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MUNICIPALITY OF ANCHORAGE

ASSEMBLY INFORMATION MEMORANDUM

AIM No. 64-2006

Meeting Date: May 23, 2006

1 **From: Mayor**

2
3 **Subject: Debt Management Report - Final Version**

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5 AR 2005-64 called for the determination of municipal debt capacity in light of factors
6 typically considered by bond rating agencies and financial best practices. The Debt
7 Management Report has been completed by Municipal staff and the Municipality's Financial
8 Advisor and is attached for review.

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13 Concurrence: Jeffrey E. Sinz, Chief Fiscal Officer

14 Concurrence: Denis C. LeBlanc, Municipal Manager

15 Respectfully submitted: Mark Begich, Mayor

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18 AIM Final Debt Management Report – May 2006

MUNICIPALITY OF ANCHORAGE DEBT MANAGEMENT REPORT

April 24, 2006

Prepared by:



60 Years of
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MUNICIPALITY OF ANCHORAGE DEBT MANAGEMENT REPORT

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- Exhibit One – Debt Statement as of December 31, 2005
- Exhibit Two – Credit Rating Agencies’ Median Debt Ratios by Rating Category
- Exhibit Three – Debt Affordability Analysis, Base Case Assumptions

EXECUTIVE SUMMARY

The Municipality of Anchorage (the "Municipality") has requested that First Southwest Company complete a Debt Management Report (the "Report") for the Municipality. The Report is intended to be used by policy makers to develop the options available to determine the allocation of limited financial resources to meet the Municipality's capital needs. The Report represents a concerted effort by the Municipality to quantify and analyze the options available to the Mayor and the Municipal Assembly in their pursuit of on-going capital programs for the Municipality.

The format of the Report is to define the methodology to be used, develop the assumptions employed and then present the Report's conclusions. The Report also includes a survey on debt instruments available to the Municipality as well as commentary on debt structuring elements and criteria employed for debt refinancing. Additionally, the Report makes certain recommendations with regard to immediate financing needs and existing market conditions.

One of the goals of the Report is to create a methodology to facilitate comparisons with other similar cities. The Report recognizes that the Municipality has many responsibilities and programs that are not common to other tax-exempt issuing entities. The Report calculates certain key financial ratios which are standard within the financial community. The analysis of these ratios will determine whether the Municipality's financial position is within accepted ranges for similarly situated issuers.

The assumptions employed are critical to the Report's conclusions. The major assumptions include:

- The Municipality will remain in its current rating levels of Aa3/AA-;
- Fixed rate borrowing cost of 5.50%;
- Debt service of each series is paid over 20 years;
- The general obligation debt of the Anchorage School District (ASD or the School District) outstanding on December 31, 2005 will continue to be reimbursed by the State of Alaska according to the present formula; and
- New general obligation debt of the ASD will not be reimbursed by the State of Alaska.

Although we believe the above assumptions to be reasonable, changes to the Report's assumptions could materially affect the Report's conclusions.

The Report's conclusions are summarized as follows:

- As of December 31, 2005, the Municipality is well within the maximum debt ratios as described by the rating agencies for similarly rated entities
- Assuming no reimbursement of new ASD general obligation debt by the State, but continuing reimbursement of currently outstanding ASD general obligation debt, the Municipality has the capacity to issue \$235 million of new general obligation bonds by December 31, 2006. The April 4, 2006 ballot measures totaling \$46.110 million, which were approved by voters, are well within the Municipality's capacity to issue additional general obligation debt.

As part of this Report, we have made several recommendations with regard to immediate financing opportunities facing the Municipality. These recommendations can be found in Section VIII of the Report.

We would recommend that the Municipality update the Report annually to reflect changes in assumptions and circumstances.

I. CONCEPT OF DEBT AFFORDABILITY ANALYSIS

Appropriate Use of Debt Provides Fiscal Stability: The Municipality regularly undertakes the financing of infrastructure assets for public safety, roads, transit, utility, economic development and education purposes through the issuance of debt. The Municipality uses a variety of mechanisms to issue debt, including general obligation bonds of the Municipality and School District, and revenue bonds of various enterprise operations. Debt financing of capital assets spreads the costs across time, enhances stability in budgeting, lowers annual funding impacts and allows faster completion of projects at today's prices (rather than inflated prices in the future). However, the issuance of debt requires the dedication of some revenues to the payment of interest costs. In contrast, pay-as-you-go capital funding reduces funding available for immediate needs and forces the timing of capital projects to match current cash flows.

Debt Affordability Balances Capital Needs and Fiscal Resources: To maintain or improve its bond ratings and to promote the market's acceptance of its bonds, the Municipality also must assure the credit rating agencies and investors that capacity exists to ensure timely payment of all existing and future debt obligations. In order to issue debt, the Municipality must have the ability to make future debt service payments without jeopardizing payments for prior debt obligations or depleting funds necessary for critical operations and services. A major element of financial management is determining the allocation of limited financial resources to meet capital needs. Scarce resources can be allocated among expenditure priorities competing for the same dollars by using debt affordability analysis as a guide. Debt affordability analysis can assist policymakers with reaching equilibrium between the necessity of infrastructure investment and the on-going budgetary commitments to programs for public safety, education, public works, health and welfare, etc. Fitch Ratings, one of the three major Wall Street credit rating agencies, has written "*Sound debt affordability policies offer benefits such as a framework for allocating resources, increased financial flexibility through limiting and adding predictability to the fixed cost burden, and greater tax rate stability. Keeping debt-related costs within a tolerable range for taxpayers may also reduce the likelihood of vocal public opposition to needed capital projects.*"¹

Debt Affordability Measured Using Debt Ratio Analysis: Debt ratios are a subset of a broad category of financial ratios that can be applied to evaluate the performance and financial condition of entities from as small as an individual home or business owner to as large as a Fortune 500 company. Debt ratio analysis is employed by municipal bond market participants as a reasonable and convenient way to compare relative debt burdens across a wide variety of borrowers. Generally speaking, better debt ratios relative to other borrowers indicate a greater likelihood of debt repayment which translates into higher credit ratings, reduced borrowing costs and greater debt capacity for a bond issuer. The ratios of debt to full value, debt per capita and debt service to operating expenditures are utilized to measure the GO bond debt capacity of the MOA and the School District, with the ratio of debt to full value the most relevant of three indicators.

The capacity of the MOA to issue GO bonds arises directly and indirectly from various factors such as the retirement and refunding of outstanding debt, a growing population, an expanding property tax base, partial reimbursement of School District debt service by the State of Alaska, increasing wealth levels, lower borrowing rates, augmented governmental revenues and reserves, and reductions in non-debt expenditures.

¹ Fitch Ratings "To Bond or Not to Bond – Debt Affordability Guidelines and Their Impact on Credit", June 21, 2005

II. CREDIT RATINGS ASSIGNED TO GENERAL OBLIGATION BONDS

Importance of Credit Ratings: A credit rating is an independent, third-party assessment of the credit risk associated with purchasing and holding a particular debt obligation. Specifically, bond ratings focus on an issuer's ability and willingness to make full and timely payments on its debt. Bond ratings remain one of the most important indicators of financial performance readily available to the investment community and have a strong, yet inverse, relationship to a bond issuer's cost of funds – higher credit ratings result in a lower borrowing rate.

The three primary bond rating agencies that assign credit ratings to tax-exempt debt are Fitch Ratings ("Fitch"), Moody's Investors Service ("Moody's") and Standard & Poor's ("S&P"). The broad rating categories for long-term debt are triple-A ("Aaa" or "AAA") for the being the best possible rating and "D" for default being the worst. (Short descriptions of the major credit rating categories are provided in Figure 1 below.) Credit ratings considered to be "investment grade" are those in the "Baa/BBB" category or higher, with rating categories then ascending from "A/A" to "Aa/AA" to "Aaa/AAA". These rating categories are often specified up or down through the use of modifiers - Moody's assigns modifiers of "1", "2" or "3" while Fitch and S&P employ "+" or "-" signs. For example, a Moody's rating of "Aa1" is considered superior to a rating of "Aa3", while an "AA+" rating from Fitch or S&P is of higher credit quality than an "AA-" rating.

Figure 1

Long-Term Credit Rating	Assessment of Creditworthiness
"Aaa/AAA"	Highest credit quality, exceptionally strong capacity for timely payment
"Aa/AA"	Very high credit quality, not significantly vulnerable to foreseeable events
"A/A"	High credit quality, low expectation of credit risk
"Baa/BBB"	Good credit quality, adequate capacity for timely payment
"Ba/BB"	Speculative, risk may develop with adverse economic change
"B/B"	Highly speculative
"Caa/CCC" descending to "D"	Default is a possibility or imminent

Credit Ratings of the Municipality's GO Debt: As of December 31, 2005, the MOA had outstanding 32 series of GO bonds issued to fund general purpose and School District capital projects. Since 2000, the Municipality's GO bonds have been assigned credit ratings of "Aa3" by Moody's Investors Service and "AA-" by Standard and Poor's. (Fitch does not rate the Municipality's GO bonds but does assign ratings to the debt issued and repaid solely from proprietary funds.)

The GO bonds are currently assigned credit outlooks of "stable" by Moody's and "positive" by S&P. Standard and Poor's recently improved their outlook from "stable" to "positive", noting "*if reserve levels are maintained as rising costs are accommodated with ongoing revenues, and the regional economy remains robust, a rating upgrade could occur.*"² These rating agencies' outlooks are predicated on the following:

- The economy and tax base will continue to grow;
- Reserves will not decrease below levels dictated by adopted policy;
- State of Alaska reimbursement of a portion of the School District debt will continue;
- Additional debt will not materially change the debt position;
- Retirement of outstanding debt will stay above average; and
- A structurally balanced budget and diversifying revenues will continue to strengthen credit quality.

² Standard & Poor's credit report dated March 15, 2005

Factors Impacting the Municipality's GO Bond Ratings: To determine a rating, rating agency analysts consider the financial, economic, debt, and administrative and management factors relating to an issuer's ability and willingness to pay debt service. The strengths and weaknesses of each factor are taken into consideration to determine the rating.

Financial Factors

Financial results have the most significant impact on the determination of a rating. The rating review involves an examination of results of operations, including evaluation of actual fiscal performance versus planned budget performance, with deviations from the plan questioned. The general fund financial statement is examined with emphasis on current financial position and fund balances, as well as three- to five-year trends in planning and budgeting procedures. Contingencies such as unfunded pension liabilities are also considered.

Economic Factors

The rating agencies' economic analysis includes an evaluation of the depth and diversity of the tax base of the debt issuer, as reflected by employment rates and employer concentration, income levels and characteristics of assessed values. Economic vitality and adequate tax structure are key determinants of the issuer's ability to repay debt.

Debt Factors

Debt factors analyzed include direct and overall debt burden, debt ratios and trends and types of security pledged to debt repayment.

Administrative/Management Factors

The review of management includes an examination of the form of government and assessment of the debt issuer's ability to implement plans as well as fulfill legal requirements. Focus is on the capabilities of managers. Key ingredients in this review are the willingness of management and the legislative body to make and follow financial policies, the effective planning and implementation of capital improvement programs, and maintaining accounting and financial information that is reliable and regularly updated.

Rating Agency Commentary Regarding Assigned GO Bond Ratings: Figure 2 below highlights the commentary from Moody's and S&P regarding the credit ratings assigned to the Municipality's GO bonds.

Figure 2

Moody's Investors Service ³	Standard and Poor's ⁴
<p><i>Financial Factors</i></p> <ul style="list-style-type: none"> Financial operations are stable Further improvement expected due to minimum GF reserve levels of 8.25%; w/ additional 2.5% in four major sub-funds, reserves are in excess of 10% For 2005, revenues and expenditures are on budget with a surplus expected 	<p><i>Financial Factors</i></p> <ul style="list-style-type: none"> Healthy reserves and a balanced budget Prudent spending reductions and revenue enhancements offset deficit at beginning of 2004 Financial challenge remains, property taxes make up 57% of general fund revenues; taxing mechanism fiscally constrained
<p><i>Economic Factors</i></p> <ul style="list-style-type: none"> Economy has enjoyed steady growth Population, employment and tax base are at record levels Diversification has been further increased by air transportation and tourism jobs Economic dependence on oil is limited Growth is primarily driven by new investment 	<p><i>Economic Factors</i></p> <ul style="list-style-type: none"> Largest economy in the state; hub for major businesses Incomes above average At 5.2%, unemployment rate on par with the nation AV of \$22.4 billion in 2005, up 5.7% from 2004 Since 1990 Census, MOA population growth at 23%; Statewide growth only 19%
<p><i>Debt Factors</i></p> <ul style="list-style-type: none"> Debt is high but manageable Full debt burden 5.6%; effective debt burden 3.5% Growing tax base, reserves, and school debt reimbursement offset full debt Relatively rapid payout of debt at 20 years provides new capacity 	<p><i>Debt Factors</i></p> <ul style="list-style-type: none"> 2005 debt levels are moderate with school debt reimbursement averaging 60% Debt pay down is rapid Overall debt per capita is \$2,417 and 3.1% of the market value of the property
<p><i>Administrative/Management Factors</i></p> <ul style="list-style-type: none"> 2003 restructuring of revenue was achieved Management of spending and reductions resulted in a budget on target ending in 2004 With challenges, the Municipality has maintained reserves and flexibility 	<p><i>Administrative/Management Factors</i></p> <ul style="list-style-type: none"> In 2004 reserves were maintained in excess of established minimum requirements 2004 budget was maintained even with elimination of state funding sources Established management practices in place for reserves maintenance

Further rating agency comments noted the Municipality's increased budget and spending controls and fund balance reserves:

Moody's⁵

- Recognized that long-term flexibility was preserved when the "Municipality adopted a fund balance policy...the effective fund balance requirement is in excess of 10% of general fund expenditures."
- Expects that "additional debt, when issued, will not significantly undermine the Municipality's debt position, given sustainable tax base growth, relatively rapid payout of outstanding debt which provides capacity for new debt, and likely continuation of state assistance for school debt repayment."

Standard and Poor's⁶

- Credits the Municipality's aggressive management to ending 2004 on a solid note, "As a percentage of general fund expenditures and school transfers, the municipality finished 2004 with a healthy 9.6% unrestricted fund balance, or \$40.115 million as of December 31, 2004."
- Acknowledged that the Municipality's "management practices, including mid-year budget tracking, should allow for spending reductions in order to maintain reserve levels should they be necessary."

