markets or made direct loans
- **Passage of the Tax Reform Act of 1986** – limited banks ability to deduct interest expense related to tax-exempt income reducing the desire to purchase tax exempt obligations
- **Bank Qualified Designation “BQ”** – Issuer limited to \$10 million in tax exempt debt per calendar year
- Most loans were no longer 7 to 10 years and under \$10 million
- Banks began to provide Letters of Credit (“LOC”) for Variable Rate Bonds Issues

History (cont.)

- **2008 Financial Crisis** – with the rating downgrades of bond insurers and commercial banks, risks began to materialize with variable rate debt backed by these entities such as VRDOs
- **Congress enacted the American Recovery and Investment Act of 2009 (ARRA)** among other things increased the “BQ” limit from \$10 million to \$30 million for 2009 & 2010. This increased Direct Purchases / Private Placements by Banks especially in Florida
- Banks in Florida were aggressively making loans and were willing to lock in rates for up to 20 years for a financing including very large financings (\$100 million)
- Bank Private Placements in many cases are cost effective, have low upfront fees, can be completed more quickly than bond issues and continuing disclosure is not required.

Bank Direct Placements

- Bank Direct Placement Issues:
 - Maintain many of the traditional bank letter of credit covenants – including interest rate gross up and yield maintenance provisions that allow banks to increase the interest rate due to changes in: the issuer ratings, corporate tax rate, costs associated with changes in laws or regulatory issues (Basel III - reserve requirements), along with default and acceleration provisions are incorporated into the bank loans.
 - Bond Investors and Rating Agencies concern on how it impact Bonds (Acceleration and Default Provisions)
 - Lack of Disclosure information (EMMA Continuing Disclosure filing are not required)
- Ability to utilize loans and securities varies by state
 - Florida law allows bank loans but some states are more limited as it relates to municipal entities
 - Securities may require a Placement Agent

Bank Loan vs Security?

- Bank Loan or Security – what’s the big deal?
 - Generically most Issuers see no difference in whether the debt obligation is classified as either a bond, promissory note, or loan
 - Many cases they use the same documents and are treated the same way for accounting purposes
- Whether it is a designated a Security or Loan does impact:
 - Municipal Advisors because MSRB Rules require that an MA cannot be both a Municipal Advisor and Underwriter / Placement Agent. Depending on how the financing is structured, it could inadvertently have regulatory consequences for the MA and subject them to major fines
 - Banks because it impacts Accounting Treatment and Mark to Market Requirements (securities may be required to be marked-to-market)
 - Issuers because securities are: subject to SEC guidelines and anti-fraud provisions, could limit bank participation and possibly increase fees associated with having a placement agent

Bank Loan vs Security? (con't)

- How do you determine if the Direct Placement is a Loan or a Security
 - “Reves v. Ernst & Young” case - presumes all debt is a security unless it bears a strong resemblance to a non-security type of debt – (consumer financing, short term notes, restricted transferability)
 - Terms and documentation, origination and approval of the bank help determine if it is treated as a loan or a security
 - Consultation with bond counsel at the beginning of the transaction
 - SEC and/or courts would make the final determination after the fact

- Key is communication between the Financial Advisor, Bond Counsel and the Issuer prior to issuing the RFP

Continuing Disclosure

Tab 4

Continuing Disclosure - SEC Rule 15c2-12

- **SEC Rule 15c2-12 (the “Rule”)**
 - Underwriters cannot buy or sell a primary offering > \$1 mil unless there is a written agreement in Final Official Statement that the Issuer will provide specified information
 - MSRB’s EMMA (Electronic Municipal Market Access) system designated sole NRMSIR (Nationally Recognized Municipal Securities Information Repository) in July 2009
 - Tower Amendment to Securities Act of 1934 prohibits direct or indirect federal regulation of municipal issuers; enacted in 1975 as part of legislation creating MSRB
 - The continuing disclosure agreement remains in place for the life of the bonds
 - Material Events List expanded May 2010 to 14 Items

What Does This Mean For Me?

