

RESOLUTION NUMBER 7167

**A RESOLUTION OF THE MISSOULA CITY COUNCIL CREATING A DEBT MANAGEMENT POLICY
OF THE CITY OF MISSOULA.**

WHEREAS a debt management policy is helpful for issuing, administering and managing municipal debt; and

WHEREAS, Title 7, Chapter 7 of the Montana Code Annotated is entitled "Debt Management" for local government; and

WHEREAS, prudent financial management encourages the Missoula City Council to establish a Debt Management Policy to serve as a guideline when the City of Missoula is issuing debt instruments; and

WHEREAS the Missoula City Council considered and adopted the attached municipal debt policy for the City of Missoula at its October 16, 2006 meeting; and

NOW, THEREFORE, BE IT RESOLVED, that the attached Policy of the City of Missoula be established as the official debt management policy.

FURTHER BE IT RESOLVED THAT this document shall also be included in the Missoula Administrative Rules and Procedures as Policy No. 33, on file in the Missoula City Clerks' Office.

PASSED AND ADOPTED this 16th day of October, 2006.

ATTEST:

/s/ Martha L. Rehbein
Martha L. Rehbein, City Clerk

APPROVED:

/s/ John Engen
John Engen, Mayor

(Seal)

Debt Management Policy

City of Missoula

Executive Summary

This debt policy for the City of Missoula is designed to provide a clear basis as to the City's policies and practices so that our creditors, elected officials and citizens will understand the basis of debt issuance by the City. This policy formally puts in writing what our past and present debt issuance practices have been.

The policy addresses the following issues:

1. Provides a statement of purpose.
2. Provides general guidelines, definitions and conditions for debt issuance.
3. Discusses the various types of debt issued by the City.
4. Identifies debt structuring characteristics addressing repayment terms, tax exempt status, prepayment provisions, sale to accredited investors and credit ratings.
5. Discusses the three methods for selling the City's debt and the preferred method of sale.
6. Provides a process for underwriter selection for negotiated sales.
7. Provides the basis of award for bond sales.
8. Provides the basic guidelines for the City's debt management:
 - Required Debt service cash flow monitoring.
 - Targeted debt level maximum for voted G.O. debt (66% of statutory debt capacity).
 - Targeted debt level maximum for non-voted General Fund debt (66% of legal debt limit).
 - Targeted debt level maximum for annual appropriation obligations (capital leases) which would be 1% of General fund Expenditures in the preceding year.
 - Basis for issuance of revenue debt (enterprise funds).
 - Criteria for securing the issuance of special improvement district debt and curb & gutter debt.
 - Guidelines for the issuance of tax increment debt.
 - Criteria for the refunding of City debt.
 - Criteria for the use of derivatives (currently illegal for Montana cities).
9. Establishes interim reporting to the Mayor and Council.
10. Other administrative procedures and guidelines for the City Finance office.

This Debt Management Policy is adopted to promote the effective use of debt as a financing tool and to guide decision-making on its application.

Debt Management Policy

I. Statement of Purpose

- A. To preserve the public trust and prudently manage public assets to minimize costs to taxpayers and ensure current decisions positively impact future citizens.
- B. To minimize borrowing costs.
- C. To preserve access to capital markets.
- D. To ensure future financial flexibility in debt financing options.

II. Guidelines for Use of Debt Financing

- A. Debt is a financing tool which should only be judiciously used within the City's legal, financial and debt market capacities.
- B. Definitions
 1. Debt. The creation of debt occurs when a governing body incurs a financial obligation that can not, or will not, be repaid from current fiscal period revenues. Debt may be in the form of bond or note.
 2. Short Term Debt. For purposes of this policy, Short Term Debt means debt with a repayment term of less than 5 years.
 3. Long term Debt. For purposes of this Policy, Long Term Debt means debt with repayment terms beyond the term of the Short Term Debt, up to the maximum term allowable by law, generally twenty years.
 4. Cash Flow Financing. Cash flow financing means tax and revenue anticipation notes (TANS and RANS) that are issued in anticipation of the receipt of the revenues, and tax dollars levied and appropriated and expected to be received in the fiscal year in which the note is issued. Because TANS and RANS are payable from current year revenues they do not constitute debt.
- C. General Conditions for the Use of Long-term Debt

