



City of Palo Alto

Finance Committee Staff Report

(ID # 5860)

Report Type: Action Items

Meeting Date: 8/18/2015

Summary Title: City Debt Policy

Title: Recommendation to Adopt City Debt Policy

From: City Manager

Lead Department: Administrative Services

Recommendation

Staff recommends that the Finance Committee recommend the Council approve the attached Proposed Debt Policy.

Background

An outstanding request by the City's Finance Committee was to draft a comprehensive citywide debt policy. Debt guidelines were adopted by Council in a report (CMR 210:97) that addressed infrastructure needs. Although staff has been following these guidelines, which are provided in the City's Annual Budget document (e.g., page 95 of the FY 2015 Adopted Budget <http://www.cityofpaloalto.org/civicax/filebank/documents/43341>), a more comprehensive and detailed document that is similar to the City's Investment Policy will be more beneficial for the City in the years ahead. The new policy follows best practices by utilizing a template from the Government Finance Officers Association (GFOA). Staff consulted other jurisdiction debt policies as well in the effort to update previous guidelines and practices.

Discussion

The attached policy discusses several important areas that are not addressed in current guidelines. These include, for example: expanding the current policy to all City Funds; providing guidelines for refinancing existing debt; detailing the responsibilities of City staff engaged in issuing debt; delineating the debt instruments or vehicles (e.g. General Obligation Bonds or Certificates of Participation) the City can utilize; and describing situations in which tax-exempt and taxable debt can be used. The depth and breadth of the policy will serve to guide future staff.

Historically, the City has been conservative in issuing debt, both in quantity and type. Whenever possible, a pay-as-you-go approach has been applied to capital projects. For capital intensive projects requiring financing, the City traditionally used fixed rate debt. This has provided certainty as to annual obligations and smooth debt levels over time. It is important to

note that the attached policy predominantly reflects these practices. Staff has not included in the policy more complex debt instruments that include “synthetic debt” whereby variable for fixed or fixed for variable interest rate swaps/exchanges are incorporated. Because of their complexity, a general policy approach is not recommended in this instance, as such instruments should be thoroughly reviewed, explained, vetted, and approved by the Council on a case by case basis.

As with all guidelines and policies, exceptions will arise in the future. For example, even though the guideline for enterprise/utility funds specifies that annual debt service cannot exceed 15 percent of the operating budget for the individual fund (10 percent for the General Fund), it will be inevitable that given the scale of the future replacement and renovation of the Water Quality Control Plant that annual debt service will exceed the 15 percent threshold. In this case, the purpose of the threshold is not to forestall a necessary project, but to ensure public review and staff explanation for the reasons for a departure from policy, and how rates will be adjusted to meet annual debt service.

In conclusion, staff recommends that the Finance Committee approve the attached Debt Policy.

Resource Impact

There is no budget impact associated with this report.

Policy Implications

This recommendation is in line with debt guidelines outlined in the Annual General Fund Operating Budget and comports with the more detailed policy document or best practices provided by the Government Finance Officers Association.

Environmental Review

The actions requested in this report do not constitute a project for the purposes of the California Environmental Quality Act (CEQA).

Attachments:

- Attachment A: Draft Debt Policy (DOCX)

CITY OF PALO ALTO DEBT POLICY
DRAFT 4
5/14/15

I. Background/General Statement

One of the keys to sound financial management is the development of a debt policy. Development of a debt policy is a recommended practice by the Government Finance Officers Association. Bond rating agencies recognize the importance of debt guidelines as a sign of prudent financial management. A debt policy establishes the parameters for issuing debt and managing the debt portfolio. It provides guidance from the Council to City staff regarding purposes for which debt may be issued, types and amounts of permissible debt, and the method of sale that may be used.

The City of Palo Alto (City) maintains conservative financial policies to assure strong financial health both in the short- and long-term. The City is an infrequent issuer of debt with debt primarily used as a tool to finance large capital investments such as property acquisitions, new building construction, and rehabilitating or replacing major assets. Maintaining the City's strong bond rating is an important objective of the City's financial policies. To this end, the City is constantly working to improve its financial policies, budgets, forecasts, and financial health.

