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TO REFUND OR NOT TO REFUND?
(When, How and Why)

When

The refunding of existing debt often presents a beneficial economic opportunity for school districts. With multiple series of debt often outstanding, a school district is advised to know when to actively explore a refunding bond issue due to available interest rate savings. The business or finance officials of the district are advised to have a schedule of each bond issue outstanding, their respective optional call dates, their range of maturity dates and interest rates. This schedule should be updated annually so as to provide a current outlook on approaching optional redemption date opportunities.

How

As optional call dates approach, the time comes to explore possible beneficial refundings using the issuance of tax-exempt or taxable bonds. Tax-exempt rates, under prevailing federal law, may be used to refund existing debt if the settlement date of the refunding issue falls within 90 days prior to the stated optional call date. If, on the other hand, the optional call date is beyond this limitation, taxable bonds may be issued for "advance refunding" purposes. As the tax-exempt refunding is limited to the 90-day constraint, the use of taxable bonds should regularly be explored, as there is no time constraint associated with the optional call date. Although taxable rates are higher than tax-exempt rates, a judgment as to their use must often be made if market projections indicate possible higher tax-exempt rates at the time when the 90-day period becomes active.

Why

There are a number of reasons to monitor and explore the refunding of existing debt:

1. Annual debt service savings
2. Saving as cash at closing
3. Refunding with the addition of new money
4. Refunding, including a restructuring of existing debt to meet prevailing or anticipated budgeting constraints

Realizing savings as a direct result of prevailing interest rates (tax-exempt or taxable) is the most common motive for undertaking the refunding process. The desired level of present value savings is typically a number equal to or greater than 2% of the par amount of bonds being refunded, i.e., *.02 X $5,000,000 = $100,000*.

Nevertheless, 2% is not a hard-and-fast rule, but rather, a benchmark. If there is a need for new money that requires budgetary restraints, a refunding of existing debt may occur that may have only nominal or no savings. However, if restructured, the refunding allows for the inclusion of the new money requirement while maintaining the existing level of annual debt service.

Refunding options for a school district are numerous and often present opportunities that are not always discernible. It is always well advised to monitor existing debt for strategic financing opportunities.

Piper Sandler's experienced team is here to help. If you have questions about your district's situation or wish to learn more, please contact Audrey Bear at audrey.bear@psc.com or 717-412-1027.