



City of Tacoma

City Council and Public Utility Board Bond Training

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Agenda

Post issuance compliance training

As an issuer of tax-exempt bonds, the City and its departments must comply with a number of tax and continuing disclosure requirements.

Today's discussion will walk through the key compliance requirements.

Federal Tax Law

- Requirements applicable to use of facilities
- Investment of proceeds

Federal Securities Law

- Overview of disclosure and antifraud requirements
- Speaking to the Market

Questions?



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Snapshot of City Debt

- General Government
 - LTGO Bonds
 - UTGO Bonds
 - LID Bonds
 - Convention Center and Parking Bonds
 - State of Washington LOCAL Program Loan
- Department of Environmental Services
 - Solid Waste Bonds
 - Sewer Bonds
 - Sewer WIFIA Loan
 - Subordinate lien obligations
- Tacoma Public Utilities
 - Electric System
 - Water System
 - Regional Water Supply System
 - Subordinate lien obligations, note purchase agreements, lines of credit, letters of credit

Role of City Council and Public Utility Board

City Council and Public Utility Board, with respect to TPU debt, oversee the authorization of debt

- Section 4.11 of the City Charter:
 - All matters relating to system expansion and the making of additions and betterments thereto or extensions thereof, the incurring of indebtedness, the issuance of bonds, and the fixing of rates and charges for utility services under the jurisdiction of the Board shall be initiated by the Board, subject to approval by the Council, and executed by the Board ...
- Board resolution and City Council ordinance delegate to authorized representatives the authority to approve the final financing terms (subject to parameters with regard to maximum aggregate principal amount, not to exceed true interest cost, maximum term, and other terms) and to sign off on disclosure document for purposes of federal securities laws
- The Council is responsible for authorizing the overall financing/borrowing

City Disclosure and Post Issuance Compliance Policy

Provides a framework for the City's compliance with primary and continuing disclosure requirements under federal securities laws and with post-issuance requirements under federal tax laws for bonds, notes and other obligations

- Guides all City departments in meeting disclosure and post-issuance bond compliance tax obligations
- Issued by Finance Department
- Primary responsibility for compliance: identifies the Director of Finance or, for obligations issued by TPU, the Director of Utilities, or other delegated City officials
- Prompts staff training
 - next joint training scheduled for June 4, 2025

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Resources

- Electronic Municipal Market Access ("EMMA")
 - <https://emma.msrb.org/Home/Index>
- Pacifica Law Group
 - [Pacifica U](https://www.pacificallawgroup.com/news-items/pacifica-u/)
 - <https://www.pacificallawgroup.com/news-items/pacifica-u/>
 - [Public Finance Articles, Resources and News](https://www.pacificallawgroup.com/)
 - <https://www.pacificallawgroup.com/>
- National Association of Bond Lawyers ("NABL") Bond Basics
 - <https://www.nabl.org/basics-start/>
- City investor relations pages
 - <https://www.cityoftacoma.org/cms/one.aspx?pageld=216423>
- Government Finance Officers Association
 - [Best Practices and Resources](#)



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Federal Tax Requirements – Overview

Internal Revenue Code and regulations govern:

- How tax-exempt bond proceeds can be spent
- Use of financed facility/assets
- The investment and arbitrage of bond proceeds

Rules with respect to refunding and defeasance

Set expectations at closing with key documents:

- Tax Certificate
- Form 8038-G

Monitor for changes:

- Post-Issuance Compliance Policy
- Private activity tracking



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Big Picture - Use of Tax-Exempt Bond Proceeds

In planning capital projects, consider

- which expenditures *can be* financed with tax-exempt bonds
- which expenditures *should be* financed with taxable bonds or equity
- what are the City's *reasonable expectations* at closing
- how much *flexibility* is desired over the term of the financing

Tax-exempt bond proceeds generally must be spent on *capital expenditures*

- "Capital expenditure" is defined as "any cost of a type that is properly chargeable to capital account (or would be so chargeable with a proper election or with the application of the definition of 'placed-in-service' under Section 1.150-2(c) under general federal income tax principles)."
- Costs of issuance and working capital related to the project (limited to 5% of proceeds) are also allowed
- Governmental issuers can finance working capital needs in some circumstances

How quickly does the City expect to spend the tax-exempt proceeds?