II. Scope of Policy

This policy sets forth the criteria for the City's issuance, repayment, and management of debt. The primary objective of the debt policy is to establish criteria that will protect the City's financial integrity while providing a funding mechanism to meet the City's capital needs. The underlying approach of the City is to borrow only for capital improvements that cannot be funded on a pay-as-you-go basis. The City will not rely on any form of debt to finance current operations unless there is a cash flow shortage requiring short-term instruments such as Tax and Revenue Anticipation Notes (TRANS). All debt issued will be in compliance with this policy along with all other City, State, and Federal laws, rules, and regulations.

This debt policy shall apply to all City of Palo Alto funds although exceptions may be requested from Council in the future.

III. Purpose of Debt Financing

The City borrows money primarily to fund long-term capital improvement projects and to refinance existing debt. Another potential use is for financing the purchase of major and multiple pieces of equipment.

With the exception of potential use of short-term TRANS, debt issued to fund operating deficits is not permitted. TRANS are used to address short-term cash flow issues and are intended to be repaid within the fiscal year of issuance. Debt will be used to finance eligible projects only if it is the most cost-effective and practical means available to the City. In addition, consideration on using debt will be analyzed when interest rates are low. While the "pay-as-you-go" method of using current revenues to pay for capital projects is often considered the preferred means of financing (to avoid interest and issuance costs), it may not be entirely practical or equitable.

The "pay-as-you-go" funding option requires revenues to accumulate to pay for capital projects. The City would be able to undertake capital projects under this method only if sufficient cash accumulates.

Prudent use of debt financing rather than “pay-as-you-go” funding of capital projects can facilitate: better allocation of resources over time, increased financial flexibility, and payment equity across generations for the use of long-term assets. The three primary borrowing purposes are summarized below:

A. Long-Term Capital Improvements

The City maintains a 5-year Capital Improvement Plan (CIP) and an annual CIP Budget for consideration and adoption by the City Council as part of the City’s budget process. The Administrative Services Department’s Treasury Division is responsible for coordinating and analyzing potential debt financing for CIP projects. Factors included in the analysis are: amount and type of debt, duration of bonds, interest rates, annual debt service cost, current outstanding debt levels, debt limitation calculations and compliance, impact on future debt burdens, credit requirements, and existing or needed revenue sources to meet annual debt service obligations. Prior to issuance of debt, the City will prepare revenue projections, such as the biennial budget or financial forecasts (e.g. financial plans for utilities or the General Fund Long Range Financial Forecast) to ensure that there is adequate capacity to make principal and interest payments. A new or enhanced revenue source may need consideration and approval to support additional debt levels.

Since the aggregate cost of desired capital projects generally exceeds available funds, the capital planning process prioritizes projects and identifies the funding needs. The City will initially rely on internally-generated funds and/or grants and contributions from other governmental agencies to finance its capital needs. Debt will be issued for a capital project only when the magnitude of costs justifies a debt financing; the project meets a critical need; if a secure revenue source is identified to repay the debt; and when it is an appropriate means to achieve a fair allocation of costs between current and future beneficiaries. All debt issuances must be approved by the City Council.

The Treasury Division of the Administrative Services Department, working with the Office of Management and Budget, City departments, and within the context of the Capital Improvement Plan and the City’s financial forecasts, oversees and coordinates the analysis, timing, processing, and marketing of the City’s bonds. Close coordination of capital and debt planning among appropriate departments will ensure that the maximum benefit from existing funding is achieved. Debt financing will be considered after a debt capacity or affordability analysis is conducted.

B. Essential Vehicle and Equipment Needs

In addition to capital projects, the City can finance essential equipment and vehicles. These assets range from public safety vehicles to utility equipment. The underlying asset must have a minimum useful life of three years. Short-term financings, including loans and capital lease purchase agreements, are executed to meet such needs. It has been the City’s practice to fund these purchases with existing resources; however, debt financing flexibility for future needs remains an option.

