GFOASC 2023 FALL CONFERENCE

Current Considerations in Public Finance

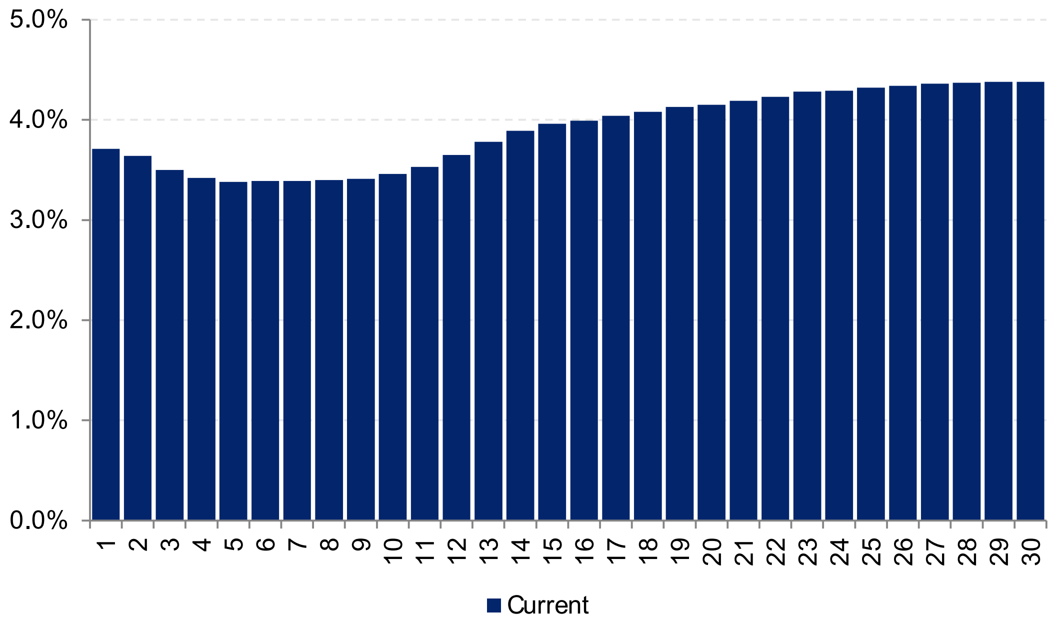
Mike Burns	Brandon Norris	David Cheatwood
Burr & Forman	Burr & Forman	First Tryon Advisors
864.271.4940	864.271.4940	704.926.2447
mburns@burr.com	bnorris@burr.com	dcheatwood@firsttryon.com

Agenda

- **Market Update**
- Rating Agency Update
- Bank vs. Public Market
- Tax Exempt Considerations
- Investment of Funds
- Continuing Disclosure

Current Tax-Exempt Yield Curve

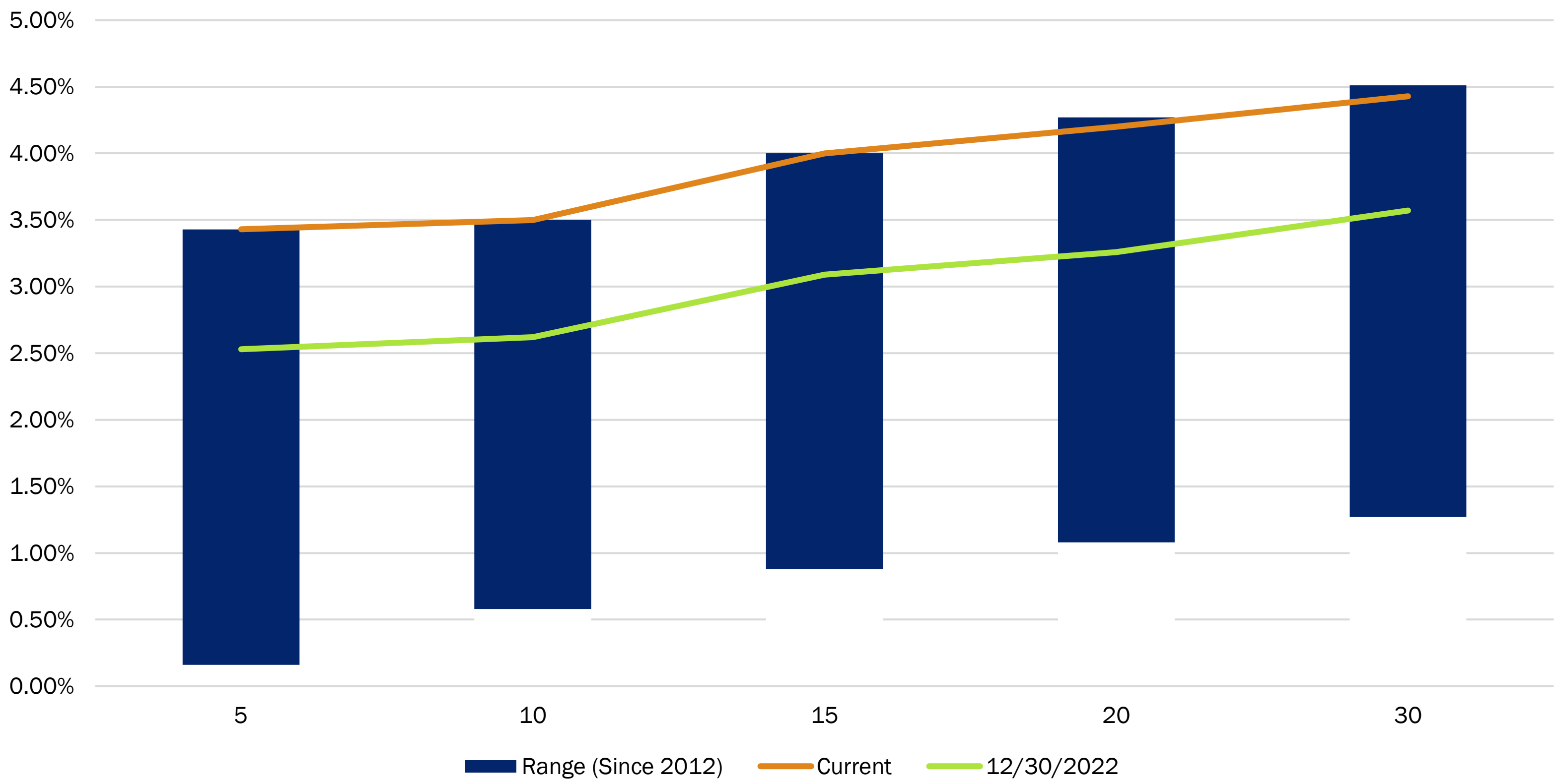
- The tax-exempt benchmark 30-year yield curve is inverted through the first 12 years.



