ITEM # 29
DATE: 06-27-17

COUNCIL ACTION FORM

SUBJECT: CITY OF AMES DEBT POLICY

BACKGROUND:

The Government Finance Officer Association's best practices recommend that local governments adopt a comprehensive written debt management policy. Debt management policies are written guidelines, allowances, and restrictions that guide the debt management practices, including the issuance process, management of a debt portfolio, and adherence to various laws and regulations. The document articulates policy goals, provides guidelines for the structure of debt issuance, and demonstrates a commitment to long-term capital and financial planning.

Adherence to a debt management policy signals to rating agencies and the capital markets that the City of Ames is well managed and, therefore, is likely to meet its debt obligations in a timely manner. **The attached policy is consistent with long standing practices followed by the City and allows for flexibility within the policy when specifically approved by the City Council. Though the written policy does not change the City's approach for management of debt, adoption of the policy by Mayor and City Council provides additional transparency and helps to ensure that there is a common understanding among elected officials and staff regarding the City of Ames approach to debt financing.**

ALTERNATIVES:

1. Adopt the City of Ames Debt Policy.

2. Refer the City of Ames Debt Policy to staff for revision.

MANAGER'S RECOMMENDED ACTION:

The City of Ames Debt Policy establishes debt management guidelines in accordance with best policy practices and provides for a common understanding of the City of Ames debt management practices to all parties.

Therefore, it is the recommendation of the City Manager that the City Council adopt Alternative No.1, thereby adopting the City of Ames Debt Policy.

City of Ames
Debt Policy

Adopted by City Council

on June 27, 2017

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SECTION 1 – POLICY

This Debt Policy sets forth debt management objectives for the City and establishes general parameters for issuing and administering the City's debt. It primarily addresses debt securities issued by the City in public or private bonds markets.

While this policy provides guidelines for general use, it allows for exceptions in extraordinary conditions. In the event there are proposed exceptions to Debt Policy guidelines when a bond issue is structured, those exceptions will be discussed in the applicable Council Action Forms or staff reports at the time the bond issue is presented for City Council consideration.

1.1. Objectives

The purpose of the policy is to assist the City in the pursuit of the following equally important objectives, while providing full and complete financial disclosure and ensuring compliance with applicable state and federal laws:

- Minimize debt service and issuance costs
- Maintain access to cost-effective borrowing
- Achieve the highest practical credit rating
- Achieve full and timely repayment of debt

1.2. Budget Integration

A bond issue can be utilized to finance a capital project. Bond proceeds are not to be used to fund operating expenses. The decision to incur new indebtedness should be integrated with the City Council adopted Operating Budget and Capital Improvement Program Budget. The annual debt service payments shall be included in the Operating Budget.

1.3. Financing Priorities

The Finance Director or designee shall be responsible for analyzing financing proposals to determine if it is beneficial to the City and conforms to the City's long-term financial planning objectives. An analysis of proposed debt may include:

- Confirmation that the capital project is eligible for bond financing
- Review of all available financing instruments for the project and determination of the most cost effective option
- Total cost of the capital project including its design, construction cost, cost of furnishings, fixtures and equipment
- Source of revenue to fund the annual debt service
- Analysis of the municipal bond market, including economic and interest rate trends
- Alternative bond structures
- Cost analysis of bond insurance
- Timing of when the City should enter the bond market

1.4. Annual Review

Recognizing that cost-effective access to the capital market depends on prudent management of the City's debt program, periodic review of the debt policy should be performed. The debt policy will be included in the fiscal policy section of the Operating Budget adopted by City Council. Any substantive changes to the policy shall be brought to City Council for consideration and approval.

SECTION 2 – METHODS OF FINANCING

The Finance Director will investigate possible project financing alternatives including, but not limited to, bonds, loans, state bond pools, and grants.

2.1. Cash Funding

The City funds a significant portion of capital improvements on a "pay-as-you-go" basis. The City will use the following criteria to evaluate pay-as-you-go versus long-term financing in funding capital improvements:

- Operating revenues produce adequate funds in excess of operating expenses to fund capital improvements
- Current revenues and adequate fund balances are available or project phasing can be accomplished
- Existing debt levels adversely affect the City's credit rating
- Market conditions are unstable or present difficulties in marketing

2.2. Interfund Borrowing

The City may borrow internally from other funds with surplus cash in lieu of issuing bonded debt. Purposes warranting the use of this type of borrowing could include short-term cash flow imbalances due to grant terms, interim financing pending the issuance of bonds, or long-term financing in lieu of bonds for principal amounts of under $3 million. The City funds from which the money is borrowed shall be repaid with an interest not less than the earning rate of the City's investment pool. The Finance Director shall also exercise due diligence to ensure that it is financially prudent for the Fund making the loan.