Debt will be considered when some or all of the following conditions exist:

 1. Estimated future revenues are sufficient to ensure the long-term viability of repayment of the debt obligation;
 2. Other financing options have been explored and they 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; and
 4. The asset useful life lends itself to long term debt financing.
- D. Debt Issuance versus Pay-As-You-Go (PAYG) Financing

The City shall seek to appropriately use PAYG financing, when feasible, based on the following criteria:

 1. The project can be adequately funded from available current revenues and fund balances;
 2. The project can be completed within an acceptable timeframe when funded from current revenues;
 3. Additional debt levels could adversely impact credit ratings or capacities to repay existing obligations;
 4. Market conditions are such that PAYG presents a favorable option; or
 5. The asset's useful life itself is not conducive to long term debt financing.

III. Types of Debt

The City may have choices as to the type of debt which would best meet the needs of the particular financing and its overall objectives. The following is a listing of the types of debt and general guidelines as to their use.

A. General Obligation and Related Debt

1. *General Obligation (G.O.).* General Obligation bonds provide the investor with its most secure City transaction, because of the City's pledge of its unlimited authority to levy ad valorem property taxes for debt service. G.O. bonds require voter approval to be issued. The overall amount of G.O. bonds is limited by statute.
2. *General Fund Bonds.* General Fund bonds are secured by a long-term pledge by the City of General Fund revenues. It differs from a G. O. bond in that it is not a long-term pledge of an unconditional levy of property taxes. The issuance of General Fund bonds has three statutory restrictions: a) no single issue can exceed 10% of the General Fund budget for each of the two preceding years; b) at the time of issuance the total of all such debt service can not exceed 2% of the General Fund's revenues for each of the two preceding years; and c) the maximum term of any issue can not exceed 20 years.
3. *Annual Appropriation Obligations.* These obligations are financial contracts which are secured solely by the City's pledge to annually consider an appropriation for their payment. As this consideration is on an annual basis, the obligations do not provide a legally binding commitment for a long-term pledge of repayment. They are less secure to the investor due to the risk of non-appropriation. The City has the potential to use annual appropriation obligations for either governmental purpose projects or as additional security for economic development projects. The City will consider its use in the latter case only in extreme situations and then only for public improvements having a city-wide benefit. In economic development applications the City will look to the related economic development revenues to provide full payment of all obligations and to have a minimum coverage level of 130%.

B. Revenue Debt

1. *Revenue Bonds* can be issued to fund certain types of revenue producing municipal enterprises, infrastructure systems or in relation to economic development projects. Revenue bonds are secured by the revenues of the particular system or project being financed. Revenue bonds are not secured by general municipal revenues or the general property tax.
2. *Tax Increment Financing (TIF) Debt;* this type of revenue bond is secured by TIF revenues from a TIF district or an individual TIF project. TIF bonds can only fund eligible project costs permitted under the statute. In certain cases TIF bonds may be issued as federally taxable securities due to the nature of expenditures and the special augmented security provided by private parties involved with a development.

C. Special Assessment Debt

1. *Special Improvement District (SID) Debt;* this type of bond is secured by special assessments levied on specific properties for related municipal infrastructure improvements which specially benefit those particular properties. The statute requires a 5% contribution to an overall SID revolving fund, and the provision for up to an additional 5% for the funding

of a debt service reserve fund specific to a particular bond issue, if necessary to secure and market the debt.

2. *Curb and Gutter Debt*; this type of bond is secured by special assessments levied on specific properties for these improvements which specially benefit those particular properties. The statute requires a 5% contribution to an overall SID revolving fund.

D. Conduit Bonds

The City may act as an issuer for a private or non-profit party. In these cases the City acts as a 'conduit' issuer of tax-exempt bonds as defined by federal and state law. Conduit bonds are secured solely by revenues of the private or non-profit party, and are not an obligation of the City.

E. Debt Structuring Characteristics

In general the City will seek to structure its debt issues with these terms. The City recognizes that certain debt transactions may require deviations from these terms given the specific financial conditions.