³ Moody's Investors Service credit report dated September 7, 2005

⁴ Standard & Poor's credit reports dated March 15, 2005 and September 1, 2005

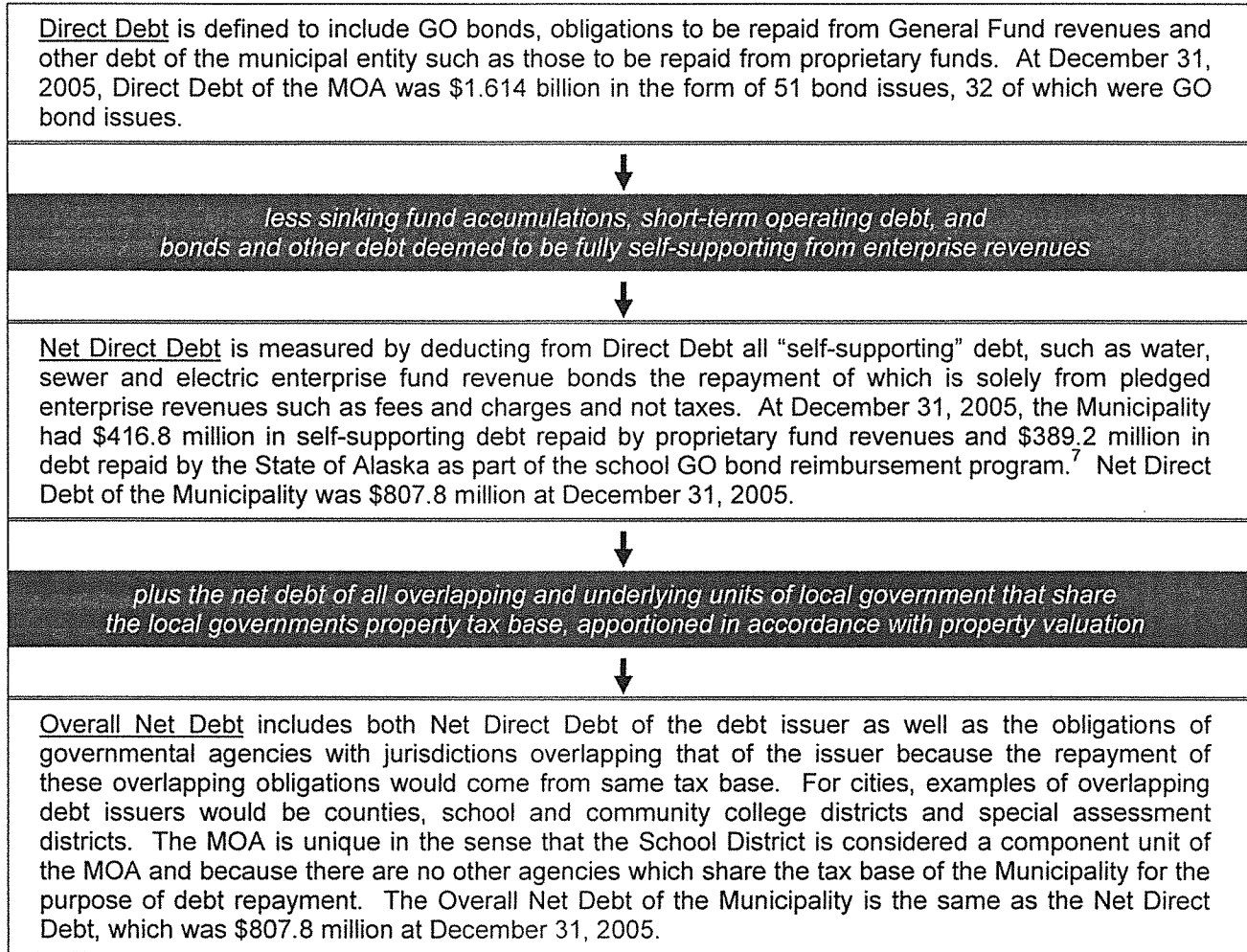
⁵ Moody's, op. cit.

⁶ S&P, op. cit.

III. CURRENT DEBT POSITION

Outstanding Bonded Indebtedness: The first step in the evaluation of debt capacity is to establish a base against which new issuances of debt will be measured. Municipal credit analysts track three descriptions, or measures, of outstanding indebtedness: Direct Debt, Net Direct Debt and Overall Net Debt. These three measurements are described in Figure 3 below.

Figure 3



⁷ The State Reimbursement Program: (1) reimburses municipalities that operate school districts for the costs of qualified and approved school construction, subject to annual appropriation; (2) applies to locally-issued GO bonds for qualified projects approved by the State Commissioner of Education and Early Development; and (3) varies reimbursement rates by bond issue based on authorization, issue and expenditure date, with school districts currently able to apply for reimbursement rates of 60% or 70% of debt service on qualified GO bonds. The reimbursement rates for the School District's outstanding bonds range from 0.0% to 66.8% and have an average reimbursement rate of 51.0%.

Using these measures of indebtedness, the outstanding debt of the Municipality as of December 31, 2005 is presented below in Figure 4. Credit ratings for the various debt obligations have been provided. Please note that not all of these obligations have been assigned ratings, and that many of these bond issues carry ratings of “Aaa/AAA” due to bond insurance policies provided by third party guarantors. More detail on the Municipality’s 51 outstanding debt issues is presented as *Exhibit One*.

Figure 4

Municipality of Anchorage Outstanding Debt as of December 31, 2005 (\$000s)							
	Direct Debt	less Self Supporting	less State Reim- bursement	Net Direct Debt	Moody's Investors Service	Standard & Poor's	Fitch Ratings
Municipality of Anchorage (1)							
GO Bonds	\$ 442,170	\$ 8,285	\$ -	\$ 433,885	Aa3	AA-	--
Certificates of Participation	3,360	3,360	-	-	--	--	--
Sub-Total	445,530	11,645	-	433,885			
School District GO Bonds (2)	763,060	-	389,161	373,899	Aa3	AA-	--
Water Utility							
Senior Lien (closed)	18,650	18,650	-	-	A1	AA-	--
Parity Lien	77,690	77,690	-	-	A2	AA-	AA-
Junior Lien	2,000	2,000	-	-	--	--	--
Sub-Total	98,340	98,340	-	-			
Waste Water Utility	27,270	27,270	-	-	A3	A+	AA-
Solid Waste Disposal Utility	1,325	1,325	-	-	--	--	--
Port of Anchorage	1,330	1,330	-	-	A2	--	--
Municipal Light & Power							
Senior Lien	192,260	192,260	-	-	A1	A+	A
Junior Lien	25,745	25,745	-	-	A2	A+	A
Sub-Total	218,005	218,005	-	-			
Correctional Facility	53,620	53,620	-	-	Aa3	AA-	A+
Performing Arts Center	5,255	5,255	-	-	--	A	A
TOTAL	\$ 1,613,735	\$ 416,790	\$ 389,161	\$ 807,784			

(1) A portion of MOA's GO bonds are expected to be repaid from proprietary fund revenues.

(2) The State of Alaska reimburses municipalities operating school districts for the costs of qualified and approved school construction, subject to annual appropriation.

Figure 5 below shows the split of Direct Debt into self-supporting debt, state reimbursed debt and Net Direct Debt, while Figure 6 separates Direct Debt by issuing entity and purpose. With all dollar figures in thousands, approximately 47 percent of the MOA's Direct Debt has been issued for capital improvements to schools, while 28 percent of the debt is for governmental use. Municipal Light & Power has the highest percentage of self-supporting debt at \$218.0 million, or 14 percent of total Direct Debt.

Figure 5

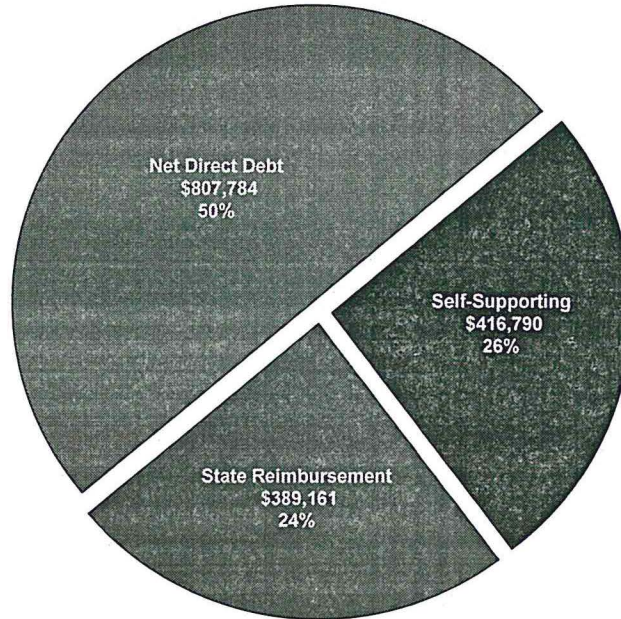
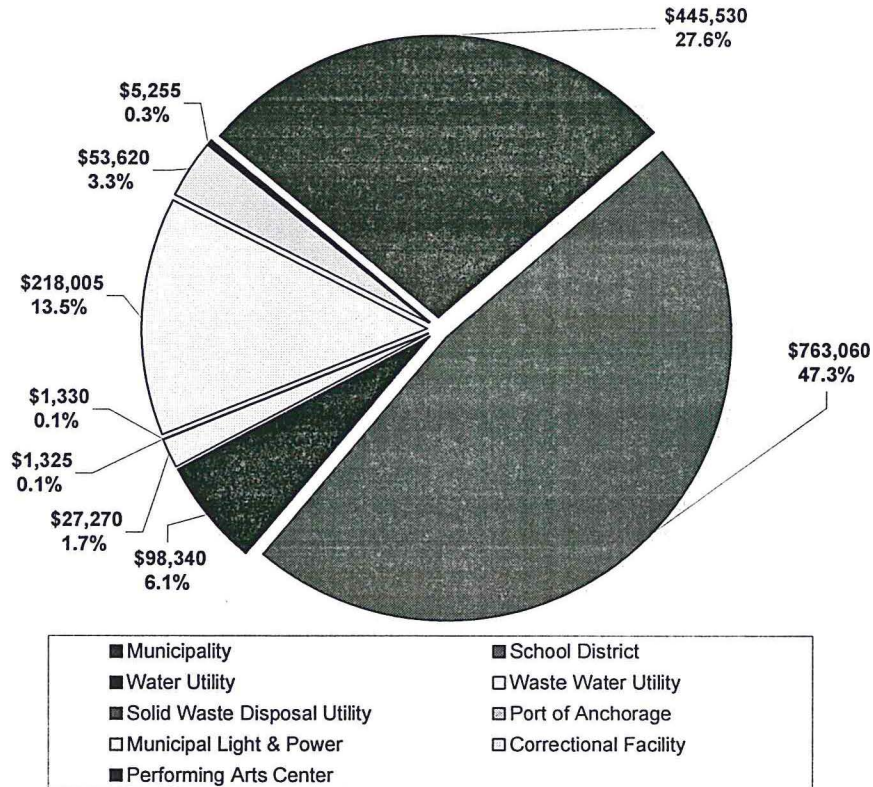


Figure 6



Debt service on the outstanding Net Direct Debt of the MOA (Figure 7) and the School District (Figure 8) are presented in the graphs below. Total debt service of \$615.0 million (\$433.9 million of principal and \$181.1 million of interest) will be paid on the Net Direct Debt of MOA between January 1, 2006 and December 31, 2025. For the School District, debt service on Net Direct Debt between July 1, 2005 and June 30, 2025 totals to \$552.5 million (\$386.6 million of principal and \$165.9 million of interest).

Figure 7

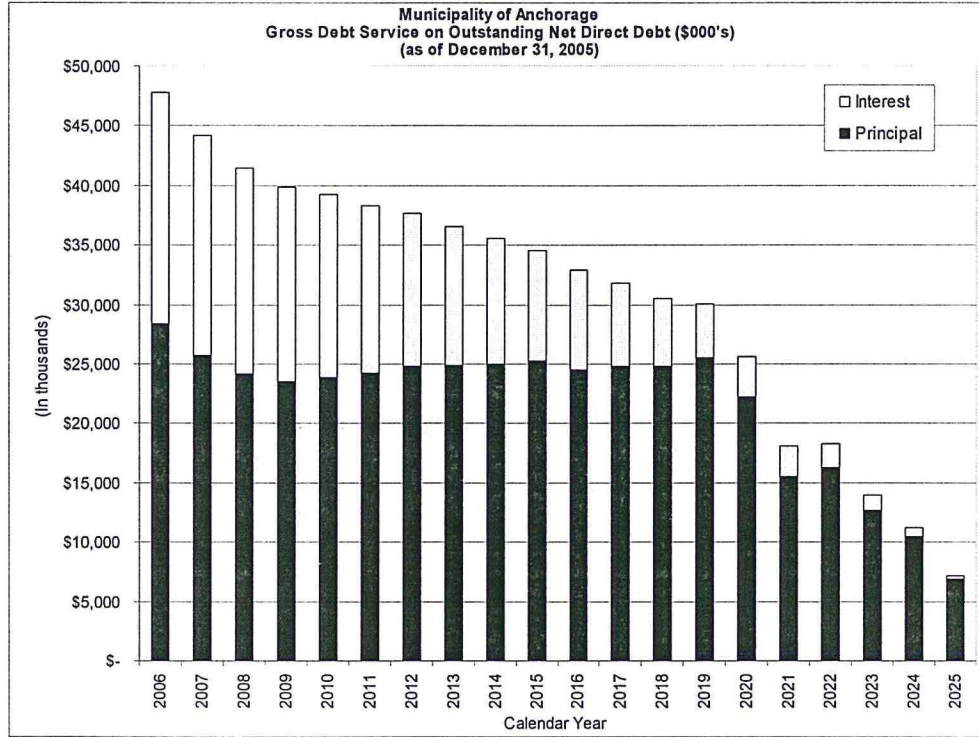
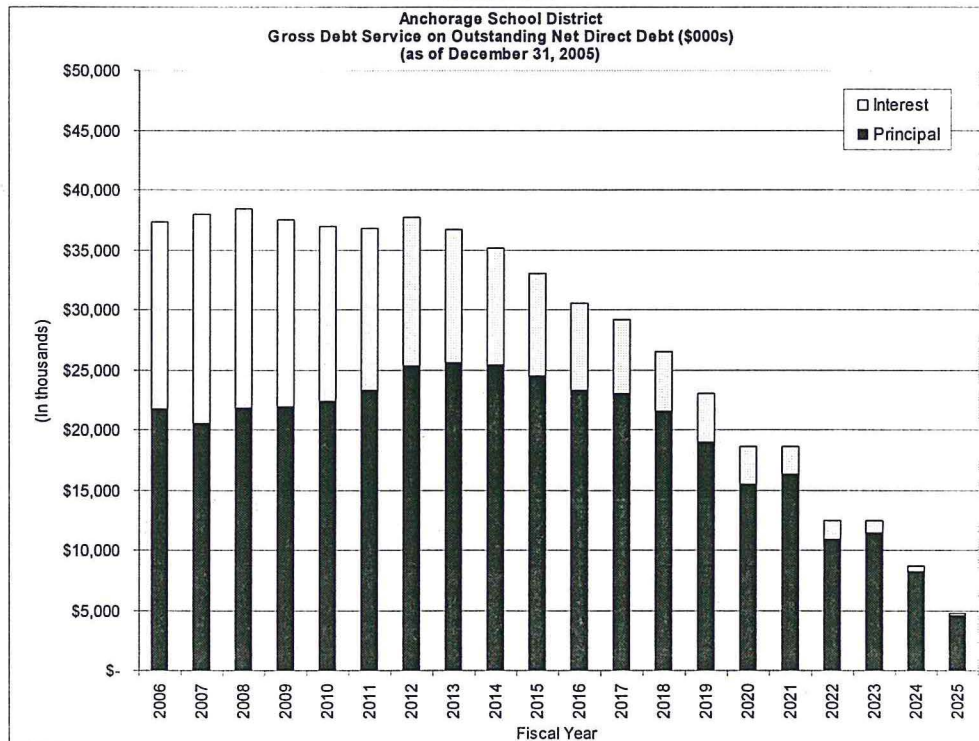


Figure 8



If the School District GO bonds scheduled for repayment by the State of Alaska are included, total debt service increases to \$1.162 billion (\$797.2 million of principal and \$365.2 million of interest) over this period.

The declining annual debt service payments exhibited are the result of the Municipality's conservative policy of amortizing principal over 20 years on each series of bonds issued. For both the MOA and the School District, approximately 34 percent and 66 percent of principal will be retired within the next five and ten years, respectively, which are above the 25 percent and 50 percent rules-of-thumb often cited by credit analysts. This relatively rapid repayment creates capacity for future issuances of GO bonds.

Calculation of Debt Ratios for Outstanding Debt/Comparison to Credit Medians: Regarding capital investment and debt levels, Standard & Poor's has stated "*The analysis of debt focuses on the nature of the pledged security, the debt repayment structure, the current debt-service burden, and the future capital needs of an issuer. Manageable debt levels are an important consideration, since accelerated debt issuance can overburden a municipality while low debt levels may indicate under-investment in capital facilities.*"⁸ In evaluating the ability of a bond issuer to repay existing and new obligations, municipal credit analysts calculate and compare an entity's current debt ratios with past figures and median levels of its peer ratings group. These ratios can have an impact on credit ratings, which in turn affect borrowing costs. However, the credit rating agencies are quick to point out that debt ratios are only one of several factors considered when assigning a rating, such that no direct correlation can be drawn between debt burden, as measured by debt ratios, and assigned credit ratings. With respect to application of their local government national medians, "*Performance relative to the guidelines is not an absolute indicator of credit quality, and a bond rating cannot be inferred within this narrow context. Each municipal credit is unique, and the consideration of numerous credit factors, each weighed separately, leads to the determination of a Moody's rating*" according to Moody's Investors Service.⁹

In the public finance arena, the debt ratios most commonly applied to cities are: (1) debt to full value and (2) debt per capita. Debt to full value, which measures outstanding indebtedness as a percent of full value, is a strong indicator of financial leverage as a GO bond issuer's ability to repay these obligations is measured against the size of the tax base. Debt per capita, which divides outstanding indebtedness by population, is a debt burden measure useful for comparing issuers with varying wealth levels since the demands for governmental services and facilities generally move in correlation with population.

