



STAFF REPORT

DATE: November 21, 2017

REGULAR

ITEM: #16

MOTION

TO: Honorable Mayor and Members of the City Council
FROM: Brian A. Swanson – Finance Director
AGENDA ITEM: Debt Management Policy Discussion
REVIEWED BY: Kristina Handt, City Administrator

BACKGROUND:

Per several Finance Committee meetings, staff presented information regarding the original Debt Management Policy and a revised Debt Management Policy for review and discussion. Based on these discussions, the Finance Committee provided clarity to the revised policy, subsequently approved it, and recommended it be considered by the City Council for approval. Therefore, staff wanted to provide the City Council with the opportunity to review the revised debt management policies, and consider adoption of the revised Debt Management Policy this evening.

ITEMS OR QUESTIONS BEFORE THE FINANCE COMMITTEE:

- 1) Should the Council approve the attached Debt Management Policy approved by the Finance Committee on November 9, 2017?

DISCUSSION:

Staff thought it would be useful to provide the City Council with some context regarding the original Debt Management Policy as well as the revised Debt Management Policy for review, comment and consideration. The main differences between the original policy, which was adopted on April 2, 2013, and the revised policy for consideration are as follows:

- 1) Enhanced discussion on key areas such as Credit Ratings, Financial Disclosure, Purposes and Uses of Debt, and Refunding of Debt.
- 2) New sections on Debt Administration and Practices, and Post Issuance Debt Compliance Policy are the result of new regulations that took effect after approval of the last policy, and are related to internal record keeping and external reporting.

By regularly analyzing, discussing and updating the policy as needed helps to ensure sound financial management concerning debt issuance and management. Further, review of governing and oversight bodies helps to ensure the policies and procedures are in congruence with the goals of those entities.

FISCAL IMPACT:

Monetarily, the impact will be absorbed by the appropriate City fund(s) as part of the legal and external administration, which occurs for each debt issuance and is usually consolidated into the issuance costs of

each bond issue. From a staffing perspective, it is opportunity cost as they prepare information for each bond issue, perform operational work over the duration of the issue, and comply with related regulations.

RECOMMENDATION:

- 1) Motion to approve the attached City of Lake Elmo Debt Management Policy – Revised - November 21, 2017.

ATTACHMENT:

- 1) City of Lake Elmo Debt Management Policy – Revised – November 21, 2017



CITY OF LAKE ELMO DEBT MANAGEMENT POLICY

PURPOSE

The use of borrowing and the issuance of debt is an important and flexible financing mechanism available to the City of Lake Elmo. The issuance of debt allows capital improvements to proceed when necessary and in advance of when it may otherwise be feasible. It can reduce long-term costs due to inflation, potentially reduce opportunity cost, and equalize the costs of improvements to present and future property owners and customers of the City.

POLICY STATEMENT

It is the policy of the City of Lake Elmo to establish guidelines for the use of debt in financing capital acquisitions, repayment of debt, and management of the overall level of debt in the city.

- A. Credit Ratings:** The City of Lake Elmo seeks to maintain the highest possible credit ratings for all categories of short-term and long-term General Obligation debt that can be achieved without compromising delivery of basic City services and achievement of adopted City policy objectives.

The City recognizes that external economic, natural, or other events may from time to time affect the creditworthiness of its debt. Nevertheless, the Mayor, City Council, and Finance Committee are committed to ensuring that actions within their control are prudent and consistent with the highest standards of public financial management, and supportive of the creditworthiness objectives defined herein.

- B. Financial Disclosure:** The City is committed to full and complete financial disclosure, and to cooperating fully with rating agencies, institutional and individual investors, City departments and agencies, other levels of government, and the general public to share clear, comprehensible, and accurate financial information. The City is committed to meeting disclosure requirements on a timely and comprehensive basis.