1. *Repayment Term*. The City will structure its debt to comply with all federal and state and local requirements as to repayment terms. The City will seek to repay its debt in an expeditious manner within the City's overall financial objectives and in consideration of the dedicated repayment revenue source(s) and the useful life of the project.
2. *Taxable debt*. The City shall primarily seek to issue and/or guarantee only tax-exempt debt and avoid taxable debt to reduce interest expenses. However, the City recognizes that in certain cases the issuance of taxable debt may be required and/or beneficial to the City in reducing its risk for a particular project. Prior to issuing taxable debt the City will complete an evaluation of the cost and risk differentials.
3. *Prepayment Provisions*. Redemption provisions and call features shall be in compliance with particular statutory provisions by type of issue, and be evaluated in the context of each bond sale to enhance marketability of the bonds; to ensure flexibility related to potential early redemption; to foster future refunding transactions; or in consideration of special conditions of the transaction. Additional cost of call premium and higher interest rates as a result of including a call provision shall also be evaluated.
4. *Sale to Accredited Investors*. Certain issues may be of a highly speculative nature due to the type of project or the revenue structure. The City wants to ensure that all of its issues are purchased by investors fully knowledgeable of the risks involved with the investment. For highly speculative issues the City will require the purchase by qualified investors, those generally defined by the Securities and Exchange Commission, Regulation D. To ensure these types of investors are maintained both in the primary and secondary bond markets, the City will require either minimum denominations of \$50,000 or that all future investors are accredited.
5. *Credit Ratings*. The City will seek to obtain investment grade credit ratings when possible. Credit ratings provide a standard for proper bond structuring, generally expand the market thereby reducing overall financing costs and provide an independent assessment of overall financial condition.

IV. Bond Sale

A. Method of Sale

Three methods of sale exist for the placement of municipal bonds:

1. *Competitive sale.* Bonds are marketed to a wide audience of investment banking (underwriting) firms. Their bids are submitted at a specified time. The underwriter is selected based on its best bid (lowest true interest cost) for its securities.
2. *Negotiated sale.* The City selects the underwriter or group of underwriters of its securities in advance of the bond sale. The City financing team works with the underwriter to bring the issue to market and negotiates all interest rates and terms of the sale.
3. *Private placement.* The City sells its bonds to a limited number of sophisticated investors, and not the general public. Private placement bonds are often characterized as having higher risk or a specific type of investor base.

B. Preferred Method of Sale

The City will sell their municipal bond issues on a competitive basis unless specific conditions exist which warrant a different manner. Such conditions may include:

1. A bond structure which is not conducive to a competitive bond sale due to its structure;
2. An issue which lacks an investment grade rating or has complex security provisions;
3. An issue with a small principal amount; and
4. A municipal bond market which is experiencing significant volatility.

Regardless of the conditions above, the City must follow the particular statutory provisions for the method of sale for each type of issue. Further, on all sales the City will obtain an opinion from its financial advisor as to the reasonableness of the financing structure and the proposed interest rates.

C. Selection of Underwriter for Negotiated Sales

For negotiated sales, the City will select an underwriter(s) through a competitive process. This process will include a request for proposals from firms considered appropriate for the underwriting of the particular issue. The Director of Finance will set criteria deemed appropriate for the evaluation of underwriter proposals and select the underwriter(s) based on such criteria.

D. Award of Sale

The City and its agencies will award the sale of its bonds on a true interest cost (TIC) basis. A TIC basis considers the time value of money in its calculation.

V. Guidelines for Debt Management

Proactive debt management is a key component to the immediate and long-term success of the City's financial objectives. A successful debt management program begins with comprehensive information on the current debt program status and definition of the future direction of the City's capital financing objectives.

The City recognizes that a negative event relating to the repayment of any of its issues will have significant long term adverse consequences for all future debt obligations regardless of type. The City will seek to incorporate into each of its issues sufficient security provisions to mitigate this risk.

A. Debt Service Cash Flow Monitoring

The City shall maintain a system of debt service revenue forecasting for each of its major debt categories. For revenue only transactions the City will assess the probability of future collections of pledged revenues.

B. Guidelines for Targeted Debt Level Maximums

Maintaining the appropriate levels of debt is important to preserve capacity for future infrastructure investments and to position for high credit quality. Each type of debt has its own appropriate level. The appropriate levels are internally determined based on a variety of factors, such as: infrastructure investment needs of the particular service area, capacity to repay debt from the specific revenue source, and the sector's credit rating objectives. Since these factors can change over time, any debt guideline must be periodically reviewed to reflect evolving City conditions.