Figure 9

Debt Ratios for Outstanding Bonded Indebtedness			
	Maximum for FY '01 - FY '05	For FY '06	Moody's and S&P Medians for "Aa/AA" Rated Cities and School Districts (8, 9)
Overall Net Debt to Full Value (%)	3.78%	3.07%	2.3% - 2.5%
Overall Net Debt per Capita (\$)	\$3,023	\$2,721	\$1,527 - \$1,931

Figure 9 above and Figure 10 on the next page present debt ratios calculated using the Overall Net Debt of the Municipality. These calculations indicate that current (for FY 2006) and recent debt ratios exceed the rating agency medians for "Aa/AA" rated bond issuers relative to full value and population, which could lead one to conclude that no amount of new GO debt would be considered affordable by the rating agencies. However, conversations with the credit analysts assigned to the Municipality

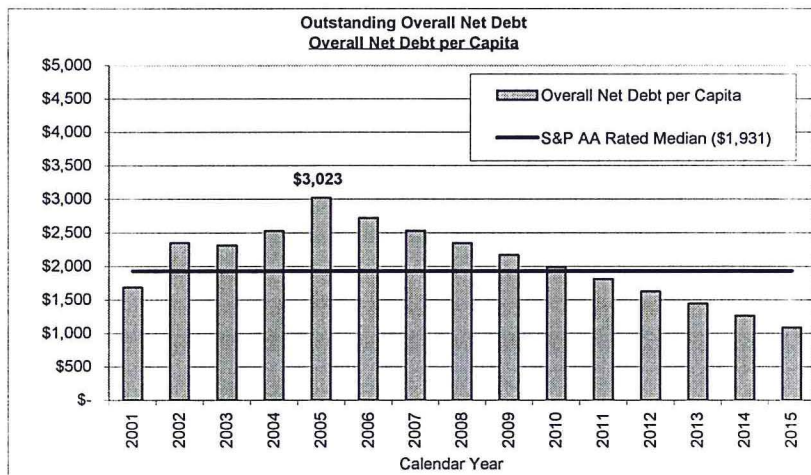
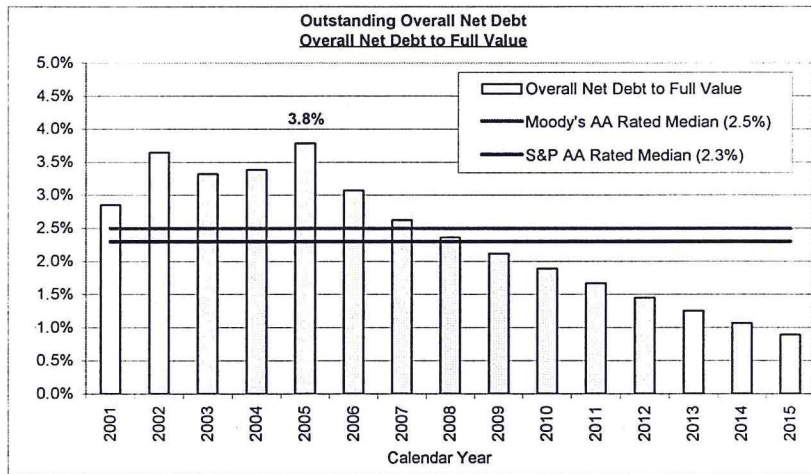
⁸ Standard and Poor's Public Finance Criteria 2005 and "Public Finance Criteria: Ratios and GO Credit Ratings" published April 23, 2003

⁹ Moody's Investors Service "2005 Local Government National Medians", November 2005

have confirmed that while MOA’s debt ratios exceed the norm for the rating category there are other mitigating, positive credit factors. These factors are: (1) the historically rapid retirement of debt; (2) sufficient reserve levels; (3) proactive financial management and policies; and (4) strength of the local economy. Moreover, the planned amortization of outstanding bonds will reduce debt ratios and create debt capacity over time even if the Municipality’s full value and population are unchanged from FY 2006 levels.

Figure 10

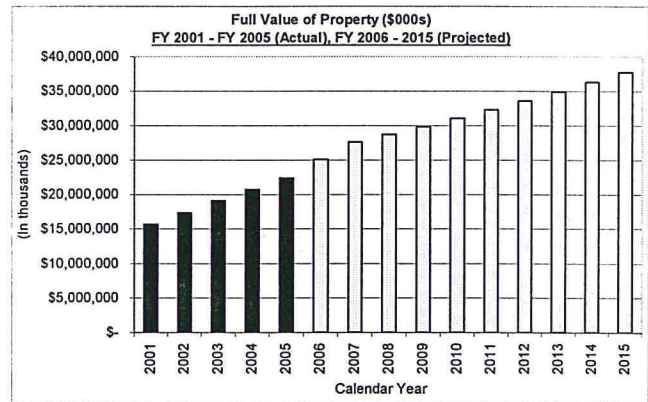
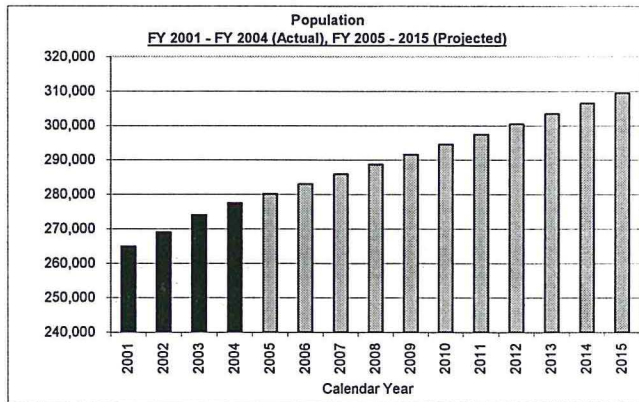
Outstanding Overall Net Debt Debt Ratios (as of December 31, 2005)			
CY for MOA FY for ASD	Overall Net Debt (\$000s)	Overall Net Debt to Full Value	Overall Net Debt per Capita
2001	\$ 446,586	2.9%	\$ 1,686
2002	631,928	3.6%	2,349
2003	633,492	3.3%	2,312
2004	701,026	3.4%	2,526
2005	847,378	3.8%	3,023
2006	770,270	3.1%	2,721
2007	723,990	2.6%	2,532
2008	677,984	2.4%	2,348
2009	632,516	2.1%	2,169
2010	586,261	1.9%	1,990
2011	538,676	1.7%	1,811
2012	488,541	1.5%	1,626
2013	438,056	1.3%	1,443
2014	387,643	1.1%	1,265
2015	337,895	0.9%	1,091



Assumptions Supporting Economic and Demographic Projections: The previously described ratios of debt to full value and debt per capita for the GO bonds outstanding at December 31, 2005 were prepared using the economic and demographic projections presented in Figure 11 below. Actual data for full values and population were incorporated for prior years, while projections were extracted from budget documents for 2005 – 2007 with the assistance of MOA Finance staff.^{10, 11} Population growth is expected to average 1.0 percent annually over the ten-year period, while full values are expected to grow by 4.0 percent per annum over the 2008 through 2015 time frame.

Figure 11

Municipality of Anchorage - Actual and Projected Economic and Demographic Data (\$000s) - Projections in Italicized Text				
Calendar Year	Full Value (10)	% Change	Population (11)	% Change
2001	\$ 15,664,818	--	264,937	--
2002	17,335,768	10.7%	269,070	1.6%
2003	19,079,921	10.1%	274,003	1.8%
2004	20,727,366	8.6%	277,498	1.3%
2005	22,404,489	8.1%	280,273	1.0%
2006	25,093,027	12.0%	283,076	1.0%
2007	27,602,330	10.0%	285,906	1.0%
2008	28,706,423	4.0%	288,766	1.0%
2009	29,854,680	4.0%	291,653	1.0%
2010	31,048,868	4.0%	294,570	1.0%
2011	32,290,822	4.0%	297,515	1.0%
2012	33,582,455	4.0%	300,491	1.0%
2013	34,925,753	4.0%	303,495	1.0%
2014	36,322,783	4.0%	306,530	1.0%
2015	37,775,695	4.0%	309,596	1.0%



If assessed values and population levels realized in the future are below the levels used herein to compute the projected debt to full value and debt per capita ratios, then the debt affordability estimates generated from these debt ratios will be overstated. It should be noted that because the projected amount of additional GO bond debt will not be issued all at one time but rather incrementally, these debt levels can be adjusted as time passes to reflect changing economic and financial conditions.

¹⁰ Full value is represented by assessed value. Actuals from ASD audited financial statements. 2006 - 2007 growth rates projected by MOA staff. 2008 - 2015 figures projected with 4.00% annual increases.

¹¹ Actuals from ASD audited financial statements. 2005 - 2015 figures projected with 1.00% growth rate.

IV. AFFORDABLE LEVEL OF ADDITIONAL GENERAL OBLIGATION DEBT

For the Municipality to maintain its bond ratings and promote the market's acceptance of additional borrowings, credit rating agencies and investors will need assurances that the resources necessary to ensure timely payment of all existing and future debt obligations are present. In order to issue additional debt, the Municipality must have the resources to cover all debt service payments without depleting funds necessary for critical operations and services.

Using the debt to full value ratio, the affordable level of additional debt is a direct function of the speed in which outstanding debt is retired, lower borrowing rates, an expanding property tax base and the reimbursement rate of School District GO debt service by the State of Alaska. Similarly, debt affordability measured using the ratio of debt per capita would be augmented by a growing population.

Maximum Debt Ratios Used to Measure Affordability of Additional GO Bonds: While the Municipality's debt ratios are above the rating agency medians for bond issuers rated "Aa/AA", the capacity to issue additional GO bond debt is present. There are not discrete debt ratios that, if exceeded, would result in an immediate downgrade for the MOA from its current "Aa/AA" level. Conversations with the credit analysts assigned to the Municipality have confirmed that while MOA's debt ratios exceed the norm for the rating category, the Municipality's historically rapid retirement of debt, sufficient reserve levels, proactive financial management and policies, as well as the strength of the local economy, all serve as mitigating credit factors.

Figure 12 below presents the suggested maximum debt ratios for estimating the Municipality's capacity for issuing additional GO debt while maintaining current "Aa/AA" credit ratings. These prescribed levels take into consideration the rating agency medians and the FY 2006 debt ratios incorporating debt outstanding as of December 31, 2005. *Exhibit Three* shows the credit rating agencies' median debt ratios for GO bond issuers in the "A/A", "Aa/AA" and "Aaa/AAA" rating categories.

Figure 12

Maximum Debt Ratios for Debt Capacity Analysis (Base Case Scenario)			
	FY 2006 Levels	Moody's and S&P Medians for "Aa/AA" Rated Cities	Suggested Maximums
Overall Net Debt to Full Value (%)	3.07%	2.3% - 2.5%	4.00%
Overall Net Debt per Capita (\$)	\$2,721	\$1,527 - \$1,931	\$4,600

* Key assumptions include maintenance of current "Aa/AA" GO bond credit ratings and State reimbursement of ASD debt service at current rates for outstanding bonds but at a 0% rate for projected GO bonds.

Debt to Full Value

In terms of Overall Net Debt to Full Value, the suggested maximum of 4.00 percent exceeds the FY 2006 level of 3.07 percent and the credit medians of 2.3 percent to 2.5 percent. This 4.00 percent maximum for Overall Net Debt does not seem quite above the norm for the Municipality when considered relative to the 3.78 percent figure for FY 2005, which is the 'high-water mark' for the last five years.

Debt per Capita

In a similar fashion, the suggested maximums for Overall Net Debt per Capita is \$4,600. The "Aa/AA" credit medians range from \$1,527-\$1,931 for Overall Net Debt per Capita. These are below the current level of \$2,721. In FY 2005, Overall Net Debt per Capita was \$3,023.

Debt Affordability Analysis – Base Case Scenario: The amount of additional GO debt deemed to be affordable at the “Aa/AA” credit rating level is calculated using the maximum debt ratios described above – 4.00 percent for Overall Net Debt to Full Value and \$4,600 for Overall Net Debt per Capita.

In addition to the projections of full value and population through 2015, our Base Case debt affordability estimate incorporates certain assumptions regarding borrowing cost (5.50 percent), term of repayment (20 years; consistent with relatively rapid retirement of principal), debt service structure (equal amounts per year) and the State of Alaska’s reimbursement rates for ASD debt service (current average reimbursement rate of 51.9 percent for outstanding bonds and 0.0 percent reimbursement rate for projected GO bonds). Please see *Exhibit Three* for more details regarding these assumptions.

With biannual issuances of GO debt over the FY 2006 through FY 2015 period, the base case estimate of debt capacity is \$1.175 billion. As is presented in the Figure 13, this \$1.175 billion total is not all immediately available for issuance, but rather incrementally over time based on the growth rates assumed for the property tax base and population. In FY 2006, the affordable level of new debt is projected to be \$235 million. Figure 15 on the next page presents the key debt ratios by combining the GO debt levels projected under the Base Case Scenario with outstanding GO debt.

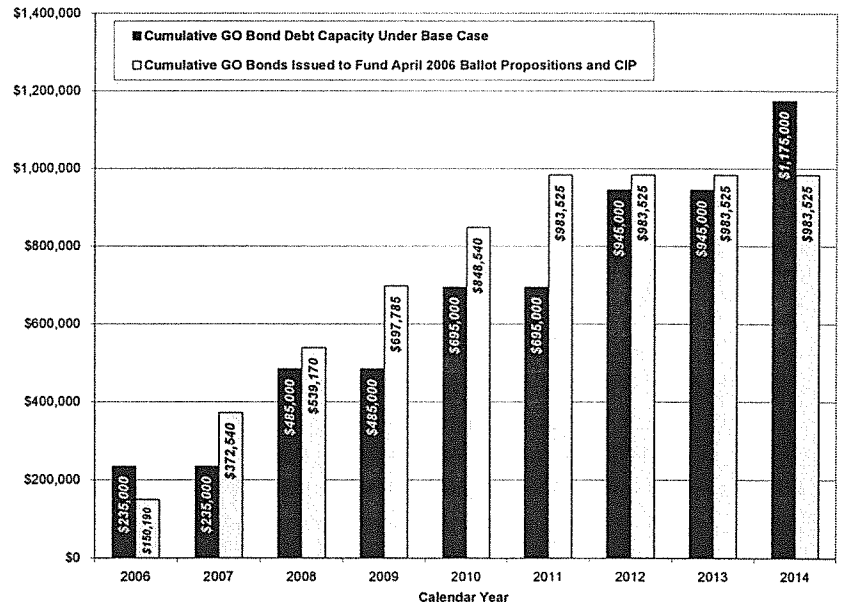
Figure 13

Base Case Capacity for Additional General Obligation Debt (\$000s) *					
FY 2006 - FY 2015	FY 2006	FY 2008	FY 2010	FY 2012	FY 2014
\$1,175,000	\$235,000	\$250,000	\$210,000	\$250,000	\$230,000

* Key assumptions include maintenance of current "Aa/AA" GO bond credit ratings and State reimbursement of ASD debt service at current rates for outstanding bonds and 0% rate for projected GO bonds.

