

DEBT POLICIES

PURPOSE

The City of McKinney recognizes the foundation of any well-managed debt program is a comprehensive debt management policy. The purpose of this policy is to establish parameters and provide guidance governing the issuance, management, continuing evaluation of and reporting on all debt obligations issued by the City, and to provide for the preparation and implementation necessary to ensure compliance and conformity with this policy and Federal, State, and local laws, rules, and regulations.

POLICY STATEMENT

Debt is a valuable source of capital project financing, and its use should be limited to projects that relate to the mission and strategic objectives of the City. The amount of debt incurred impacts the financial health of the City, its' credit rating, and its' cost of capital. The City will consider other funding opportunities (e.g., grants for federal, state, and other sources; current revenues, fund balances; etc.) when appropriate and advantageous to the City.

Under the governance and guidance of Federal and State laws and the City's Charter, ordinances and resolutions, the City will periodically enter into debt obligations to finance the construction, improvement or acquisition of infrastructure and other assets or to refinance existing debt for the purpose of meeting its governmental obligations to its residents. It is the City's desire and direction to ensure that such debt obligations are issued and administered in such fashion as to obtain the best long-term financial advantage to the City and its residents, while making every effort to maintain and improve the City's bond ratings and reputation in the investment community.

ADMINISTRATIVE PROCEDURES

DEBT MANAGEMENT COMMITTEE

Members

The Debt Management Committee (the Committee) will consist of the City Manager, Assistant City Managers, and the Chief Financial Officer. The City's municipal advisor and bond counsel shall act as consultants to the Committee.

Scope

The Committee shall meet at least annually to review the debt program or as necessary. Topics for discussion should include: the Capital Improvement Program, status of outstanding debt, unspent bond proceeds, unissued voter authorized debt, timing of additional financing needs and financing options, and the effect of proposed financing activity on the related rates supporting the debt (i.e., property tax rate, utility rates, user fees, etc.)

RESPONSIBILITY AND STANDARD OF CARE

The primary responsibility for developing financing recommendations rests with the Chief Financial Officer. In developing the recommendations, the Chief Financial Officer shall be assisted by the Director of Finance, Investment and Treasury Manager, and the Accounting Manager. The Chief Financial Officer shall hold as follows:

- Meet no less than annually with Department Directors to consider the need for financing, review debt capacity and assess progress on the Capital Improvement Program;
- Meet as necessary in preparation for financing;
- Review changes in state and federal legislation;

- Review annually the provisions of ordinances authorizing issuance of obligations and to;
- Annually review services provided by the Municipal Advisor, Bond Counsel, Paying Agent and other service providers to evaluate the extent and effectiveness of services being provided.

Prior to the meetings, the Financial Services Department shall prepare a written report on the status of Capital Improvement Program financing. The report shall be based in part on information collected from the primary capital improvement project managers and shall include a projection of near term financing needs compared to available resources, and an analysis of the impact of contemplated financing on the property tax rate and user charges, and a financing recommendation.

In developing financing recommendations, consideration will be given as follows:

- The time proceeds of obligation are expected to remain on hand and the related carrying cost;
- The options for interim financing including short term and interfund borrowing, taking into consideration federal and state reimbursement regulations;
- The effect of proposed action on the tax rate and user charges;
- Trends in interest rates;
- Other factors as appropriate.

1. Conflicts of Interest

All participants in the debt management process shall seek to act responsibly as custodians of public assets. Officers and employees involved in the debt management process shall refrain from personal business activity that could impair their ability to make impartial financing decisions.

2. Reporting

The Chief Financial Officer shall include in the Annual Comprehensive Financial Report (ACFR) a report summarizing all debt outstanding by type (tax-supported and self-reported general obligation and revenue debt), update of arbitrage liability, and update of pertinent legislative changes.

3. Investor Relations

The City shall endeavor to maintain a positive relationship with the investment community. The Chief Financial Officer and the City’s Municipal Advisor shall, as necessary, prepare reports and other forms of communications regarding the City’s indebtedness, as well as its future financing plans. This includes information, but is not limited to, the annual program of services, ACFR, financial plans, capital improvement plans, and comprehensive development plans.