C. Re-financings/Refunding of Existing Debt

The Chief Financial Officer or Director of Administrative Services, supported by Treasury Division, will periodically evaluate its existing debt and execute re-financings when economically beneficial. A refinancing may include the issuance of bonds to refund existing bonds or the issuance of bonds in order to refund other obligations. A net present value analysis, both in dollar and percentage terms, will be conducted to determine whether a re-financing is optimal. As a “rule of thumb,” a minimum 3 percent net present value savings will be used as a basis to begin re-financing efforts. As with new debt, all re-financings must be approved by Council.

IV. Responsibilities of City Personnel

Authority to issue and manage debt is derived from Palo Alto Municipal Code 2.08.150, section 13.

This section gives the Director of Administrative Services (Chief Financial Officer or CFO) authority to perform the duties of debt management. This section also authorizes the CFO to appoint a subordinate employee from the Department to assist in the performance of the duties of City Treasurer. The CFO has appointed an Assistant Director and a Senior Management Analyst to oversee debt issuance and subsequent responsibilities such as: making interest and principal payments via a Trustee; managing debt service reserves and project funds; and following bond indenture requirements and all other Federal and State regulations. The CFO is responsible for assuring that the activities related to the issuance and payment of bonds or other obligations do not materially impact the City's bond rating which currently stands at a Triple A level (the highest possible rating).

V. Guidelines for Use of Debt and Other Financing

A. Debt may be judiciously used when some or all of the following conditions exist:

1. Estimated future revenue is sufficient to ensure the payment of annual debt service
2. Other financing options have been explored and are not viable for the timely or economic acquisition or completion of a capital project
3. A capital project is mandated by federal or state authorities with no other viable funding option available
4. The capital project or asset lends itself to debt financing rather than pay-as-you-go funding based on the expected useful life of the project
5. Debt will not be used to fund ongoing operating expenses of the City except for situations in which cash flow problems arise and the City may need to issue short-term Tax or Revenue Anticipation Notes.
6. Annual debt service shall not exceed 10 percent of annual operating expenses for the General Fund unless an exception is approved by Council. For all other City funds annual debt service shall not exceed 15 percent of annual operating expenses unless an exception is approved by Council.

B. Minimize borrowing costs by:

1. Maximizing the use of existing resources for capital projects and equipment needs.
2. Issuing tax-exempt debt except in instances where IRS regulations require taxable bonds.
3. Striving to obtain the highest credit ratings possible.
4. Maintaining a competitive bid process on bond sales except for situations in which negotiated or private placement sales meet City objectives. In negotiated or private placement sales, City staff will work with its Financial Advisor to review proposed interest rates and proposed fees.
5. Ensuring that the type of debt and debt structure developed ensure advantageous marketing of each issue.

C. Linking debt to appropriate revenue sources and project users:

1. When possible, tie project financing directly to users of a specific facility or use. Examples include renovation of the Golf Course where user fees can offset debt service or replacing gas mains where gas rates can be increased to cover debt expense.
2. Using debt in the Enterprise Funds so as to avoid significant spikes in user rates by smoothing out costs over time.

VI. Types of Financing Instruments

As outlined by the California Debt and Investment Advisory Commission (CDIAC), there are numerous options or debt instruments to fund projects. These range from General Obligation Bonds to Mello-Roos Districts, to State Revolving Funds to Certificates of Participation. The list below represents the most typically used debt vehicles and the general guidelines for their use.

A. General Obligation Bonds (G.O.)

G.O. bonds provide investors with the most secure credit and the City with the lowest cost of funds. Through a super majority vote, residents agree to place a lien/tax on all properties to pay annual debt service. A lien on property, especially with land values in the City of Palo Alto, along with a City pledge to use its unlimited authority to levy property taxes for debt service provides significant assurance to investors and bondholders. Proceeds from G.O. bonds are strictly limited for acquisition of land, capital projects and the purchase of fixed equipment. These bonds cannot be used for operating expenses or moveable equipment. The sum of all G.O. debt outstanding is governed by a statutory legal debt limit that is disclosed in the City's annual Comprehensive Annual Financial Report and the City's budget documents.