This debt capacity estimate for FY 2006 exceeds the \$164.805 million in GO bonds presented to the voters with the April 2006 ballot propositions (\$64.940 million for the Municipality and \$99.865 million for the School District of which \$41.7 million, 42 percent, is expected to be reimbursed by the State of Alaska) of which \$150.190 million was expected to be issued in FY 2006.¹² The amount of GO bonds anticipated to be issued to fund these propositions and the CIP is \$983.525 through FY 2011. This amount is less than the \$1.175 billion is calculated GO debt capacity through FY 2015; however, the timing of the bond issuances for the CIP are such that the suggested maximum debt ratios would be exceeded from FY 2007 through FY 2013 (see Figure 14)

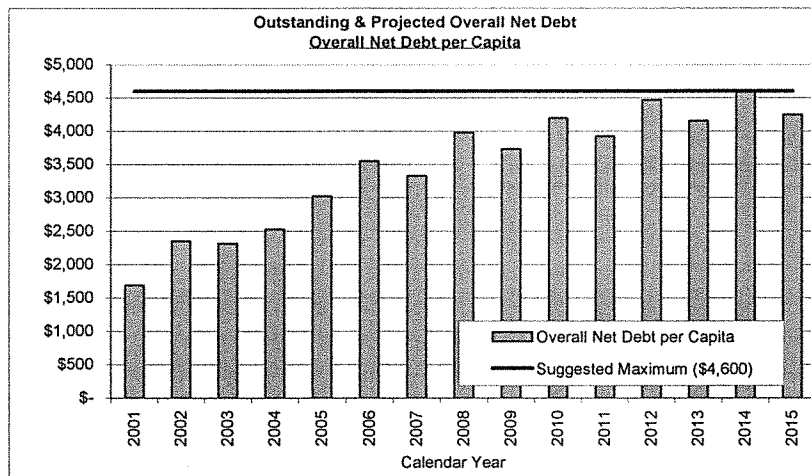
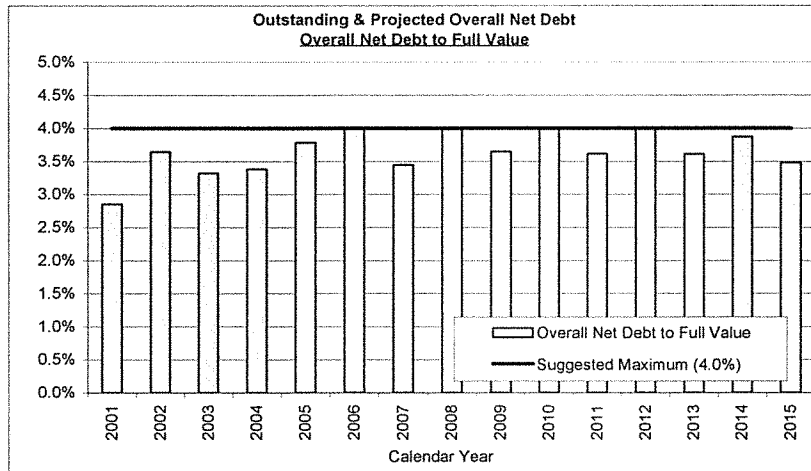
Figure 14



¹² Of the \$164.805 million in GO bonds put to the voters in April 2006, only \$46.110 million were approved.

Figure 15

Outstanding & Projected Overall Net Debt Debt Ratios (as of December 31, 2005)			
CY for MOA FY for ASD	Overall Net Debt (\$000s)	Overall Net Debt to Full Value	Overall Net Debt per Capita
2001	\$ 446,586	2.9%	\$ 1,686
2002	631,928	3.6%	2,349
2003	633,492	3.3%	2,312
2004	701,026	3.4%	2,526
2005	847,378	3.8%	3,023
2006	1,005,270	4.0%	3,551
2007	952,250	3.4%	3,331
2008	1,149,134	4.0%	3,979
2009	1,088,996	3.6%	3,734
2010	1,237,261	4.0%	4,200
2011	1,167,321	3.6%	3,924
2012	1,343,601	4.0%	4,471
2013	1,261,061	3.6%	4,155
2014	1,406,838	3.9%	4,590
2015	1,314,825	3.5%	4,247



Debt Affordability Analysis – Additional Scenarios Considered: The base case estimate of debt affordability at the “Aa/AA” credit rating level has been modified through changes to key assumptions, and the impacts to debt capacity have been quantified. Please see Figure 16 below for these four sensitivity analyses.

Figure 16

Sensitivity Analyses to Base Case Capacity for Additional General Obligation Debt (\$000s)					
	Base Case	Scenario #1	Scenario #2	Scenario #3	Scenario #4
Changes to Base Case Assumptions: >>		Reimbursement Rates of New ASD Debt Service Increased from 0% to 50%	Borrowing Cost Increased from 5.5% to 6.0%	Repayment Term Increased from 20 years to 25 years	Growth Rates of Full Value & Population Reduced by 50%
FY 2006	\$235,000	\$370,000	\$235,000	\$235,000	\$180,000
FY 2008	250,000	375,000	250,000	245,000	175,000
FY 2010	210,000	325,000	210,000	205,000	155,000
FY 2012	250,000	365,000	250,000	235,000	170,000
FY 2014	230,000	350,000	230,000	205,000	195,000
Total	\$1,175,000	\$1,785,000	\$1,175,000	\$1,125,000	\$875,000

While the Municipality and the School District are one obligor in the eyes of bondholders, and therefore share the same credit ratings, the affordability of new GO debt issued by the Municipality is directly tied to the amount of School District debt service reimbursed by the State of Alaska since approximately 50 percent of the debt service on outstanding School District is not considered Net Direct Debt of the Municipality. With Scenario #1, the reimbursement rate of debt service due on new issuances of GO bonds was adjusted upwards from our base case assumption of 0% to 50%, with the result being an increase in debt capacity from \$1.175 billion to \$1.785 billion.

With Scenario #2, the assumed borrowing cost of 5.50 percent was increased to 6.00 percent to measure the change in tax-exempt interest rates on debt capacity. This modification has no impact on debt affordability since the ratios of debt to full value and debt per capita are based on outstanding principal and not debt service which includes interest costs. Extending the term of repayment from 20 to 25 years (Scenario #3) has a slight impact on debt capacity since the slower amortization of principal and resultant higher total interest cost reduces debt capacity in later years. As is shown by Scenario #4, adjusting downward the assumed growth rates of full value and population causes a measurable reduction in debt capacity from \$1.175 billion to \$875.0 million due to the direct relationship between these two variables and the debt ratios employed.

V. REVIEW OF DEBT FINANCING INSTRUMENTS

With a wide variety of debt financing instruments, the Municipality can tailor the issuance of debt to best match the purpose, repayment source and useful life of the funded capital project. Debt financing instruments differ by issuing entity, procedural requirements, pledged revenue, term of repayment and interest cost. By considering the costs and risks of these various debt features, the Municipality can issue and manage its debt in a meaningful, portfolio approach with optimum results. The following pages provide a review of the various types of debt financing instruments utilized by issuers like the Municipality, organized by short and long terms of repayment.

Short-Term and Interim Financing Instruments: Short-term obligations (those due in one to three years) may be issued in anticipation of receipt of particular revenues like taxes or grants, with such revenues pledged for repayment of the debt issuance. Most types of short-term obligations can be issued quicker than long-term obligations and thus can be used in situations where funds are needed before a long-term financing instrument can be approved and arranged. Short-term debt may also be issued on an interim basis to finance projects or portions of projects for which the Municipality ultimately intends to issue long-term debt when long-term interest rates are more favorable. Short-term and interim obligations include:

Lines of Credit

The Municipality may establish a tax-exempt line of credit with a financial institution or other provider. The line of credit would be utilized when the need for financing is so urgent that time does not permit the issuance of long-term debt, or when the funding need is too large to be covered from current revenues yet too small to justify the issuance costs of publicly offered debt.

Pooled Financings

If it is financially or strategically beneficial, the Municipality may participate in debt pools operated by state agencies or organizations, taking low-interest loans to be repaid on a short- or long-term basis.

Interfund Borrowings

Interfund borrowing, short-term cash lending between funds, may be considered if it is in the Municipality's best interests to do so as determined by the Chief Financial Officer.

Internal Financing

Should the Municipality desire to issue bonds for large capital projects, upon Assembly passage of an intent-to-issue resolution, non-restricted reserve funds can serve as interim financing for project costs to be later reimbursed with bond proceeds. This type of financing would be reviewed by bond counsel to ensure the Municipality is in compliance with applicable federal tax rules.

Tax Anticipation Notes/Revenue Anticipation Notes/Grant Anticipation Notes

The proceeds of tax anticipation notes (TANs) and revenue anticipation notes (RANs) are not used to fund capital projects but rather to better manage the seasonal operating cash flow requirements of general government or enterprise operations, respectively. Anticipated taxes or revenues are pledged for repayment of the notes and fixed interest thereon. The repayment term is typically twelve (12) months, with the possibility of extending an additional six (6) months if tax receipts are not received. Grant Anticipation Notes (GANs) are sold to finance capital projects the costs of which are expected to be reimbursed from state and federal grants. Upon receipt, grant funds are used to pay debt service on the GANs.

Commercial Paper

Commercial paper (CP) is a short-term obligation (maturities range from 1 to 270 days) providing incremental and interim funding for capital projects through periodic issuance at variable rates. Most

commonly utilized by enterprise funds, CP is typically repaid with the proceeds of long-term revenue bonds or cash when a project is placed in service.

Long-Term Debt Instruments: While short-term and interim financing instruments are appropriate for certain needs, many capital expenditures require a longer term of repayment, typically ranging from 10 to 30 years. Long-term debt should be used to finance essential capital facilities, projects and certain equipment where it is cost effective and fiscally prudent. The scope, requirements, and demands of the Municipality's Biennial Budget or Capital Improvement Program (CIP), and the ability or need to expedite or maintain the programmed schedule of approved capital projects will also be factors in the decision to issue long-term debt.

Figure 17 on the following page presents a summary comparison of the long-term debt instruments employed by bond issuers at the local level, while the accompanying text provides a more in-depth review of their features. Most of these obligations are legally available for issuance in the State of Alaska by the Municipality, while certain others would require legislative approval at the state and/or local level.

General Obligation Bonds

Description and Purpose – General obligation (GO) bonds are debt instruments used to finance capital improvements such as roads, schools, public buildings, parks, etc. which benefit the general population.

Procedural Requirements – The Assembly must approve an ordinance which contains a description of the projects to be funded with bond proceeds, the terms for repayment for the bonds and the ballot proposition language. The authorization to issue GO bonds for new projects (refundings excluded) comes from Assembly action and majority voter approval at an election.¹³

GO bonds may be issued to fund service area improvements such as roads, with taxes levied in the service area for payment of debt service. The project may be approved only by voters in the service area, or by voters in the service area and all voters in the Municipality. A vote of all taxpayers is required to pledge the full faith and credit of the Municipality to repayment of the bonds. This pledge typically secures a lower borrowing cost (interest rate) on the GO bonds while debt service is paid by property owners in the service area.¹⁴

Repayment Pledge – GO bonds are secured by the full faith, credit and unlimited taxing power of the Municipality.

Borrowing Cost & Flow of Funds – The cost of issuing GO bonds is generally one of the lowest of all long-term financing mechanisms due to the unlimited tax pledge. Bond proceeds are used for voter approved capital projects. Property tax receipts collected by the Municipality, without limitation as to rate or amount, are transferred to a paying agent for payment of debt service on the GO bonds.

¹³ Authorization for issuing general obligation bonds is provided through the Alaska Statutes (AS 29.47.180-200) and Municipal Charter (Article XV. Municipal Borrowing Section 15.01-15.05) and Municipal Code (6.20.20 – 6.20.060)

¹⁴ Authorization for service area debt is granted to the Municipality through Alaska Statute 29.47.450.

Figure 17

Summary Comparison of Long-Term Debt Instruments										
	General Obligation Bonds	Lease Revenue Bonds & COPs	Revenue Bonds	Special Assessment District Bonds	Special Tax Bonds	Pension Obligation Bonds	Non-Recourse Private Activity Bonds	63/20 Financing (Non-Profit Issuer)	GARVEE Bonds	Asset Securitization Bonds
Description and Purpose	Projects for general public use i.e., roads, schools, public buildings, etc.	Forms of lease-purchase financing. Voter approval generally not required.	Generally, enterprise facilities, i.e. water, sewer and electric systems, ports, redev., etc.	Streets, roads, sidewalks, lighting, etc. Cost apportioned throughout district based on benefits.	Infrastructure, improvements, and services. Cost apportionment not based on benefits to property owners. Not yet authorized for use in AK.	Financing for all or part of unfunded pension liability. Not yet authorized for use in AK.	Issuance of tax exempt securities by conduit issuer to finance certain projects of non-profit or for profit borrowers.	Tax exempt debt issued by non-profit borrower, often for the benefit of governmental agency.	Interim funding source for transportation-related projects expecting grant reimbursement.	Trust purchases existing or anticipated assets of agency with bonds. Interests in pooled assets are sold to investors.
Procedural Requirements	Assembly approval of ordinance and majority voter approval.	Assembly approval. Annual appropriation of lease payments.	Assembly approval of ordinance.	Approval of assessment and term by owners bearing 50% of cost or Assembly. Assessment approved and levied.	Maximum tax and debt approved by 2/3 of qualified voters or landowners. Legislative approval, taxes levied, indebtedness approved.	Assembly approval. Proceeds are invested in the pension system to offset unfunded liability.	Assembly approval of ordinance; reimbursement resolution by third party; TEFRA hearing.	Authorizing ordinance and resolutions by Assembly and non-profit. Resolution accepting completed project.	Assembly approval following execution of grant agreement with federal and state agencies.	Assembly approval of sale or transfer of assets to trust.
Repayment Pledge	Full faith, credit and unlimited taxing power.	Lessor's right to receive payments under the lease.	Generally net revenues of the issuer.	Limited pledge of assessments.	Limited pledge of special taxes.	Typically, unconditional obligation of issuer, payable from the general fund.	Borrowers pledge general revenues, project revenues or assets.	Generally cash flow from the project but can be a variety of sources.	Expected grant funds are primary security; other revenues typically also pledged.	Asset pool is pledged for payment of debt service. Non-recourse to agency.
Borrowing Cost & Flow of Funds	Low cost of funds. Property taxes are used to pay debt service.	Moderate cost of funds. Lease payments pass from lessor to bondholders.	Cost of funds varies; tied to strength of revenue pledge.	Moderate to high cost of funds; tied to quality of assessments. Assessments generally due with property taxes.	High cost of funds due to undeveloped nature of property. Special taxes due with property taxes.	High cost of funds because bond interest is taxable. Debt service payments appropriated from general fund.	Cost of funds varies; tied to strength of revenue pledge.	Cost of funds may be higher than from revenue bonds. Revenues from facility or another source pay debt service.	Cost of funds varies; tied to likelihood of grant appropriation and strength of secondary revenue pledge.	Generally high cost due to complexity of transaction. Receivables collected on assets pay debt service.

Financing Lease Obligations (Lease Revenue Bonds and Certificates of Participation)

Description and Purpose – The issuance of financing lease obligations are a routine alternative to issuing GO bonds to finance capital assets over a multi-year period. Lease obligations can be short-term or long-term in nature depending on the need but may not exceed the useful life of the leased assets. Generally speaking, because payments due under a financing lease are subject to annual appropriation if the lessee has use of the leased asset, the lease obligation is not considered debt and does not require voter approval (see Procedural Requirements below). Therefore, financing leases serve as an expedient and flexible financing method for projects such as public buildings, parking structures, correctional facilities and technology upgrades. These instruments should be considered where lease financing will be more beneficial, either economically or from a policy perspective.

Lease Revenue Bonds are a variant of revenue bonds where the revenue stream backing the bond is created from lease payments made by the occupying entity to the governmental financing entity which issues the bonds, constructs the facility, and retains title to the facility until the debt is retired. Certificates of participation (COPs) are similar to lease revenue bonds in that lease payments made by the governmental entity are used to repay the COPs; however, COPs are tax-exempt securities issued by a trustee, not by a financing corporation, whereby the lease payments are “certificated out” to investors.