All forms of media deemed appropriate and immediately available to the City will be utilized to disseminate information to all investors. Examples include the Texas Municipal Report, The Bond Buyer, Electronic Municipal Market Access (EMMA), and the Municipal Advisory Council of Texas (MAC). Bond counsel will advise on the use of electronic media in connection with the City’s debt program.

4. Municipal Advisor

The City shall retain an independent municipal advisor for advice on the structuring of new debt, financial analysis of various options, the rating review process, the marketing of debt issues, marketability of city obligations, sale and post-sale services, the review of the official statement, and other services, as necessary. The City will seek the advice of the municipal advisor on an

ongoing basis. The municipal advisor will not bid on nor underwrite any city debt issues in accordance with Municipal Security Rulemaking Board (MSRB) rules.

5. Bond Counsel

The Bond Counsel will issue an opinion as to the legality and tax-exempt status of any obligations. The City will also seek the advice of Bond Counsel on all other types of financings and on any other questions involving federal tax or arbitrage law. Bond Counsel is also responsible for the preparation of the ordinance authorizing issuance of obligations and all the closing documents to complete their sale and will perform other services as needed.

OFFICIAL STATEMENT

The preparation of the Official Statement is the responsibility of the municipal advisor in concert with the Chief Financial Officer. Information for the Official Statement is gathered from departments throughout the City.

The City will take all appropriate steps to comply with the federal disclosure rule (i.e., Securities and Exchange Commission Rule 15c2-12). The City will provide annual and material disclosure to information repositories throughout the term of securities for the benefit of the primary and secondary municipal markets as required by Rule 15c2-12.

DISCLOSURE

A. With each bond offering, and at least annually, in the preparation of Financial Reports or Official Statements or any other offering document, the City will follow a policy of full and complete disclosure of operating, financial and legal conditions of the City, in conformance with the Government Finance Officers Association Disclosure Guideline, and as advised by disclosure counsel or municipal advisor.

B. Notice of Events

Securities and Exchange Commission (SEC) Rule 15c2-12 lists certain events that must be reported in a timely fashion to Municipal Security Rulemaking Board (MSRB) via the Electronic Municipal Market Access (EMMA) system and, if required by Rule 15c2-12, to the State Information Depository (SID), the Municipal Advisory Council of Texas (MAC). Rule 15c2-12 requires the events be reported to the MSRB within 10 business days after the occurrence of the event.

1. The events that must be reported, if material are:

- Nonpayment related defaults;
- Modifications of rights of security holders;
- Bond calls and tender offers;
- Release, substitution, or sale of property securing repayment of the securities;
- Mergers, consolidations, acquisitions, the sale of all or substantially all of the assets of the obligated person or their termination;
- Appointment of a successor or additional trustee or the change of the name of a trustee;
- Incurrence of *a financial obligation* of the issuer or obligated person, *if material*, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the issuer or obligated person, *any of which affect security holders*.

2. The events that must be reported, regardless of materiality, are:
 - Principal and interest payment delinquencies;
 - 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 events affecting the tax exempt status of the security;
 - Defeasances;
 - Rating changes;
 - The issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the securities;
 - Bankruptcy, insolvency, receivership or similar proceeding;
 - Default, event of acceleration, termination event, modification of terms, or other similar events under the terms of the financial obligation of the issuer or obligated person, any of which *reflect financial difficulties*.

3. Rule 15c2-12 also requires the City to report to the MSRB failure of the City to provide the required annual financial information or operating data on or before the dates specified under a continuing disclosure undertaking. In addition, the following proposals became effective in May 2011:
 - Underwriters shall indicate on the EMMA system whether the issuer has agreed to provide secondary market disclosure information, when it will be provided, and the name of the obligated entity.
 - The MSRB shall indicate on the EMMA system the issues that voluntarily agree to provide the following:
 - a. Annual financial information within 120 days after the fiscal year ends;
 - b. An undertaking to prepare audited financial statements in compliance with accounting standards established by the Governmental Accounting Standard Board; and
 - c. The website link to the issuer's financial information.

Full disclosure of the operations will be made to the bond rating agencies. The City staff, with the assistance of the municipal advisors and bond counsel, will prepare the necessary material for presentation to the rating agencies.