2.3. Bank Loans/Lines of Credit

Although the City does not typically utilize lines of credit for the financing of capital projects, financial institution credit is an option for municipal issuers and may be evaluated as a financing option.

2.4. Other Loans

The City will evaluate other loan programs, including but not limited to State loans such as the Iowa State Revolving Fund loans for the construction of water and wastewater infrastructure projects.

2.5. Bond Financing

The City may issue any bonds which are allowed under federal and state law including but not limited to general obligation bonds, revenue bonds, and special assessment bonds.

While conduit financings do not constitute a general obligation of the issuer, the same level of due diligence prior to bond issuance is required. The City will consider requests for conduit financing on a case-by-case basis using the following criteria:

- The City's bond counsel will review the terms of the financing, and render an opinion that there will be no liability to the City in issuing the bonds on behalf of the applicant.
- There is a clearly articulated public purpose in providing the conduit financing.
- The applicant is capable of achieving this public purpose.
- The applicant is a strong credit risk and will provide credit enhancements.

This means that the review of requests for conduit financing will generally be a two-step process:

- Asking the City Council if they are interested in considering the request, and establishing the ground rules for evaluating it.
- Providing the City Council with the results of this evaluation, and recommending approval of appropriate financing documents, if warranted.

This two-step approach ensures that the issues are clear for both the City and applicant, and that key policy questions are answered. The work scope necessary to address these issues will vary from request to request, and will have to be determined on a case-by-case basis. Additionally, the City should generally be fully reimbursed for the cost of evaluating the request; however, this should also be determined on a case-by-case basis.

2.6. Joint Powers Authority (JPA)

In addition to some of the long and short term financing instruments described in Sections 2.1 through 2.5, the City may also consider joint arrangements with other governmental agencies when a project serves the public interest beyond City boundaries. Issuance of Joint Powers debt will be in accordance with Chapter 28E of the Iowa Code.

SECTION 3 - FINANCING TEAM – ROLES AND SELECTION PROCESS

3.1. Financing Team Definitions and Roles

The Financing Team is the working group of City staff and outside consultants necessary to complete a debt issuance including but not limited to bond counsel, underwriter, financial advisor, trustee, pricing consultant and/or arbitrage analyst. Typically, the Finance Director, Assistant Finance Director, City Treasurer, Budget Officer and other appropriate staff members form the City staff portion of the Financing Team. Other staff members or designees may be appointed to the Financing Team as needed.

3.2. Consultant Selection

The City will consider the professional qualifications and experience of consultants as it relates to the particular bond issue or other financing under consideration. Selection and contracting will be done in accordance with the Council-approved Purchasing Policies and Procedures manual.

If the City determines from the initial analysis phase that a negotiated sale (Section 5.1) is the best method of sale for an issue, the Finance Director shall select an underwriter and a separate financial advisor.

SECTION 4 –STRUCTURE AND TERM

4.1. Term of Debt

Debt will be structured for the shortest period practical, consistent with a fair allocation of costs to current and future users. The standard final maturity term of long-term debt borrowing is typically 12-20 years.

Consistent with its philosophy of keeping its capital facilities and infrastructure systems in good condition and maximizing a capital asset's useful life, the City will make every effort to set aside sufficient current revenues to finance ongoing maintenance needs and to provide reserves for periodic replacement and renewal. Generally, no debt will be issued for periods exceeding the useful life or average useful lives of projects to be financed.

4.2. Debt Repayment Structure

In structuring a bond issue, the City will manage the amortization of the debt and, to the extent possible, match its cash flow to the anticipated debt service payments. In addition, the City will seek to structure debt with aggregate level debt service payments over the life of the debt. Structures with unlevel debt service will be considered when one or more of the following exist:

- Natural disasters or extraordinary unanticipated external factors make payments on the debt in the early years prohibitive;
- Such structuring is beneficial to the City's aggregate overall debt payment schedule;
- Such structuring will allow debt service to more closely match revenues.