Official statements accompanying debt issues, Comprehensive Annual Financial Reports, and continuing disclosure statements will meet (at a minimum) the standards articulated by the Municipal Standards Rulemaking Board (MSRB), 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 Finance Department shall be responsible for ongoing disclosure to established nationally recognized municipal securities information repositories (NRMSIRs) and for maintaining compliance with disclosure standards promulgated by state and national regulatory bodies.

C. Debt Capacity: The City will keep outstanding debt within the limits prescribed by State statute and at levels consistent with its creditworthiness objectives.

D. Purposes and Uses of Debt: The City will normally rely on existing funds, project revenues, and grants from other governments to finance capital projects such as major maintenance, small equipment acquisition, and small development projects. Debt may be used for purchases of large equipment, and for capital projects, which may generate revenues over time that are used to retire the debt entirely, have a property tax levy contribution and project revenue component, or are fully supported by a property tax levy. It is the intent to determine which financing mechanism(s) are the most beneficial to the City, while also considering the appropriate means to achieve a fair allocation of costs between current and future beneficiaries.

a. Asset Life: The City will consider the use of debt for the acquisition, development, replacement, maintenance, or expansion of an asset only if it has a useful life of at least five years. Debt will not be issued for periods exceeding the useful life or average useful lives of the project or projects to be financed.

b. Project Financing: If possible, the City's goal is to make a cash contribution to any project with an expected useful life of less than 10 years, rather than relying on 100% debt financing.

c. Debt Standards and Structure: Debt will be structured for the shortest period consistent with a fair allocation of costs to current and future beneficiaries or users. Debt will be structured to achieve the lowest possible net cost to the City given market conditions, the urgency of the capital project, net revenues expected from the project (if any), and the nature and type of security provided. Moreover, to the extent possible, the City will design the repayment of its overall debt so as to recapture rapidly its credit capacity for future use. The City shall strive to repay at least 50 percent within ten years.

d. Backloading: The City will seek to structure debt with reasonably consistent principal and interest costs over the life of the debt. "Backloading" of costs will be considered only when natural disasters or extraordinary or unanticipated external factors make the short-term cost of the debt prohibitive, when the benefits derived from the debt issuance can clearly be demonstrated to be greater in the future than in the present, when such structuring is beneficial to the City's overall amortization schedule, or when such structuring will allow debt service to more closely match project revenues during the early years of the project's operation.

E. Refunding of Debt:

a. Advance refunding bonds shall not be utilized unless present value savings of 4% to 5% of refunded principal is achieved and unless the call date is within 3 years. The state law minimum is 3% of refunded principal. Bonds shall not be advance refunded if there is a reasonable chance that revenues will be sufficient to pre-pay the debt at the call date.

- b. Current refunding bonds shall be utilized when present value savings of 3% of refunded principal is achieved or in concert with other bond issues to save costs of issuance.
- c. Special assessment or revenue debt will not be refunded unless the Finance Director determines that special assessments or other sufficient revenues will not be collected soon enough to pay off the debt fully at that call date.

F. Debt Administration and Practices: In general, City debt will be issued through a competitive bidding process. Bids will be awarded on a true interest cost basis (TIC), providing other bidding requirements are satisfied. In the event that the City receives more than one bid with identical TICs, the tie may be broken by a flip of a coin.