RATINGS AGENCY COMMUNICATIONS & CREDIT OBJECTIVES

The City will seek to maintain and improve its current bond rating so its borrowing costs are reduced to a minimum and its access to credit is preserved.

In conjunction with the municipal advisor, the City shall maintain a line of communication with at least two of the rating agencies (Moody's, Standard & Poor's, and Fitch), informing them of major financial events in the City as they occur. The Annual Comprehensive Financial Report, Annual Budget, and Capital Improvement Program, shall be distributed to the rating agencies after they have been accepted/adopted by the City Council on an annual basis.

When necessary, a conference call or personal meeting with representatives of the rating agencies will be scheduled when a major capital improvement program is initiated, or to discuss economical and/or financial developments which might impact credit ratings. The following documents may be required by the rating agencies:

- Most recent annual audit reports, including a description of accounting practices. Accounting changes in the past three years and the impact on financial results should be explained;
- Current budget;
- Current Capital Improvement Program;
- Official statements for new financing;
- Description of projects being financed;
- Sources and uses statement for bond issuance. If additional funds are required to complete specific projects being financed, the source of the funds and any conditional requirements may be discussed;
- Engineering and feasibility report (if applicable);
- Zoning or land-use map (if applicable);
- Cash flow statement, in the case of interim borrowing. Statement of long- and short-term debt with annual and monthly maturity dates as appropriate. Also, a report of any lease obligations, their nature and term;
- Indication of appropriate authority for debt issuance;
- Investment policy;
- Statement concerning remaining borrowing capacity plus tax rate and levy capacity or other revenue capacity.

LIMITATIONS ON INDEBTEDNESS AND AFFORDABILITY STATEMENT

City staff, in conjunction with the municipal advisor and bond counsel, will complete a comprehensive analysis of debt capacity prior to issuing bonds. The analysis should cover a broad range of factors, including:

- Legal debt limits, tax expenditure ceilings;
- Coverage requirements or additional bonds test in accordance with bond covenants;
- Measures of the tax and revenue base, such as projections of relevant economic variables (e.g., assessed property values, employment base, unemployment rates, income levels, and retail sales);
- Population trends;
- Utilization trends for services underlying revenues;
- Factors affecting tax collections, including types of property, goods, or services taxed, assessment practices and collection rates, evaluation of trends relating to the City's financial performance, such as revenues and expenditures, net revenues available after meeting operational requirements;
- Reliability of revenues expected to pay debt service;
- Unreserved fund balance levels;
- Debt service obligations, such as existing debt service requirements;
- Debt service as a percentage of expenditures or tax or system revenues;
- Measures of debt burden on the community, such as debt per capita, debt as a percentage of full or equalized assessed property, value, and overlapping or underlying debt;

- Tax-exempt market factors affecting interest costs, such as interest rates, market receptivity, and credit rating.

The target length of maturity for the City's long-term debt is not to exceed 20 years. In addition, the target percentage of tax rate allocated to debt service will not be more than 35%.

The City has revenue bonds and other indebtedness of the Water and Wastewater Funds. The City will maintain coverage ratios as dictated by the City's outstanding bond covenants, including other indebtedness of the Water and Wastewater Funds (e.g. 1.10 times the maximum annual debt service, and/or 1.25 times the annual average debt service, or as required by individual bond covenants).

The Water and Wastewater Funds/ total long-term debt outstanding shall not exceed the amount of combined fund equity.

CAPITAL IMPROVEMENT PROGRAM

- A. The City will seek all possible federal, state and local reimbursement for mandated projects and/or programs. The City will pursue a balanced relationship between issuing debt and pay-as-you-go financing as dictated by prevailing economic factors and directed by the City Council.
- B. Current operations will not be financed with long-term debts.
- C. Debt incurred to finance capital improvements will be repaid within the useful life of the asset.
- D. High priority will be assigned to the replacement of capital improvements when they have deteriorated to the point where they are hazardous, incur high maintenance costs, negatively affect property values, or no longer serve their intended purposes.
- E. An updated Capital Improvement Program will be presented to the City Council for approval on an annual basis. The program will be used for the long-range financial planning process.