Tenor	Current MMD	Tenor	Current MMD
1Yr	3.71%	16Yr	3.99%
2Yr	3.64%	17Yr	4.04%
3Yr	3.50%	18Yr	4.08%
4Yr	3.42%	19Yr	4.13%
5Yr	3.38%	20Yr	4.15%
6Yr	3.39%	21Yr	4.19%
7Yr	3.39%	22Yr	4.23%
8Yr	3.40%	23Yr	4.28%
9Yr	3.41%	24Yr	4.29%
10Yr	3.46%	25Yr	4.32%
11Yr	3.53%	26Yr	4.34%
12Yr	3.65%	27Yr	4.36%
13Yr	3.78%	28Yr	4.37%
14Yr	3.89%	29Yr	4.38%
15Yr	3.96%	30Yr	4.38%

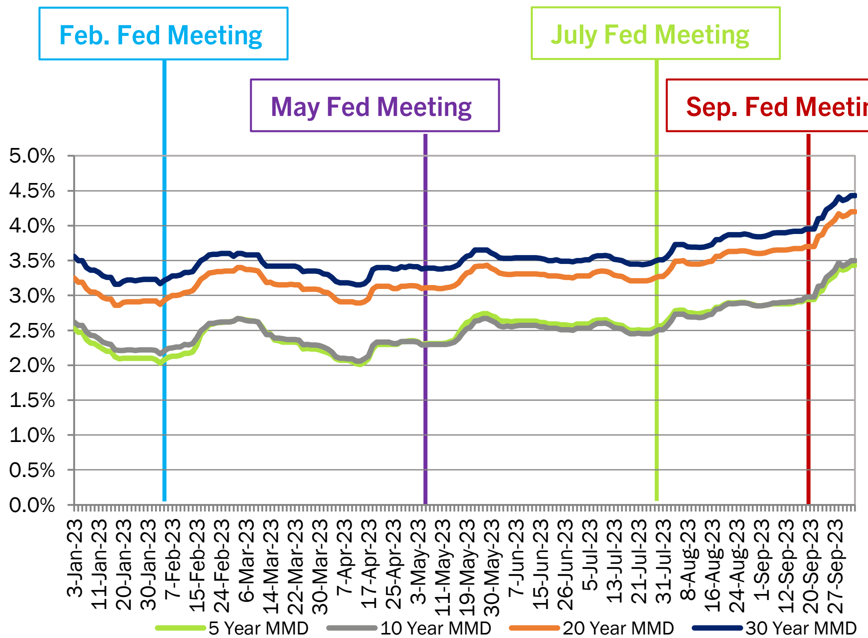
Historical Tax-Exempt Borrowing Rates

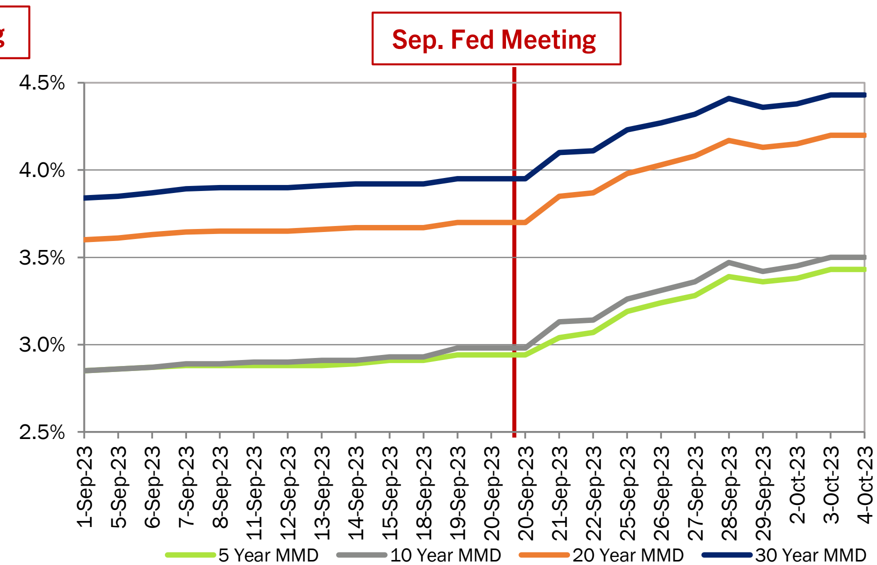
- Tax-exempt interest rates are currently at their highest levels since 2012.



