DISTRESSED MUNICIPAL DEBT

NEWSLETTER

JUNE 2017

PUERTO RICO UPDATE

On May 3, 2017, a petition was filed by the Financial Oversight and Management Board for Puerto Rico in the U.S District Court for the District of Puerto Rico on behalf of the Commonwealth. This action was authorized under special bankruptcy ruled created by Congress under the Puerto Rico Oversight Management and Economic Stability Act of 2016 ("PROMESA"). This represents a reset of all the negotiations which have been ongoing for a year. Those negotiations demonstrated a clear conflict among bondholders as to their priority and a clear shortfall in what resources the island has available to meet its debts and continue to function for its populace. Added to this are the estimated $49 billion in unfunded pension claims where the situation is so dire that there will not even be enough assets in the fund to meet current payments in another two years. It is a situation where those who struck a deal with the island today would probably leave nothing for later claimants. In short, it needs the discipline of a bankruptcy structure in order to achieve any equity in a global settlement.

The filing promises to extend out the time period for achieving any agreement since the magnitude of the problems is staggering. Over $125 billion in claims are at stake from a populace that has shrunk from over 6 million when much of this debt was incurred to only some 3 million today. And as you can guess, the poorest component is not the one that shrank. While bonds have been trading over the last year based on some anticipation of what a settlement might be and a perception of how strong a collateral claim each issue had, much of this must now be reconsidered and in a much longer time frame. Bondholder reliance of revenue pledges will probably receive no more respect than the full faith and credit pledges which used to define general obligations. In addition, unless the government of the island is allowed to provide some hope for its residents, the population and economic decline will accelerate leaving a bankruptcy settlement a hollow commitment. It was the Wall Street Bankers, not the islands politicians, who were expected to be the adults in the room. Their failure to stop what was a kind of Ponzi scheme will harm mainly investors and taxpayers. It is a lesson we need to take to heart since there are many similar situations building up in the municipal universe making this once safe haven into a casino.

DEFAULT SUMMARY BY YEAR

		2000/2004	2005/2009	2010/2014	2015	2016	2017
TOTAL	#	595	511	381	59	47	13
DEFAULTS	$(000)	9,935,734	20,990,190	22,124,084	75,022,501	946,655	226,150
INSURED DEFAULTS	$(000)	666,262	2,125,902	2,116,110	8,358,853	6,570	36,405
SETTLED DEFAULTS*	$(000)	8,429,677	13,479,632	13,702,546	886,903	89,410	40,450
DISTRESSED ISSUES	#	32	116	216	20	16	12
	$(000)	453,880	2,442,058	28,369,704	697,094	226,265	345,784

*Not Insured

DEFAULT UPDATES

ACCOMACK CNTRY VA IDA HLTHCARE FACS - AMERICAN FAMILY SERVICES

American Family Services, Inc. (“AFS”) is a Louisiana not-for-profit corporation which was formed to acquire and own a 60-bed nursing facility currently operating as Arcadia Nursing & Rehabilitation Center (“Arcadia”) and to construct and own a 42-bed assisted living facility currently operating as Quail Run (“Quail Run”). The facilities are located on a common site in Nelsonia, Virginia. AFS has suffered losses from operations from its inception and as of December 31, 2015, has an accumulated deficit of· approximately $4,625,000 which is greater than the amount of bonds outstanding. Management has been monitoring the situation noting that the driving factors were poor census levels and the payor mix of the census in place.

The trustee for the $4.565 million bond went to court on March 22, 2017 to seek injunctive relief and seek the appointment of a trustee to take over the administration of this medical clinic run by American Family Services Inc, the not for profit originator of this 2007 bond issue. Their request was granted on April 14, 2017 and subsequently, the trustee was given a $60,000 advance from bondholder funds out of the debt service reserve to cover expenses necessary for ongoing operations. What’s unusual here is that the trustee claims to have notified bondholders previously that the bonds were in default, but no such filing appears with the MSRB on the EMMA site. The bonds have been trading in a range of 45 cents on the dollar as far back as 2007 and as low as 1 cent to 11 cents in 2017. CUSIP 004341AX1

BURLINGTON CNTY NJ BRIDGE COMM ECON DEV - THE EVERGREEN PROJ

This $44.5 million issue financed a non-profit retirement facility in New Jersey. The facility was notified by the trustee that it failed to meet its debt service coverage ration requirement of 1.2o, achieving only a level of 0.85. The operator has been actively searching for a strategic partner in order to improve operations and restructure its debt. It has identified such a partner, ACTS Retirement-Life Communities, Inc., a large non-profit , multi-state operator. It is not known at this time whether a merger would result in any negative impact on the bonds, however, the bonds traded at a price of 100 on May 4, 2017 indicating a confidence that there will be little change. CUSIP 121649AA5