B. Certificates of Participation (COPs)

COPs are a form of lease obligation in which the City enters into an agreement to pay a fixed amount annually to a third party, usually a private leasing company or trust structure. These leases are issued for land acquisition and capital improvements. In addition, the purchase of moveable equipment is permitted. It is typical for the asset being acquired or improved to act as the credit for the financing, but the City's General Fund is ultimately liable for all annual debt service limits. COPs can be tied, for example, to revenue streams such as Golf Course fees or rents from a newly constructed facility. The City has established a leasing structure with the Public Improvement Corporation (PIC) that allows the issuance of COPS

C. Revenue Bonds

Revenue bonds may be issued to fund capital improvements related to enterprise functions (e.g. water, sewer, electric) or for special projects supported by discrete revenue sources. They are designed to be self-supporting through user fees or other special earmarked receipts or taxes and do not rely on the general taxing powers of the City. Principal and interest is paid from net the revenues of enterprise operations. Unlike General Obligation bonds, revenue bonds are not subject to the City's statutory debt limitation. Electric and gas bonds, for example, do not require voter approval while other enterprise funds such as the Storm Drain Fund may be subject to Proposition 218 requirements in raising revenue levels sufficient to pay debt. Net revenues generated by the applicable Enterprise Funds must be sufficient to maintain required debt service coverage levels specified in bond indentures.

D. Special District Bonds.

These bonds are typically used for a specific purpose such as garage construction, landscape and lighting improvements, or utility work. They are subject to voter or property owner approval where special taxes or assessments are levied on properties to pay debt service for constructed facilities or services. With the passage of Proposition 218 by voters, specific steps and requirements must be followed to implement such districts. The City's downtown parking assessment district is one such example.

E. State Revolving Fund (SRF) and Federal Loans

The SRF provides a low interest loan program for construction of water and wastewater infrastructure projects. The City's Regional Water Quality Control Plant, for example, has an outstanding SRF loan. Both the State and rating agencies require the City to disclose all incurred debt as they determine whether the City is able to meet required debt service coverage ratios (the basic concept of coverage is that after covering all operating expenses, the fund issuing debt has sufficient revenue (at a specified level) to cover annual debt service).

In addition to the SRF, the City **may** participate in advantageous Federal loans as they become available. For example, the City has issued Clean Renewable Energy Bonds for a photovoltaic project and Build America Bonds to construct water system improvements. Such bonds typically offer incentives for investors and a low cost of funds for the City.

VII. Debt Limits

A standard guideline, and one that has been inserted annually in the City's General Fund budget document, is that debt service payments should not exceed 10 percent of the annual expenditure budget. Moreover, California Government Code, Section 43605 sets the debt limit at 15% of the assessed value of all real and personal property of the City. Because this Code section was enacted when assessed value was 25% of market value, the limit is calculated now at one-fourth of that amount or 3.75 percent. For details on current General Fund debt service levels as a percent of budget and for where the City stands on the State's legal debt margin, see the Comprehensive Annual Financial Report's (CAFR) Statistical section for the Computation of Legal Bonded Debt Margin calculation. Similar, but abbreviated information also is provided in the Operating Budget's Debt Service Funds Overview section.

Enterprise or other fund debt is not subject to legal debt margin described above. For Enterprise and all other funds, debt service payments should not exceed 15 percent of the annual expenditure budget.

Any exceptions to the above guidelines will be presented to Council for approval.

VIII. Term and Structure of Debt

A. The duration of a debt issue is typically tied to the economic or useful life of an asset. This is consistent with standard practice and further serves the concept of allocating debt service costs to current and future beneficiaries of the asset. It is possible, though uncommon, for the term of debt to exceed 30 years duration. For long-term assets such as a building or a parking garage, the City has issued 30 year bonds. Wherever possible and to save on interest costs, the City should consider shorter-term borrowings where appropriate. Additional factors to include in the analysis of the term of debt are: current market conditions, institutional interest, and the durability and consistency of revenue sources covering debt service payments.

Structure

A. Fixed and Variable Rate Debt.

The City's practice has been to issue fixed rate debt. Such debt provides absolute certainty, at the time of a bond sale, as to the level of principal and interest owed annually. Moreover, it allows the City to have even debt service payments over time. This conservative practice has served the City well over the past decades.