Tax Exempt Borrowing Rates Since January 2023

- After an extremely volatile year in 2022, interest rates held mostly steady through July of this year.
- However, volatility returned in late summer due to economic data exceeding expectations and the Federal Reserve resuming its tightening cycle while indicating that rates will remain higher for longer.
- Since the beginning of the year, the 5-, 10-, 20-, and 30-year MMD (tax-exempt benchmark yield curve) is up approximately 85-95 basis points with 60-65 basis points of that increase coming since the beginning of September.





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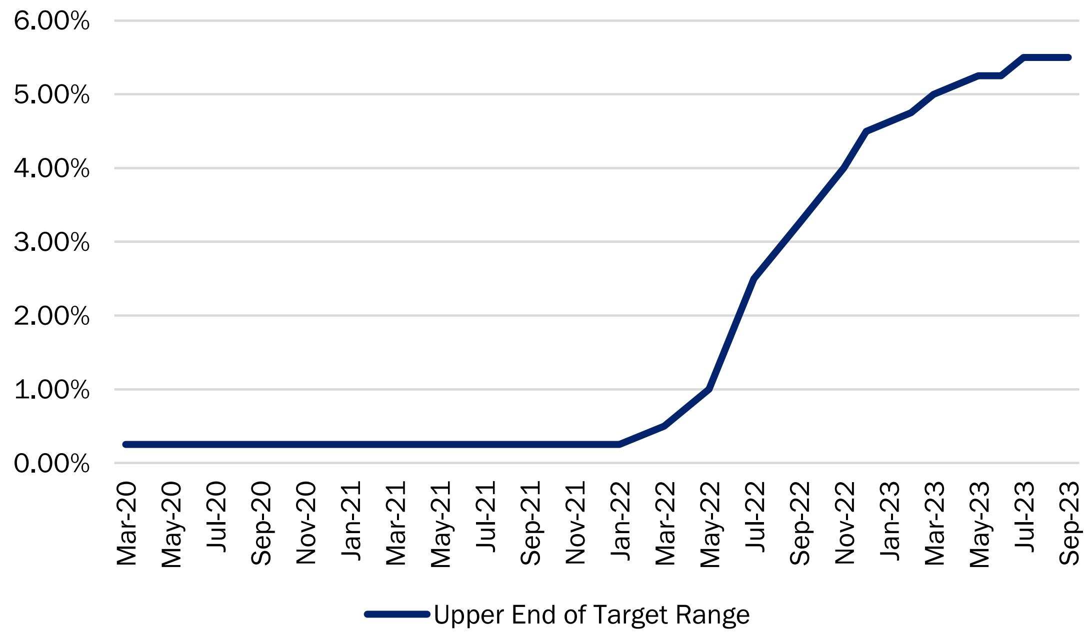
Fed Funds Rate History

- After maintaining a target range of 0.00% - 0.25% from March 2020 – January 2022, the Fed has increased the target range by 5.25% in the following increments:
    - 0.25% in March 2022;
    - 0.50% in May 2022;
    - 0.75% in each of June, July, September, and November 2022;
    - 0.50% in December 2022; and
    - 0.25% in February, March, May, and July 2023.

- The current target range of the Fed Funds rate is now 5.25% - 5.50%.



Fed Funds Rate Projections

- Based on commentary from the most recent Fed meeting on September 20th, the market is now forecasting a greater probably of an increase of 0.25% at one of the remaining two meetings in 2023.

- The market expects that the Fed Funds rate will remain at this level into mid-2024 before rate cuts totaling 0.50% - 0.75% by the end of 2024.

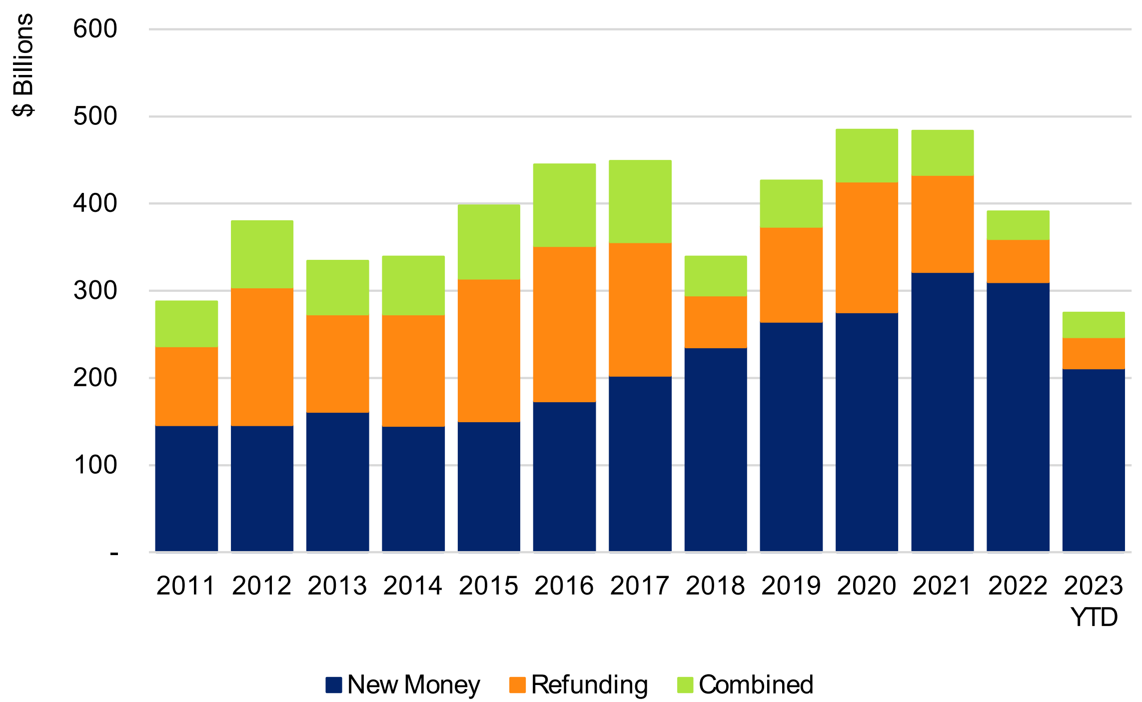
	FOMC Meeting Date									
Target Rate (Upper Bound)	1-Nov	13-Dec	31-Jan	20-Mar	1-May	12-Jun	31-Jul	18-Sep	7-Nov	18-Dec
6.25%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
6.00%	0.0%	1.6%	1.5%	1.2%	0.8%	0.4%	0.2%	0.1%	0.0%	0.0%
5.75%	9.2%	25.5%	24.2%	18.4%	12.0%	6.4%	3.0%	1.4%	0.7%	0.3%
5.50%	90.8%	72.9%	70.5%	57.2%	42.6%	27.4%	15.7%	8.5%	4.9%	2.2%
5.25%	0.0%	0.0%	3.8%	22.0%	35.2%	38.9%	32.5%	22.9%	15.7%	8.6%
5.00%	0.0%	0.0%	0.0%	1.2%	9.0%	22.0%	31.4%	32.0%	27.4%	19.7%
4.75%	0.0%	0.0%	0.0%	0.0%	0.5%	4.7%	14.4%	24.1%	28.0%	27.6%
4.50%	0.0%	0.0%	0.0%	0.0%	0.0%	0.2%	2.7%	9.4%	16.8%	24.2%
4.25%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	1.6%	5.5%	12.9%
4.00%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.9%	3.9%
3.75%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.6%

