MEMO TO: BOARD MEMBERS
DR. JOHN SIMPSON

FROM: BRUCE ELLERMAN

DATE: OCTOBER 9, 2017

RE: POSSIBLE BOND REFUNDING OPPORTUNITY

The potential opportunity for the Webster Groves School District to refund a portion of its existing Bonded Indebtedness has been identified that is projected to save about $891,000 in future interest costs. This opportunity has been created by the "spread" (or difference) between current low interest rates in the bond market compared to the interest rates on certain outstanding District bonds—specifically, $17.8 million of Build America Bonds (BAB's) maturing in the year 2020 and later that were issued by the District in 2010. This spread differential is due more to the difference between taxable versus tax exempt bonds than any movement in overall bond interest rates, as rates have been at relatively and historically low levels for many years now.

One of the initial areas of review after I joined Webster Groves as Interim CFO in 2016 was to look at the District's Debt Service Fund and bonded indebtedness. The objective was to determine if any portion of the District's long-term debt could be refinanced:

1) At lower interest rates;
2) In a manner that would relieve some cash flow pressure from the Debt Service Fund—which at the time was no longer cash flow self-supportive at certain points during the fiscal year; and/or
3) In a manner that would positively affect the bonding capacity available to the District without requiring an increase in the tax rate. Based on financial projections at the time, the District was not projected to have any "no tax increase" bonding capacity available until around the year 2026.

Inquiries were then made of a couple different underwriter/bond advisor firms. At the time, no one was able to identify any significant refinancing opportunity available to the district. One of the firms (Stifel Nicolaus & Co, hereafter referred to as "Stifel"), however, continued of their own accord and without compensation to monitor the District's debt, the bond market and interest rates for future opportunities.

In the meantime, the district took some internal steps to support and bolster the Debt Service Fund. These steps included the transfer of about $400,000 of unspent bond proceeds and about $1.3 million in Classroom Trust state funding to the Debt Service Fund. At the same time, the

District's tax base increased substantially due to reassessment this year (in 2017), further strengthening the Debt Service Fund's finances. As a result, not only is the Debt Service Fund once again cash flow self-supporting at all times throughout the fiscal year, but district projections indicate a significant amount of additional bonding capacity (about $8 million) actually now exists that could be supported without an increase in the current $.5699 Debt Service Levy. (NOTE/Any bond issue would, of course, be subject to future district needs and voter approval.)

Moreover, this positive trend can now be further enhanced by refinancing $17.8 million of the District's outstanding BAB's. Specifically, Stifel has estimated that the District taxpayers could save about $891,000 in net interest costs over the life of the BAB's, representing about 5% of the par amount of bonds being refinanced. This level of savings is well above the minimum feasible refunding savings threshold recommended by the State of Missouri under its Direct Pay program of 1.5%. Please note that this is an estimate based on current interest rates and organizations with similar credit ratings to Webster Groves School District's AA+ rating. Actual savings may differ from this estimate depending on interest rate fluctuations between now and the time any new bonds are sold and depending on how the market responds to actual Webster Groves School District bonds in particular. Because the BAB's are not callable (i.e. technically cannot be paid off early) until March, 2020, this refinancing would involve a temporary escrow to hold the proceeds of the refunding bond sale until such time as the BAB's could technically be paid off in March, 2020. This escrow would also pay the normal interest payments on the applicable BAB's from the time of the refunding until the time of the March, 2020 call.

At the same time, depending on the year by year timing of the interest savings, there could be a second benefit of refinancing the BAB's. That is, if the interest saving occur at strategic (cash flow tight) times within the current amortization schedule, then refinancing could further increase the no tax increase bonding capacity of the district by as much as a few million dollars.

As you may recall, BAB's are special kinds of bonds that were only issued during a very limited time as part of a federal budget stimulus program. As a result, the BAB's are actually taxable bonds, meaning the interest payments to bondholders are subject to income taxes. This is in contrast to school district bonds normally being exempt from income taxes. As a result of this taxability difference, the interest rates on BAB's are higher than interest rates on normal tax exempt district debt. As part of the BAB incentive, however, this interest rate premium was subsidized by payments from the federal government to school districts (or other bond issuers) so that the net interest cost was actually less than tax exempt bond interest would have been. Since Webster initially issued its BAB's in 2010, the differential between taxable and tax exempt rates in particular and the bond interest market in general has changed enough to make a refunding of taxable BAB's with tax exempt debt financially advantageous.

To proceed with this refinancing, the district needs to execute a nonbinding Underwriter Engagement Agreement with Stifel. This Agreement authorizes Stifel to represent Webster Groves School District in making preparations for the eventual issuance of new bonds to refund the 2020 maturity and later BAB's. Because this Agreement is nonbinding and at no cost to the District, it does not require Board approval but can be executed by a district administration official instead.

Formal Board approval will not be needed until the details and specifics of the actual refunding bond issuance are determined, which is expected to be at the December 11th Board meeting. At that time, a formal Bond Sale Resolution will be presented to the Board for approval. Stifel's compensation would then be paid from the proceeds of the new bond sale, which has already been factored into the aforementioned $891,000 projected savings. This compensation represents .5% of the new bond issue, which is extremely competitive compared to prevailing market underwriting spreads.

Additional information from Stifel regarding details of the proposed refunding and the underwriting fee comparison to market is attached for your reference.

RECOMMENDED BOARD ACTION….report only; no action necessary at this time; action on Bond Sale Resolution will be requested at the December Board meeting after bonds are "priced" in the market.