- Reasonable expectations are determined at closing
- General rule – three years from closing



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Private Business Use

Generally, “private business use” means:

- Use (directly or indirectly)
- Of a financed facility
- In a “trade or business”
- Carried on by any nongovernmental person
 - Corporations, partnerships or any other entity engaged in business
 - Federal government and federal government agencies
 - For Tacoma Power, includes Bonneville Power Administration
 - Natural persons engaged in a trade or business
 - Nonprofit organizations

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General Management Contracts

Service and Management Agreements can sometimes create private use

Exceptions:

- Incidental services are not private use
- Disguised leases are generally private use
- “Qualified management contracts” do not create private use

Example: Food Services Contract or Parking Contract based on net profits

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Output Contracts

“Output facility” means:

- electric and gas generation, transmission, distribution, and related facilities, and
- water collection, storage, and distribution facilities.

Private use of output contracts measured under the “benefits and burdens” test

Regulations discuss these types of contracts separately:

- take contracts
- take or pay contracts
- requirements contracts



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Common Exceptions to Private Business Use

General Public Use

- Use by a member of the general public (natural persons not engaged in trade or business) or another governmental entity is not private use

Incidental Use

- For example, kiosks, vending machines, pay phones
- Use is non-possessory and the non-possessory uses do not exceed 2.5% of the financed facility

Short Term Use

- Less than 50 days of use under a single lease or use agreement
- Payments must be fair market value
- E.g. facility rental at Tacoma Convention Center

Use incidental to financing arrangements

Temporary use by developers



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When Things Change

Change in use and deliberate action

Types of remedial action

- Redeem or defease “nonqualified bonds”
- Alternative use of disposition proceeds
- Alternative use of the facility
- Ask for mercy (i.e. VCAP)

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Investment Considerations – General Concepts

Arbitrage is borrowing in one market (tax-exempt) and investing in a different market (taxable) at a higher rate.

Tax Certificate signed at closing will document “reasonable expectations” of the City with respect to how proceeds will be invested and which tests will be met

Two rules when it comes to arbitrage

- Yield Restriction – can you earn it?
- Rebate – if you earn it, can you keep it?

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Federal Securities Laws

Overview

Although municipal bond issuers are exempt from the SEC's registration and filing requirements that apply to corporate issuers, all issuers (including municipalities) are subject to the antifraud requirements that apply when issuers speak to the market

- Disclosure Framework
 - Antifraud Rules
 - Rule 15c2-12
 - Continuing Disclosure



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Disclosure Framework; Antifraud Laws

Antifraud Requirements Apply Whenever an Issuer Speaks to the Market

Rule 10b-5, promulgated under Section 10(b) of the Securities Exchange Act of 1934, prohibits fraud in connection with the purchase and sale of securities. Among other provisions, it makes unlawful:

- any untrue statement of a material fact or
- omitting to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading,
 - in connection with the purchase or sale of any security.

Similar language under Section 17(a) of the Securities Act.

- SEC settlements under Section 17(a) have been based on a negligence standard
 - “knew or should have known” standard for establishing negligence
 - Failure by an actor to conform conduct to the standard of a reasonable person under like circumstances



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Materially Accurate and Complete

Materiality

Whether a statement or omission can give rise to a securities law violation depends on whether the statement or omission is material.

The definition of “material” has been established by case law.

- There is a substantial likelihood
- That a reasonable bond investor
- Would consider it important in making an investment decision
 - There must be a substantial likelihood that a fact "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."



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Speaking to the Market

Initial disclosure (e.g. offering document)

Secondary disclosure (e.g. annual financial statements and other filings made pursuant to ongoing disclosure undertaking, voluntary disclosures, investor relations webpage, etc.)