TYPES OF DEBT

The City's bond counsel and municipal advisor will present different types of debt best suited and legally permissible under state law for each debt issue and assist in analyzing the use of capital lease purchase or the use of lines of credit. These types may include:

- Short-term vs. long-term debt;
- General obligation vs. revenue debt;
- Fixed debt;
- Lease-backed debt;
- Special obligation debt;
- Certificates of obligation debt;
- Combination tax and revenue debt;
- Tax increment debt;
- Conduit issues;
- Taxable debt.

The Chief Financial Officer will be responsible for evaluating variable rate debt or interest rate swap debt and will present a recommendation to the City Council as necessary.

BOND STRUCTURE

Structural features that may be considered are:

- Maturity of debt;
- Setting the final maturity of the debt equal to or less than the useful life of the asset;
- Use of zero-coupon bonds, capital appreciation bonds, deep discount bonds, or premium bonds;
- Debt service structure (level debt service payments, level principal payments or other repayment structure defined by state law);
- Redemption provisions (mandatory and optional call features);
- Use of credit enhancements;
- Use of senior lien and junior lien obligations;
- Others, as deemed appropriate in consultation with municipal advisor and bond counsel.

SHORT-TERM DEBT

GENERAL

Short-term obligations may be issued to finance projects or portions of projects for which the City ultimately intends to issue long-term debt, i.e., it will be used to provide interim financing which will eventually be refunded with the proceeds of long-term obligations.

Short-term obligations may be backed with a tax and/or revenue pledge or a pledge of other available sources.

The amount of short term obligations due to mature in a year shall not exceed 2% of outstanding long term debt.

Interim financing may be appropriate when long-term interest rates are expected to decline in the future. In addition, some forms of short-term obligations can be obtained quicker than long-term obligations and thus can be used in emergencies until long term financing can be obtained. In some cases when the amount of financing required in the immediate future is relatively small, it may be cheaper for the City to issue a small amount of short term obligations to provide for its immediate needs than to issue a larger amount of long term obligations to provide financing for both immediate and future needs when carrying costs of issuing obligations which are not immediately needed are taken into account.

COMMERCIAL PAPER

Interest rates on commercial paper are generally favorable to an issuer relative to interest on other forms of debt. However, it is not feasible for the City to issue commercial paper because the cost of issuance for small issuers is too great and the market for commercial paper from a small issue is poor. In addition, cities may legally only issue commercial paper for revenue supported projects. However, should the opportunity to participate in commercial paper issuance present itself the advantages and disadvantages shall be evaluated by the Chief Financial Officer.

ANTICIPATION NOTES

Anticipation Notes empower municipalities to issue debt without giving notice of intent. Anticipation Notes may be secured and repaid by a singular pledge, but not plural pledge, of revenue, taxes, or the proceeds of a future debt issue. Anticipation Notes may be authorized by an ordinance adopted by the City Council.

Anticipation notes may be used to finance projects or acquisitions that could also be financed using Certificates of Obligation and have the following restrictions:

1. Anticipation Notes may not be used to repay interfund borrowing or a borrowing that occurred up to/or more than 24-months prior to the date of issuance, and
2. A governing body may not issue Anticipation Notes that are payable from general obligation bond proceeds unless the proposition authorizing the issuance of the general obligation bonds has already been approved by the voters.

LINE OF CREDIT

To the extent authorized by state law and with approval of the City Council, the City may establish a tax-exempt line of credit with a financial institution selected through a competitive process. Draws shall be made on the line of credit when (1) the need for financing is so urgent that time does not permit the issuance of long-term debt, or (2) the need for financing is so small that the cost of issuance of long-term debt including carry cost of debt proceeds not needed immediately is significantly higher. Draws will be made on the line of credit to pay for projects designated for line of credit financing by the City Council. Borrowing under the line of credit shall be repaid from current revenues. The Chief Financial Officer will authorize all draws on the line of credit, as authorized in the agreement approved by City Council.

CAPITAL LEASING

Capital leasing is an option for the acquisition of a piece or package of equipment.

Leasing shall not be considered when funds are on hand for the acquisition unless the interest expense associated with the lease is less than the interest that can be earned by investing the funds on hand or when other factors such as budget constraints or vendor responsiveness override the economic consideration.

