Policy 7.1.8 **Fiscal – Debt Management Policy**

POLICY PURPOSE:

This Debt Management Policy is to provide clear and comprehensive guidelines for the issuance and financial management of debt issued by the City of Sunnyvale. This policy supports the City's mission of providing responsive and high quality public services for its citizens and ensures that the City is financially self-sustaining and fiscally strong. This Debt Policy is not to be so restrictive that it interferes with the City's legitimate efforts to prudently provide public services and facilities.

POLICY STATEMENT:

Generally, the method of financing selected for debt issuance should be based on who will benefit and who should pay for the cost of improvements. Changes in the capital markets and other unforeseen circumstances may require action which may deviate from this Debt Management Policy. In any case that requires exceptions to this Debt Management Policy, the City Council approval will be necessary for implementation. This policy will ensure compliance with all applicable federal and state laws.

1. The policy goals related to the City's planning goals and objectives:

   a. The City is committed to long-term financial planning, maintaining appropriate reserve levels and employing prudent practices in governance, management and budget administration. The City intends to issue debt for the purposes stated in this Policy and to implement decisions incorporated in its annual budget.

   b. The City will protect taxpayers, ratepayers and constituents by utilizing conservative financing methods and techniques to obtain the highest practical credit ratings to minimize borrowing costs and preserve access to credit.

   c. The City will comply with applicable state and federal law as it pertains to the maximum term of debt and the procedures for levying and imposing any related taxes, assessments, rates and charges.

   d. When refinancing debt, the City will realize, whenever possible, and subject to any overriding non-financial policy considerations, minimum net present value debt service savings equal to or greater than 3.0% of the refunded principal amount, or to remove burdensome or restrictive bond covenants.

2. The purposes for which the Long-Term Debt proceeds may be used:

   a. To finance the construction, acquisition, and rehabilitation of capital improvements and facilities, equipment and land to be owned and operated by the City (a Project) to provide basic services and/or benefit constituents over multiple years.

   b. To refinance outstanding debt to produce debt service savings or to realize the benefits of a debt restructuring (such as changes to the term or amendments to any prohibitive covenants).

3. The City may use long-term debt financing subject to the following conditions:

   a. The project to be financed must be approved by the City Council.

   b. The City determines that the issuance of the debt will comply with the applicable state and federal law.

   c. Debt service should not affect the City's ability to meet future operating, capital and reserve requirements.

   d. The maximum term of each debt financing should be no longer than the expected useful life of the asset or improvement financed.

   e. Debt should be used only to finance improvements that cannot be paid for with current revenues, unless the purpose of the debt is to spread improvement costs over a longer period and ensure that future users become responsible for portions of the cost.

   f. The City will not use long-term debt for current operations.

4. The City may use short-term debt financing subject to the following conditions:

   a. Short-term debt may be issued to provide financing for short-lived capital projects: e.g. the City may undertake lease-purchase financing for equipment.

   b. Short-term debt, such as bond anticipation notes, grant anticipation notes, commercial paper or a line of credit, may be used to provide interim financing in connection with the implementation of a capital program or to smooth out the City's cash flow requirements.

5. The types of debt that may be issued:

   a. New Money Bonds: New Money bonds are bonds issued to finance the cost of capital improvement projects or other large and extraordinary costs as approved by the City Council.

   b. Refunding Bonds: Refunding of outstanding bond issues shall be considered if the net present value savings is at least 3%, or if it is necessary to remove a burdensome or restrictive bond covenant.

   c. Revenue Bonds: all City utility-related improvements shall be funded only from revenues of the respective utilities.

   d. Fixed vs.Variable Rate Debt: Fixed or variable rate financing may be used, depending on the cost benefit and risk assessment for each option.

e. Variable Rate Debt Obligation (VRDO): Predetermined intervals (e.g.: daily, weekly, or monthly) are set where the rate can be reset to current market conditions. VRDOs can be redeemed at the City's option. Therefore, VRDOs with a long maturity can be priced as short- term instruments making it potentially a less costly option in a normal upward sloping yield curve environment.

f. General Obligation (GO) Bonds: For major improvements that are of community-wide benefit and use, such as general municipal facilities and parks. These are funded by ad valorem taxes and require a 2/3 voter approval.

g. Certificate of Participation: (COPs) and Lease Revenue Bonds: These are used where backing by the City's general fund is the most cost effective and feasible method, such as in the financing a public facilities. Annual general fund appropriations are made to fund annual lease payments.

h. Derivative Products: Because of their complexity, unless otherwise amended, Derivative Products such as Interest Rate Swaps, Inverse Floaters, and other hybrid securities are prohibited.

i. Land-Secured Financings: Land-secured financings, such as special tax revenue bonds issued under the Mello-Roos Community Facilities Act of 1982, as amended, assessment bonds and bonds secured by voter-approved parcel taxes.

j. Conduit Financing: The City will consider requests for conduit financing, such as financings for affordable rental housing and qualified 501(c)(3) organizations, on a case-by-case basis, taking into consideration the borrower's credit worthiness, the purpose of the borrowing and its relationship to City priorities, any impact on the City's financial position and administrative impact on City staff.

k. The City may find from time to time that other forms of debt would be beneficial to further its public purposes and the City Council may approve such debt without an amendment of this Debt Policy.

6. The relationship of the debt to, and the integration with, the City's capital improvement program or budget, if applicable:

   a. The City is committed to long-term capital planning. The City intends to issue debt for the purposes stated in this Debt Policy and to implement policy decisions incorporated in the City's capital budget and the capital improvement plan.

   b. The City shall integrate its debt issuances with the goals of its capital improvement program by timing the issuance of debt to ensure that projects are available when needed in furtherance of the City's public purposes.

   c. The City shall seek to issue debt in a timely manner to avoid having to make unplanned expenditures for capital improvements or equipment from its general fund.