A caution regarding the scope of the antifraud requirements

The SEC Office of Municipal Security (OMS) released a Staff Legal Bulletin summarizing existing law regarding the application of the antifraud requirements to *public statements* by issuers and borrowers.

- Rule 10b-5 under Section 10(b) of the Securities Exchange Act
 - Applies to primary disclosure and secondary market disclosure
 - Prohibits making any untrue statement of material fact or omitting to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading

Any public statement (at least by officials who may be viewed as having knowledge regarding the financial condition and operation of an issuer) may be reasonably expected to reach investors and therefore be subject to the antifraud requirements.



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Secondary Market Disclosure

Antifraud Requirements Apply Whenever an Issuer Speaks to the Market

Secondary market disclosure includes required EMMA filings and voluntary disclosure.

- SEC Rule 15(c)(2)-12
 - Underwriter must confirm the issuer has entered into a written undertaking to provide annual information and notice of listed events
- Contractual obligation of the issuer and/or obligated party to provide:
 - Annual financial statements
 - Annual operating or other information as stated in the undertaking
 - Notice of certain events within 10 business days of the *occurrence* of the event



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Required Filings on EMMA

Certain events require notice

An undertaking to provide continuing disclosure is required, under Rule 15(c)(2)-12 to include a commitment to provide notice within 10 business days of the *occurrence* of certain events.

- Certain events must be noticed in all cases, such as:
 - Rating changes
 - Unscheduled draws on debt service reserves or credit enhancement reflecting financial difficulties
 - Defeasances and redemptions
- Other events must be noticed *if material*, such as:
 - Non-payment related defaults, if material
 - Incurrence of a new financial obligation, if material



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SEC Enforcement

SEC will initiate an enforcement investigation when it has reason to suspect that the federal securities laws have been violated

Looking for disclosure-based violations

Investigation typically involves scrutiny of all persons involved in the conduct in question

- issuer, its officers and key employees (whether or not still employed), the underwriters, the municipal advisor, legal counsel

Seeking financial penalties

- Wenatchee PFD (failure to disclose feasibility report)

Finding individuals liable; control person liability

- Allen Park, Michigan (Mayor an active champion of the project, in a position to control the actions of the City and the City Administrator)

Bringing parallel criminal fraud charges

- Ramapo, New York (accounting fraud)

Second guessing legal risk disclosure

- Port of NY & NJ (internal counsel noted questions of statutory authority)
- Board approved projects on consent calendar without discussion or disclosure of legal risks of the analysis



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SEC Enforcement Proceedings Takeaways

- Cases against both municipal entities and individuals
 - In addition to charging issuer, charges against Mayors, CFOs
 - Several cases also charge municipal advisors; in one case, charges against outside auditor
- Cases involve both primary (including private placements), secondary market disclosures
- Cases also involve misrepresentations to evaluators
 - Ratings agencies, state board
- Outdated information: stale financial statements, outdated projections
- Failure to disclose conflicts of interest

Highlight importance of Internal controls and procedures

- Include more than one individual in the preparation, review and approval of disclosures
- Careful review of financial and other information provided to intermediaries as well as to the bond market
- Practice awareness and care when disclosing financial information that may be outdated and no longer reflective of current financial conditions



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A Note About Tax Reform

119th Congress

- Faces several critical fiscal deadlines
- Looming federal debt ceiling, funding federal programs, etc.
- Largest tax reform debate since 2017
 - Expiration of many key provisions of the Tax Cuts and Jobs Act at end of 2025
- Many proposals and many unknowns at this time
- Priority of industry groups
 - Preserve tax-exempt financing options for State and local governments. Reducing or eliminating tax exemption on municipal bond interest will result in increased borrowing costs, requiring less infrastructure investment or increase revenue to pay debt service.



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Wrap Up

Questions?

Comments?

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Thank you!



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