Procedural Requirements – A local ordinance that details the parties in the lease arrangement, project description, cost, method of sale, payment of debt service, etc. must be approved by the Assembly. Staff would also evaluate the useful life of the capital equipment or infrastructure, the terms and conditions of the lease, and the direct impact on debt capacity and budget flexibility prior to the implementation of a lease program. Voter approval is not required for leases under \$1 million.¹⁵

Repayment Pledge – Lease obligations are secured by the lessor’s right to receive payments under the lease. The Assembly appropriates the amount required to fulfill the lease payments on an annual basis; these can be backed by additional voter approved revenues. Lease payments are commonly paid out of the General Fund. Although financing leases are not legally considered debt, they “are considered obligations of the issuer and are fully reflected in the debt statement and ratios. As a result, failure to make an appropriation will result in a down-grade of both the appropriation-backed obligation and the general obligation of the entity.”¹⁶

Borrowing Cost & Flow of Funds – The borrowing cost is usually moderate and reflects the credit rating of the General Fund. Lease payments flow from the lessee to the lessor as outlined in the lease-purchase agreement, incrementally reducing the purchase price to zero over time. Investors receive lease payments payable by the lessee through a pledge of the lessor’s leasehold interest.

¹⁵ A lease purchase agreement with respect to acquisition of a capital improvement valued in excess of \$1 million must be approved by a majority of the qualified voters voting on the question (Municipal Charter 13.08 (b)).

¹⁶ Standard and Poor’s Public Finance Criteria 2005

Revenue Bonds

Description and Purpose – Revenue bonds are long-term debt obligations issued by governmental enterprises to finance capital improvements which are expected to generate an independent revenue stream. As described below, revenue bonds are generally issued to pay for capital improvements to facilities such as water, sewer and electric systems, tax increment districts and ports.

Water, Wastewater, Electric, Solid Waste, and Port Revenue Bonds

The Municipality has issued revenue bonds to fund the capital needs of its business type units, such as Municipal Light and Power (ML&P), Port of Anchorage, and Anchorage Water and Wastewater Utility (AWWU). Revenue bonds issued by these entities are limited obligations payable solely from and secured by the net revenues generated by their operations.

Housing Bonds

Housing bond are issued to finance the purchase of residential mortgage loans. Payment of debt service on these bonds is restricted to the principal and interest received from the mortgages or from other amounts pledged by the Municipality, except tax revenues.¹⁷

Parking Revenue Bonds

Parking revenue bonds are often issued to finance the construction of parking facilities, with the revenue stream of parking fees pledged to payment of debt service on the bonds. Lease options, another alternative, are employed for several existing municipal parking areas and parking has been incorporated into project development throughout Anchorage. If parking bonds are issued, fees may be collected by the Anchorage Parking Authority for payment of debt service on the bonds.

Sales Tax Revenue Bonds

Sales tax revenue bonds are typically used by local governments to finance public projects. If sales tax bonds are issued, sales tax receipts would provide a dedicated source of payment for debt service on the bonds. Actual debt service coverage levels of sales tax revenue bonds range from 1.10x – 3.0x, with most coverage levels and additional bonds tests ranging from 1.25x to 1.50x.¹⁸ Additionally, sales tax bonds often do not need voter approval. At this time, Anchorage does not have a sales tax. A proposition for a 3.0% sales tax was on the April 4, 2006 ballot, but it was not approved by 60% of the voters.

Tax Increment Bonds

Tax increment financing (TIF) allows the local governing body or redevelopment agency to designate a blighted area as a TIF district, set the base property valuation at that point in time, and then earmark any incremental growth in property tax revenues in that district to pay for anticipated infrastructure improvements. Tax increment bonds are issued to upfront fund these improvements, with repayment expected to come from the incremental property tax revenues.¹⁹ Standard and Poor's "*prefers to examine at least four years of project area assessed values*" when evaluating the creditworthiness of tax increment bonds.¹⁷ Compared to other forms of special district debt, TIF bonds have favorable aspects. Unlike special assessment and special tax bonds, no additional tax burden is created for taxpayers, and tax collection rates are generally less of a concern, unless project area tax payments are concentrated in a few taxpayers. Additionally, while undeveloped land can be a credit concern for other financing mechanisms, undeveloped land in a tax increment district is generally a favorable factor since revenues will increase to the extent new development occurs and taxable property values grow. The credit risks of TIF bonds include volatility in property values, widespread tax appeals, construction risk and taxpayer concentration.

¹⁷ At this time, the Municipality does not issue housing development and mortgage revenue bonds. Within the Municipality, Alaska Housing Finance Corporation (AHFC) provides state debt issuance for housing. The payment of debt service on the issues is secured by the projects or mortgage payments and is not debt incurred by the Municipality. Authorization for the Municipality to issue housing revenue bonds is defined under AS 29.47.240 (b).

¹⁸ Tax Secured Debt, Standard and Poor's Public Finance Criteria 2005

¹⁹ At this time, a TIF district hasn't been implemented within the Municipality, but the financing structure has been considered. TIF districts are authorized under the Alaska Statutes at AS 29.47.460 (b).

Procedural Requirements – The structure of revenue bonds is more complex than a general obligation bond. Along with Assembly approval through an ordinance or resolution detailing the purpose, amount, and terms of indebtedness, revenue bonds have a primary legal document (indenture or master resolution) which defines all aspects of the issuer's agreement with bondholders. One legal provision in this document, the rate covenant, is an important credit factor which defines that rates must be set by the enterprise in amounts sufficient for pledged revenues to fund operating and maintenance expenses (net revenues) and cover debt service by a specified margin. Rate covenants of 1.10-1.25 times are typical, offering bondholders a safety margin of 10-25%. Another common legal provision afforded to owners of revenue bonds is the additional bonds test (ABT). The ABT specifies the minimum debt service coverage level of existing and proposed bonds margin by the issuer's historical or proposed net revenues.²⁰

Repayment Pledge – Revenue bonds are expected to be repaid from the net revenues of the enterprise. In addition, a debt service reserve fund is generally funded from bond proceeds and available to cover shortfalls of net revenues in the payment of debt service.

Borrowing Cost & Flow of Funds – For revenue bonds, the borrowing cost depends on the credit ratings assigned to the bonds, and the median revenue bond rating of municipal utilities is "A". Revenues of the enterprise are applied first to the payment of operating and maintenance expenses and then to the payment of debt service on bonds. The issuer is often required to make monthly deposits to a debt service fund held by the paying agent for the benefit of bondholders. Revenue bonds may be issued with senior, subordinate or junior repayment liens.

Special Assessment District Bonds

Description and Purpose – Special assessment district bonds are issued to provide financing for construction and maintenance improvements such as street landscaping, street lighting, traffic signals, streets, sewers, gas lines, sidewalks, and parks and recreation.²¹

Procedural Requirements – Property owners can initiate these proceedings via a petition within the boundaries of the proposed assessment district, or the Assembly can begin the proceedings. If initiated via petition, approval by owners bearing 50% of the cost is required. Upon receipt of the petition, the Mayor must report to the Assembly on the necessity for the proposed service. Either way, the districts are formed through a process that usually involves mailing notices to all affected property owners, holding public meetings and hearings conducted by the Assembly, and consideration of the percentage of those in opposition to the district.

Project costs are assessed within the boundaries of the designated benefit area of the Municipality. The overall cost of the project is weighed against the individual properties within the benefit area to determine the benefit each area or each parcel will receive from the public improvements, with an intent to match costs with benefits received.

With this financing tool, a property owner can either pay the assessment amount in cash or allow a lien to be placed on their property in the amount of the benefit assessment. Annual benefit assessments received over the term of the special assessment bonds are used to pay debt service and often certain operating costs. Since these are tax-exempt bonds and payable over a period of many years, financing the lien with special assessment bonds is usually advantageous for property owners.

²⁰ Authorization for the Municipality to issue revenue bonds is outlined in the Municipal Charter (Section 15.01) and in the Alaska Statutes (AS 29.47.240-250). Likewise, Alaska Statute 29.47.300 provides authorization for refunding of all or part of the outstanding revenue bonds.

²¹ Authorization for special assessment district indebtedness can be found in Alaska Statute 29.47.440 and in the Municipal Code at 19.10-19.90.

Repayment Pledge – Assessments levied and collected from taxpayers in the district provide security for repayment of the bonds. Total annual assessment and term of levy are approved by the voters. The cost within the district is proportionate to the benefit received from and the burden imposed upon the improvement service area.

Borrowing Cost & Flow of Funds – The borrowing cost of special assessment bonds are usually moderate to high, reflecting a limited assessment pledge and the size and diversity of the district. Debt service coverage of 1.20x or better will reduce the cost of funds. Annual assessments are collected by the Municipality with property tax collections and provided to the paying agent for payment of debt service.

Special Tax (Community Facilities District) Bonds

There is currently no statutory or local authority for the issuance of community facilities district bonds in Alaska. This debt instrument is provided for informational purposes only.²²

Description and Purpose – Community facilities district (CFD) bonds are issued to finance a wider range of public improvements and facilities than do assessment district bonds. Projects may include the purchase, construction, expansion or rehabilitation of facilities the local government is authorized to construct, own or operate. Community facilities districts can even be used to fund private improvements in some cases, such as when seismic, fire safety, or hazardous waste standards must be met. Also, funds can be used for police and fire protection, ambulances, recreation, library services, parkways, maintenance, flood control and storm drain maintenance.

Procedural Requirements – Generally, formation of a community facilities district requires a public hearing and a favorable two-thirds (2/3) vote of the registered voters who live within the proposed district. However, these districts are most often used by developers who are single owners of large sites that require a substantial investment in infrastructure. After the district is formed, the local governing body typically is required to hold an annual public hearing to authorize the special tax to be levied on the properties. This type of hearing is not required for assessment districts. Special taxes are not required to be levied in proportion to the benefit although it is often the case.

Repayment Pledge – Total annual maximum tax and maximum amount of bonds are approved by the voters. Community facilities bonds differ from special assessment bonds in that they usually have the ability to raise the tax rate up to a maximum level to cover taxpayer delinquencies.

Borrowing Cost & Flow of Funds – Due to the often undeveloped nature of property in the CFD, borrowing costs of CFD bonds are high. CFD bonds typically are sold with a value to lien ratio of no less than 3:1 to reduce the cost of funds. The special taxes are collected by the local government and are provided to the paying agent to pay debt service on the bonds.

²² Background on Community Facilities Districts in California. In 1978, Proposition 13 limited the ability of local public agencies to increase property taxes based on a property's assessed value. In 1982, the Mello-Roos Community Facilities Act of 1982 (Government Code Section 53311-53368.3) was created to provide an alternate method of financing needed improvements and services (www.californiataxdata.com), with repayment to come from special taxes that are not levied in relation to property values. The Act allows any county, city, special district, school district or joint powers authority to establish a Community Facilities District (a "CFD") which allows for the financing of public improvements and services. The services and improvements that CFDs can finance include: streets, sewer systems and other basic infrastructure, police protection, fire protection, ambulance services, schools, parks, libraries, museums and other cultural facilities. By law, the CFD is also entitled to recover expenses needed to form the CFD and administer the annual special taxes and bonded debt.

Pension Obligation Bonds

Description and Purpose – Pension obligation bonds (POBs) are issued to finance, over the long-term, all or a portion of an unfunded accrued actuarial liability (UAAL). The UAAL is the difference between the present value of all benefits estimated to be payable to plan members as a result of their service through the valuation date and the actuarial value of plan assets available to pay those benefits. Typically, governments reduce the unfunded liability over time with their required pension contributions. However, in recent years, as costs have exceeded projections and the unfunded liability has grown, issuers have considered other financing measures to manage pension costs.

When pension obligation bonds are issued at taxable rates, the borrowed amount is invested in the financial assets of the pension system. These assets are anticipated to bring a higher return than the cost of the bonds, but the risks should be considered carefully.²³ When issuing POBs, three basic facts must be considered: (1) when pension bonds are issued, the underlying liability associated with the funding gap is not extinguished; it is essentially recast from a footnoted contingent liability to an on-balance sheet debt; (2) issuing bonds for the purpose of investing the proceeds in pension fund assets is risk arbitrage and; (3) pension bonds increase the overall level of financial risk for the plan sponsor.

When considering issuing POBs, the following determinations should be made:²⁴

- Reasonable capacity to bear increased financial risk exists;
- The size of the bond issue will not constrain additional borrowing;
- The size of borrowing will not be more than a maximum of approximately twenty percent (20%) of the pension fund's assets (limiting financial leverage);
- The issue should be callable providing the opportunity to refinance;
- The pension bonds should not be used to fund plans that require substantial liquidity to meet net cash outflows; and
- Debt service should be paid in equal annual amounts.

Procedural Requirements – Procedural requirements will depend on the options available for issuing POBs in Alaska. Currently, pension obligation bonds are not authorized under the Alaska Constitution which requires that debt be issued for capital purposes, nor are they defined in state law.²⁵ However, House Bill 278 now under consideration may provide a structure for local governments to have access to pension obligation funding through the Alaska Municipal Bond Bank Authority (AMBBA).²⁶ Pension obligation bonds could be issued by the AMBBA, and the Municipality could cover debt service payments through annual appropriation or the proceeds of a COP issue. Under the Municipal Charter, voter approval may be required to issue COPs in excess of \$1 million.²⁷

Repayment Pledge – The pledge to repay POBs is generally an unconditional obligation of the issuer, payable from its general fund. The bondholders are unsecured, general fund creditors of the issuer. The funds to pay the debt service on the POBs are the funds that were pledged to paying the unfunded UAAL prior to the bonds being issued.

²³ Evaluating the Use of Pension Obligation Bonds, 1997 and 2005 (Government Finance Officers Association (GFOA))

²⁴ Section: *The Case for Pension Bonds* (Risky Business, Evaluating the Use of Pension Obligation Bonds, Government Finance Review, June 2003)

²⁵ Alaska Constitution; Article 9. Finance and Taxation. Section 8 State Debt. "No state debt shall be contracted unless authorized by law for capital improvements or unless authorized by law for housing loans for veterans, and ratified by a majority of the qualified voters of the State who vote on the question."

²⁶ House Bill 278 http://www.legis.state.ak.us/basis/get_bill.asp?session=24&bill=hb278

²⁷ (Municipal Charter 13.08) The Assembly by ordinance may authorize a contract, lease, or obligation requiring funds from future appropriations. A lease purchase agreement with respect to acquisition of a capital improvement valued in excess of \$1 million is not valid until approved by a majority of the qualified voters voting on the question.

Borrowing Cost & Flow of Funds – Borrowing cost is expected to be high because the debt must be issued on a taxable basis. The bond proceeds are invested in the pension fund. The debt service payments replace the obligation of the issuer to make annual contributions to the unfunded liability financed with the pension bonds. Debt service payments are transferred from the general fund to the paying agent.

Non-Recourse Private Activity Bonds

Description and Purpose – Private activity bonds (PABs) are a vehicle for the Municipality to issue bonds to provide tax-exempt financing for certain private activities. The definition of a qualified private activity bond includes an exempt facility bond or qualified mortgage, veterans' mortgage, small issue, redevelopment, 501(c)(3), or student loan bond. The governmental entity generally acts as a conduit, but the entity receiving the benefit of tax-exempt financing is generally the obligor ("conduit borrower") on the bonds.

The municipal security must meet either of two sets of conditions set out in Section 141 of the Internal Revenue Code. A municipal security is considered a private activity bond if, with certain exceptions, more than 10% of the proceeds of the issue are used for any private business use and the payment of principal of and interest on more than 10% of the proceeds of such issue is secured by or payable from property used for a private business use. A municipal security also is a private activity bond if, with certain exceptions, the amount of proceeds of the issue used to make loans to non-governmental borrowers exceeds the lesser of 5% of the proceeds or \$5 million. Most categories of private activity bonds are subject to the alternative minimum tax (AMT).

In addition, most qualified private activity bonds are subject to volume cap which is the maximum amount of private activity bonds that may be issued by each state in a calendar year. Within the State of Alaska, the limit is allocated by the State Bond Committee (AS 37.15.800 (a)). In general, each year, twenty-five percent (25%) of the State's limit will be allocated to municipalities.