CITY CENTER CMMTY DEV DIST POLK CNTY FLA

This Florida Community Development District defaulted in May 2009 on some $30.1 million in two bonds issued in 2005 and 2007. The CDD was originally approved as a theme park for Barnum and Bailey Circus which could not compete with the nearby Disney park. It subsequently became the spring training facility for the Kansas City Royals. They left in 2002 when their lease expired. The property owners became Coleridge Corp. with 235 acres and the estate of Victor Posner with 132 acres. Caught up in the 2007 real estate collapse, the developer got into litigation and eventually filed bankruptcy in 2014. As a result of the bankruptcy, the property was put up for auction and the District gained ownership and control. Since the collateral properties were distinct, a second series of bonds were issued in 2015 with a separate income stream. Operations are still not producing any income for bondholders as per the latest trustee’s report which reported that the May 2017 interest and principal payments would not be made. The bonds have not traded since 2011. CUSIP 17776NAA3

CLARK CNTY NV ECON DEV BOND BISHOP GORMAN HIGH SCHOOL PROJ

This $25 million bond issue is guaranteed by the Bank of America through a letter of credit. The developer of the project got into a dispute with the construction company doing the project and filed for bankruptcy to prevent an asset seizure. Bank of America is negotiating an agreement with the construction company to facilitate a settlement, but meanwhile is obligated to continue the debt service. Bondholders are secure and, since the bonds are monthly pay at market rates, trade at par. CUSIP 180858BP6

DARDENNE TOWN SQUARE TRANSPORT SALES TAX

This $17.6 million sales tax bond was issued in 2006 with a 5.00% coupon. Bond proceeds were used to fund transportation infrastructure improvement in the Dardenne Town Square area, such as road construction and improvements. The bond service is to be collected from sales tax collected on the businesses in the project area. The bond initially defaulted on November 2, 2009, when a draw on reserve funds of $174,709 was made to help make the debt service payment. The bonds next event of default occurred on November 2011 when a draw on reserve funds of $146,983 was needed to make debt service, the left $539,885 in reserve funds. The reserve funds have been depleted and November 1, 2013 interest payment of $412,500 was not made in full. Since that time, no further interest or principal payments have been made up to the May 1, 2017 scheduled interest and principal payments. The bonds last traded at 16 on December 12, 2016. CUSIP 23719TAC4

DOUGLAS CNTY NB SANITARY & IMPROV DIST DISTRICT # 544 NEWPORT HILL

This is the latest Nebraska sanitation district to default on the terms of its warrants and negotiate a new set of terms. I suspect in most of these cases, the warrant holders are local banks who use warrants instead of making loans since the income is then tax free to them. In this case the $4.045 million in, 7% warrants due 4/7/2016 were refinanced at the same rate of interest, but with the maturity now extended to December 31, 2037. The warrants also allow for interest to be paid with more warrants if needed. No CUSIPS.

EVELETH MN MFAMILY REV MANOR HOUSE & WOODLAND PRJ

This $9.2 million assisted living and memory care facility bond was issued in 2006 with a 5.7% coupon. The project changed management companies in June 2011. The new management applied for state coverage of its eligible residents. However, because of state budget disputes the company did not receive compensation for its residents. The bond became distressed when the October 1, 2011 debt service required a draw of $157,723 from the reserve fund. The management anticipates that when the state can review its application the arrearage can be made up. However, it turns out the problems of this project go deeper than a temporary halt in payments from the state. The bond began missing payments a year later. After drawing down reserve funds, the bond went into payment default on all three series of bonds. The October 1, 2016 debt service payment was not made. Since then interest and principal payments have been missed through April 1k 2017. The trustee reported that the project is earning enough only to pay operating costs but not debt service. They hope to fill the facility to capacity since its current partial occupancy situation makes the facility hard to sell at a fair value. The bond last traded at 40 on April 10, 2017. CUSIP 299725BZ