4.3. Bond Maturity Options

For each issuance, the City will select serial bonds or term bonds, or both. The decision to use term or serial is typically driven by market conditions.

4.4. Interest Rate Structure

The City currently issues securities on a fixed interest rate basis only. Fixed rate securities ensure budget certainty through the life of the issue and avoid the volatility of variable rates.

4.5. Credit Enhancement

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

4.6. Debt Service Reserve Fund

Debt service reserve funds are created by the City to make principal and interest payments to bondholders in the event that pledged revenues are insufficient to do so. The City will fund debt service reserve funds when it is in the City's overall best financial interest.
The size of the reserve fund is generally the lesser of:

- 10% of par
- 125% of average annual debt service
- 100% of maximum annual debt service

The City may decide not to utilize a reserve fund if the Finance Director, in consultation with the underwriter and financial advisor, determines there would be no adverse impact to the City's credit rating or interest rates.

4.7. Call Options/Redemption Provisions

A call option or optional redemption provision gives the City the right to prepay or retire debt prior to its stated maturity date. This option may permit the City to achieve interest savings in the future through the refunding of the bonds. Often the City will pay a higher interest rate as compensation to the buyer for the risk of having the bond called in the future. In addition, if a bond is called, the holder may be entitled to a premium payment ("call premium"). Because the cost of call options can vary depending on market conditions, an evaluation of factors will be conducted in connection with each issuance. The Finance Team shall evaluate and recommend the use of a call option on a case by case basis.

4.8. Debt Limits

The State of Iowa limits total outstanding local general obligation debt bonds to five percent of total assessed valuation for local government subdivisions. The City of Ames further limits debt capacity by reserving 25% of the State allowed maximum. The annual budget document demonstrates compliance with this policy. The City will carefully monitor its levels of general obligation debt.

Because the City's general obligation debt capacity is limited, it is important that general obligation debt only be used for financing projects where other financing methods cannot reasonably be used. If the City debt management analysis shows that adequate debt capacity is available and will remain available, general obligation bonds may be issued for City enterprise fund activities. The repayment of this debt will be provided by the activity receiving funding. The City's annual budget will provide a report of all abated debt and the source of funding for repayment of the debt.

Bond issues supported by Enterprise Funds should maintain a minimum ratio of net operating income to annual debt service that the Finance Director concludes is beneficial to the City. Typically, the higher the ratio the better the rating and the lower the interest rate paid by the City.

4.9. Derivatives

Derivative products may have application to certain City borrowing programs. In certain circumstances these products can reduce borrowing costs and assist in managing interest rate risk. However, these products carry with them certain risks not faced in standard debt instruments. The Finance Director shall evaluate the use of derivative products on a case-by-case basis to determine whether the potential benefits are sufficient to offset any potential costs.

4.10. Bond Refunding

The City shall refinance debt to achieve savings as market opportunities arise. The Finance Director shall remain cognizant of fluctuations in interest rates for the purpose of identifying refunding opportunities and prepare a present value analysis identifying the economic effects of a refunding to determine the value of refunding. Bond refunding may be undertaken in order to:

- Take advantage of lower interest rates and achieve debt service costs savings.
- Eliminate restrictive or burdensome bond covenants.
- Restructure debt to either lengthen the duration of debt or free up reserve funds.

Generally, the City shall strive to achieve a minimum of three percent net present value savings for a current refunding and a minimum of five percent net present value savings for an advance refunding. Upon the advice of the Finance Director and with the assistance of the financial advisor and bond counsel, the City will consider undertaking bond refunding for other than economic purposes upon a finding that such a restructuring is in the City's overall best financial interest.

SECTION 5 – METHOD OF ISSUANCE AND SALE

5.1. Method of Sale

Debt issues are sold to a single underwriter or to an underwriting syndicate, either through a competitive sale or a negotiated sale. A negotiated sale may involve the sale of securities to investors through an underwriter or the private placement of the securities with a financial institution or other sophisticated investor. The selected method of sale will be that which is most beneficial to the City in terms of lowest net interest rate, most favorable terms in financial structure, and market conditions.

The City will use competitive sales as the primary means of selling bonds. The City, however, reserves the option of pursuing a negotiated sale if there is evidence of volatile market conditions, complex security features, or other overriding factors. If the negotiated sale option is utilized, the Finance Director, with the approval of City Council, will negotiate the best possible interest rates for the City. The overall objective is to obtain the lowest possible interest cost and provide pricing transparency.