1. General Obligation Debt

The sum of all City direct debt by type shall not exceed the lesser of:

Percent of Assessed Valuation	66% of legal debt limit
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2. General Fund Debt

Principal Of Each Debt Issue Not To Exceed : (a) 10% of General Fund Budget each preceding two years, and (b) total debt service for all outstanding debt (66 % of General Fund Legal limit = $66\% \times 2\% \text{ Revenues for each preceding two years} = 1.32\%$ (of General Fund revenues) which is the targeted limit for General Fund debt issuance.

3. Annual Appropriation Obligations (i.e. capital leases)

Percent of General Municipal Expenditures in preceding year: - 1.0 %

4. Revenue (Enterprise) Obligations

Each type of enterprise fund revenue debt has an estimated capacity caused by its financial position, user rate revenue generation capability, and existing and anticipated future debt requirements.

5. Special Improvement District; Curb and Gutter Revenue Bonds;

The City will seek to maintain a security profile which will assist in mitigating any exposure of revenue deficiency draws against the overall revolving fund and funded reserve levels, and where possible obtain investment-grade credit ratings. The City recognizes that having to draw upon the revolving fund, supplemental reserves or a payment default puts at risk

the City's ability to efficiently fund all outstanding and future related issues. To maintain appropriate security the City will generally require the following security profile to each of these issues;

- a. Funding of the 5% SID revolving Fund is mandatory,
- b. Financing improvements to properties where at least 50% have structures on the parcels, and
- c. Assessments to Market Value being less than 33%.

If these conditions can not be met and the City still wishes to issue the bonds, then the City may seek one or more of the following additional risk mitigation approaches

- d. Debt Service Reserve equal to an additional 5% may be established for a specific debt issue,
- e. Require the project to be constructed and financed in multiple phases, or
- f. Require supplemental private party guarantees in the form of direct pay letters-of-credits from financial institutions with industry credit ratings of good or higher.

6. Tax Increment Financing Debt;

Where possible the City will seek to have pay-as-you-go TIF debt, wherein the project's private beneficiary receives debt payments over a period of time only from actual revenue collections. Where the project or financing does not lend itself to a PAYG approach, the City will require the individual TIF issues to have a funded debt service reserve, coverage at a minimum of 125%, an executed development contract clearly specifying the developer's requirements as to timing and valuation of development with suitable remedies for the City in the event of non-performance. Where appropriate the City will seek such other security guarantees as are deemed necessary solely by the City, regardless of the tax standing of the particular issue.

7. Defeasance, Prepayment and Refunding

The accelerated retirement and restructuring of debt can be valuable debt management tools. Accelerated retirement occurs through the use of defeasance and the exercise of prepayment provisions. Debt is often restructured through the issuance of refunding bonds.

The federal government has placed significant conditions on the tax-exempt refunding of outstanding issues. Refundings have two general categories:

Current refundings, where the refunding bonds are settled within 90 days of an optional prepayment date; and

Advance refundings, where refundings are settled more than 90 days in advance of an optional prepayment date. The federal restrictions are that any issue can only be advance refunded once on a tax-exempt basis.

On advance refundings the City will seek to obtain a minimum present value savings level of 3% of the present value of refunded debt service.

State law requires a demonstration of savings of 0.5% reduction in the average coupon interest rate between the refunding and refunded bonds.

8. Derivatives

Montana municipalities are not currently authorized to use derivatives. If state law authorizes municipalities to use derivatives, the City would consider their use in conjunction with significant evaluation as to the risks and benefits and with the advice of independent industry professionals. If used, the City would follow the Government Finance Officers Association's Recommended Practice on the use of Derivatives.

VI. Interim Reporting

The Director of Finance will provide the Mayor, City Council and Chief Administrative Officer a summary debt report at minimum at six-month intervals within 30 days of each December 31st and June 30th. While the contents of the summary debt report may vary over time, at minimum it will cover the actual experience to the Guidelines for Targeted Debt Maximums.