- a. **Municipal Advisor:** The City will retain an external municipal advisor, selected by the City's Finance Department. The utilization of the municipal advisor for particular bond sales will be at the discretion of the Finance Director on a case by case basis and pursuant to the municipal advisory services contract. The municipal advisors will have comprehensive municipal debt issuance experience with diverse financial structuring requirements and pricing of municipal securities.
- b. **Bond Counsel:** The City will retain external bond counsel for all debt issues. No debt will be issued by the City without a written opinion by bond counsel affirming that the City is authorized to issue the debt, stating that the City has met all state constitutional and statutory requirements necessary for issuance, and determining the debt's federal income tax status.
- c. **Fiscal Agents:** The Finance Department will utilize a fiscal agent on all City indebtedness. Fiscal agent fees for outstanding bonds will be paid from the Bond Interest and Redemption Fund, unless specified otherwise by the Finance Director.
- d. **Disclosure:** The city shall comply with SEC rule 15(c)2(12) on primary and continuing disclosure. Continuing disclosure reports shall be filed no later than 180 days after receipt of the city's annual financial report.
- e. **Arbitrage:** The city shall complete an arbitrage rebate report for each issue no less than every five years after its date of issuance.
- f. **Communication:** The city will maintain frequent and regular communications with bond rating agencies about its financial condition and will follow a policy of full disclosure in every financial report and bond prospectus. The city will comply with Securities Exchange Commission (SEC) reporting requirements.
- g. **Reporting:** The City will report at least annually the outstanding bonds to the City Council and Finance Committee.

G. Post Issuance Debt Compliance Policy: The City of Lake Elmo, Minnesota (the "Issuer") issues tax-exempt governmental bonds ("TEBs") to finance various public projects. As an issuer of TEBs, the Issuer is required by the terms of Sections 103 and 141-150 of the Internal Revenue Code of 1986, as amended (the "Code"), and the Treasury Regulations promulgated

thereunder (the “Treasury Regulations”), to take certain actions after the issuance of TEBs to ensure the continuing tax- exempt status of such bonds. In addition, Section 6001 of the Code and Section 1.6001-1(a) of the Treasury Regulations impose record retention requirements on the Issuer with respect to its TEBs. This Post-Issuance Compliance Procedure and Policy for Tax-Exempt Governmental Bonds (the “Policy”) has been approved and adopted by the Issuer to ensure that the Issuer complies with its post-issuance compliance obligations under applicable provisions of the Code and Treasury Regulations.

1. Effective Date and Term. The effective date of this Policy is the date of approval by the City Council of the Issuer and this Policy shall remain in effect until superseded or terminated by action of the City Council of the Issuer.

2. Responsible Parties. The City’s Finance Director of the Issuer (the “Compliance Officer”) shall be the party primarily responsible for ensuring that the Issuer successfully carries out its post-issuance compliance requirements under applicable provisions of the Code and Treasury Regulations. The Compliance Officer will be assisted by the staff of the Issuer and other officials when appropriate. The Compliance Officer of the Issuer will also be assisted in carrying out post-issuance compliance requirements by the following organizations:

(a) Bond Counsel (as of the date of approval of this Policy, bond counsel for the Issuer is Dorsey & Whitney, LLP);

(b) Municipal Advisor (as of the date of approval of this Policy, the municipal advisor of the Issuer is Northland Securities, Inc.);

(c) Paying Agent (the person, organization, or officer of the Issuer primarily responsible for providing paying agent services for the Issuer); and

(d) Rebate Analyst (the organization primarily responsible for providing rebate analyst services for the Issuer).

The Compliance Officer shall be responsible for assigning post-issuance compliance responsibilities to members of the Finance Department and other staff of the Issuer, Bond Counsel, Paying Agent, and Rebate Analyst. The Compliance Officer shall utilize such other professional service organizations as are necessary to ensure compliance with the post-issuance compliance requirements of the Issuer. The Compliance Officer shall provide training and educational resources to Issuer staff responsible for ensuring compliance with any portion of the post-issuance compliance requirements of this Policy.

3. Post-Issuance Compliance Actions. The Compliance Officer shall take the following post-issuance compliance actions or shall verify that the following post-issuance compliance actions have been taken on behalf of the Issuer with respect to each issue of TEBs:

(a) The Compliance Officer shall prepare a transcript of principal documents (this action will be the primary responsibility of Bond Counsel).

(b) The Compliance Officer shall file with the Internal Revenue Service (the “IRS”), within the time limit imposed by Section 149(e) of the Code and applicable Treasury Regulations, an Information Return for Tax-Exempt Governmental Obligations, Form 8038- G (this action will be the primary responsibility of Bond Counsel).