5.2. Initial Disclosure Requirements

The City acknowledges its disclosure responsibilities. Under the guidance of Bond Counsel, the City will distribute or cause an underwriter to distribute its Preliminary Official Statement and final Official Statement (neither is typically required in a private placement, although in some cases a "private placement memorandum" may be required by the investor).

The Financing Team shall be responsible for soliciting "material" information (as defined in Securities and Exchange Commission Rule 10b-5) from City departments and identifying contributors who may have information necessary to prepare portions of the Official Statement or who should review portions of the Official Statement. In doing so, the Financing Team shall confirm that the Official Statement accurately states all "material" information relating to the decision to buy or sell the subject bonds and that all information in the Official Statement has been critically reviewed by an appropriate person.

In connection with an initial offering of securities, the City and other members of the Financing Team will:

- Identify material information that should be disclosed in the Official Statement;
- Identify other persons that may have material information (contributors);
- Review and approve the Official Statement;
- Ensure the City's compliance, and that of its related entities, with federal and state securities laws.

The City's Finance Director shall contact the individuals and departments identified as contributors as soon as possible in order to provide adequate time for them to perform their assigned tasks. Contributors shall assist in reviewing and preparing the Official Statement using his or her knowledge of the City and, if appropriate, by discussing the Official Statement with other members of the contributor's department to ensure accuracy.

The Finance Director shall review the Official Statement, identify any material differences in the presentation of financial information from the financial statements and ensure there are no misstatements or omissions of material information in any sections that contain information prepared by the Finance Department or of relevance to the finances of the City.

The City Attorney (or designee) shall review the Official Statement descriptions of (i) any material current, pending or threatened litigation, (ii) any material settlements or court orders and (iii) any other legal issues that are material information for purposes of the Official Statement.

The approval of an Official Statement shall be placed on the Department Reports portion of the City Council agenda and shall not be considered as a Consent agenda item. The staff report will summarize the City Council's responsibilities with respect to the Official Statement and provide the City Council the opportunity to review a substantially final Official Statement. The City Council shall undertake such review as deemed necessary by the City Council to fulfill the City Council's securities law responsibilities.

The Securities and Exchange Commission (the "SEC"), the agency with regulatory authority over the City's compliance with the federal securities laws, has issued guidance as to the duties of the City Council with respect to its approval of the POS. In the "Report of Investigation in the Matter of County of Orange, California as it Relates to the Conduct of the Members of the Board of Supervisors" (Release No. 36761 / January 24, 1996) (the "Release"), the SEC stated that, if a member of the City Council has knowledge of any facts or circumstances that an investor would want to know about prior to investing in the bonds, whether relating to their repayment, tax-exempt status, undisclosed conflicts of interest with interested parties, or otherwise, he or she should endeavor to discover whether such facts are adequately disclosed in the Official Statement. In the Release, the SEC stated that the steps that a member of the City Council could take include becoming familiar with the POS and questioning staff and consultants about the disclosure of such facts.

For any privately placed debt with no Official Statement, the City Council must be provided with the final staff report describing the issue and such other documents the City Council may request before the transaction is approved.

SECTION 6 – CREDITWORTHINESS OBJECTIVES

Ratings are a reflection of the general fiscal soundness of the City and the capabilities of its management. Typically, the higher the credit ratings are, the lower the interest cost is on the City's debt issues. To enhance creditworthiness, the City is committed to prudent financial management, systematic capital planning, and long-term financial planning. The City recognizes that external economic, natural, or other events may, from time to time, affect the creditworthiness of its debt.

The most familiar nationally recognized bond rating agencies are Standard and Poor's, Moody's Investors Service, and Fitch Ratings. When issuing a credit rating, rating agencies consider various factors including but not limited to:

- City's fiscal status.
- City's general management capabilities.
- Economic conditions that may impact the stability and reliability of debt repayment sources.
- City's general reserve levels.

- City’s debt history and current debt structure.
- Project being financed.
- Covenants and conditions in the governing legal documents.

6.1. Bond Ratings

The Financing Team will assess whether a credit rating should be obtained for an issuance. The City typically seeks a rating from at least one nationally recognized rating agency on new and refunded issues being sold in the public market. The Finance Director, working with the Financing Team, shall be responsible for determining which of the major rating agencies the City shall request provide a rating. When applying for a rating on an issue, the City shall prepare a formal presentation of the City’s finances and developments within the City which will be reviewed by the Financing Team (Section 7.5) before its presentation to a rating agency.