*Current Target Rate is 5.25 - 5.50%

Source: CME FedWatch Tool

Annual Issuance Volume

- After 2022 produced the lowest municipal bond issuance volume since 2018, volume is down 13% through the first 9 months of 2023 as compared to the same period in 2022 due to:
  - Federal money / grants
  - High interest rates
  - Project redesigns / deferrals due to high costs
  - No advance refundings (per tax law change at the end of 2017) and high rates reducing the number of current refunding opportunities.



Source: Bond Buyer

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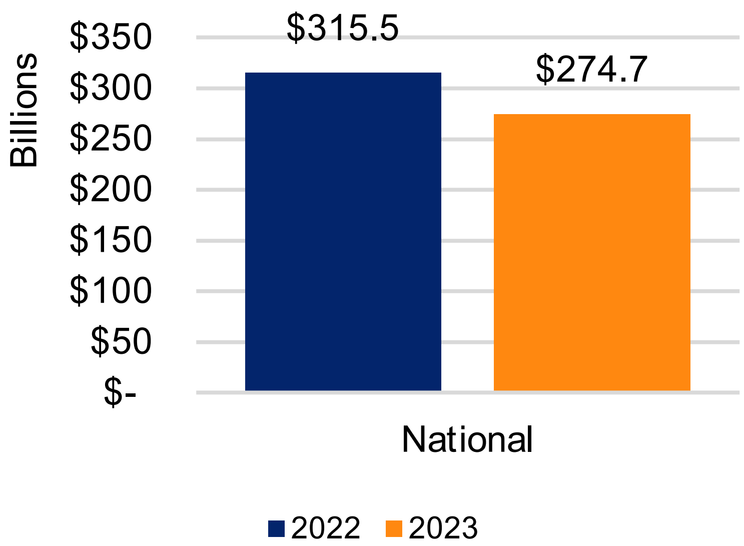
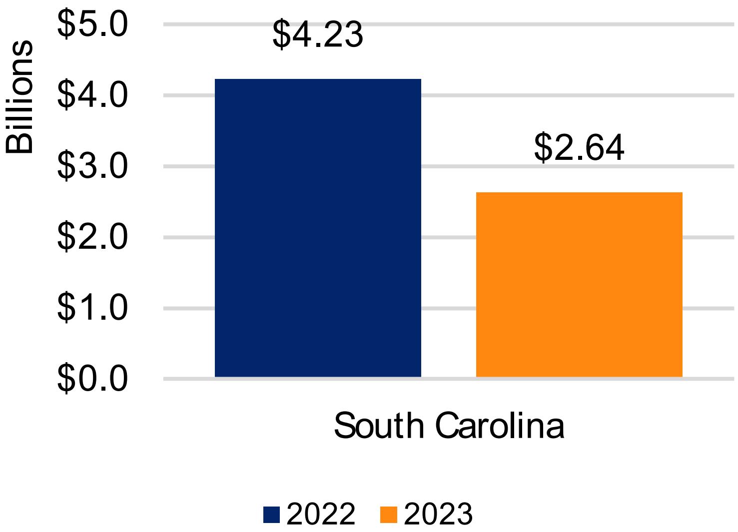
Annual Issuance Volume – National and South Carolina

- While national volume is down 13% year over year, South Carolina volume is down 38% through the first 9 months of 2023 as compared to the same period in 2022.