ILLINOIS FINANCE AUTHORITY GREENFIELDS OF GENEVA PJ

This continuous care facility retirement center was financed in 2010 with $100 million of unrated securities with an 8.25% coupon. Since interest rates for rated munis were going for 4%, one would suspect that trouble was anticipated. For its last two years, the project lost $12 million on revenues of $15 million. The trustee went through two forbearance agreements while it sought a buyer for the facility. Such a buyer was found, albeit at a price of $52.8 million which amounts to about 52 cents on the dollar. To effect the sale, a bankruptcy filing was made on April 20, 2017 and a public auction was scheduled with the only known buyer acting as a stalking horse bidder for a fee of $750,000. The market seems to think that no higher bid is in the offing since the last trade of the bonds was Feb. 24, 2017 at a price of 51.79. CUSIP 45200F5M7

INDIANAPOLIS IND MULTIFM HSNG STONEKEY APTS PROJ-A

This $6.2 million housing project operates under a housing assistance agreement with the Department of Housing and Urban Development (HUD). On August 19, 2016 HUD notified the project that it was not maintaining the project at a level in compliance with the requirements under their HAP contract. The authority did not notify the trustee until January 26, 2017 of this violation, or well past the date for remedying the situation. The trustee considered this a default under the indenture, but has not accelerated the bonds for now. HUD is giving the authority additional time to remedy the deficiencies, but it is not known whether they will be able to comply. A failure to do so may result in an acceleration of the bonds which would then be redeemed under agreement with HUD. This may well only be a ploy to allow the retirement of a 7% bond in order to refinance the project at a lower rate and with additional funds to fix things up. We should know soon. Bonds are trading between 98 and 102 and are vulnerable to being called in shortly. CUSIP 45528TAK0

MAGNOLIA CREEK CMNTY DEV DIST WALTON CNTY FLA

This $21.6 million community development district bond (CDD) was issued in 2007 with a 5.60% coupon. The district manager advised in April 2009 that the district has not received all assessments due and payable because of delinquent assessments. The bond defaulted when the November 2009, interest payment required a draw of $64,943 on reserve funds. No further debt service payments have been made on the bonds since then. In a notice dated April 10, 2017, the reporting service for the district advised that foreclosure proceedings have begun against the arreared properties. Bonds have not traded since issuance. CUSIP 559597AB5

OKLAHOMA HSG. FIN AGENCY REV GO YE VILLAGE PROJECT

This $13.3 million housing bond was issued in 1985 with a 10.25% coupon. Go Ye Village, Inc. is a Christian based continuum of care retirement community ("CCRC") founded in late 1971 in Tahlequah, Oklahoma. Initially designed as an offshoot of Go Ye Missions, part of the facility is located on land that operated as a dairy farm belonging to the grandparents of renowned evangelist, Dr. Billy Graham. Over one-third of the almost 300 residents at Go Ye Village are retired North American and international missionaries, or retired employees of over a dozen different mission sending organizations. Bondholders have allowed a deferral of interest payments and a forbearance of default remedies since defaults commenced in 1989 in order to ensure that some payments continue to be made. Trustee did not exercise default remedies as long as further events of default occur. This was agreed to in 1994. Since then then a series of continuing forbearance agreements have come and gone and come again. On February 26, 2014 the trustee reported the latest forbearance agreement was implemented and was to last two years.

On December 1, 2015 the trustee announced that the December 1, 2015 payment of principal and interest was not made. On December 3, 2015 the trustee announced that the obligor has filed for bankruptcy protection. The petition was filed in the Bankruptcy Court for the Eastern District of Oklahoma in Case Number 15-81287. Go Ye Village operated at a deficit for twenty-two of the twenty-five most recent years for which audits are available. To fund deficit operations, management borrowed in excess of $21 million, seventy percent of which came from Residents and deferred Residents. The balance was loaned by non-Residents. Go Ye Village paid annual interest rates of five to seven percent on the borrowed funds. Over the previous twenty-five years, interest payments consumed 22-33% of the annual operating budget of Go Ye Village. Due to the perpetual deficit, proactive maintenance work was non-existent and on-going maintenance needs were barely met. The deferred maintenance needs at the Village now exceed $4.3 million. Prior to Chapter 11 filing, 26% of all independent living units were not occupied by Residents due to being uninhabitable or being in use for offices and storage.