6.2. Rating Agency Communications

The Finance Director is responsible for maintaining relationships with the rating agencies that assign ratings to the City’s various debt obligations. This effort shall include providing the rating agencies with the City’s financial statements, if applicable, as well as any additional information requested.

SECTION 7 - POST ISSUANCE ADMINISTRATION

7.1. Investment of Proceeds

The City Treasurer shall invest bond proceeds and reserve funds in accordance with each issue’s indenture or trust agreement, utilizing competitive bidding when possible. All investments will be made in compliance with the City’s Investment Policy objectives of safety, liquidity and then yield.

7.2. Use of Bond Proceeds

The Finance Director is responsible for ensuring bond proceeds are spent for the intended purposes identified in the bond documents and that the proceeds are spent in the time frames identified in the tax certificate prepared by the City’s bond counsel.

7.3. Arbitrage Compliance

The City shall follow a policy of full compliance with all the arbitrage and rebate requirements of the federal tax code and Internal Revenue Service regulations. If needed, the City shall engage qualified third parties for the preparation of arbitrage and rebate calculations. All necessary rebates will be filed and paid when due.

7.4. Ongoing Disclosure

The City shall comply with the requirements of the Continuing Disclosure Certificate(s) entered into at the time of each bond issue. The Finance Director shall be responsible for providing ongoing disclosure information to the Municipal Securities Rulemaking Board’s (MSRB’s) Electronic Municipal Market Access (EMMA) system, the central depository designated by the Securities and Exchange Commission for ongoing disclosure by municipal issuers.

The Finance Team will prepare the annual disclosure reports in accordance with the Continuing Disclosure Certificates. The Finance Team will identify material information that should be disclosed and identify other persons that may have knowledge of material information.

In addition to annual reports, Securities and Exchange Commission Rule 15c2-12(b)(5)(i)(C) obligates the City to disclose, in a timely manner to the MSRB, notice of certain specified events with respect to the City's securities, including the following:

- Principal and interest payment delinquencies;
- Non-payment related defaults;
- Unscheduled draws on debt service reserves reflecting financial difficulties;
- Unscheduled draws on credit enhancements reflecting financial difficulties;
- Substitution of credit or liquidity providers, or their failure to perform;
- Adverse tax opinions or event affecting tax-exempt status of security;
- Modifications to rights of securities holders, if material;
- Bond calls, if material, or tender offers;
- Defeasances;
- Release, substitution, or sale of property securing repayment of the securities, if material;
- Rating changes;
- Bankruptcy, insolvency, receivership of an obligated person;
- Consummation of a merger, consolidation, or acquisition or sale of substantially all of the assets of an obligated party (other than in the ordinary course of business), the entry into a definitive agreement to undertake such an action, or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material;
- Change of fiscal agent or trustee;
- Failure to provide annual financial information or event notification as required.

The Finance Team, with Finance Director approval, may file notice with the MSRB of specified events listed in the Continuing Disclosure Certificates if the City is contractually obligated to file and the Disclosure Document contains no discretionary content.

7.5. Disclosure Documents

Disclosure documents shall include, but are not limited to, the following:

- Preliminary and final official statements;
- Private placement memoranda and remarketing memoranda;
- Any filing made by the City with the MSRB, whether made pursuant to a continuing disclosure undertaking to which the City is a party or made voluntarily;
- Rating agency presentations, and other communications, reasonably likely, in the determination of the Financing Team to reach investors or the securities market;
- Offering documents prepared by related entities if such documents are subject to the approval of the City Council;
- Management's discussion and analysis and transmittal letter portions of the City's audited financial statement;
- Press releases to the extent that such releases are intended as communication to the financial markets.

Any person preparing a document for release to the public that may be considered a Disclosure Document shall notify the Finance Director of such information and its proposed or mandatory dissemination date. If the document is not on the list of Disclosure Documents and the Finance Director determines it is intended as communication to the financial markets, Bond Counsel or Financial Advisors may be consulted for advice.

7.6. Compliance with Other Bond Covenants

In addition to financial disclosure and arbitrage, the City is also responsible for verifying compliance with all undertakings, covenants, and agreements of each bond issuance on an ongoing basis. This typically includes ensuring:

- Annual appropriation of revenues to meet debt service payments;
- Taxes/fees are levied and collected where applicable;
- Timely transfer of debt service payments to the trustee;
- Compliance with insurance requirements;
- Compliance with rate covenants.

