

WILKES-BARRE CITY

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PENNSYLVANIA

Statement of Mayor Thomas M. Leighton, City of Wilkes-Barre, before the House Financial Services Capital Markets, Insurance, and Government Sponsored Enterprises Subcommittee

Introduction

Chairman Kanjorski and members of the House Financial Services Capital Markets, Insurance, and Government Sponsored Enterprises Subcommittee, thank you for the opportunity to testify today on the need to find a solution to the turmoil in the bond insurance industry.

My name is Thomas M. Leighton and I am the Mayor of the City of Wilkes-Barre, a city in Northeastern Pennsylvania. I am a constituent of Chairman Kanjorski, who has been a leader in economic development issues. I would like to thank Chairman Kanjorski for inviting me here today and commend him for taking the initiative on this very important issue.

Wilkes-Barre is the urban core and seat of Luzerne County, welcoming nearly 100,000 people to our city each day. We have the 4th largest downtown workforce in Pennsylvania, but this number drastically decreases after the 9-5 rush. We face significant challenges providing municipal services for this

substantial workforce because only 45,000 residents contribute to the city's tax base.

In addition, our city is home to many nonprofits, including 2 hospitals, 2 colleges and the regional headquarters of many large organizations. These community assets contribute to the outstanding quality of life in Northeastern Pennsylvania, but are, unfortunately, nontaxable entities.

Upon taking office in 2004, my administration was faced with over \$10 million in unpaid bills and a technical bond default by one of the city's authorities. Because of this default in 2002, the city could not utilize traditional bank financing because of our weak credit standing. These circumstances, combined with inherent regional economics, created a bleak financial outlook for the city.

After working diligently to reestablish the city's finances and maintain our fiscal responsibility, AMBAC Financial Group agreed to insure \$40 million of debt restructuring and new money. Without AMBAC's willingness to help the city, major layoffs or tax increases would have been necessary. AMBAC's confidence in the city's future gave us the opportunity to access the marketplace, allowing the city continue on our path to a solid financial future.

Despite making great strides financially, the City of Wilkes-Barre still struggles to obtain bond insurance, especially at competitive rates. As a

result, turmoil in the municipal bond market is a significant concern for the City of Wilkes-Barre. Similar to many other mid-sized cities across the nation, we rely on the monolines. When they are faced with volatility in the market, there is inevitably volatility for us.

Many small issuers, such as the City of Wilkes-Barre, are dependent on credit enhancements. Without them, we cannot access much-needed capital for public projects, such as road paving, sewer repairs and other infrastructure improvements. As we work to reinvigorate our city, cutbacks in basic services like these are not an option.

Turmoil in the Marketplace, Struggles in Wilkes-Barre

Currently, the economic climate in Wilkes-Barre is weakening due to growing expenditures and declining revenues. For example, the subprime mortgage crisis has resulted in an increase in the number of foreclosures, removing properties from the tax rolls. As homeowners in the City of Wilkes-Barre strain to make ends meet, we see an increased need for services which can not easily be met due to lower revenues and budget challenges. Wilkes-Barre is not alone in this struggle. Mid-sized governments in Pennsylvania, and around the country, are forced to turn to the debt market to avoid raising taxes, but are unable to do so because of instability in the market.

The City of Wilkes-Barre currently has a BBB credit rating. We are faced with \$65 million in outstanding bonds and notes, \$43 million of which are AMBAC

insured. All past issuances must have a credit enhancement in order to be attractive to investors. While some governments across the country have been adversely affected by the disruptions in the insured variable rate markets, Wilkes-Barre is extremely fortunate that our variable rate debt is enhanced by a letter of credit from PNC Bank, which has not been affected by the subprime crisis.

Included in the City of Wilkes-Barre's 2008 plan are issuances for \$4 million in refunding to fill budget gaps and \$5 million in economic development for the Coal Street Park Renovation Project. Coal Street's renovation will transform a blighted park, situated along a gateway to our downtown, into the region's premier recreational facility. The park will include ice hockey rinks, playgrounds and athletic fields. The effects of this project will be far-reaching, removing an eyesore from the city, injecting new energy into the community and bolstering pride in the City of Wilkes-Barre. With a renovated Coal Street Park, both permanent residents and first-time visitors will experience Wilkes-Barre in a very different, yet very positive, way. Under the current market conditions, this necessary development will be extremely difficult for the City of Wilkes-Barre to complete.