Procedural Requirements – A resolution or ordinance detailing the project, cost and repayment details must be approved by the Assembly. Then, in order for bond proceeds to be used to finance the project prior to adoption by the issuer, a reimbursement resolution is generally adopted by the issuer while the project is still in the planning stages. Allocations on volume cap may be required. Additionally, a Tax Equity and Fiscal Responsibility Act (TEFRA) hearing is required to provide issuing authority.

Repayment Pledge – The Municipality is not obligated to pay debt service on private activity (conduit) bonds and has issued them for entities such as the United Way of Anchorage, the Alaska Pacific University, and the Alaska Native Heritage Center.

Borrowing Cost & Flow of Funds – Borrowing costs would be moderate to high and reflect the strength of the conduit borrower's revenue pledge and other security provisions. Bonds would be issued and provided to the private entity for the capital project. Funds pledged for repayment would be assigned directly to the paying agent for payment of debt service.

63/20 Financing (82-26) (Non Profit Issuer)

Description and Purpose – U.S. Treasury Revenue Ruling 63-20 created the ability for non-profits, qualified under the laws of the state, to issue tax exempt debt. In instances where a typical issuer (local government) needs a strict separation from liability of issuing debt for public infrastructure; this vehicle further insulates it from repayment obligation or the appearance thereof. The non-profit can issue the debt instead of the Municipality.

Procedural Requirements – Resolutions authorizing the issuance are required from the non-profit and likewise from the governing body approving the project. In addition, the governing body is required to adopt a resolution agreeing to accept future delivery of the unencumbered title to the property. This method of financing may or may not require voter approval depending on any additional sources used for payment of debt service or if there are any political reasons for which it may be desirable. Annual appropriation of funds to pay debt service on the bonds may be required by the governing body.

The tenant of the facility is required to be a governmental entity or a charitable organization (qualified under Section 501(c)(3) of the Internal Revenue Code and in the state).

Repayment Pledge – The repayment pledge is generally the cash flow from the project but can be a variety of dedicated streams including specific taxes, revenues or contributions for repayment of debt service. The project security must be in place at the time of debt issuance and must remain in place so long as the bonds are outstanding.

Borrowing Cost & Flow of Funds – Borrowing costs would be moderate and reflect the repayment pledge of the issuer.

Grant Anticipation Revenue Vehicles (GARVEE Bonds)

There is currently no local authority for the issuance of GARVEE bonds by the Municipality. This debt instrument is provided for informational purposes only.

Description and Purpose – Grant Anticipation Revenue Vehicles (GARVEE Bonds) are authorized to receive federal reimbursement of transportation-related debt service and financing costs. They are bonds, notes, or other financial instruments issued based on future projections of federal-aid transportation funding. GARVEEs can be used for any transportation purpose identified in the Transportation Equity Act for the 21st Century (TEA-21). These projects are highway projects, transit projects, the purchase of transit vehicles, or connections to intermodal ports and stations. They cannot be used to build rail lines or for private purposes. *“The main intent behind developing new approaches has been to allow projects to be implemented sooner. While GARVEEs are used to finance a wide variety of projects, they are mostly going to new roads and capacity increases.”*²⁸

Normally, the state requests funds from the U.S. DOT and applies for a reimbursement. With GARVEEs, states take the reimbursement and use it to secure the principal and debt service of the bonds for another project. The debt itself remains a state responsibility, but the source of debt service is federal transportation funds.

There are a wide variety of GARVEEs: short term, long term, back stopped (additional revenues pledged), direct (grant is the only source of repayment), and indirect (repaid indirectly from federal funds from other transportation projects).

Procedural Requirements – The project(s) to be funded with the GARVEEs must be on the Statewide Transportation Improvement Program (STIP) list to be eligible.²⁹ Then, the Municipality, Anchorage Metropolitan Transportation Solutions (AMATS), and the State Department of Transportation would need to work through the GARVEE process with the Federal Highway Administration. If the

²⁸ Brookings Institution Washington DC, Today's Roads with Tomorrow's Dollars (GARVEEs) March 2005

²⁹ GARVEEs are tools generally only useful for states, “GARVEE projects may benefit local governments and Metropolitan Planning Organizations and are often chosen from their plans or with their approval, local governments and MPOs are not able to use GARVEE financing to accelerate transportation projects. **California’s MPOs are an exception** since, starting in 1998, the state has suballocated all of the funds from the federal Congestion Mitigation and Air Quality (CMAQ) program as well as 75 percent of the remaining program funds to the metropolitan level. In other states, however, even where metropolitan suballocation exists, it is generally not enough to leverage the future funds.” Brookings Institution Washington DC, Today's Roads with Tomorrow's Dollars (GARVEEs) March 2005 http://www.brookings.edu/metro/pubs/20050322_garvee.htm

Municipality worked with the State to secure sub-allocation of transportation funds to the local level, funding would follow the local level process. Assembly approval of the funding ordinance specifying the projects, level of funding, terms of the agreement, and reimbursement details would be required. Voter approval would be required if funding sources for the projects included a match using taxpayer dollars.³⁰

Repayment Pledge – Federal transportation funds anticipated to be received are the security for repayment of the notes. The result is that future federal highway funds may shift to payment of debt service on these bonds. GARVEE bonds are subject to the non-appropriation of grant funds by the federal government, therefore repayment of these bonds is the responsibility of the issuer.

Borrowing Cost & Flow of Funds – Borrowing costs would be tied to the likelihood of grant appropriation and the strength of the secondary revenue pledge, ultimately reflecting the repayment pledge of the issuer. Receiving federal funds early through GARVEEs would result in a reduction in future funding, generally allocated across a number of years.³¹ If GARVEEs were performed at the State level, federal funding would be received by the State and provided to the Municipality for local designated projects. If funding was sub allocated by the State to the Municipality and AMATS, the funding would flow directly to the local level.

Asset Securitization Bonds

Description and Purpose – Through the issuance of bonds, a trust purchases existing or anticipated assets of a governmental agency and securitizes interests in these assets to investors. This securitization of assets can lower risk, add liquidity, and improve economic sufficiency. This financing mechanism provides an opportunity to receive funding now based on revenues that will be received in the future. Examples of assets that can be securitized include accounts receivable, lease payments, corporate or sovereign debt, student loans, and mortgages, etc. In Alaska, tobacco bonds are an example of assets that have been securitized so forthcoming receipts can be spent on projects now.

Procedural Requirements – Approval of the sale or transfer of assets and the bond issuance would require Assembly approval with the ordinance detailing creation of a Special Purpose Vehicle (SPV) that is legally insulated from the Municipality. This may be a corporation which has been specifically established to facilitate the securitization. Further, the ordinance would detail the sale or assignment of assets to be securitized by the SPV, and its obligation for debt service on the bonds. Then, the SPV would issue debt against the pooled securitized assets, dividing up the benefits (and risks) among investors on a pro-rata basis.

Repayment Pledge – The pooled assets are pledged for repayment of debt service on the bonds. The amount of risk, and therefore the cost, is based on the assets being securitized. The governmental agency would not be liable for payment of debt service.

Borrowing Cost & Flow of Funds – The borrowing cost is higher than a typical revenue bond due to the increased risk (variations in cost would depend on the type of asset being secured), and the issuing transaction itself can be complex. In some instances, ongoing servicing is required, for example, when receivables are collateral for repayment, invoicing and collections are still required. This service could either continue internally, and the originating entity would receive a small fee for it, or it could be contracted out. Receivables from the assets would be provided to the trustee to pay debt service on the bonds.

³⁰ In November 2002, Alaska Voters approved a combined GARVEE and general obligation bond issue to finance communities' most critically needed priorities. http://www.innovativefinance.org/news_innovations/02242003_garvees_advance_in.asp

³¹ Alaska statewide projects partially funded by GARVEEs are anticipated to have a net reduction impact on federal funds from one to two percent in total projects that can be constructed over the next 18 years.

http://www.innovativefinance.org/news_innovations/02242003_garvees_advance_in.asp

VI. CONSIDERATION OF DEBT STRUCTURING ELEMENTS

The debt structure of a bond issue involves features such as the maturity dates, provisions for redemption, debt service schedule, interest rate coupons and yields, and security for the issue. Details of the funded capital project with regards to construction timing, certainty of project revenues, and a project useful life can affect the debt structure of an issue. Choices made regarding debt structure will impact the cost of the issue as well as refinancing options in the future. In structuring its debt, the Municipality will evaluate the costs and benefits various types of debt and strive to achieve the lowest possible net cost to the Municipality according to the guidelines described below.

Tax Status: Unless otherwise required, debt of the Municipality should be issued on a tax-exempt basis in order to obtain the lowest borrowing rates. The Municipality should maintain a system of record keeping and reporting to meet the arbitrage rebate compliance requirements of the Federal tax code and ensure compliance with other Federal tax regulations as required by bond counsel at the time of issuance of tax-exempt debt. These efforts should include tracking investment earnings on proceeds, the necessary retention of rebate consultants to calculate rebate payments pursuant to tax law, and the remitting any rebatable earnings to the Federal government in a timely manner to preserve the tax-exempt status of outstanding debt issues.

Principal Repayment (Amortization): The Municipality's GO debt is structured to minimize the impact on property taxes yet maintain a relatively rapid payment of principal. The Municipality amortizes principal on its GO bonds to recapture debt capacity for future use. To the extent possible, the Municipality should strive to repay at least 50% of the initial principal amount of a GO bond issue within ten years.

As is often the case with revenue bonds, principal can be amortized to wrap around existing obligations to achieve aggregate level debt service each year on all debt or to achieve other financial planning goals. Bonds repaid on a level debt service basis, along with other debt service structures, may be used to take advantage of market conditions present at the time of sale.

Factors to be considered when determining the final maturity of debt include the average life of the assets being financed, the relative level of interest rates along the yield curve, and the year-to-year differential in interest rates. When issuing tax-exempt debt, the final maturity of borrowings should not exceed, and preferably be less than, the projected economic life of the improvements that are financed, or such shorter period as required by Federal tax law and regulations.

Capitalized Interest: Capitalized interest increases the issuance amount of long-term debt to finance bond interest payable during the project construction period. This structuring element is often employed by revenue bond issuers to avoid the payment of debt service from net revenues until the project is operational and generating revenues. Capitalized interest is also utilized in financing lease obligations, like COPs, where lease payments cannot be appropriated until the lessee has beneficial use and occupancy of the leased asset being funded from bond proceeds. Because monies held as capitalized interest are limited to investment at the yield on the bonds, which is less than the true cost of funds, the costs and benefits of funding capitalized interest from bond proceeds should be evaluated relative to other funding options such as funding capitalized interest from issuer equity and the issuance of commercial paper.

Debt Service Reserve Funds: It may be cost-effective for the Municipality to provide additional security to bondholders by establishing a debt service reserve fund requirement for each bond issue. With each issuance of debt, the costs of funding the reserve requirement from bond proceeds should be compared with the costs of satisfying the reserve requirement through the use of a reserve fund surety bond.

External Credit Enhancement: When appropriate for the type of debt, the costs and benefits of bond insurance or other credit enhancements shall be evaluated. The Municipality shall procure any credit enhancement purchases in order to minimize costs and interest expense under current circumstances.

Price Structure: Bond pricing may include par, discount, premium and capital appreciation bonds. Discount, premium, and capital appreciation bonds are to be used when they demonstrate an advantage relative to par structuring.

Redemption Features: Redemption features will be established on a case-by-case basis, taking into consideration market conditions and the costs of call options prior to the time of sale. Non-callable bonds may be considered if the cost of the call option for the particular bond exceeds the expected present value debt service savings provided by the future exercise of such call option. Because the issuance of non-callable bonds may restrict future financial flexibility, cost is not the sole determinant in the decision to issue non-callable bonds. It is the preference of the Municipality to issue bonds with standard ten-year redemption provisions.

Variable Rate Debt: The municipal bond market has developed several debt instruments that allow municipalities to borrow at variable (floating) interest rates. Structured as a rolling series of short-term investments that are periodically remarketed to investors, and therefore priced at the short-end of the yield curve with typically lower interest rates, these variable rate obligations are typically available in three types: (1) commercial paper, (2) variable rate demand obligations (“VRDOs”) and (3) auction rate securities (“ARS”).

Types of Variable Rate Debt

Commercial Paper (CP) – Commercial paper is a short-term obligation (maturities range from 1 to 270 days) providing incremental and interim funding for capital projects, generally repaid with long-term bonds or cash when a project is placed in service. CP is typically secured by a subordinate revenue pledge and a bank credit facility.

Variable Rate Demand Obligations (VRDOs) – Variable rate demand obligations are long-term bonds with nominal maturities of 10 to 30 years. VRDOs have variable rates of interest which are reset at predetermined intervals of one, seven, 30 or 180 days through a remarketing process wherein the investor can demand that the bonds be purchased by the issuer at par on each reset date. This tender, or “put”, option necessitates the purchase of third-party liquidity support by the issuer. VRDOs are callable at par on any interest payment date, which is typically the first business day of the month. Bond documents for VRDOs usually include a “multi-modal” feature which allows for a conversion of interest rate mode to CP, ARS or fixed rate upon notice to investors.

Auction Rate Securities (ARS) – Auction rate securities are long-term bonds with nominal maturities of 10 to 30 years. ARS have variable rates of interest which are reset at predetermined intervals of seven, 28 or 35 days using a modified Dutch auction process. Unlike VRDOs, the interest rate reset process for ARS is such that investors do not have the option to tender the bonds to the issuer, which negates the need for and cost of liquidity support. Like VRDOs, ARS are callable at par on any interest payment date at the issuer’s option, and a “multi-modal” feature is typically included in bond documents. The broker-dealer fees common to ARS are higher than the remarketing fees paid with VRDOs but the liquidity cost is avoided.

Purposes of Variable Rate Debt

To Reduce Cost of Funds – Since the inception of municipal variable rate products in the early 1980’s, variable interest rates have borne an average rate that is substantially below (2-3 percent) the

average for fixed rates. Accordingly, issuers who have accepted a moderate amount of variable rate risk have experienced reduced costs of borrowing.

As an Interim Financing Tool – The ability of certain variable rate products, such as commercial paper, to be issued incrementally as capital funds are needed can reduce financing costs for a project. CP often serves as a lower-cost alternative to the issuance of long-term debt with funded capitalized interest.

To Provide Restructuring Flexibility – Since the expectations of variable rate investors are short-term in nature, variable rate debt can be redeemed at short notice without incurring penalties in the form of a call premium or higher initial interest rates. This feature makes variable rate debt a preferred tool for financing projects where prepayment or restructuring is a high probability. Variable rate debt can be currently refunded with fixed rate debt, thereby preserving the later use of the one-time advance refunding for the fixed rate issue. This future flexibility will prove valuable as future capital improvements may require additional debt funding or a restructuring of existing fixed rate debt obligations.

For Better Management of Negative Arbitrage – Issuing debt in a variable rate mode reduces or at times may even eliminate negative arbitrage in construction, capitalized interest and debt service reserve funds. These funds are generally invested in short-term securities earning taxable rates of return which usually exceed the variable rate, tax-exempt borrowing cost.

To Offset Risks of Variable Rate Assets – The maintenance of variable rate debt liabilities in an amount equal to or less than the amount of variable rate assets prudently reduces the Municipality's risk of exposure to changes in interest rates earned on investments.

To Diversify the Investor Base and Lower Costs – Typically, variable rate debt is sold to a different segment of the capital markets than are long-term bonds. By tapping short-term investors, an issuer broadens and diversifies its investor base which serves to lower its cost of funds. As a familiar and respected credit among short-term investors, the debt issuer would be in a better position to access these buyers at those times when it is less advantageous to borrow in the fixed rate market.

Guidelines for Use of Variable Rate Debt

Refinancing Flexibility – The Municipality may consider funding capital projects with variable rate obligations in lieu of long-term fixed rate debt when a refunding or restructuring of the debt is likely due to potential changes in use of the project or an improvement in credit quality is anticipated.

Interim Financing Needs – The Municipality may consider issuing CP to finance its capital projects when interest earnings on construction and capitalized interest funds are at rates below the interest cost of long-term, fixed rate bonds. Pursuant to rating agency guidelines, any outstanding CP anticipated to be redeemed within the current fiscal year shall not be considered variable rate debt expected to be outstanding on a permanent basis, and therefore shall be excluded from any calculations of variable rate debt exposure for internal debt management purposes.