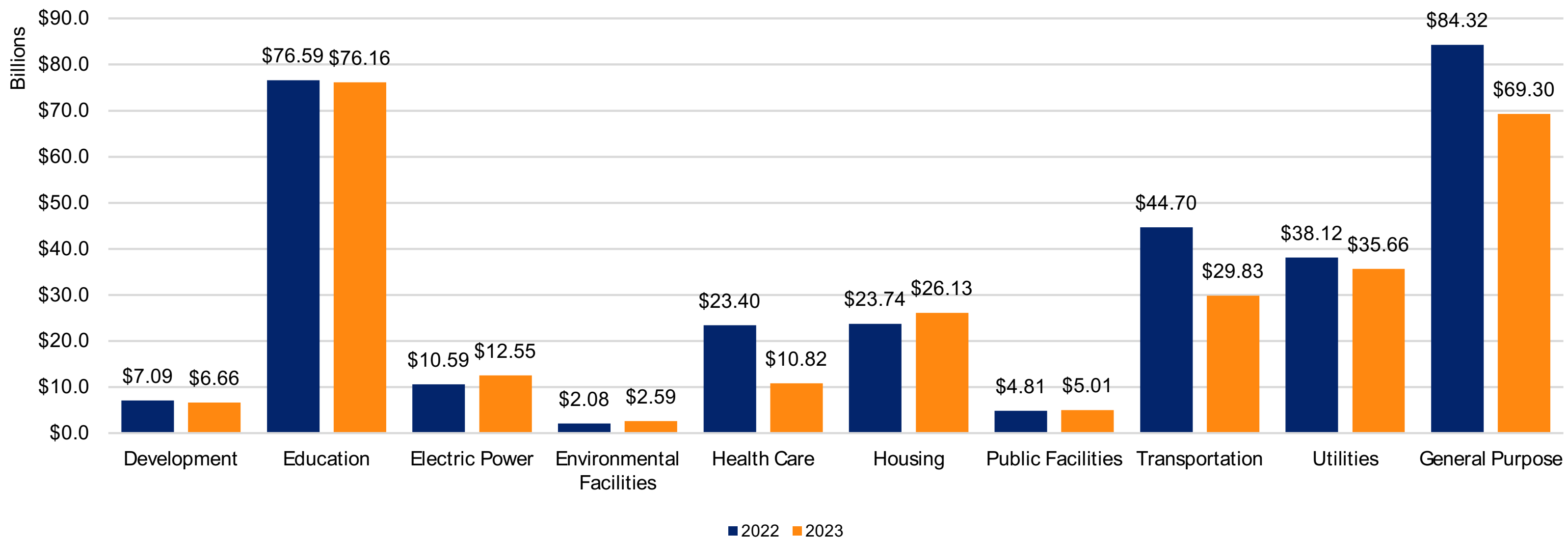




Source: Bond Buyer

Annual Issuance Volume – By Sector

- Through September 2023, the lower bond issuance volume nationwide is driven by:
  - General Purpose – Down 18% ($15.0 billion)
  - Transportation – Down 33% ($14.9 billion)
  - Healthcare – Down 54% ($12.6 billion)



Source: Bond Buyer

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Moody's Methodology

- In November 2022, Moody's released a new rating methodology for cities and counties.

- While Moody's generally maintained the same rating categories of Economy, Finances, Management, and Debt / Pensions / Leverage, the underlying components and the weighting distribution were revised.

- A few of the main revisions included:
  - Moving away from the size of an issuer's tax base to economic growth in the area (as compared to the US)
  - Moving 10% of the weighting from Management to Leverage; and
  - Assessing Financial Performance (Cash / Fund Balance) and Leverage (Debt / Pension) across all funds (governmental and enterprise) vs. focusing on just the fund or funds impacted by the proposed issuance (typically General Fund and Debt Service Fund).

- A summary of the previous methodology and the new methodology are provided on the following slide.

Moody’s Methodology

- Moody’s G.O. Scorecard Factors (as of December 2016)

Economy / Tax Base
- Tax Base Size (10%)
- Full Value Per Capita (10%)
- Wealth Levels (10%)

30%

Finances
- Fund Balance (% of Revenues) (10%)
- Fund Balance Trend (5Y Change) (5%)
- Cash Balance (% of Revenues) (10%)
- Cash Balance Trend (5Y Change) (5%)

30%

Management
- Institutional Framework (10%)
- Operating History (10%)

20%

Debt / Pensions
- Debt to Full Value (5%)
- Debt to Revenue (5%)
- Moody’s-adjusted Net Pension Liability (3Y average) to Full Value (5%)
- Moody’s-adjusted Net Pension Liability (3Y average) to Revenue (5%)

20%

- Moody’s G.O. Scorecard Factors (as of November 2022)

Economy
- Resident Income (10%)
- Full Value Per Capita (10%)
- Economic Growth (10%)

30%

Financial Performance
- Available Fund Balance Ratio (20%)
- Liquidity Ratio (10%)

30%

Institutional Framework
- Institutional Framework (10%)

10%

Leverage
- Long-term Liabilities Ratio (20%)
- Fixed Costs Ratio (10%)

30%

Fitch Methodology

- In September 2023, Fitch released a request for commentary on a proposed new methodology to rate local governments.

- The methodology seeks to provide a more scorecard-based approach to assessing credit ratings and focuses on three key rating drivers:
  - Financial Profile (38%).
  - Demographic and Economic Strength (42%).
  - Long-Term Liability Burden (20%).

- The proposed new methodology places a greater emphasis on the issuer's Demographic and Economic Strength, which hadn't been explicitly quantified under the prior methodology.

- A summary of the previous methodology and the proposed new methodology are provided on the following slide.