In addition to this venture, the City of Wilkes-Barre will continue to maintain and improve its aging infrastructure. For example, work on the remaining two bridges that span Solomons Creek will be completed. The area surrounding the creek is prone to severe flooding, devastating thousands of

residents and an area hospital three times in the past four years. We will also continue paving roads, repairing catch basins and reconstructing sewer systems to improve the quality of life for our residents. In order to meet these basic needs of our residents, we must be able to access affordable bond insurance.

Turmoil in the Marketplace, Struggles Around the Country

Similar to the marketplace conditions facing Wilkes-Barre, state and local governments across the country are also seeing increased bond issuance costs due to market disruption and are finding it difficult to enter the market as they had planned to in 2008. This is due, in part, to the inability to access affordable bond insurance. Many governments – especially small governments - need to purchase insurance either because their own rating is relative low or because they are an infrequent issuer, often without their own credit rating, and secure bond insurance to attract investors. Thus, the predicament Wilkes-Barre and other governments face in this climate are significantly higher issuance costs than what were expected, or postponing projects altogether – the latter choice being, of course, anti-stimulative.

Additionally, many governments with insured debt with rates that are reset on a short-term basis, are experiencing immediate and substantial increases in interest costs due to declining investors' interest in insured bonds¹. In the case of auction rate debt, when the short term debt is 'reset' (which can be

¹ "Bond Insurance Turns Toxic for Cities, Colleges as Rates Soar," Bloomberg News, 2/11/08.

on a daily, 7-21-28 day, or longer basis) and there are not enough buyers, interest rates are set at a “failed auction rate” or maximum rate that is much higher than the rate which was anticipated when the debt was issued. This is an unexpected cost to many governments, who have to absorb the extra costs nonetheless.

It is very important to note that while these current market conditions are impacting budgets and project financings, these disruptions are not caused by the underlying governmental credits that have been insured. For over 100 years, the municipal bond market has proved to be the best and most efficient way for our country to provide schools, roads, hospitals, and vital infrastructure to its citizens. Indeed, in 2007, a record \$427 billion in bonds were issued.² This market allows infrastructure and service-needs decision making at the level closest to its citizens – state and local governments.

Although it is a fragmented market with tens of thousands of governmental entities issuing tax-exempt debt, historically, investors’ appetite for municipal bonds has remained high with a majority of municipal bonds held by households, including money market mutual funds holdings.³ Investors buy and hold these bonds, knowing that they are one of the safest instruments available, and many of the underlying credits are backed by the full faith and credit of the governmental entity.⁴ With half of the municipal bond market being insured, it allows investors a more streamlined way of making an

² *Volume at a Record \$427.6 Billion* (2007), The Bond Buyer, 1/2/08.

³ *Flow of Funds Accounts of the United States*, Board of Governors of the Federal Reserve System, 12/6/07, page 44.

⁴ Mark Lackritz, “For investors, municipal bonds have an impressive record of safety with a default rate of less than a 0.1% over the past 37 years.” 7/26/2007

investment, without having to research each particular bond issuance. Thus, finding a way to stabilize the current market conditions and to enable affordable access to bond insurance is vital for continued state and local government growth in the years ahead.

As Congress, the Federal Government, regulators and the marketplace look to find ways to solve the problems in the municipal bond marketplace, one helpful piece of legislation is H.R. 2091, which would allow bonds guaranteed by the Federal Home Loan Banks to be treated as tax exempt bonds.

In essence, this legislation would change the tax code and allow Federal Home Loan member banks to offer letters of credit to communities like Wilkes-Barre, thus providing access to another AAA financial guarantee source, which will help lower borrowing costs for governments across the country. Chairperson Kanjorski, we want to thank you for supporting this helpful legislation.

Conclusion

The City of Wilkes-Barre is undergoing a comprehensive social and economic revitalization. Without access to capital, we will be unable to continue the progress that we have worked so hard to accomplish over the past four years. We will be forced to halt work on major projects, such as the Coal Street Recreational Park, or limit the basic services that we provide to our

residents. Mid-sized cities nationwide must have access to the bond insurance market to improve their credit ratings. Also, there must be stabilization in this market so that Wilkes-Barre and other cities can continue to provide basic, quality-of-life services for their residents and participate in catalytic economic development projects.

Thank you for the opportunity to address this Subcommittee and for considering my perspective as a Mayor of a mid-sized city.