- Required: Annual Audit filed on EMMA; may require Budget too
 - Usually due within 6 to 9 months of FYE
- Required: Annual Financial Information compiled from Issuer financial and operational records (Tables) filed on EMMA
 - Usually due at the same time as the Annual Audit
- Material Event Notice filed on EMMA within 10 business days of occurrence
- Voluntary: Information that may be selected to make publicly available on EMMA (not required by SEC Rule 15c2-12)

SEC Rule 15c2-12 - Required Material Events Filing

Required Material Events – Within 10 Business Days of Their Occurrence

- Principal and interest payment delinquencies
- Non-payment related defaults, if material
- Unscheduled draws on debt service reserves reflecting financial difficulties
- Unscheduled draws on credit enhancements reflecting financial difficulties
- Substitution of credit or liquidity providers, or their failure to perform
- Adverse tax opinions, IRS notices or material events affecting the tax status of the security
- Modifications to rights of security holders, if material
- Release, substitution or sale of property securing repayment of the securities, if material

SEC Rule 15c2-12 - Required Material Events Filing (cont.)

Required Material Events – Within 10 Business Days of Their Occurrence

- **Bond calls, if material, and tender offers**
- **Defeasances**
- **Rating changes**
- Bankruptcy, insolvency, receivership or similar event of the obligated person
- Merger, consolidation or acquisition of the obligated person or issuer, if material
- Appointment of a successor or additional trustee or name change of a trustee, if material

Why is Compliance with SEC Rule 15c2-12 Important?

- According to the Rule, Underwriters/institutional investors cannot bid on transactions until all required information is filed and a notice of late filing (if applicable) is made (5-year lookback)
- **Non-compliance language must be included in any public offering documents for the subsequent five years**
- Serious or ongoing non-compliance issues could limit access to the capital markets, which may increase borrowing costs
- Inaccurate statements in bond offering documents is considered securities fraud and subject to increased SEC enforcement, including **financial penalties for Issuers and Government Officials**

Recent Developments in Continuing Disclosure

- SEC Proposes Two New Material Event Categories
 - Other Financial Obligations (Private Placements/Leases), if material
 - Financial Difficulties, such as default, acceleration or termination event, if material
 - Would require 10-business day filing requirement on EMMA
- Other Hot Topics
 - Voluntary disclosure of items not mandatory under 15c2-12
 - Heightened industry awareness about continuing disclosure due to MCDC
 - Focus on **Best Practices**, including Issuer training for persons responsible for disclosure; adopting Disclosure policy
 - GFOA has best practices for continuing disclosure

Impact of Proposed Tax Reform on Municipal Issuers

Tab 5

Proposed Impact of Tax Reform (to be updated)

- Lowering the Corporate Tax Rate from current level (35%) could trigger increased interest rates on Loans with gross up provisions
- Increased interest rates / yields on tax-exempt borrowings because tax exemption is worth less.
- Elimination of tax-exempt advance refunding will reduce ability to refund for debt service savings or for restructuring reasons
- Elimination of tax exempt financing for 501(c3) not for profits.
- Eliminates use of tax exempt financing for private activity bonds (such as airport, seaports, and P3s)
- Eliminates use of tax exempt financing for private colleges and universities



Questions?

Disclosure

This communication is intended for issuers for educational and informational purposes only and does not constitute legal or investment advice, nor is it an offer or a solicitation of an offer to buy or sell any investment or other specific product or service. Graphs included in this presentation depict historical interest rates and their respective relationships. Financial transactions may be dependent upon many factors such as, but not limited to, interest rate trends, tax rates, supply, change in laws, rules and regulations, as well as changes in credit quality and rating agency considerations. The effect of such changes in such assumptions may be material and could affect the projected results. Any outcome or result HilltopSecurities, or any of its employees, may have achieved on behalf of our clients in previous matters does not necessarily indicate similar results can be obtained in the future for current or potential clients. HilltopSecurities makes no claim the use of this communication will assure a successful outcome. This communication is intended for institutional use only. For additional information, comments or questions, please contact Hilltop Securities Inc.