Whenever a lease is arranged with a private sector entity, a tax-exempt rate shall be sought. Whenever a lease is arranged with a government or other tax-exempt entity, the City shall obtain an explicitly defined taxable rate so that the lease will not be counted in the City's total annual borrowings subject to arbitrage rebate.

The lease agreement shall permit the City to refinance the lease at no more than reasonable cost should the City decide to do so. A lease which may be called at will is preferable to one which may merely be accelerated.

The City shall seek to obtain at least (3) competitive proposals for any lease financing, unless lease financing is provided in conjunction with a cooperative contract purchase and cannot be competitively bid. The net present value of competitive bids shall be compared, taking into account whether payments are in advance or in arrears, and how frequently payments are made. The purchase price of equipment shall be competitively bid, as required by state law, as well as the financing costs.

The Chief Financial Officer will ensure any leasing agreement is compared to other financing options to ensure the lease is cost beneficial. Alternate financing options will include revenue bonds, contractual obligations, certificates of obligation, and lines of credit. The Chief Financial Officer will be the person responsible for evaluating this financing source and will make a recommendation to the City Council for approval.

INTERFUND LOANS

As allowed by the City, the Chief Financial Officer will review opportunities whereby interfund loans may be utilized to meet short-term financing needs. Interfund loans will only be utilized if, at the inception of the loan, it is economically beneficial to the lending fund and only if the rate of return is comparable or higher than the rate of return the lending fund would otherwise receive by keeping funds in the City's investment pool. Any interfund loan must be approved by the City Council.

LONG-TERM DEBT

GENERAL

Proceeds from the sale of long-term obligations will not be used for operating purposes, and the final maturity of the obligations will not exceed the estimated useful life of the asset financed. Voter approved general obligation bonds will strive to have a final maturity of twenty (20) years or less. Revenue bonds and certificates of obligations will strive to have a final maturity of twenty (20) years or less. If deemed appropriate, staff may present to the City Council extraordinary circumstances in which longer final maturities may be necessary but never in excess of the useful life of an individual asset.

A level debt service structure will be used unless operational matters and marketing considerations dictate otherwise.

The cost of issuance of private activity bonds is usually higher than for governmental purpose bonds. Consequently, private bonds will be issued only when they will economically benefit the City.

The cost of taxable debt is higher than for tax-exempt debt. However, the issuance of taxable debt may be required or may be appropriate in some circumstances and may allow valuable flexibility in subsequent contracts with users or managers of the improvement constructed with the bond proceeds. Therefore, the City will usually issue tax-exempt obligations but may occasionally issue taxable obligations.

BONDS

Long-term general obligation, including certificates of obligation, or revenue bonds shall be issued to finance significant and desirable capital improvements. The general obligation bonds will be used for purposes set forth by voters in bond elections or set forth in the notices of intent or to refund previously issued general obligation bonds, certificates of obligations or revenue bonds. All bonds shall be sold in accordance with applicable law.

CERTIFICATES OF OBLIGATION

- Finance permanent improvements and land acquisition;
- Finance costs associated with capital project overruns;
- Acquire equipment/vehicles;
- Leverage grant funding;
- Renovate, acquire, construct facilities and facility improvements;
- Construct street improvement;
- Provide funding for master plans/studies;
- Address necessary life safety needs;
- Finance revenue supported projects/assets if determined to be more economical than revenue bonds.

In accordance with state law, a resolution authorizing publication of notice of intent to issue certificates of obligations shall be presented for the consideration of the City Council. The notice of intent shall be

published continuously on the City's website for at least (45) days and in a newspaper of general circulation in the City once a week for two consecutive weeks with the first publications to be at least (45) days prior to the sale date.

Certificates of obligation may be backed by a tax pledge under certain circumstances as defined by law. They may also be backed by a combination tax and revenue pledge eligible under state law. Some revenues are restricted as to the uses for which they may be pledged. Water and Wastewater revenues may be pledged without limit for Water and Wastewater purposes but may only be pledged to a limit of \$1,000 for any one series of bonds issued for non-utility system purposes.