The City shall comply with all covenants and conditions contained in governing law and any legal documents entered into at the time of the bond offering. The Finance Director will coordinate verification and monitoring of covenant compliance.

7.7. Retention

A copy of all relevant documents and records will be maintained by the Finance Department for the term of the bonds (including refunding bonds, if any) plus five years. Relevant documents and records will include sufficient documentation to support the requirements relating to the tax-exempt status, including the following:

- Bond transcripts, official statement and other offering documents.
- All documents relating to capital expenditures financed by bond proceeds. Such documents will include construction contracts, purchase orders, invoices and payment records. Such documents will include documents relating to costs reimbursed with bond proceeds.
- Records will be maintained identifying the assets or portion of assets that are financed with bond proceeds.
- All contracts and arrangements involving private use of the bond financed assets.
- All reports relating to the allocation of bond proceeds and private use of bond financed assets.
- All records of investments, investment agreements, arbitrage reports, return filings with the IRS and underlying documents, trustee statements, rating correspondence, and continuing disclosure.

7.8. Investor Relations

While the City shall post its annual financial report as well as other financial reports on the City's website, this information is intended for the citizens of Ames. Information with the intention of reaching the investing public, including bondholders, rating analysts, investment advisors, or any other members of the investment community shall be filed on the EMMA system.

7.9. Additional Requirements for Financial Statements

It is the City's policy to hire an auditing firm that has the technical skills and resources to properly perform an annual audit of the City's financial statements. More specifically, the firm shall be a recognized expert in the accounting rules applicable to the City and shall have the resources necessary to review the City's financial statements on a timely basis.

APPENDIX A – GLOSSARY AND MUNICIPAL SECURITIES TERMINOLGY

Advance Refunding: Refunding bonds that are issued more than 90 days prior to the date upon which the refunded bonds will be redeemed. 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.

Arbitrage: The gain that may be obtained by borrowing funds at a lower (often tax-exempt) rate and investing the proceeds at higher (often taxable) rates. The ability to earn arbitrage by issuing tax-exempt securities has been severely curtailed by the Tax Reform Act of 1986, as amended.

Assessed Valuation: The appraised worth of property as set by a taxing authority through assessments for purposes of ad valorem taxation.

Bond: A security that represents an obligation to pay a specified amount of money on a specific date in the future, typically with periodic interest payments.

Bond Counsel: An attorney retained by the issuer to give a legal opinion concerning the validity of securities. The bond counsel's opinion usually addresses the subject of tax exemption. Bond counsel may prepare or review and advise the issuer regarding authorizing resolutions, trust indentures and litigation.

Bond Insurance: A type of credit enhancement whereby an insurance company indemnifies an investor against default by the issuer. In the event of failure by the issuer to pay principal and interest in full and on time, investors may call upon the insurance company to do so. Once issued, the municipal bond insurance policy is generally irrevocable. The insurance company receives its premium when the policy is issued.

Bond Resolution: Resolution adopted by the City Council authorizing the issuance of bonds, approving the Notice of Sale and the Official Statement.

Call Option: The right to redeem a bond prior to its stated maturity, either on a given date or continuously. The call option is also referred to as the optional redemption provision. Often a "call premium" is added to the call option as compensation to the holders of the earliest bonds called.

Bond: A municipal security on which the investment return on an initial principal amount is reinvested at a stated compounded rate until maturity, at which time the investor receives a single payment representing both the initial principal amount and the total investment return.

CAFR: The City's Comprehensive Annual Financial Report.

Competitive Sale: A sale of bonds in which an underwriter or syndicate of underwriters submit sealed bids to purchase the bonds. Bids are awarded on a true interest cost basis ("TIC"), providing that other bidding requirements are satisfied. Competitive sales are recommended for simple financings with a strong underlying credit rating. This type of sale is in contrast to a Negotiated Sale.

Conduit Financing: The issuance of securities by a governmental entity to finance a project that will primarily benefit a third party. The security for this type of financing is the credit of the third party.

Usually such securities do not constitute general obligations of the issuer since the private entity is liable for generating the pledged revenues for repayment. Industrial development bonds are a common type of conduit refinancing.