Management of Interest Rate Risk – Credit rating agency analysts suggest that 20% to 25% of outstanding debt can be in permanent variable rate mode (not expected to be refinanced with fixed rate debt) without creating undue risk, although evaluations are made on a case-by-case basis. The analysis of variable rate risk exposure should be performed on the basis of "net" risk; that is, variable rate liability net of any interest rate hedge provided by the availability of cash and short-term investments and risk mitigation instruments such as interest rate swaps or caps. For example, an issuer may create a synthetic fixed rate obligation by issuing variable rate debt and simultaneously entering into a corresponding interest rate swap agreement wherein the issuer pays a fixed rate and

receives a floating rate. This arrangement may create a net fixed rate obligation with an interest cost lower than that available from issuing traditional fixed rate debt, subject to certain additional risks. Some portion of the notional amount of synthetic fixed rate debt should be considered permanent variable rate debt to the extent that the interest rate swap exposes the issuer to a situation where the payments received from the swap counterparty may be insufficient to completely offset the interest payable on the variable rate debt.

Budgeting Methodology – The Municipality should determine an appropriately conservative method for budgeting the interest cost of variable rate debt by considering historic interest rates, projected interest rates and the effect of risk mitigation instruments such as interest rate swaps or caps. The use of an interest rate stabilization fund may be considered.

Diversification of Counterparties – In selecting remarketing agents (for VRDOs) and broker-dealers (for ARS) for variable rate debt, the Municipality should choose providers that diversify its exposure and foster competition among the various agents. For similar reasons, the Municipality should seek to diversify counterparties when selecting institutions to provide liquidity or credit enhancement for variable rate debt.

Monitoring and Reporting Requirements – The Municipality should monitor the performance of actual interest rates on variable rate debt against the interest rates assumed at the time of budget formulation. The Municipality should ensure that variable rate debt is reported in accordance with Generally Accepted Accounting Principles (GAAP) and with rules promulgated by the General Accounting Standards Board (GASB). With the assistance of its financial advisor, the Municipality should regularly review the performance of the assigned remarketing agents/broker-dealers in relation to each other, to the variable rate programs of similar debt issuers and to market indices.

Use of Derivative Products and Development of a Derivatives Management Policy: A derivative is a financial arrangement whose returns are limited to, or derived from, some underlying published index, interest rate, or rate of exchange, stock, bond, currency, or other asset. The Municipality can enter into agreements utilizing derivative instruments such as interest rate swaps, interest rate caps, floors and collars, as well as swaptions. One of the most commonly used derivative products is an interest rate swap, which is an agreement between two parties to exchange future flows of interest payments based on a notional dollar amount. One party agrees to pay the other a fixed rate, while the counterparty pays the first party a variable rate which resets at regular dates and is usually based upon the London Interbank Offered Rate (LIBOR) index, Bond Market Association (BMA) index or other published interest rate index. The settlement is payment or receipt of the net amount, or “spread” between interest rates, as provided under the terms of the swap agreement.

The Municipality may consider the utilization of derivative products (1) to finance or enhance the financing of capital facilities and (2) to refinance or enhance the refinancing of outstanding debt obligations. Derivative products should not be employed as investment instruments or for the purpose of speculation. Although they are potentially beneficial debt management tools, derivative products involve inherent risks which must be managed. Therefore, prior to entering into any derivative financial arrangement, the Municipality should develop and adopt a comprehensive Derivatives Management Policy which establishes guidelines regarding the use and management of these instruments, and specifically addresses the following key considerations:

1. Purpose of the transaction;
2. Form of the agreement;
3. Cash flow payment analysis;
4. Risks and mitigating factors;

VII. EVALUATION OF DEBT REFUNDING OPPORTUNITIES

Tax-exempt debt issuers with sizeable debt portfolios, like the Municipality, continuously analyze the expected savings from refunding (refinancing) outstanding debt, particularly during periods of low or falling interest rates.³² This analysis is often performed on a maturity-by-maturity basis since all the maturities of a particular series of tax-exempt bonds are not required to be refunded at the same time. Economic refundings are accomplished through the issuance of new tax-exempt bonds, typically on the same terms as the outstanding debt, to purchase an escrow portfolio of U.S. Treasury securities which funds the debt service to the redemption date plus any redemption premiums due on the refunded bonds. Refunding transactions may be executed for other than economic purposes, such as to restructure debt service in response to the receipt of lower than anticipated revenues, to change the type of debt instruments being used, or to retire a bond issue and indenture in order to remove undesirable covenants.

Legal and In-Substance Defeasance: Outstanding bonds are considered legally defeased when the payment of debt service has been assured through the structuring of an escrow portfolio of cash or government securities, the principal and interest on which will be sufficient to pay debt service on the outstanding bonds. When the maturities of a bond issue have been legally defeased, the rights and interest of the bondholders are terminated pursuant to the bond documents, and the bond issue is no longer an obligation of the issuer for financial reporting purposes. An in-substance defeasance of outstanding bonds occurs when the bond documents do not permit a legal defeasance yet the debt is economically defeased through the structuring of a sufficient escrow portfolio. With an in-substance defeasance, the issuer is not relieved of its responsibilities under the bond documents and the debt remains an obligation for financial reporting purposes.

Advance, Current and Forward Refundings: An advance refunding involves the issuance of refunding bonds more than 90 days in advance of a bond's first optional redemption date. Conversely, a current refunding involves the issuance of refunding bonds within 90 days in advance of a bond's first optional redemption date. A forward refunding is similar to a current refunding in that the refunding bonds are delivered no sooner than 90 days prior to the bond's first optional redemption date; however, the interest rates on the forward refunding bonds are set up to 18 months prior to the delivery date, compared to bonds which are normally delivered within one month of their pricing date.

Currently, tax-exempt bonds subject to the AMT, or considered private activity bonds, may not be advanced refunded. For bonds issued after December 31, 1985, only one advance refunding may occur under Federal tax law.³³ Federal tax law does not limit the number of current refundings of any bond.

³² Because tax-exempt interest rates are typically higher for longer terms of repayment (an ascending yield curve), an issuer can realize savings from refunding a bond even if the general level of interest rates have not declined since the debt was first issued. By "sliding down the yield curve", a 20-year bond with a coupon rate of 5.00% issued 10 years ago could now be refunded for savings through the issuance of a 10-year bond having an interest cost of 3.75%, for example.

³³ Original issues sold prior to December 31, 1985 are limited to two advance refundings.

Parameters Impacting Refunding Savings:*Technical Parameters*

When analyzing the economics of a refunding bond issuance, numerous technical parameters having a direct impact on annual and present value savings are taken into consideration (see Figure 18). Factors that can increase savings include: a lower refunding interest cost and a higher escrow yield³⁴; a lower call premium and lower financing costs; a shorter period of time to the call date of the refunded bond and a longer period of time to the maturity date of the refunded bond; and, lower yielding transferred proceeds.

Figure 18

Technical Parameters Increasing Refunding Savings

- | |
|---|
| <ul style="list-style-type: none"> • Lower refunding interest cost • Lower call premium on refunded bond • Shorter time between issuance of refunding bonds and call date • Longer time between call date and maturity date of refunded bonds • Higher yield on escrow securities • Lower financing costs • Lower yielding transferred bond proceeds |
|---|

Non-Technical (Qualitative) Parameters

Non-technical parameters related to the federal tax implications, structure and risk of a refunding transaction are more difficult to quantify but must also be considered. As previously mentioned, any tax-exempt bond issued after December 31, 1985 may only be advance refunded one time, and thus the projected savings of executing the advance refunding today should be evaluated against the opportunity cost of waiting to execute this transaction at a later date when refunding savings might be higher (or lower).

Regarding refunding structure and risk, although most refundings are executed through the issuance of fixed rate bonds with legal provisions similar to the refunded bonds, some refundings are executed through the issuance of variable rate obligations with or without interest rate hedges in place. While historically interest rates on variable rate debt are 2 to 3 percent lower than fixed rate debt, if variable rates rise and stay above the fixed rate of the refunded bond, the issuer would incur a net cost, not savings, from the transaction. The refunding of fixed rate bonds with variable rate debt hedged through interest rate swaps or caps would reduce, but not eliminate, interest rate risk in most cases. The use of such synthetic financial products creates additional risks (basis, counterparty, termination, tax, etc.) that cannot be quantified with certainty and are often not incorporated into projections of refunding savings.

Review of Refunding Criteria Used by Tax-Exempt Debt Managers: Tax-exempt debt managers employ various criteria, or methodologies, when evaluating the economics of a refunding transaction. The three most common are: (1) the net present value savings methodology, (2) the call option efficiency methodology, and (3) the parameter methodology. The following text describes these methodologies, including strengths and weaknesses, as well as the typical benchmarks/thresholds for refunding savings. Figure 19 summarizes how these methodologies to incorporate the previously mentioned technical and non-technical parameters impacting refunding savings. For all

³⁴ With an advance refunding, the yield on escrow securities is limited to the arbitrage yield of the refunding bonds, which is often less than the coupon rate of the refunded bond in lower interest rate environments. Negative arbitrage in the escrow occurs when the escrow yield is less than the arbitrage yield. With a current refunding, there is no limit on the escrow yield; however, the life of the escrow is limited to 90 days.

methodologies, the best practice is to measure projected refunding savings on a maturity-by-maturity basis, as opposed to on a bond issue basis, in order to eliminate the refunding of maturities that do not meet the minimum savings criteria. However, exceptions are made in cases where the legal defeasance of all maturities of a series is necessary to terminate the provisions of the refunded bond documents.

Figure 19

Primary Methodologies to Evaluating Refunding Transactions - Incorporation of Refunding Parameters			
	NPV Savings Methodology	Call Option Efficiency Methodology	Parameter Methodology
Technical Parameters			
Refunding interest cost	Static	Dynamic	Static w/ adjustments
Call premiums and dates	Static	Dynamic	Static w/ adjustments
Time between delivery and call dates	Static	Dynamic	Static w/ adjustments
Yield on escrow securities	Static	Set to arbitrage yield	Static w/ adjustments
Financing costs	Acceptable	Acceptable	Acceptable
Transferred bond proceeds	Acceptable	Acceptable	Acceptable
Non-Technical Parameters			
Advance refunding limitation	Not incorporated	Dynamic	Static w/ adjustments
Risks of synthetic financial products	Not incorporated	Not incorporated	Static w/ adjustments

Net Present Value Savings Methodology

The majority of tax-exempt debt managers use net present value (NPV) savings, which factors in all transaction costs, as the criteria for executing refunding transactions. NPV savings are calculated by discounting the savings at each semi-annual period back to the delivery date of the refunding issue using the all-in interest cost (AIC) of the refunding issue. NPV savings are measured as a percentage of refunded par for benchmarking purposes. Most debt managers will not execute a refunding transaction unless the NPV savings meet or exceed the threshold of 3.0% of the par amount refunded.

The main benefit of employing the NPV savings methodology for evaluating refunding candidates is its simplicity of use, which works best for benchmarking savings for current refunding transactions. The main drawback of the NPV savings methodology is its inability to assess the economics of deferring the refunding to a later date for potentially greater savings. Specifically, the NPV savings methodology uses static measures of refunding interest cost, call features, escrow yield, and the time between the delivery date of the refunding bonds and the call date of the refunded bonds. Changes to these technical parameters, such as a lower refunding interest cost or less negative arbitrage in the escrow, would increase refunding savings. Additionally, the NPV savings methodology also does not present projected refunding savings in the context of the non-technical (qualitative) parameters such as risks from the use of synthetic financial products. Lastly, the industry standard NPV savings benchmark of 3.0% is less relevant in evaluating the projected refunding savings of bonds that are callable within one to two years of their maturity date. It is often the case that this short time period is not adequate to generate 3.0% NPV savings even with a very low refunding interest cost. The observation that call options are a “wasting asset” is particularly relevant for these bonds, such that they are deemed “use it or lose it” candidates which should be evaluated using NPV savings benchmarks below 3.0%, or for simply positive NPV savings.

Call Option Efficiency Methodology

A more sophisticated approach to evaluating refunding opportunities is the call option efficiency methodology. This methodology computes an efficiency ratio by dividing the projected NPV savings of executing a refunding by the current value of the refunded bond's call option. Option values are functions of call price, call date, maturity date, current interest rates (levels and term structure), interest rate volatility and transaction costs. The benchmark efficiency ratio employed by bond issuers to execute an advance refunding has ranged from 70% to 95%. At a minimum efficiency ratio of 70%, the projected NPV savings would be capturing 70% of the current value of the call option. As option values have been relatively low in recent years due to the low level of rates and the flat yield curve, most bond issuers that have employed the call option efficiency methodology now use a 90-95% efficiency ratio as their savings benchmark.

The main benefit of this methodology is its usefulness in evaluating the execution of one-time only, advance refunding transactions. Specifically, because the call option efficiency methodology utilizes dynamic measures of the most relevant technical parameters to incorporate hypothetical savings from refundings executed at future dates into the call option value, it is a more exhaustive approach to the decision of when to proceed with a refunding. The drawbacks to call option efficiency methodology are its inherent complexity and its inability to incorporate the risks of synthetic financial products into projected refunding savings.

Parameter Methodology

Utilizing a baseline benchmark of NPV savings which is adjusted higher or lower to reflect certain refunding parameters specific to the proposed transaction, the parameter methodology to evaluating refunding opportunities can be viewed as a hybrid of the NPV savings and call option efficiency methodologies. The refunding parameters which are adjusted typically include: (1) the interest costs on the refunding bond and escrow yield (to account for the current level on interest rates relative to historical averages); (2) the time period between the call date and the maturity date of the refunded bond (to adjust for the lower savings potential of bonds with shorter maturities); and (3) the risks associated with synthetic financial products. It is because the first two adjustments involve refunding parameters which are dynamic in the call option efficiency approach that this methodology can be considered a hybrid of the other two methodologies.

Figure 20 presents the baseline benchmarks of NPV savings and the magnitude of adjustments normally made for the aforementioned refunding parameters. For example, the NPV savings benchmark used to evaluate an advance refunding of a bond with a refunding interest cost in the 35th percentile of historical levels and a six year period between the call date and the maturity date would be 3.5% (3.0% - 0.5% + 1.00% + 0.0%). And if a synthetic fixed rate refunding was utilized wherein the issuer received a floating swap rate equal to a percentage of LIBOR, this particular NPV savings benchmark would increase by 4.0% from 3.5% to 7.5%.

Figure 20

Parameter Methodology – NPV Savings Benchmarks with Adjustments						
Baseline Benchmark		Current Level of Interest Rates		Time Period Between the Call Date and the Maturity Date		Risks Associated with Synthetic Financial Products
3.0%	+	Subtract 0.5% for each tenth of a percent below the 40 th percentile or Add 0.5% for each tenth of a percent above the 60 th percentile	+	Subtract 0.50% for less than 6 months, 0.25% for 6 months to 1 year or Add 0.25% for each year from 2-5 years; 1.00% for 5-10 years; 1.25% for 10-15 years; 1.50% for >15 years	+	If interest rate swap includes tax risk or an option product, then add 4.0%; if not, then add 2.5%

The strength of the parameter methodology is that its adjustments to NPV savings benchmarks attempt to incorporate the risks associated with synthetic financial products, unlike the other two methodologies. The weakness of the parameter methodology is that its adjustments to refunding parameters are somewhat arbitrary and may possibly understate the risks of synthetic financial products in high interest rate environments.

Recommended Refunding Criteria:

The Municipality, with assistance from its financial advisor, should continue to monitor refinancing opportunities for all outstanding debt obligations by applying recommended refunding criteria.

Advance, Current or Forward Refundings

When analyzing advance, current or forward refunding transactions through the issuance of fixed rate bonds, the recommended refunding criteria will incorporate both the NPV savings and call option efficiency methodologies, whereby a bond may be refunded if projected NPV savings are at least equivalent to 3.0% of refunded par or the call option efficiency ratio is at least 90%.