7. Debt Management procedures:

   a. The Director of Finance shall report to the City Council annually at the same time as the City's annual audited financial statements on the actual use of bond proceeds to ensure the use is consistent as intended.

   b. The City will diligently monitor its compliance to any continuing disclosure requirements under applicable Security and Exchange Commission rules (e.g.: SEC Rule 15c2-12), bond covenants, or any other applicable disclosure requirements.

   c. The City will diligently monitor its compliance to federal arbitrage regulations.

   d. Debt service reserves shall be maintained for each debt issue as required by the respective bond covenants. These reserves will be invested as allowed per the bond statements.

   e. Whenever reasonably possible, proceeds of debt will be held by a third-party trustee and the City will submit written requisitions for such proceeds. The City will submit a requisition only after obtaining the signature of the Finance Director. In those cases where it is not reasonably possible for the proceeds of debt to be held by a third-party trustee, the Finance Director shall retain records of all expenditures of proceeds through the final payment date for the debt.

8. General Debt Policy:

   a. Total bonded indebtedness supported by -ad valorem taxes (i.e.,general obligation bonds) should not exceed 5% of assessed valuation of property within the City. Bond issues supported by the General Fund should be restricted to annual debt service of 5% of annual General Fund revenue.

   b. The City will utilize inter-fund loans when possible to reduce the cost of financing capital improvements.

   c. Land based financings should maintain a minimum property value-to-debt ratio of 3:1, with exceptions made for special circumstances at Council's discretion.

   d. An internal feasibility analysis will be prepared for each long-term financing which analyzes the impact on current and future budgets.

   e. In general, bond issuances shall be structured with level annual debt service unless circumstances warrant a different approach.

   f. The City may issue both tax-exempt and taxable debt.

   g. The City may issue debt through (i) competitive sale at which its debt will be offered at a fixed date and time and with the opportunity for any financial institution to submit a bid; (ii) negotiated sale at which its debt will be purchased by an investment banking firm or syndicate; or (iii) private placement at which its debt will be purchased directly by a commercial bank.

h. The method of sale will be determined in consultation with the City's independent financial advisor, with the objective of providing the City with the lowest overall cost of financing and the most efficient market access and execution.

9. Delegation of Authority:

Pursuant to the provisions of Sections 37209 and 40805.5 of the Government Code of the State of California, the Finance Director (Director of Finance) shall be the head of the Finance Department and shall be responsible for all the financial affairs of the City. This City Debt Policy grants the Director of Finance the authority to select the financing team, coordinate the administration and issuance of debt, communicate with the rating agencies, as well as to fulfill all the pre-issuance and post-issuance disclosure information requirements. The Director of Finance will be responsible for maintaining relationships with investors, credit analysts, and rating agencies.

10. Debt Capacity:

Article XVI, Section 18 of the California Constitution (the "debt limit") prohibits cities from entering into indebtedness or liability that in any year exceeds the income and revenue provided for such year unless the City first obtains two-thirds voter approval for the obligation. In the development of this Debt Policy, the goal is to serve as a framework within which the City can evaluate each potential debt issuance.

Glossary of Debt Management Terms

Arbitrage: In the case of municipal financing is the prohibited use of lower rate, tax free, bond funding to invest in higher return financial instruments**.**

Conduit Financing: A financing arrangement involving a government of other qualified agency using its name in an issuance of fixed income securities for a non-profit organization's capital project.

Derivative Product: A product, such as an option or futures contract, whose value is derived from the performance of an underlying security. A commonly used derivative is an interest rate swap. Given the complexity of derivative products, the City and its related entities will not utilize derivative products in its debt issuances.

Mello-Roos Community Facilities Act of 1982: Community Facilities Districts (CFDs), more commonly known as Mello-Roos, are special districts established by local governments in California as a means of obtaining additional public funding. Cities, counties, special districts, joint powers authorities, and school districts in California use these financing districts to pay for public works and some public services.

SEC Rule 15c2-12: The SEC requirement that defines the required continuing disclosure requirements for municipal security issuers. Continuing disclosures consist of periodic reporting on the status of the debt issuance to the Municipal Securities Rulemaking Board (MSRB).

501c3 Organizations: The most common type of US tax-exempt nonprofit organization, whereby the organization is exempt from federal income tax if its activities have the following purposes: charitable, religious, educational, scientific, literary, testing for public safety, etc.

Comparison of Financing Methods

General Obligation (GO) Bonds
* Strong market acceptance
* Significant structuring flexibility
* Favorable interest rates
* No reserve fund requirement
* No trustee required
* Voter approval usually required
* Pledge of general credit required
* Difficult to enter market

Revenue Bonds
* Debt is secured by system users
* Debt limits not applicable
* Higher interest costs than GO Bonds
* Debt service reserve required
* Trustee required
* Voter approval usually not required
* Coverage covenants usually included
* Limited revenues available to secure debt

Special Assessment Bonds
* Voter approval usually not required
* Debt limits may not apply
* Debt is secured by beneficiaries
* Complexity greater than GO Bonds
* Market concerns about defaults
* Limited revenues to secure debt
* Higher interest costs due to higher risk

Certificates of Participation
* Voter approval usually not required
* Debt limits not applicable
* Good market acceptance
* Complexity greater than GO Bonds
* Risk of citizen opposition
* Limited revenues to secure debt
* Less secure than GO Bonds