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Specific conditions may arise where the City would consider the use of variable interest rate bonds. Variable bonds have interest rates that reset on a periodic basis (e.g. daily, weekly, monthly). Conditions which would cause consideration of variable rate debt are:

1. An adverse fixed-rate municipal market
2. Uncertainty over the level of annual revenues to cover debt service
3. The potential for rapid repayment of debt
4. The need or desire to optimize the City's asset/liability balance

Variable interest rate debt, however, exposes the City to interest rate risk over the term of the financing. While credit rating agencies are supportive of variable rate debt, the magnitude of any unhedged variable rate debt could raise concerns. Rating agencies suggest the aggregate amount of such debt be capped at a level not exceeding 20-25 percent of debt outstanding.

It is possible to issue a combination of both fixed and variable rate debt. The City could use this tool, as well as others, such as front or back ending debt to manage its debt portfolio. These structures should be used in a manner which best supports the City's long-term financial condition. There are other types of debt that are a variation of fixed and variable debt. These can involve swaps of fixed for variable debt (or vice versa) depending on the interest rate environment and the City's general financial position. These instruments can become most complex and sensitive to shifts in the interest rate and economic environment. They require careful analysis and monitoring.

B. Tax-exempt versus Taxable Debt

The City's primary mode is to issue tax-exempt debt. This debt reduces the City's interest expense and provides considerable savings over time. There are, however, instances in which the City may want or need to issue taxable debt. For example, if the City builds a garage and plans retail space within it, it may, depending on square footage used, have to issue both exempt and taxable debt. The Internal Revenue Service (IRS) has specific guidelines on public and private usage of facilities and when taxable debt must be issued. Working with the City's Bond Counsel to understand and comply with IRS regulations is essential.

C. Prepayment Provisions

Redemption provisions and call features shall be evaluated in the context of each bond sale to: enhance marketability of the bonds; ensure flexibility related to potential early redemption; and to foster future refunding transactions. The potential for additional costs such as a call premium and potentially higher interest rates will be evaluated in the decision to redeem bonds. The following are different redemption provisions to be evaluated:

1. Optional redemption allows the City the ability to redeem bonds early.
2. Mandatory redemption includes provisions for redeeming bonds under specific and pre-determined conditions.
3. Extraordinary redemption provides ability to redeem bonds given fortuitous events.

IX. Attention to Credit-Worthiness

A. Credit Ratings

The City seeks to maintain the highest possible credit rating on debt that can be achieved without compromising its policy objectives or transparency. Achieving the highest possible credit rating translates into lower interest cost and annual debt service. At a high level, rating

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agencies will look for the ability to repay debt, prudent financial management, systematic capital planning, interdepartmental cooperation and coordination, long-term labor agreements, and long-term financial planning. More specifically, agencies such as Standard and Poor's focus on:

- Fiscal soundness of the General and Enterprise Funds
- Community demographics such as education and income levels
- Property values and business concentration
- Management capability
- State and Federal regulations
- The credits, revenue sources, and coverage ratios pledged to repay debt
- Fund reserve levels and policies
- City's debt history and current debt structure
- The capital improvement project being funded
- Covenants and conditions in the governing legal documents
- Cost adjustments to balance budgets during an economic downturn

The City recognizes that external legislative, economic, natural, or other events may, from time to time, affect the creditworthiness of its debt. Such events could lead to a downgrade or upgrade to City ratings. Naturally, when new debt is proposed, rating agencies will evaluate its potential impact upon the City's outstanding debt rating. The major source of risk rating agencies consider is the stability and reliability of revenue sources to service the debt. Projects with volatile or risky debt repayment revenue will receive a lower rating and that could potentially impact the ratings on other City debt.

B. Rating Agency Relationships

The Chief Financial Officer (CFO) is responsible for maintaining relationships with the rating agencies (e.g. Standard and Poor's and Moody's) that assign ratings to debt issuances. The CFO performs this function in conjunction with the Assistant Director, Senior Financial Analyst, and outside consultants such as the City's Financial Advisor and Bond Counsel. This effort shall include providing periodic updates on a Fund's financial conditions when requested and providing documents such as the Comprehensive Annual Financial Report and Adopted Budget. Rating agencies may require payments from the City to update their bond ratings.