A settlement plan has been prepared and is to be voted on by all creditors. The plan calls for bondholders to receive the balance of their outstanding principal of $8,247000 and interest of $2,420,000, but to be paid from future cash flow. A retirement of most of the bondholder claim is expected through obtaining a $5 million thirty year loan. This leaves some uncertainty of when full recovery can be expected. A hearing has been scheduled for July 26, 2017 to confirm a final settlement. Prior to the settlement disclosure the bonds were trading in the 70 range. Following the plan proposal the bonds last traded at 48 on April 17, 2017. CUSIP 678865BX3

PARKWAY EAST MS PUBLIC IMPT DST SPECIAL ASSESSMENT

This $30.7 million public improvement bond was issued in 2005 with a 4.625% coupon. The trustee reported an event of default on May 2, 2012. Specifically, the full principal payment due on May 1, 2012 was not made. The trustee reported that several landowners in the district failed to pay special assessments resulting in a substantial shortfall in the pledged revenues, which secure the bonds. The county has provided funds to cover the shortfall on the series 2005 bonds, however, subsequent shortfalls were not covered leading to a draw on the bond insurance policy with Radian (now a part of Assured Guaranty Corp). This lead to a lawsuit against Madison County the guarantor, which motion to compel the count to pay up was granted. The bonds trade at par. CUSIP 701555AL8

PHOENIX AZ IDA YUMA ASSISTED LIVING PROJ

This $11.7 million assisted living project issue was launched in 2014 with local management support. Things apparently did not go well and in October, the trustee advised that it had to invade a $904,000 debt service reserve to make the November 1, 2016 interest payment. The shocker, however, was a letter from the project manager and developer advising that they have decided to close the facility and transfer out all the residents. There was no indication why such a relatively new facility should cease operations so quickly. In response to the closing, the trustee went into the Arizona State Superior Court and obtained an order appointing a trustee to take control of the facility. The receiver is now operating the facility, but the trustee is required to fund a cash shortfall in op0erations. The latest draw on the debt service reserve fund for this purpose was for $58,000 on April 17,

2017. The bonds traded at 20 on May 3, 2017. CUSIP 718903RL3

PHILADELPHIA HOSP & HIGHER EDUC FAC AUTH NORTH PHILADELPHIA HLTH SYS

This FHA insured hospital bond filed for Chapter 11bankruptcy December 30, 2016 with a bond balance of $25.5 million outstanding. As a result, the January interest and principal payments were not made. In addition, certain properties of the hospital were sold and title of the property passed to the control of the trustee. At present, the trustee is planning to make the January interest and principal payments in July along with $8.75 million of proceeds from asset sales. It appears that FHA will refinance the facility for a new owner and bondholders will be taken out at their full value. No details on the cause of the filing were given. The bonds traded in October 2016 at par. CUSIP 717903YQ5

PIMA CNTY AZ IDA EDUCATION FAC PARK VIEW SCHOOL PROJ

This $7.62 million bond financed a charter school in Pima County Arizona. The bonds were issued in April, 2016 and notified the trustee in April 2017 that they would not have sufficient cash to make the July 1, 2017 interest payment. In a direct appeal to bondholders, the new school administration is asking bondholders to agree to a two year deferral of interest payments or sooner if the enrollment reaches 300 and with a 2% interest payment policy if it reaches 225. The current enrollment is 173. They are hopeful given that a nearby charter high school is closing at the end of this school year. We note that charter schools seems to be a troubled industry in Arizona with several recent defaults. The bonds traded as low as 16 in March of this year and recovered to 81 in May after the plan became known. Just noting in case you thought you couldn't make money in muni defaults. CUSIP 72177MRE9

SUFFOLK NY TOBACCO ASSET SECURITIZATION TOBACCO SETTLEMENT FUND

The Suffolk Tobacco Asset Securitization Corporation has advised it will have to draw $3.26 million from the LIquididty Reserve Account to make the $7.7 million December 1, 2017 interest payment on this bond issue. The reason given was insufficient pledged tobacco settlement revenues received in April 2014 under the Master Settlement Agreement with the tobacco companies. This leaves a balance of $15.5 million in the reserve account for future draws. This type of problem has so far affected 8 issuers on a total of $26.2 billion dollars which are in distress. Note that the total for all tobacco bonds is over $100 billion, so we may have a way to go, but time is working against a favorable outcome. Nevertheless, bonds traded at 106 for $2 million on April 7, 2017. This is not unlike the profile for Puerto Rico where the likely outcome was clear, but the signs were ignored. CUSIP 864809AM0

TOLOMATO FLA CMNTY DEV DIST FORMERLY SPLIT PINES CDD

This $32 million bond issue was issued in May 20, 2007 just as the Florida housing market suffered its steepest decline ever. In May 2015, after eight years of struggle, bondholders were convinced to accept a new series of bonds with better terms and longer maturities based on anticipated cash flows. It did not take long before it was apparent this did not resolve the problem since no interest payments have been made since May 2015. This appears to be a closely held issue since 100% of bondholders have consented to the non-payment and no default has been declared by the trustee. CUSIP 889560AF5