Continuing Disclosure: The requirement by the Securities and Exchange Commission for most issuers of municipal debt to provide current financial information to the Municipal Securities Rulemaking Board for access by the general marketplace.

Credit Rating Agency: A company that rates the relative credit quality of a bond issue and assigns a letter rating. These rating agencies include Moody's Investors Service, Standard & Poor's, and Fitch Ratings.

Current Refunding: Refunding bonds are issued 90 days or less before the date upon which the refunded bonds will be redeemed.

Debt Limit: The maximum amount of debt that is legally permitted by a jurisdiction's charter, constitution, or statutes.

Debt Service: The amount necessary to pay principal and interest requirements on outstanding bonds for a given year or series of years.

Default: The failure to pay principal or interest in full or on time and, in some cases, the failure to comply with non-payment obligations after notice and the opportunity to cure.

Defeasance: Providing for the payment of principal, premium (if any) and interest on debt through the call date or scheduled principal maturity in accordance with the terms of the debt. A legal defeasance usually involves establishing an irrevocable escrow funded with only cash and U.S. Government obligations.

Derivative: A financial instrument which derives its own value from the value of another instrument, usually an underlying asset such as a stock, bond, or an underlying reference such as an interest rate index.

Discount: The difference between a bond's par value and the price for which it is sold when the latter is less than par.

Financial Advisor: A consultant who provides the issuer with advice on the structure of the bond issue, timing, terms and related matters for a new bond issue.

Financing Team: The working group of City staff and outside consultants necessary to complete a debt issuance.

General Obligation Bond: A bond secured by an unlimited property tax pledge. Requires a two-thirds vote by the electorate. GO bonds usually achieve lower rates of interest than other financing instruments since they are considered to be a lower risk.

Indenture: A contract between the issuer and the trustee stipulating the characteristics of the financial instrument, the issuer's obligation to pay debt service, and the remedies available to the trustee in the event of default.

Industrial Development Bonds: Securities issued to finance the construction or purchase of industrial, commercial or manufacturing facilities to be purchased by or leased to a private user. These securities are backed by the credit of the private user and generally are not considered liabilities of the governmental issuer.

Issuance Costs: The costs incurred by the bond issuer during the planning and sale of securities. These costs include but are not limited to financial advisory, bond counsel, disclosure counsel, printing, advertising costs, rating agencies fees, and other expenses incurred in the marketing of an issue.

Lease: An obligation wherein a lessee agrees to make payments to a lesser in exchange for the use of certain property. The term may refer to a capital lease or to an operating lease.

Letter of Credit: An unconditional pledge of the bank's credit which is used to guarantee payment of principal and interest on debt in the event insufficient funds are available to meet a debt service obligation. Letters of credit are most often employed when the stated interest on the City's securities is variable.

Line of Credit: A contract with a financial institution, usually a bank, that establishes a maximum loan balance that the bank will permit the borrower to maintain. The borrower can draw down on the line at any time, as long as the maximum set in the agreement is not exceeded.

Mortgage Revenue Bonds: Bonds issued for the purpose of providing single-family mortgage financing or acquisition and construction funds for multi-family housing projects. The bonds are secured by the mortgage repayments and project revenue. See Conduit Financing.

Municipal Securities Rulemaking Board (MSRB): A self-regulating organization established on September 5, 1975 upon the appointment of a 15-member board by the Securities and Exchange Agreement. The MSRB, comprised of representatives from investment banking firms, dealer bank representatives, and public representatives, is entrusted with the responsibility of writing rules of conduct for the municipal securities market.

Negotiated Sale: A sale of securities in which the terms of the sale are determined through negotiation between the issuer and the purchaser, typically an underwriter, without competitive bidding. The negotiated sales process provides control over the financing structure and issuance timing. Negotiated sales are recommended for unusual financing terms, periods of market volatility and weaker credit quality. A thorough evaluation of market conditions will be performed to ensure reasonable final pricing and underwriting spread.

Net Interest Cost (NIC): A method of computing the interest expense to the issuer of bonds, which may serve as the basis of award in a competitive sale of a new issue of municipal securities. NIC takes into account any premium or discount applicable to the issue, as well as the dollar amount of coupon interest payable over the life of the issue. NIC does not take into account the time value of money (as would be done in other calculation methods, such as the "true interest cost" (TIC) method). The term "net interest cost" refers to the overall rate of interest to be paid by the issuer over the life of the bonds.