C. Bond Ratings

The CFO and his staff are responsible for providing factual, well-organized, and germane presentations to the agencies rating proposed bonds. These presentations will involve coordination among the City Manager's and City Attorney's Offices, Administrative Services, and the department responsible for the debt issuance such as the Public Works, Utilities or Community Services departments. In addition, the City's Financial Advisor and Bond Counsel will attend these presentations.

D. Credit Enhancement

Credit enhancement may be used to establish or improve a credit rating on a City debt obligation. Types of credit enhancement include bond insurance, surety policies, or a Letter of Credit. The CFO and staff will consider the use of credit enhancement if it reduces the overall cost of the proposed financing, or if in the opinion of the CFO, the use of such credit enhancement furthers the City's overall financial objectives.

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Bond insurance is an unconditional pledge by an insurance company to make principal and interest payments on the City's debt in the event insufficient funds are available to meet a debt service obligation. Bond insurance, when available, may be purchased from an insurance company and is a potential means of enhancing the debt's rating. The cost of the insurance is to be weighed against the potential interest costs savings generated by the assurance. A Letter of Credit may be obtained from a major bank, for a fee, to enhance the credit rating. This letter is an unconditional pledge of the bank's credit to make principal and interest payments on the City's debt in the event insufficient funds are available to meet a debt service obligation. Again, the cost of the credit Letter is to be weighed against savings from the Letter.

E. Debt Service Reserve Fund

With the exception of G.O. bond indebtedness, the City may size the debt issuance such that a debt service reserve fund is established at the time of issuance. The debt service reserve funds will be held by and are available to the Trustee to make principal and interest payments to bondholders in the event that pledged revenues are insufficient to do so. The maximum size of the reserve fund is generally governed by tax law, which permits the lesser of: 1) 10 percent of par; 2) 125 percent of average annual debt service; and 3) 100 percent of maximum annual debt service. Debt reserve funds for the City are typically equal to one year's maximum debt service. On a case-by-case basis and assuming there is no economic or credit disadvantage, the City may issue bonds with a debt service reserve fund that is sized at a lower level.

X. Method of Sale

The CFO/Director of Administrative Services will select the method of sale that best fits the type of bonds being sold, the prevailing market conditions, and the desire to structure bond maturities to enhance the overall performance of the entire debt portfolio. Three general methods exist for the sale of municipal bonds:

A. Competitive Sale

Bonds are marketed to a wide audience of investment banking (underwriting) firms. Their bids are submitted at a specified time (generally the day of the bond sale). The underwriter then is selected based on the best bid (lowest interest rate) for the securities. Pursuant to this policy and within the parameters approved by the City Council, the CFO or his/her designee (Assistant Directors of ASD) is hereby authorized to sign the bid form on behalf of the City fixing the interest rates on bonds sold on a competitive basis

B. Negotiated Sale

The City selects the underwriter or group of underwriters of its securities in advance of the bond sale. This method of sale is warranted for complex or unique bonds that require education and marketing in the investment community. Underwriters will perform this service on the City's behalf given ties to large institutional investors and large brokerage houses. Moreover, it is only through competitive sales that City staff can arrange the sale of its bonds to residents. When feasible and effective, staff will give local residents and investors domiciled in the City first priority to purchase bonds.

The City's financing team (ASD staff and the Financial Advisor) works with a selected underwriter to bring a bond issue to market. In advance of the sale, the City will determine a selected underwriter's compensation, their liability, and the designation rules and priority of

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orders under which the sale will be conducted. The Financial Advisor is responsible for advising staff on whether the fees and interest rates terms offered by the underwriter are consistent with prevailing market conditions. The City adheres to a strict policy of separating its Financial Advisor function from the underwriter function. Pursuant to this policy and conditions described herein, the City Council authorizes the CFO or his/her designee (Assistant Directors of ASD) to negotiate the terms of sale and to sign bond purchase agreements (that fix interest rates on bonds sold) in a negotiated sale.

C. Private placement

This method involves the City selling its bonds to a bank or limited number of sophisticated investors. Bonds are not sold to the general, investor community. City staff will perform due diligence in comparing interest costs and fees in a private placement to those using a competitive or negotiated sale. There are potential benefits in securing a private placement such as:

- a. lower fees or costs compared to selling bonds on the open market e.g. no fees for a Disclosure Counsel or rating agencies.
- b. the time frame for selling City is shorter and subject to less uncertainty in the event market rates move upward and against the City by the time a competitive bid process is held.
- c. the lack of a reserve requirement through a private placement could reduce the amount of principal outstanding and lead to lower annual debt service costs.