Fitch General Obligation Rating Criteria (April 2016)

- Fitch General Obligation Rating Criteria (April 2016)

Revenue Framework
Expectations for growth prospects for revenues

Expenditure Framework
Expectations for pace of spending growth

Long-Term Liability Burden
Expectations for affordability of liabilities

Operating Performance
Expectations for ability of revenues to support spending needs throughout economic cycles over time

- Fitch General Obligation Rating Criteria (Proposed)

Financial Profile (38%)
Financial Resilience (38%)
Revenue Volatility (Treated Asymmetrically)

Demographic & Economic Strength (42%)
Population Trend (6%)
Employment Trend (4%)
Unemployment Rate (8%)
MHI as a % of Portfolio Median (8%)
% of Population w/ Bachelor's Degree or Higher (8%)
Population Size (3.5%)
Economic Concentration (3.5%)

Long-Term Liability Burden (20%)
Liabilities (Overall) / Personal Income (8%)
Liabilities (Direct) / Governmental Revenues (4%)
Carrying Costs / Governmental Expenditures (8%)

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Marketplace to Issue Debt

- Issuers have two primary marketplaces to issue bonds – public market and bank placement.
  - Bonds sold in the public market are sold to a variety of different investors (mutual funds, insurance companies, individuals) and require the preparation of an offering / disclosure document and obtaining credit ratings.
  - Bonds sold via a direct placement are sold directly to a single bank / lender and do not require an offering / disclosure document or credit ratings.
- In addition, issuers can look to state (i.e. State Revolving Fund loans) or federal (i.e. USDA) sources if the entity and project meet their requirements.
- The appropriate marketplace for a financing depends on several factors including size, security, credit quality, desired term, interest rate and market conditions.

Public Sale vs. Bank Placement vs. SRF vs. USDA

Marketplace	Public Sale	Bank Placement	SRF	USDA
Cost of Issuance	High	Medium	Low	Low
Staff Time Commitment	High	Medium	Medium	Medium
Maximum Fixed Term Likely	40 Years	15-20 Years	20-30 Years	30-40 Years
Flexibility to Customize Repayment	High	Medium	Low	Low
Covenants	Medium	Medium	Low	Low
Credit Rating / Public Disclosure	High	Low	Low	Low
Interest Rate Risk	High	Medium	Low	Low

Pros and Cons of Bank vs. Public Market

Bank Placement		
Pros	1)	More streamlined issuance process with lower staff time commitment and the ability to lock in interest rates sooner
	2)	Lower upfront costs of issuance
	3)	Greater prepayment flexibility
	4)	No credit rating requirements
	5)	No (or limited) ongoing reporting requirements
Cons	1)	Subject to changes in interest rate / market environment
	2)	Subject to changes in banks' interest / willingness to lend

Public Sale		
Pros	1)	Large market with broad buyer base
	2)	No issue securing long-term financing (20+ years)
Cons	1)	Not able to lock in interest rate until closer to closing
	2)	More in-depth issuance process with greater staff time commitment
	3)	Higher upfront costs of issuance
	4)	More restrictive prepayment provisions (typically 10-year no prepayment option)
	5)	Ongoing reporting / continuing disclosure requirements
	6)	Initial and periodic rating agency interactions

Current Environment

- Given the sharp and continuous increase in rates over the first 10 months of 2022, many issuers "flipped" from the public market to the bank market due to:
  - Less day-to-day volatility in the bank market;
  - Lower interest rates in the bank market; and
  - Ability to lock in the interest rate earlier in the process.

- However, following the collapse of Silicon Valley Bank in March 2023 and the ensuing liquidity crunch that many banks faced, many issuers have "flipped" from the bank market to the public market due to:
  - Tightening of credit conditions by certain banks;
  - Shortening of financing terms by certain banks;
  - Higher interest rates than the public market; and
  - Heightened focus by banks on existing / prospective clients (i.e. those that come with deposits)

- The dynamic between the bank market and the public market can change quickly.

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Tax-Exempt Considerations

- GENERAL CONSIDERATIONS
  - COMPARATIVE RATE ADVANTAGE
    - BUT, CONSIDER THE LIMITATIONS AND RISKS
  - TAX-EXEMPT RULES APPLY TO BOTH PUBLIC OFFERINGS AND PRIVATE PLACEMENT DEALS
  - RULES APPLY TO ANY TYPE OF BORROWING DONE ON A FEDERAL TAX-EXEMPT BASIS
  - GENERAL OBLIGATION, REVENUE BOND, BAN, TAN, EQUIPMENT LEASE/PURCHASE, ETC.

Tax-Exempt Considerations

- REIMBURSEMENT
  - ADOPTION OF OFFICIAL INTENT
    - COVERS EXPENDITURES PAID UP TO 60 DAYS PRIOR TO ADOPTION
    - GENERALLY, REIMBURSEMENT ALLOCATION MUST BE MADE NOT LATER THAN 18 MONTHS AFTER THE LATER OF (A) THE DATE THE ORIGINAL EXPENDITURE IS PAID, OR (B) THE DATE THE PROJECT IS PLACED IN SERVICE, BUT IN NO EVENT MORE THAN 3 YEARS AFTER THE ORIGINAL EXPENDITURE IS PAID
    - OFFICIAL INTENT SHOULD DESCRIBE THE PROJECT AND MAXIMUM PRINCIPAL AMOUNT OF OBLIGATIONS EXPECTED TO BE ISSUED
    - FORM OF INTENT: RESOLUTION, LEGISLATIVE AUTHORIZATION FOR ISSUANCE, OR ACTION BY AUTHORIZED OFFICER
    - BEWARE OF INTENTS DECLARED AS A MATTER OF COURSE, OR IN AMOUNTS SUBSTANTIALLY IN EXCESS OF AMOUNT EXPECTED TO BE NECESSARY