Synthetic Advance Refundings

When analyzing current or advance refunding transactions involving synthetic financial products, a bond may be refunded if it meets the criteria required for a fixed rate bond refunding (minimum NPV savings of 3.0% or call option efficiency ratio of 90%) and the transaction as a whole is projected to generate NPV savings of at least 5.5% if the interest rate swap does not involve tax risk or an option product, or NPV savings of at least 7.0% if the swap does involve tax risk or an option product. This criterion would also apply to any bonds subject to optional redemption but not eligible for advance refunding, such as bonds that have been advance refunded already or bonds subject to the AMT.

VIII. RECOMMENDATIONS

Based upon our review with the staff of the Municipality, and our understanding of the financing goals of the Municipality, we offer the following specific recommendations:

Variable Rate Debt: We recommend that the Municipality of Anchorage consider variable rate debt as part of its debt portfolio. We believe that the most conservative strategy for the Municipality is to always have a portion of its debt portfolio in variable rate debt. The amount and percentage should not exceed 35% of the Municipality's total outstanding portfolio.

Anchorage Water and Wastewater Utility (AWWU): We recommend that the AWWU consider the use of a derivative product to complete at least a portion of its capital program prior to the completion of its rate cases with the Regulatory Commission of Alaska (RCA).

City Hall: We recommend that the Municipality consider the issuance of debt to finance the purchase of City Hall. The purchase of the building has the potential for considerable savings for the Municipality when compared to the current costs of renting.

To accomplish the recommendations, we propose that the Municipality adopt:

Debt Issuance Guidelines defining the:

- Types of debt to be issued;
- Maturity structure of future debt;
- Amount and type of variable rate exposure;
- Circumstances to issue competitive and negotiated debt;
- Criteria for issuing conduit debt;
- Circumstances under which the Municipality will issue Tax Anticipation Notes (TANs).

Derivative Guidelines defining the:

- Types and amount of derivative products to be issued;
- Exposure to a variety of risk, including but not limited to counterparty risk, interest rate risk and basis risk.

EXHIBITS

Municipality of Anchorage – Debt Management Report (April 24, 2006)

Exhibit One – Debt Statement as of December 31, 2005

Municipality of Anchorage Debt Statement (as of December 31, 2005)							
	Issued Amt. (000's)	Dated Date	Final Maturity	Outstanding Amount at December 31, 2005 (\$000's)			
				Self-Support.	AK Reimburse.	Net Direct Debt	Total
Municipality (1)							
1. 1993 GO Bonds, Series A (Refunding)	\$ 26,135	02/01/93	02/01/06	\$ 2,310	\$ -	\$ 1,160	\$ 3,470
2. 1993 GO Bonds, Series B (Refunding)	70,185	06/15/93	08/01/10	2,280	-	11,780	14,060
3. 1995 GO Bonds, Series B (Refunding)	29,210	11/01/95	10/01/12	-	-	8,455	8,455
4. 1997 GO Bonds, Series A	18,610	09/01/97	09/01/07	-	-	1,685	1,685
5. 1996 GO Bonds, Series A Road Bonds	16,500	05/01/96	04/01/06	-	-	760	760
6. 1999 GO Bonds, Series A (Refunding and New Money)	83,565	04/01/99	04/01/14	-	-	34,125	34,125
7. 2000 GO Bonds, Series A	94,115	09/01/00	09/01/10	-	-	19,865	19,865
8. 2002 GO Bonds, Series A (Refunding and New Money)	140,180	06/27/02	06/01/22	3,695	-	94,105	97,800
9. 2003 GO Bonds, Series A	35,000	09/04/03	09/01/23	-	-	32,500	32,500
10. 2004 GO Bonds, Series A (Refunding)	21,465	09/16/04	12/01/17	-	-	20,670	20,670
11. 2004 GO Bonds, Series C	52,375	10/28/04	12/01/24	-	-	50,720	50,720
12. 2005 GO Bonds, Series C (Refunding)	18,145	04/13/05	03/01/20	-	-	18,145	18,145
13. 2005 GO Bonds, Series D (Refunding)	43,110	07/13/05	06/01/20	-	-	43,110	43,110
14. 2005 GO Bonds, Series F	96,805	09/22/05	09/01/25	-	-	96,805	96,805
15. 1995 Pension Fund COPs (Refunding)	27,485	12/01/95	02/15/06	3,360	-	-	3,360
Sub-Total	\$ 772,885			\$ 11,645	\$ -	\$ 433,885	\$ 445,530
School District (2)							
16. 1995 GO Bonds	\$ 60,000	11/01/95	10/01/15	\$ -	\$ 10,236	\$ 9,834	\$ 20,070
17. 1995 GO Bonds (Refunding)	29,765	11/01/95	10/01/12	-	10,654	10,236	20,890
18. 1996 GO Bonds, Series A	65,000	08/01/96	08/01/06	-	1,971	1,894	3,865
19. 1997 GO Bonds, Series A	43,850	12/01/97	12/01/07	-	1,981	1,904	3,885
20. 1998 GO Bonds (Refunding)	20,735	10/15/98	07/01/14	-	10,139	9,741	19,880
21. 1999 GO Bonds	55,900	02/01/99	12/01/09	-	5,256	5,049	10,305
22. 2000 GO Bonds, Series A	35,000	08/01/00	12/01/12	-	5,531	5,314	10,845
23. 2000 GO Bonds, Series B	77,900	10/01/00	12/01/20	-	14,540	13,970	28,510
24. 2001 GO Bonds, Series A	65,000	06/01/01	06/01/21	-	17,093	16,422	33,515
25. 2001 GO Bonds (Refunding)	51,805	06/01/01	07/01/13	-	25,791	24,779	50,570
26. 2002 GO Bonds, Series B	131,800	06/27/02	07/01/22	-	52,923	50,847	103,770
27. 2002 GO Bonds, Series B (Refunding)	70,345	06/27/02	07/01/15	-	34,445	33,095	67,540
28. 2003 GO Bonds, Series B	126,770	09/04/03	09/01/23	-	60,009	57,656	117,665
29. 2004 GO Bonds, Series B (Refunding)	80,735	09/16/04	12/01/17	-	41,144	39,531	80,675
30. 2004 GO Bonds, Series D	86,240	10/28/04	12/01/24	-	42,496	40,829	83,325
31. 2005 GO Bonds, Series A	63,850	04/13/05	03/01/25	-	32,564	31,287	63,850
32. 2005 GO Bonds, Series B (Refunding)	29,155	04/13/05	12/01/20	-	14,846	14,264	29,110
33. 2005 GO Bonds, Series E (Refunding)	14,790	07/13/05	12/01/18	-	7,543	7,247	14,790
Total	\$ 1,108,640			\$ -	\$ 389,161	\$ 373,899	\$ 763,060
Water Utility							
34. 1998 Water Revenue Bonds, Sr. Lien (Refunding and New Money)	\$ 28,930	06/01/98	08/01/14	\$ 18,650	\$ -	\$ -	\$ 18,650
35. 1999 Water Revenue Bonds (Refunding and New Money)	68,515	10/15/99	09/01/29	59,465	-	-	59,465
36. 2004 Water Revenue Bonds (Refunding and New Money)	18,595	06/10/04	05/01/34	18,225	-	-	18,225
37. 2004 Water Revenue Bonds, Jr. Lien (Mini Bonds)	2,000	10/14/04	10/14/14	2,000	-	-	2,000
Sub-Total	\$ 116,040			\$ 98,340	\$ -	\$ -	\$ 98,340
Waste Water Utility							
38. 1999 Wastewater Revenue Bonds	\$ 5,180	10/15/99	09/01/29	\$ 4,650	\$ -	\$ -	\$ 4,650
39. 2004 Wastewater Revenue Bonds	22,620	06/10/04	05/01/34	22,620	-	-	22,620
Sub-Total	\$ 27,800			\$ 27,270	\$ -	\$ -	\$ 27,270
Solid Waste Disposal Utility							
40. 1995 Revenue Bonds (Refunding)	\$ 3,465	09/01/95	04/01/09	\$ 1,325	\$ -	\$ -	\$ 1,325
Port of Anchorage							
41. 1995 Revenue Bonds (Refunding)	\$ 10,400	11/01/95	02/01/06	\$ 1,330	\$ -	\$ -	\$ 1,330
Municipal Light & Power							
42. 1993 Electric Revenue Bonds, Sr. Lien (Refunding)	\$ 67,715	01/01/93	12/01/11	\$ 26,535	\$ -	\$ -	\$ 26,535
43. 1996 Electric Revenue Bonds, Sr. Lien (Refunding)	48,855	12/01/95	12/01/15	45,875	-	-	45,875
44. 1996 Electric Revenue Bonds, Series B, Sr. Lien	42,530	08/01/96	02/01/07	1,980	-	-	1,980
45. 1996 Electric Revenue Bonds, Series C, Sr. Lien	78,245	12/01/96	12/01/06	1,595	-	-	1,595
46. 1999 Electric Revenue Bonds, Sr. Lien (Refunding)	42,785	05/15/99	06/01/06	6,925	-	-	6,925
47. 2005 Electric Revenue Bonds, Series A, Sr. Lien (Refunding)	109,350	11/03/05	12/01/26	109,350	-	-	109,350
48. 2005 Electric Revenue Bonds, Series B, Jr. Lien (Refunding)	25,745	11/03/05	12/01/08	25,745	-	-	25,745
Sub-Total	\$ 415,225			\$ 218,005	\$ -	\$ -	\$ 218,005
Correctional Facility							
49. 2000 Lease Revenue Bonds	\$ 60,440	04/15/00	02/01/10	\$ 12,785	\$ -	\$ -	\$ 12,785
50. 2005 Lease Revenue Bonds (Refunding)	40,835	04/14/05	02/01/20	40,835	-	-	40,835
Sub-Total	\$ 101,275			\$ 53,620	\$ -	\$ -	\$ 53,620
Performing Arts Center							
51. 2004 AK Municipal Bond Bank Authority Revenue Bonds, Series B	\$ 5,365	09/01/04	08/01/34	\$ 5,255	\$ -	\$ -	\$ 5,255
TOTAL	\$ 2,561,095			\$ 416,790	\$ 389,161	\$ 807,784	\$ 1,613,735

(1) A portion of MOA's GO bonds are expected to be repaid from proprietary fund revenues.

(2) The State of Alaska reimburses municipalities operating school districts for the costs of qualified and approved school construction, subject to annual appropriation. A reimbursement rate of 51.0% is assumed for each series; actual reimbursement rates will vary by series.

Exhibit Two – Credit Rating Agencies' Median Debt Ratios by Rating Category

Credit Rating Agencies' Views on Relevant Debt Ratios						
	Net Direct Debt		Overall Net Debt		Debt Retirement	
	to Full Value (%)	per Capita (\$)	to Full Value (%)	per Capita (\$)		
Moody's Investors Service (1)						
All Cities						
"AAA" Rated Median	0.9%	not available	1.9%	not available	not available	
"AA" Rated Median	1.0%		2.4%			
"A" Rated Median	1.3%		2.7%			
All School Districts						
"AAA" Rated Median	0.9%		1.9%			
"AA" Rated Median	1.1%		2.5%			
"A" Rated Median	1.6%		2.8%			
Standard & Poor's (2)						
All Cities						≥ 25% within 5 yrs. ≥ 50% within 10 yrs. is acceptable
"AAA" Rated Median	0.9%	\$938	1.9%	\$2,196		
"AA" Rated Median	0.9%	\$667	2.3%	\$1,527		
"A" Rated Median	1.1%	\$519	2.8%	\$1,345		
All School Districts						
"AAA" Rated Median	0.6%	\$609	2.8%	\$2,864		
"AA" Rated Median	1.1%	\$859	2.3%	\$1,931		
"A" Rated Median	1.5%	\$819	2.9%	\$1,538		
All "AA" Rated						
Mean	1.3%	\$860	2.9%	\$1,960		
Mean + 1 Stan. Deviation	2.8%	\$1,657	5.1%	\$3,590		
Mean + 2 Stan. Deviations	4.3%	\$2,454	7.3%	\$5,220		

Sources:

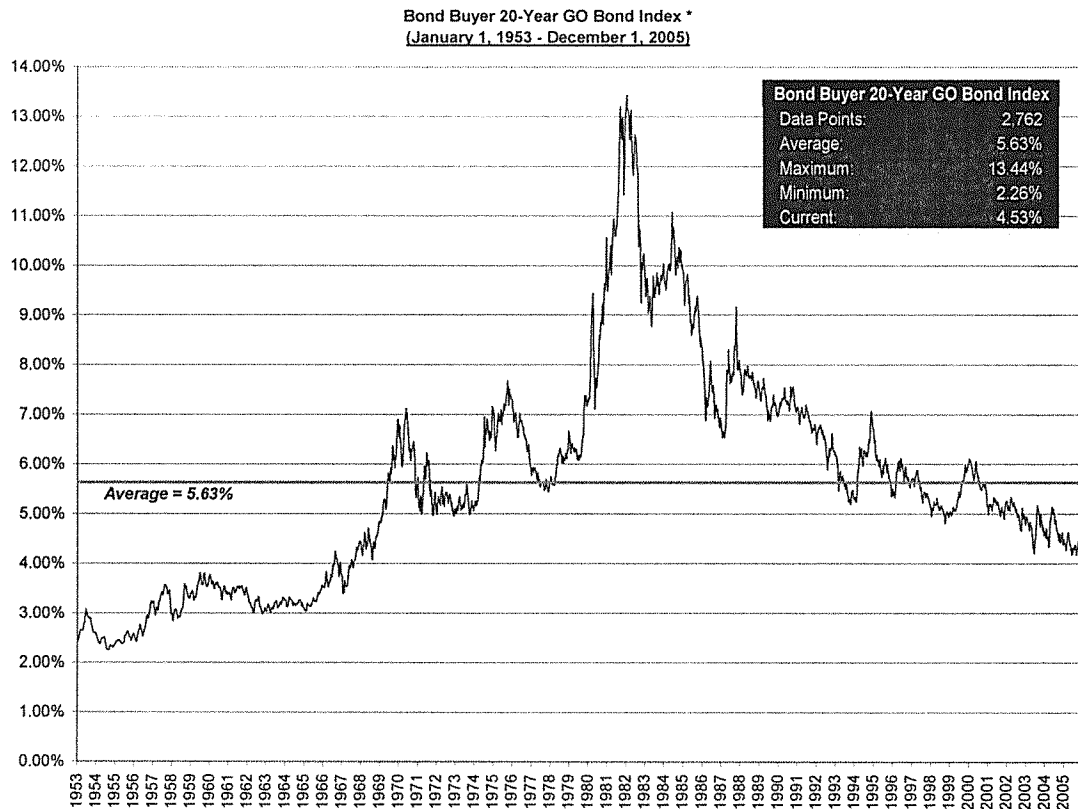
(1) Data from Moody's "2005 Local Government National Medians" published November 2005

(2) Data from Standard & Poor's "Public Finance Criteria: Ratios and GO Credit Ratings" published April 23, 2003 and "2005 Criteria" from standardandpoors.com. Assuming a normal distribution, 68% of values will be within one standard deviation of the mean and 95% of values will be within two standard deviations of the mean.

Exhibit Three – Debt Affordability Analysis, Base Case Assumptions

- Credit Ratings: Maintenance of “AA” level
- Principal Repayment: Annually over 20 years
- Interest Frequency: Semi-annual
- Debt Service: Equal per fiscal year
- Issuance Frequency: Biannually from 2006 through 2014
- Interest Rate Mode: Fixed rate
- Borrowing Cost: 5.50% (see below)
- Bond Pricing: Sold at premium to fund financing costs
- Debt Service Reserve Fund: None
- Capitalized Interest: None
- State Reimbursement Rate of ASD Bonds: Current rates for outstanding GO bonds; 0% rate for new GO bonds

Assumed borrowing cost of 5.50% is based on 5.63% average rate of Bond Buyer 20-Year GO Bond Index minus 0.13% adjustment for “Aa3” and “AA-” ratings.



* The Bond Buyer 20-Year GO Bond Index is comprised of 20 general obligation bonds with 20-year maturities. The Moody's arithmetic average rating of the bonds in the index is "A1".

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