VII. Compliance

A. Compliance with Statutory and Code of Ordinances

The authority and manner in which the City issues its bonds are in large part dictated by the conveyed state statutory authority. The statutes provide numerous requirements on the issuance and structuring of City bonds, with variations by type of debt. The City will follow all statutory requirements in the issuance and structuring of its debt obligations, as well as ordinances provisions relative to debt issuance, term of debt, structuring, method of sale, etc.

B. Monitoring of Covenant Compliance

The City's revenue bonds generally have a number of bond covenants requiring ongoing compliance and conditions for future bond issuance on an equal security ('parity') basis. The City will maintain a compliance monitoring system by revenue bond type of all bond covenants. The system will track trends in coverage levels over time and capacity availability under the additional bonds covenants.

C. Federal Arbitrage and Rebate Compliance

1. The City will fully comply with the federal arbitrage and rebate regulations. Concurrent with this policy, the City will take all permitted steps to minimize any rebate liability through proactive management in the structuring and oversight of its individual debt issues.
2. All of the City's tax-exempt issues and obligations are subject to arbitrage compliance regulations. The Finance Department and the requesting departments shall be responsible for the following:
 - a. Using bond proceeds only for the purpose and authority for which the bonds were issued. Tax-exempt bonds will not be issued unless it can be demonstrated that 85% of the proceeds will be expended within the three-year temporary period.
 - b. Performing rebate calculations on certain construction funds as determined by IRS. The City will engage an arbitrage consulting firm to perform annual rebate calculations.

- c. Performing rebate computations annually, but in no event later than each five-year anniversary date of the issuance and at the final maturity for all bonds. Examining whether the City met the rebate exception calculation rules.
- d. Maintaining detailed investment records, including purchase prices, sale prices and comparable market prices for all securities.
- e. Monitoring expenditure of the bond proceeds and exercising best efforts to spend bond proceeds in such a manner that the City shall meet one of the spend-down exemptions from rebate.
- f. Monitoring the investment of bond proceeds with awareness of rules pertaining to yield restrictions.

To the extent rebate liability exists, the City will report such liability in its comprehensive annual financial report (CAFR).

VIII. Disclosure Compliance

A. Introduction

Disclosure is both a regulatory requirement and a highly advisable means to enhance the marketing of the City's bonds. The Securities and Exchange Commission (SEC) regulates both primary disclosure, the initial marketing of a bond issue, and continuing disclosure, the ongoing information to the market about the status of the issue and issuer. Initial and ongoing disclosure are subject to the anti-fraud provisions of the securities laws, requiring an issuer to provide all material information about a bond issue and the security for the bond issue. In addition to general anti-fraud issues, the SEC regulates the manner in which bond underwriters can underwrite municipal securities. SEC Rule 15c2-12 (the "Rule") requires, among other things, that an underwriter obtain an official statement meeting certain requirements. The Rule also prohibits an underwriter from marketing municipal securities unless the issuer enters into an undertaking to provide continuing disclosure to the market.

Adequate disclosure on both a primary and continuing basis can enhance the marketability of the City's bonds by providing potential investors with current and professional information regarding the City. Timely and accurate completion of these tasks both influences investors' decisions on purchasing the City's bonds and contributes to the competitive audience for the City's bonds.

The City will fully comply with disclosure regulations.

B. Primary

In the preparation of official statements the City will follow professional and market standards in the presentation of disclosure about its bond issues. The City will facilitate the distribution of the official statements in a timely manner to allow investors adequate time to make their investment decisions in an informed manner. The City will disclose all material information about its bond issue and the security for the bond issue.

The City will execute continuing disclosure undertakings in a manner to fully comply with regulatory provisions and ensure a full disclosure of appropriate information to the market.

C. Secondary

The City will meet all substantive and time requirements in its annual continuing disclosure filings, which include making the City's CAFR available to the public 180-270 days after the fiscal year end. The City will keep current with any changes in both the administrative aspects of its filing requirements and the national repositories responsible for ensuring issuer compliance with the continuing disclosure regulations. In the event a 'material event' occurs requiring immediate disclosure, the City will ensure information flows to the appropriate disclosure notification parties in a timely manner.

Any filing may be made solely by transmitting such filing to the Texas Municipal Advisory Council (the "MAC") as provided at <http://www.disclosureusa.org.>, unless the United States Securities and Exchange Commission has withdrawn the interpretive advice in its letter to the MAC dated September 7, 2004.