(c) The Compliance Officer shall prepare an “allocation memorandum” for each issue of TEBs in accordance with the provisions of Treasury Regulations, Section 1.148-6(d)(1), that accounts for the allocation of the proceeds of the tax-exempt bonds to expenditures not later than the earlier of:

(i) eighteen (18) months after the later of (A) the date the expenditure is paid, or (B) the date the project, if any, that is financed by the tax-exempt bond issue is placed in service; or

(ii) the date sixty (60) days after the earlier of (A) the fifth anniversary of the issue date of the tax-exempt bond issue, or (B) the date sixty (60) days after the retirement of the tax- exempt bond issue.

Preparation of the allocation memorandum will be the primary responsibility of the Compliance Officer (in consultation with the Municipal Advisor and Bond Counsel).

(d) The Compliance Officer, in consultation with Bond Counsel, shall identify proceeds of TEBs that must be yield-restricted and shall monitor the investments of any yield-restricted funds to ensure that the yield on such investments does not exceed the yield to which such investments are restricted.

(e) In consultation with Bond Counsel, the Compliance Officer shall determine whether the Issuer is subject to the rebate requirements of Section 148(f) of the Code with respect to each issue of TEBs. In consultation with Bond Counsel, the Compliance Officer shall determine, with respect to each issue of TEBs of the Issuer, whether the Issuer is eligible for any of the temporary periods for unrestricted investments and is eligible for any of the spending exceptions to the rebate requirements. The Compliance Officer shall contact the Rebate Analyst (and, if appropriate, Bond Counsel) prior to the fifth anniversary of the date of issuance of each issue of TEBs of the Issuer and each fifth anniversary thereafter to arrange for calculations of the rebate requirements with respect to such TEBs. If a rebate payment is required to be paid by the Issuer, the Compliance Officer shall prepare or cause to be prepared the Arbitrage Rebate, Yield Reduction and Penalty in Lieu of Arbitrage Rebate, Form 8038-T, and submit such Form 8038-T to the IRS with the required rebate payment. If the Issuer is authorized to recover a rebate payment previously paid, the Compliance Officer shall prepare or cause to be prepared the Request for Recovery of Overpayments Under Arbitrage Rebate Provisions, Form 8038-R, with respect to such rebate recovery, and submit such Form 8038-R to the IRS.

4. Procedures for Monitoring, Verification, and Inspections. The Compliance Officer shall institute such procedures as the Compliance Officer shall deem necessary and appropriate to monitor the use of the proceeds of TEBs issued by the Issuer, to verify that certain post-issuance compliance actions have been taken by the Issuer, and to provide for

the inspection of the facilities financed with the proceeds of such bonds. At a minimum, the Compliance Officer shall establish the following procedures:

- (a) The Compliance Officer shall monitor the use of the proceeds of TEBs to:
 - (i) ensure compliance with the expenditure and investment requirements under the temporary period provisions set forth in Treasury Regulations, Section 1.148-2(e);
 - (ii) ensure compliance with the safe harbor restrictions on the acquisition of investments set forth in Treasury Regulations, Section 1.148-5(d);
 - (iii) ensure that the investments of any yield-restricted funds do not exceed the yield to which such investments are restricted; and
 - (iv) determine whether there has been compliance with the spend-down requirements under the spending exceptions to the rebate requirements set forth in Treasury Regulations, Section 1.148-7.

- (b) The Compliance Officer shall monitor the use of all bond-financed facilities in order to:
 - (i) determine whether private business uses of bond-financed facilities have exceeded the *de minimis* limits set forth in Section 141(b) of the Code as a result of leases and subleases, licenses, management contracts, research contracts, naming rights agreements, or other arrangements that provide special legal entitlements to nongovernmental persons; and
 - (ii) determine whether private security or payments that exceed the *de minimis* limits set forth in Section 141(b) of the Code have been provided by nongovernmental persons with respect to such bond-financed facilities. The Compliance Officer shall provide training and educational resources to any Issuer staff who have the primary responsibility for the operation, maintenance, or inspection of bond-financed facilities with regard to the limitations on the private business use of bond-financed facilities and as to the limitations on the private security or payments with respect to bond-financed facilities.