370 MO BOTTOM ROAD TAUSSIG ROAD TRANSPRTN DEV DIST

This $39.4 million Missouri bond was issued in 2002 to build a road interchange and create a development district in the city of Hazelwood Missouri. It began having payment problems in 2012 when the debt service reserve was invaded to make the interest payments. In its latest financial report for the year 2015, it shows sales tax and other tax revenues of $1.6 million (down from $2.2 million in 2014) versus an expense level of $3.8 million a year. In 2014 the shortfall was made up with a $1.3 million special assessment, but this declined to $368 thousand in 2015. Given their cash position, the district may run into difficulty in a year or two, depending on debt maturities and an economic turnaround for the district. The issue has been upgraded to payment default following the May 1, 2017 failure to redeem bonds then coming due. The bonds have not traded since issuance. CUSIP 88575UAL7

VILLA VIZCAYA CMNTY DEV DIST SPECIAL ASSMT

This $9.27 million community development bond was issued in 2007 with a 5.35% coupon and a maturity of 2017.

Proceeds of the issue were used, in part, to acquire and construct certain roadway improvements, storm water management facilities, water and wastewater facilities and related improvements. The trustee reported an event of default occurred when the May 2010 interest payment required a draw on reserve funds. The November 2010 interest payment was missed and the bonds haven't made a payment since. The latest missed payment occurred on May 1, 2017. Principal payments have been missed since May 3, 2010. The bonds have not traded on the secondary market since they were issued. Cusip 92704QAB4

WASHINGTON CNTY ARK IMPT DIST DISTRICT 14 SADDLE BROOK

This $3.9 million development district bond first defaulted on February 1, 2013 when there were insufficient funds to make the interest and principal payments then due. The trustee advised the debt service reserve had been depleted albeit with no previous notice that previous payments had been made from reserves. On May 23, 2007 the district filed for Chapter 9 bankruptcy. After a long process, bondholders were offered a plan on November 11, 2016 whereby they were given two choices. The first choice was to receive new 30 year bonds bearing interest at 0.5% equal to 53% of the face value of their old bonds. The alternative was to receive a cash payment equal to 22% of the face value of their old bonds. The cash was to come from James P Knight who was taking over the district development role. Since this plan was being voted on 9 years after the bankruptcy was filed, only 22% of the bondholders bothered to vote, hence they received the new bonds. The bonds will have specific lots assigned as collateral and the proceeds from the sale of such lots will be used to retire them. A new series D bond was also created to provide the funding for property taxes while the lot sales is conducted. Hence, the total amount of new debt will be about equal to the old balance. The plan was approved April 14, 2017 but notice was not received by the MSRB until May 1, 2017. The bonds last traded at a price of 8 on February 27, 2017. CUSIP 93754TAB5

WESTSIDE CMNTY DEV DISTRICT OSCEOLA CNTY FLA

This $35 million Community Development District has been in default since 2009 and involved in litigation with the developer. In the latest advisory from the attorneys, the district will begin foreclosure proceedings if arrearages are not remedied by May 1, 2017. The bonds have not traded since issuance. CUSIP 96149TAB2

HARRISBURG REDEV AUTHORITY DAUPHIN CNTY PENN

Harrisburg added to its list of defaulted issues with this zero coupon bond which came due May 1, 2017. The Authority drew on the debt service reserve for $440,000 of the bonds which came djue and the city of Harrisburg came up with $500,000 as per a Settlement Agreement called the Harrisburg Strong Plan. Assured Guaranty Municipal Corportion is the insurer of the bond, so they may be the eventual loser. CUSIP 414763BU5

LARGEST DISTRESSED ISSUES

Issuer	Project	$ Amount (Millions)
Golden State CA	Tobacco Settlment	11,398
Buckeye OH	Tobacco Settlment	5,531
Tobacco Settlement New Jersey		3,622
Tobacco Settlement Virgina		1,149
Rhode Island Tobacco		800

LARGEST UNSETTLED DEFAULTS

Issuer	Project	$ Amount (Millions)
Puerto Rico	Var Gov	63,500
Puerto Rico	PREPA	8,500
Mashantucket Wstrn	Pequot Tribe CT	2,200
Louisiana	Pub Facs La Pellets	393
NY City IDA	Brookly Navy Yard	307
Lombard IL	Public Facs Corp	246

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