Official Statement (Prospectus): A document published by the issuer in connection with a primary offering of securities that discloses material information on a new security issue including the purposes of the issue, how the securities will be repaid, and the financial, economic and social characteristics of the security for the bonds. Investors may use this information to evaluate the credit quality of the securities.

Original Issue Discount Bonds: Bonds sold at a substantial discount from their par value at the time of the original sale.

Par Value: The face value or principal amount of a security.

Preliminary Official Statement: A version of the Official Statement prepared by or for an issuer of municipal securities for potential customers prior to the availability of the final Official Statement. Under SEC Rule 15c2-12, the difference between a Preliminary Official Statement and a final Official Statement is that the final Official Statement includes "pricing information," i.e., offering price(s), interest rate(s), selling compensation, aggregate principal amount, principal amount per maturity, delivery dates, any other terms or provisions required by an issuer of such securities to be specified in a competitive bid, ratings, other terms of the securities depending on such matters, and the identity of the underwriter(s).

Premium: The excess of the price at which a bond is sold over its face value.

Present Value: The value of a future amount or stream of revenues or expenditures.

Pricing Consultant: The Pricing Consultant provides a fairness letter to the City or its agent regarding the pricing of a new issue of municipal securities.

Private Placement: A bond issue that is structured specifically for one purchaser. Private placements are typically carried out when extraneous circumstances preclude public offerings. A private placement is considered to be a negotiated sale.
Refunding: A procedure whereby an issuer refinances an outstanding debt issue by issuing a new debt issue.

Related Entities: Those independent agencies, joint power authorities, special districts, component units, or other entities created by the City Council or by State law for which the City Council serves as the governing or legislative body in his or her official capacity, or for which the City has agreed to provide initial or continuing disclosure in connections with the issuance of securities.

Rule 10b5: Rule adopted by the Securities and Exchange Commission that requires the disclosure of all material facts and prohibits the omission of facts necessary to make statements not misleading.

Rule 15c2-12: Rule adopted by the Securities and Exchange Commission setting forth certain obligations of (i) underwriters to receive, review and disseminate official statements prepared by issuers of most primary offerings of municipal securities, (ii) underwriters to obtain continuing disclosure agreements from issuers and other obligated persons to provide ongoing annual financial information on a continuing basis, and (iii) broker-dealers to have access to such continuing disclosure in order to make recommendations of municipal securities in the secondary market.

Reserve Fund: A fund established by the indenture of a bond issue into which money is deposited for payment of debt service in case of a shortfall in current revenues.

Revenue Bond: A bond which is payable from a specific source of revenue and to which the full faith and credit of an issuer is **not** pledged. Revenue bonds are payable from identified sources of revenue, and do not permit the bondholders to compel a jurisdiction to pay debt service from any other source. Pledged revenues often are derived from the operation of an enterprise.

Secondary Market: The market in which bonds are sold after their initial sale in the new issue market.

Serial Bonds: Bonds of an issue that mature in consecutive years or other intervals and are not subject to mandatory sinking fund provisions.

Special Tax Bonds: Bonds issued to fund eligible public improvements and paid with special taxes levied in a community facilities district formed under the Mello-Roos Community Facilities Act of 1982, as amended. The City's policy on Community Facilities Districts and Special Tax Bonds is further outlined in City Council Resolution 2009-103.

State Revolving Funds: The State Revolving Fund ("SRF") loan is a low interest loan program for the construction of water and wastewater infrastructure projects.

Term Bonds: Bonds that come due in a single maturity whereby the issuer may agree to make periodic payments into a sinking fund for mandatory redemption of term bonds before maturity or for payment at maturity.

True Interest Cost (TIC): Under this method of computing the interest expense to the issuer of bonds, true interest cost is defined as the rate necessary to discount the amounts payable on the respective principal and interest payment dates to the purchase price received for the new issue of bonds. Interest is assumed to be compounded semi-annually. TIC computations produce a figure slightly different from the "net interest cost" (NIC) method because TIC considers the time value of money while NIC does not.

Trustee: A bank retained by the issuer as custodian of bond proceeds and official representative of bondholders. The trustee ensures compliance with the indenture. In many cases, the trustee also acts as paying agent and is responsible for transmitting payments of interest and principal to the bondholders.

Underwriter: A broker-dealer that purchases a new issue of municipal securities from the issuer for resale in a primary offering. The bonds may be purchased either through a negotiated sale with the issuer or through a competitive sale.