- (c) The Compliance Officer shall undertake the following with respect to each outstanding issue of TEBs of the Issuer:
 - (i) an annual review of the books and records maintained by the Issuer with respect to such bonds; and
 - (ii) an annual physical inspection of the facilities financed with the proceeds of such bonds, conducted by the Compliance Officer with the assistance with any Issuer staff who have the primary responsibility for the operation, maintenance, or inspection of such bond-financed facilities.

5. Record Retention Requirements. The Compliance Officer shall collect and retain the following records with respect to each issue of TEBs of the Issuer and with respect to the facilities financed with the proceeds of such bonds: (i) audited financial statements of the Issuer; (ii) appraisals, demand surveys, or feasibility studies with respect to the facilities to be financed with the proceeds of such bonds; (iii) publications, brochures, and newspaper articles related to the bond financing; (iv) trustee or paying agent statements; (v) records of all investments and the gains (or losses) from such investments; (vi) paying agent or trustee statements regarding investments and investment earnings; (vii) reimbursement resolutions and expenditures reimbursed with the proceeds of such bonds; (viii) allocations of proceeds to expenditures (including costs of issuance) and the dates and amounts of such expenditures (including requisitions, draw schedules, draw requests, invoices, bills, and cancelled checks with respect to such expenditures); (ix) contracts entered into for the construction,

renovation, or purchase of bond-financed facilities; (x) an asset list or schedule of all bond-financed depreciable property and any depreciation schedules with respect to such assets or property; (xi) records of the purchases and sales of bond-financed assets; (xii) private business uses of bond-financed facilities that arise subsequent to the date of issue through leases and subleases, licenses, management contracts, research contracts, naming rights agreements, or other arrangements that provide special legal entitlements to nongovernmental persons and copies of any such agreements or instruments; (xiii) arbitrage rebate reports and records of rebate and yield reduction payments; (xiv) resolutions or other actions taken by the governing body subsequent to the date of issue with respect to such bonds; (xv) formal elections authorized by the Code or Treasury Regulations that are taken with respect to such bonds; (xvi) relevant correspondence relating to such bonds; (xvii) documents related to guaranteed investment contracts or certificates of deposit, credit enhancement transactions, and financial derivatives entered into subsequent to the date of issue; (xviii) copies of all Form 8038-Ts and Form 8038-Rs filed with the IRS; and (xix) the transcript prepared with respect to such TEBs. The records collected by the Issuer shall be stored in any format deemed appropriate by the Compliance Officer and shall be retained for a period equal to the life of the TEBs with respect to which the records are collected (which shall include the life of any bonds issued to refund any portion of such TEBs or to refund any refunding bonds) plus three (3) years.

6. Remedies. In consultation with Bond Counsel, the Compliance Officer shall become acquainted with the remedial actions under Treasury Regulations, Section 1.141-12, to be utilized in the event that private business use of bond-financed facilities exceeds the *de minimis* limits under Section 141(b)(1) of the Code. In consultation with Bond Counsel, the Compliance Officer shall become acquainted with the Tax Exempt Bonds Voluntary Closing Agreement Program described in Notice 2008-31, 2008-11 I.R.B. 592, to be utilized as a means for an issuer to correct any post-issuance infractions of the Code and Treasury Regulations with respect to outstanding tax-exempt bonds.