Tax-Exempt Considerations

- REIMBURSEMENT (CONTINUED)

  - PRELIMINARY EXPENDITURES
    - ARCHITECTURAL, ENGINEERING, SURVEYING, SOIL TESTING, BOND ISSUANCE AND SIMILAR COSTS INCURRED PRIOR TO COMMENCEMENT OF ACQUISITION, CONSTRUCTION OR REHABILITATION, OTHER THAN LAND ACQUISITION, SITE PREPARATION AND SIMILAR COSTS INCIDENT TO COMMENCEMENT OF CONSTRUCTION, AND
    - MAY NOT EXCEED 20% OF ISSUE PRICE

  - DE MINIMIS
    - COSTS OF ISSUANCE, OR
    - NOT EXCEEDING THE LESSER OF $100,000 OR 5% OF PROCEEDS

Tax-Exempt Considerations

- PRIVATE USE AND PRIVATE PAYMENT/SECURITY
  - GENERALLY LIMITED TO 10% (5% FOR QUALIFIED 501(C)(3) BONDS)
  - GENERALLY, PRIVATE USE DOES NOT ARISE IN THE CASE OF USE BY THE GENERAL PUBLIC ON THE SAME BASIS AS OTHER MEMBERS OF THE GENERAL PUBLIC. HOWEVER, THERE ARE MANY ADDITIONAL RULES/EXCEPTIONS
  - ARISES IN UNEXPECTED WAYS
    - CONCESSIONS
    - MANAGEMENT CONTRACTS
    - NAMING RIGHTS
    - SPECIAL ARRANGEMENTS FOR USE (PARKING)
  - NOT EXPECTED TO SELL OR DISPOSE OF THE FINANCED PROJECTS FOR TERM OF BONDS

Tax-Exempt Considerations

- ARBITRAGE
  - WHAT IS IT?
    - GENERALLY, INVESTMENT OF BOND PROCEEDS AT A YIELD IN EXCESS OF THE YIELD ON THE BOND
    - BEWARE OF “SINGLE ISSUE” RULE
  - WHY IS IT SUCH A FOCUS OF CONCERN NOW?
    - INVERTED YIELD CURVE (RECENT)
    - INVESTMENT RATES ARE RELATIVELY HIGH

Tax-Exempt Considerations

- ARBITRAGE (CONTINUED)
  - CAN YOU EARN IT?
    - GENERALLY, PROJECT FUND PROCEEDS MUST BE SPENT WITHIN [3][5] YEARS FROM THE ISSUE DATE
    - ESCROW OR DEFEASANCE FUND (REFUNDING) – 90 DAYS (30 DAYS FOR CERTAIN SHORT-TERM OBLIGATIONS (MATURING IN 270 DAYS OR LESS))
    - COSTS OF ISSUANCE FUND – GENERALLY SAME AS PERIOD FOR PROJECT FUND OR ESCROW FUND
    - BONA FIDE DEBT SERVICE FUND – 13 MONTHS
    - DEBT SERVICE RESERVE FUND – SIZE LIMITATION ("4 R FUND")(3 PRONG TEST)
    - MINOR PORTION – LESSER OF 5% OR $100,000
    - CERTAIN OTHER FUNDS THAT ARE RESTRICTED OR PERMITTED
    - IF NOT PERMITTED, ISSUER MUST NOT INVEST AMOUNTS AT A YIELD IN EXCESS OF THE BOND YIELD (MUST BE "YIELD RESTRICTED")

Tax-Exempt Considerations

- ARBITRAGE (CONTINUED)
  - CAN YOU KEEP IT?
    - SMALL ISSUER EXCEPTION: (1) GOVERNMENTAL UNIT WITH GENERAL TAXING POWERS; (2) NOT A PRIVATE ACTIVITY BOND; (3) 95% OF PROCEEDS USED FOR LOCAL GOVERNMENTAL ACTIVITIES; AND (4) AGGREGATE PRINCIPAL AMOUNT OF TAX-EXEMPT OBLIGATIONS ISSUED DURING THE CALENDAR YEAR NOT REASONABLY EXPECTED TO EXCEED $5,000,000. POTENTIALLY INCREASED BY AS MUCH AS $10,000,000 FOR CONSTRUCTION OF PUBLIC SCHOOL FACILITIES.
    - 24 MONTH SPEND-DOWN (10%, 45%, 75%, 100%)(GENERALLY LIMITED TO CONSTRUCTION/REAL PROPERTY ISSUES: 75%)
    - 18 MONTH SPEND-DOWN (15%, 60%, 100%)(GENERALLY EQUIPMENT)
    - 6 MONTH SPEND-DOWN (100%)(AVAILABLE TO REFUNDING ISSUES)
    - DEBT SERVICE RESERVE FUND – NO
    - DEBT SERVICE FUND – YES, TO THE EXTENT IT IS A BONA FIDE DEBT SERVICE FUND (GENERALLY, MATCHES REVENUES WITH DEBT SERVICE EACH YEAR WITH A MINIMAL CARRY-OVER)
    - CERTAIN OTHER EXCEPTIONS
    - OTHERWISE, GENERALLY, EARNINGS ABOVE THE BOND YIELD MUST BE PAID TO THE U.S. TREASURY

Tax-Exempt Considerations

- ARBITRAGE (CONTINUED)

  - YIELD REDUCTION / ARBITRAGE REBATE COMPUTATION DATES – GENERALLY EVERY 5 YEARS, AND ON THE FINAL REDEMPTION OR MATURITY DATE

  - YIELD REDUCTION / ARBITRAGE REBATE PAYMENT DATES – 60 DAYS FROM COMPUTATION DATE

  - ENGAGE AN ARBITRAGE REBATE CONSULTANT!

