SALT LAKE CITY COUNCIL STAFF REPORT

DATE: June 7, 2005

SUBJECT: **TAX AND REVENUE ANTICIPATION NOTES**

STAFF REPORT BY: Gary Mumford

REQUESTED ACTION:

Salt Lake City issues Tax and Revenue Anticipation Notes each year to assist with cash flow needs of the General Fund. Property taxes, one of the City's major sources of revenue, are primarily received in December. The City normally borrows funds for General Fund operations in anticipation of receiving property taxes. The federal government restricts the amount of borrowing (at the lower tax-exempt rates) to actual needs as determined by a formula. Based on the formula, the City Treasurer is proposing to issue $21 million for fiscal year 2005-06. The closing and receipt of funds is scheduled to take place in July 2005. The notes mature and will be repaid on June 30, 2006.

MATTERS AT ISSUE/POTENTIAL QUESTIONS FOR ADMINISTRATION:

By issuing Tax and Revenue Anticipation Notes, the City can typically earn a significant amount of additional interest income. However, the overall interest rate environment during the period that the notes are outstanding is a key factor in determining the effectiveness of the borrowing. The City Treasurer is expecting to earn between 25 and 50 basis points (0.25% and 0.50%) on the amount borrowed over the amount of interest that it pays.

The notes will be sold using the competitive method of sale, whereby the notes are awarded to the firm offering the lowest interest rate bid. Bids are scheduled to be opened on June 14, 2005. That evening, the Administration will ask the Council to authorize the award of the sale of the Notes to the lowest bidder. The City Treasurer will provide the Council with a summary of the results of the sale including the number of bids received and the net effective interest rate of the low bid.

The Mayor's proposed budget includes $750,000 of interest expense for the Tax Notes, which assumed that the City would borrow $25 million at 3.00%. Since the City Treasurer is recommending borrowing $21 million, interest expense will be approximately $630,000 assuming the same 3.00% coupon. Forecasted interest income should also be reduced with the lower amount of tax notes proceeds to invest. After June 14, when the actual interest expense amount is known, Council staff can include these adjustments on your budget motion sheets for your formal consideration when adopting the annual budget.

During the 2004-05 fiscal year, the City met the following federal spend-down requirements to allow the City to keep excess interest earned over interest expense:

- 90% of the proceeds plus interest on the Tax and Revenue Anticipation Notes must be spent within six months;

or

- At some point within the first six months, the actual cash flow ending balance must be less than or equal to 5% of the prior year's actual disbursements.

An analysis of the cash flows forecasted by month for next fiscal year (July 2005 through June 2006) shows that the General Fund anticipates incurring a maximum deficit of $14.2 million without considering the planned $21 million borrowing. As per federal tax law regulations, this cash flow deficit coupled with 5% of the prior year's actual disbursements, or $9.7 million, will only permit a maximum TRAN's size of $23.9 million. After analysis of the timing of expected receipts and disbursements, the City Treasurer is recommending that a more conservative figure of $21 million in Notes be issued to ensure compliance with federal spend-down requirements.

cc: Rocky Fluhart, Sam Guevara, Dan Mulé, Randy Hillier, DJ Baxter

DANIEL A. MULE´
CITY TREASURER

SALT LAKE CITY CORPORATION

DEPARTMENT OF MANAGEMENT SERVICES
TREASURER

ROSS C. "ROCKY" ANDERSON
MAYOR

TO: Rocky J. Fluhart, Chief Administrative Officer

DATE: June 1, 2005

FROM: Daniel A. Mulé, City Treasurer

SUBJECT: Tax and Revenue Anticipation Notes, Series 2005 (the Tax Notes)

STAFF CONTACT: Daniel A. Mulé, City Treasurer

TELEPHONE NUMBER: 535-6411

RECOMMENDATION: That the City Council hold a discussion on June 9, 2005 and schedule the adoption of a resolution on June 14, 2005 authorizing the issuance and confirming the sale of $21 million in Tax and Revenue Anticipation Notes for fiscal year 2006.

DOCUMENT TYPE: Briefing/Discussion

BUDGET IMPACT: Current estimates provided by the City's financial advisor indicate that the City should expect a coupon of about 3.0%. Issuing $21 million in Tax Notes would translate into interest expense for the General Fund of $630,000. The Mayor's Recommended Budget includes a $750,000 budget for interest expense. Once the actual coupon is known, the budgets for interest expense and interest income will be adjusted accordingly. With the expectation of rising interest rates, locking in the yield on the Tax Notes now will likely result in an even greater spread between interest earnings and interest expense throughout the new fiscal year.

DISCUSSION: Tax Notes are short-term borrowing instruments (debt) issued for one year or less in anticipation of future tax collections. The purpose of the borrowing is to provide financial assistance to the City's General Fund during its "cash-poor" period until the major portion of property taxes are received, usually in December. The exact amount to be budgeted for interest expense will not be known until the Notes are sold on June 14, 2005 at which time the actual coupon will be determined. To assure compliance with applicable federal and state regulations, sizing restrictions are adhered to when determining an allowable principal amount, and actual cash flows relative to spend down requirements are regularly monitored to avoid rebate. Sizing restrictions allow for a maximum amount of $23.9 million of Tax Notes to be issued. However, after a prudent analysis of the timing of expected receipts and disbursements included in the Mayor's Recommended Budget, I am recommending that only $21 million of Tax Notes be issued.

H:\Treas\DansDocs\Council Cover Letters\TRAN's 2005 Briefing.doc