XI. Initial Disclosure Requirements

The Administrative Services Department, together with the City Attorney's Office and an outside Disclosure Counsel, shall coordinate all the necessary documents for disclosing the City's financial condition. The City's practice is to use separate law firms for the Disclosure and Bond Counsel functions.

Each publicly offered debt issuance will meet the disclosure requirements of the Securities and Exchange Commission (SEC) and other government agencies before and after the bond sale takes place. The disclosure documents, specifically the Preliminary and Final Official Statements, will provide the potential investor with full and accurate information necessary to make prudent investment decisions. Information for City backed transactions generally includes: a City government description; a description or scope of project being financed; annual financial data and statements; disclosure of liabilities; the tax or rate base; current debt burden; the history of tax collections and bond repayments; future borrowing plans; the source of funds for the proposed debt repayments; and specific bond data and bond holder risk factors.

XII. Post Issuance Administration

A. Investment of Bond Proceeds

The proceeds of the bond sales will be invested until used for the intended project in order to maximize utilization of the public funds. The investments will be made to obtain the highest level of safety and will be guided by the City's Investment Policy and bond indenture guidelines. City staff will provide investment guidance to a Trustee or management firm holding bond proceeds whether for project or debt service reserve funds.

B. Arbitrage Compliance

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ASD shall establish and maintain a system of record keeping and reporting to meet the arbitrage rebate compliance requirements as required by the Federal tax code. This effort shall include tracking investment earnings on bond proceeds, calculating rebate payments in compliance with tax law, and remitting any rebate earnings to the federal government in a timely manner. These activities preserve the tax-exempt status of the City's outstanding debt issuances. Additionally, financial reporting and other tax certification requirements embodied in bond covenants shall be monitored to ensure the City is in compliance with its bond covenants.

C. Ongoing Disclosure

ASD shall be responsible for providing annual disclosure information to established national information repositories and for maintaining compliance with disclosure requirements by state and national regulatory bodies. Securities and Exchange Commission (SEC) disclosure, stipulated by the SEC Rule 15c2-12, shall occur by the date designated in the bond ordinance. Disclosures shall include the Comprehensive Annual Financial Report (CAFR) at a minimum and any other information required by the bond indenture or regulatory body.

The Chief Financial Officer (CFO) shall be responsible for providing ongoing disclosure information to the Municipal Securities Rulemaking Board's (MSRB's) Electronic Municipal Market Access (EMMA) system. This is the central depository designated by the SEC for ongoing disclosures by municipal issuers. The CFO is responsible for maintaining compliance with disclosure standards promulgated by state and national regulatory bodies, including the Government Accounting Standards Board (GASB), the National Federation of Municipal Analysts, the Securities and Exchange Commission (SEC), and Generally Accepted Accounting Principles (GAAP). The City may also employ the services of firms that improve the availability of or supplement the City's EMMA filings. [These updates reflect recent changes by the SEC to Rule 15c2-12, effective July 1, 2009.] The City will provide full and complete financial disclosure to rating agencies, institutional and individual investors, other levels of government, and the general public to share clear, comprehensible, and accurate financial information using the appropriate channels/policies/procedures.

In order to facilitate the City's receipt of financing proposals associated with existing or contemplated debt, the City will have in place as Independent Registered Municipal Advisor (IRMA). The IRMA will provide advice to the City on proposals from broker-dealers or banks and will be required to be registered as a Municipal Advisor with the SEC and the MSRB. To attract financing proposals and assuage underwriter concerns about federal requirements, the City has posted on its website that an IRMA is under contract with the City.

D. Compliance with Other Bond Covenants

In addition to financial disclosure and arbitrage compliance, once bonds are issued, the City is responsible for verifying compliance with all activities, agreements, and requirements outlined in the bond documents on an ongoing basis. This typically includes: ensuring an annual appropriation to meet debt service payments; that relevant taxes, rates, and fees are levied and collected at a level sufficient to meet indenture requirements and debt service payments; the timely payment of debt service to a trustee or paying agent is completed; and compliance with insurance and other requirements.