7. Continuing Disclosure Obligations. In addition to its post-issuance compliance requirements under applicable provisions of the Code and Treasury Regulations, the Issuer has agreed to provide continuing disclosure, such as annual financial information and material event notices, pursuant to a continuing disclosure certificate or similar document (the “Continuing Disclosure Document”) prepared by Bond Counsel and made a part of the transcript with respect to each issue of bonds of the Issuer that is subject to such continuing disclosure requirements. The Continuing Disclosure Documents are executed by the Issuer to assist the underwriters of the Issuer’s bonds in meeting their obligations under Securities and Exchange Commission Regulation, 17 C.F.R. Section 240.15c2-12, as in effect and interpreted from time to time (“Rule 15c2-12”). The continuing disclosure obligations of the Issuer are governed by the Continuing Disclosure Documents and by the terms of Rule 15c2-12. The Compliance Officer is primarily responsible for undertaking such continuing disclosure obligations and to monitor compliance with such obligations.

8. Other Post-Issuance Actions. If, in consultation with Bond Counsel, Municipal Advisor, Paying Agent, Rebate Analyst, or the City Council, the Compliance Officer determines that any additional action not identified in this Policy must be taken by the Compliance Officer to ensure the continuing tax-exempt status of any issue of governmental bonds of the Issuer, the Compliance Officer shall take such action if the Compliance Officer

has the authority to do so. If, after consultation with Bond Counsel, Municipal Advisor, Paying Agent, Rebate Analyst, or the City Council, the Compliance Officer determines that this Policy must be amended or supplemented to ensure the continuing tax-exempt status of any issue of governmental bonds of the Issuer, the Compliance Officer shall recommend to the City Council that this Policy be so amended or supplemented.

9. Taxable Governmental Bonds. Most of the provisions of this Policy, other than the provisions of Section 7, are not applicable to governmental bonds the interest on which is includable in gross income for federal income tax purposes. On the other hand, if an issue of taxable governmental bonds is later refunded with the proceeds of an issue of tax-exempt governmental refunding bonds, then the uses of the proceeds of the taxable governmental bonds and the uses of the facilities financed with the proceeds of the taxable governmental bonds will be relevant to the tax-exempt status of the governmental refunding bonds. Therefore, if there is any reasonable possibility that an issue of taxable governmental bonds may be refunded, in whole or in part, with the proceeds of an issue of TEBs, then for purposes of this Policy, the Compliance Officer shall treat the issue of taxable governmental bonds as if such issue were an issue of TEBs and shall carry out and comply with the requirements of this Policy with respect to such taxable governmental bonds. The Compliance Officer shall seek the advice of Bond Counsel as to whether there is any reasonable possibility of issuing TEBs to refund an issue of taxable governmental bonds.

10. Qualified 501(c)(3) Bonds. If the City issues bonds to finance a facility to be owned by the City but which may be used, in whole or in substantial part, by a nongovernmental organization that is exempt from federal income taxation under Section 501(a) of the Code as a result of the application of Section 501(c)(3) of the Code (a “501(c)(3) Organization”), the City may elect to issue the bonds as “qualified 501(c)(3) bonds” the interest on which is exempt from federal income taxation under Sections 103 and 145 of the Code and applicable Treasury Regulations. Although such qualified 501(c)(3) bonds are not governmental bonds, at the election of the Compliance Officer, for purposes of this Policy, the Compliance Officer shall treat such issue of qualified 501(c)(3) bonds as if such issue were an issue of tax-exempt governmental bonds and shall carry out and comply with the requirements of this Policy with respect to such qualified 501(c)(3) bonds. Alternatively, in cases where compliance activities are reasonably within the control of the relevant 501(c)(3) Organization, the Compliance Officer may determine that all or some portion of compliance responsibilities described in this Policy shall be assigned to the relevant organization.

ROLE OF THE CITY COUNCIL, FINANCE COMMITTEE AND STAFF

Relevant information will be brought to the City Council and Finance Committee when applicable to aid in policy, procedure and other key decision or direction regarding City business. As such, staff will provide applicable debt service information and where appropriate, suggest revisions to the policy for consideration. In addition, as the business needs and vision of the City Council and Finance Committee change, this policy can be reviewed and updated as necessary.