THE BOND BUYER

Wisconsin will use Clarity system on variable-rate note issue

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Wisconsin next week will place $53.8 million of variable-rate general obligation notes that will use the Clarity Bidrate Alternative Trading System for competitive remarketing.

The issue will also mark a first for the state as it plans to provide self-liquidity. Previous issues under its various floating-rate programs have tapped banks for support.

“We are excited about this opportunity, which we’ve been exploring for a couple years,” said Wisconsin's capital finance director, David Erdman.**Brian Tumulty, The Bond Buyer**

Use of the platform has long been on state Capital Finance Director David Erdman's radar, and a series of lawsuits accusing banks and broker-dealers of widespread fraud in the variable-rate demand obligation market helped cement the decision. Wisconsin's Clarity plan was first announced in January.

"We are excited about this opportunity, which we've been exploring for a couple years," Erdman said. "The state is excited about the transparency the platform provides to the market in pricing of variable rate demand obligations. We are hoping that with the transparency interest rates will go down."

A series of lawsuits publicly revealed over the last year were filed by Minnesota-based municipal advisor Johan Rosenberg via Edelweiss Fund LLC accusing banks and broker dealers of defrauding issuers. The latest to be unsealed was a New York case. It brings damage claims to $1.6 billion across four states: New York, Illinois, California and Massachusetts.

At the heart of the accusations is that the banks "bucketed" large groups of VRDOs and set their rates en masse, without regard to the characteristics of the securities, which the complaints argue is a violation of the remarketing agreements binding those banks.

Two cities, Philadelphia and Baltimore, have also filed lawsuits in federal court leveling the same allegations as those in the Edelweiss lawsuits.

In making the switch to Clarity for the upcoming sale, Erdman said he expects fees will be in line with the use of a traditional marketing agent. The state is seeking ratings from Fitch Ratings and S&P Global Ratings on the notes.

Ohio uses the platform and Erdman said he hopes that others will join in testing the system. Siebert Cisneros Shank & Co. LLC will initially place the notes Wednesday. The first re-marketing cycle on Clarity will occur on June 5. Quarles & Brady LLP is bond counsel. Ohio also provides self-liquidity.

Clarity, a division of Arbor Research & Trading LLC, launched its first issuer deal in November 2016 when Ohio sold $32.3 million of variable-rate bonds.

Clarity promotes itself as creating "a new opportunity in the variable-rate securities market that is designed to level the playing field for issuers, investors, banks and broker-dealers. The common thread for issues pricing on Clarity is that they are priced through a competitive bid process and are traded exclusively on Clarity," the firm's website says.

The firm’s aim is to rejuvenate the variable-rate municipal market that collapsed during the 2008 financial crisis.

The decision to save on bank costs and go with self-liquidity was driven by the state’s fiscal developments. As a large and frequent issuer, the state is well-known to the market and now has “an improved liquidity position and ratings,” Erdman said. “Ten years ago our ending cash position was negative; now our ending cash position is $1.4 billion.”

In 2017, Moody’s Investors Service raised the state’s GO rating one notch to Aa1 and Fitch and Kroll Bond Rating Agency raised the state’s rating one notch to AA-plus. All assign a stable outlook. S&P rates the state at the AA level with a stable outlook.

The state’s Legislative Fiscal Bureau recently revised revenue estimates upward by $753 million through the next fiscal biennium due in large part to the tax windfall being seen by many states in response to the federal tax law changes.

In a first for the state, first-year Gov. Tony Evers announced he’s tapping a portion of the surplus to pay down $56 million of debt. Evers also wants to direct $18 million to the technical colleges system and $15 million for job training, both of which requires legislative approval.

Wisconsin Gov. Tony Evers is earmarking a portion of the state's surplus to pay down debt. **Bloomberg News**

“Once the above critical investments have been made, the governor supports transferring the ending surplus balance at the close of the fiscal year to the budget stabilization fund,” the governor’s announcement says.

Erdman said the Wisconsin Building Commission empowers his office to pay down debt early so no approval is needed. That means Evers, a Democrat, can bypass the hostile Republican-controlled legislature that is in the process of rewriting his proposed two-year budget, tossing aside his capital plan and many of his proposals to raise revenue and increase spending.

Paying down state debt early with the use of surplus revenue is a first, Erdman said. “From a credit perspective we think it’s a good move,” even though it’s a modest amount because the state is taking a “one time general fund surplus and reducing future expenditure pressures,” Erdman said.

The capital finance office intends to pay off callable and near callable debt from the state’s past scoop-and-toss debt restructurings. The early payoff carries a net present value savings of $60 million.