  - RECORD KEEPING
    - RETAIN FOR AT LEAST 3 YEARS AFTER FINAL MATURITY DATE (INCLUDING REFUNDING)
    - ALL RECORDS – BOND DOCUMENTS, TRANSCRIPT, INVOICES, INVESTMENT RECORDS
    - BE PREPARED TO PROVIDE DETAILED RECORDS RELATING TO BOND PROCEEDS, INVESTMENTS, EXPENDITURES, ETC. TO THE PENNY
    - CAUTION REGARDING COMMINGLED ACCOUNTS

  - ADOPT POST-ISSUANCE TAX-COMPLIANCE POLICIES/PROCEDURES

Tax-Exempt Considerations

- IRS Tax-Exempt Bond office – increase in agents

  - October 13, 2022: "what you should expect to see is increased revenue agent presence now, but even more so in the future" – Allyson Belsome – IRS TEB Manager

  - Inflation Reduction Act: $80 billion (reduced to $60 billion) funding increase for IRS, a significant portion of which is intended for enforcement.

Tax-Exempt Considerations

- BANK QUALIFICATION
  - BANK QUALIFICATION – STILL AT $10 MILLION EACH CALENDAR YEAR DESPITE INFLATION
  - $10 MILLION SINCE 1986 (EXCEPT $30 MILLION IN 2009 AND 2010 - ARRA)
  - LEGISLATIVE PROPOSALS COME AND GO . . .

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Investment of Funds

- SC Local Government Investment Pool “LGIP”

- 6-5-10: Permitted Investments for Local Governments
  - Obligations of U.S. and its agencies, guaranteed by the U.S.
  - Certain other federal agencies
  - Certain general obligation or revenue obligations of the State or its political units
  - CDs collaterally secured by obligations of U.S. and certain agencies
  - Repurchase agreements collaterally secured by certain securities
  - Money Market Funds that invest in certain securities

- 6-5-15: Securing Deposit of Funds of Local Governments
  - Certain collateral requirements for amounts in excess of FDIC

Investment of Funds

- ARISES IN SURPRISING CONTEXTS

  - Escrow Agreements for Lease Purchase Arrangements

  - Investment vehicles for project fund, debt service fund, debt service reserve fund

  - Outside auditors will inquire

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Continuing Disclosure

- Background – Primary Market Disclosure
  - Rules 10b-5 and 15c2-12 (Securities and Exchange Act) - Require the production of an “Official Statement” for underwriters to purchase public bond offerings
  - Applies to underwriters of public bond offerings over $1M
    - SEC does not directly regulate government issuers
    - Does not relate to private placements
  - Official Statement must include “financial information or operating data”

Continuing Disclosure

- Rule 15c2-12 also imposes requirements to update or provide additional disclosure after issuance of bonds:
  - "U/W shall not purchase or sell municipal securities . . . unless . . . [the] issuer . . . has undertaken . . . in a written agreement or contract for the benefit of holders of such securities, to provide, either directly or indirectly through . . . a designated agent":
  - **Annual Report**, includes financial statements or ACFR and update to financial/statistical information and operating data in OS (usually 2/1)
  - **Listed Event Notices** (also referred to as Notice Events) within 10 business days from event

Continuing Disclosure

- Annual Report
  - An update of certain financial information and operating data from the Official Statement
  - Prepared annually until underlying bonds have matured or been redeemed or defeased

Continuing Disclosure

- Old Listed Events
  - Principal and interest payment delinquencies
  - Non-Payment related defaults, if material
  - Unscheduled draws on debt service reserves reflecting financial difficulties
  - Unscheduled draws on credit enhancements reflecting financial difficulties
  - Substitution of credit or liquidity providers, or their failure to perform
  - Adverse tax opinions, IRS notices or events affecting the tax status of the security
  - Modifications to rights of securities holders, if material
  - Bond calls, if material

Continuing Disclosure

- Old Listed Events (continued)
  - Defeasances
  - Release, substitution, or sale of property securing repayment of the securities, *if material*
  - Rating changes;
  - Tender offers
  - Bankruptcy, insolvency, receivership or similar event of the obligated person;
  - Merger, consolidation, or acquisition of the obligated person, *if material*; and
  - Appointment of a successor or additional trustee, or the change of name of a trustee, *if material*

Continuing Disclosure

- "New" Listed Events – Applicable to Continuing Disclosure Agreements executed on or after February 27, 2019

  - Incurrence of a **<u>financial obligation</u>**, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a **<u>financial obligation</u>**, any of which affect security holders, if material.

  - Default, event of acceleration, termination event, modification of terms, or other similar events under the terms of the **<u>financial obligation</u>**, any of which reflect financial difficulties.

Continuing Disclosure

- “Financial Obligation” means –
  - Debt obligations
  - Derivative instruments (swaps, caps, forwards)
  - Guarantees
  - “Debt, debt-like or debt-related”
  - Capital leases

Continuing Disclosure

- “Financial Obligation” does not mean or include:
  - Ordinary financial and operating liabilities
  - Securities for which OS is posted on EMMA
  - Monetary obligations from judicial, administrative or arbitration proceeding

- Materiality:
  - Facts and circumstances
  - Size of the loan vs. issuer
  - Source of security pledged (e.g. senior vs. subordinate)
  - Inconsistent covenants, defaults and remedies
  - Effect on credit worthiness

QUESTIONS?