XIII. Professional Services

The Administrative Services Department shall be responsible for the solicitation and selection of financial professional services that are necessary to issue and manage debt.

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A. Financial Advisor

A Financial Advisor(s) will be used to assist in the issuance of the City's debt. The Financial Advisor, or IRMA, will provide the City with objective advice and analysis on debt issuance. This includes, but is not limited to, monitoring market opportunities, structuring and pricing debt, and advising on official statements of disclosure.

B. Underwriters

An Underwriter(s) will be used for all debt issued in a negotiated sale. The Underwriter is responsible for purchasing negotiated debt and reselling it to investors.

C. Fiscal Agent

A Fiscal Agent or Trustee will be used to provide accurate and timely securities processing and timely payment to bondholders.

The City Attorney's Office shall be responsible for the appointment of Bond and Disclosure Counsels

D. Bond Counsel

All debt issued by the City will include a written opinion by Bond Counsel affirming that the City is authorized to issue the proposed debt. The opinion shall include confirmation that the City has met all City and State constitutional and statutory requirements necessary for issuance; a determination of the proposed debt's federal income tax status; and any other components necessary for the proposed debt. Bond Counsel shall provide a comprehensive and complete document of resolutions, indentures, disclosure statements and all related bond documents in binder and in electronic form.

E. Disclosure Counsel

This Counsel is responsible for drafting Preliminary and final Official Disclosure statements. While City staff provides Counsel with information required for these statements, it is Counsel's responsibility to know all regulatory and legal requirements necessary for full disclosure to investors.

XIV. Refunding Debt

Refunding of debt may be undertaken to:

- Take advantage of lower interest rates and achieve debt service cost savings.
- Restructure debt to either shorten or lengthen its duration or eliminate a debt service reserve.
- Refund outstanding indebtedness when existing bond covenants or other financial structures impinge on prudent and sound financial management or are too complex.

Generally, the City will consider a refunding only when there is a net economic benefit. This is when there is an aggregate net present value savings expressed as a percentage and dollar value of the par amount of the refunded bonds. A net present value savings of at least 3 percent is a standard guideline for initiating a refunding; however, a higher savings level may be considered. A net present value savings of 4 percent is a reasonable guideline for an advance refunding. The savings guideline for an advanced refunding may be waived by the Chief Financial Officer upon determining that such a restructuring is in the City's overall best financial interest. Exceptions shall be made only upon the approval of the Chief Financial Officer.

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Types of Refunding include:

A. Current Refunding

A current refunding is one in which the refunding bonds are issued less than 90 days before the date upon which the refunded bonds will be redeemed.

B. Advance Refunding

An advance refunding is one in which the refunding bonds are issued more than 90 days prior to the date upon which the refunded bonds will be redeemed. An advance refunding is used to refinance outstanding debt before the date the outstanding debt becomes due or callable. Proceeds of the advance refunding bonds are placed into an escrow account with a fiduciary and used to pay interest and principal on the refunded bonds and then used to redeem the refunded bonds at their maturity or call date. Internal Revenue Code §149(d)(3) provides that governmental bonds issued after 1985 may only be advanced refunded once over the life of a bond issuance.

XV. Arbitrage Rebate Monitoring and Reporting

The City will, unless otherwise justified, use bond proceeds within the established time frame pursuant to the bond ordinance, contract or other documents to avoid arbitrage. The general rule is that the City must spend all bond proceeds for a project within three (3) years of project initiation. Arbitrage is the interest earned on the investment of the bond proceeds above the interest paid on the debt. If arbitrage occurs, the City will pay the amount of the arbitrage to the Federal Government as required by Internal Revenue Service Regulation 1.148-11. The City will maintain a system of recordkeeping and reporting to meet the arbitrage rebate compliance requirement of the IRS regulation. For each bond issue not used within the established time frame, the recordkeeping shall include tracking investment earnings on bond proceeds, calculating rebate payments, and remitting any rebate earnings to the federal government in a timely manner in order to preserve the tax-exempt status of the outstanding debt.