PUBLIC PROPERTY FINANCE CONTRACTUAL OBLIGATION

Public property finance contractual obligations may be issued to finance the acquisition of personal property.

REVENUE BONDS

In addition to the policies set forth above, when cost-beneficial and when permitted under applicable state law, the City may consider the use of surety bonds, letters of credit, or similar instruments to satisfy mandated debt service reserve fund requirements on outstanding and/or proposed revenue bonds.

COMBINATION TAX AND REVENUE BONDS

In addition to the policies set forth above, when cost-beneficial and when permitted under applicable state law, the City may consider the use of Combination Tax and Revenue Bonds for refunding obligations of Water/Wastewater and Solid Waste or any other self-supporting revenue producing City enterprise. Combination Tax and Revenue Bonds will comply with applicable state law and are assigned the full faith and credit of the City, thereby enhancing the credit rating otherwise obtained from revenue supported only debt (Revenue Bonds).

CREDIT ENHANCEMENTS

Credit enhancements are mechanisms which guarantee principal and interest payments. They include bonds insurance, lines of credit, surety bonds, and letters of credit. A credit enhancement, while costly, is intended to bring a lower interest rate on debt and a higher rating from the rating agencies, consequently lowering overall costs.

The City's municipal advisor will advise the city whether or not a credit enhancement is cost effective under the circumstances and what type of credit enhancement, if any, should be purchased. In a negotiated sale, bids will be taken during the period prior to the pricing of the sale. In a competitive sale, bond insurance may be provided by the purchaser if the purchaser finds it cost effective.

Other credit enhancements may arise in the future, which may be beneficial. The City's municipal advisor will present these options for consideration.

REFUNDING AND RESTRUCTURING OPTIONS

The City shall consider refunding debt whenever an analysis indicates the potential for present value savings above the costs of refunding the bonds. Refunding for savings should not exceed the final maturity of the original obligations, unless specifically approved by the City Council.

REIMBURSEMENT ORDINANCES

The Chief Financial Officer will review and approve all reimbursement ordinances from City departments, including enterprise fund departments, before forwarding to the City Council for consideration. In no event will a reimbursement ordinance exceed the unreserved fund equity of the respective operating fund.

Reimbursement ordinances must be adopted (60) days from the date the original expenditures were paid. Bonds must be issued and the reimbursement allocation made no later than eighteen (18) months after the latter of (1) the date the original expenditures were paid, or (2) the date the project is placed in service or abandoned, but in no event more than three (3) years after the original expenditures were paid.

USE OF ANTICIPATED BOND PROCEEDS

The use of anticipated bond proceeds will be limited to preliminary (soft) costs, which may include engineering fees, architect fees, feasibility studies, etc. The Chief Financial Officer may provide additional parameters regarding qualifying uses and will review and approve all requests for the use of anticipated bond proceeds. Departments may not use anticipated bond proceeds for preliminary costs earlier than sixty (60) days from the date the City Council adopts an ordinance authorizing the sale of said bonds. In no event will the use of anticipated bond proceeds exceed the unreserved fund equity of the Water/Wastewater requests or the operating fund of any other department making a request.

METHOD OF SALE

BOND ELECTIONS

Before a bond election, the City Manager, Bond Election Committee members, and City Council members will be provided with competent debt capacity analyses, tax and user fee impact projections, and other information as directed by the City Manager's Office. The Bond Counsel and Municipal Advisor will provide support during this process.

COMPETITIVE SALE

Favorable conditions for a competitive method of sales include the following:

- The market is familiar with the issuer, and the issuer is a stable and regular borrower in the public market;
- An active secondary market with a broad investor base for the issuer's bonds;
- The issue is neither too large to be easily absorbed by the market nor too small to attract investors without concerted sales effort;
- The issue is not viewed by the market as carrying overly complex features or requiring explanation as to the bonds' soundness;
- Interest rates are relatively stable, market demand is strong, and the market is able to absorb a reasonable amount of buying or selling at reasonable price changes.

Bidding Parameters

The notice of sale will be carefully constructed so as to ensure the best possible bid for the City, in light of existing market conditions and other prevailing factors. Parameters to be examined may include:

- Limits between lowest and highest coupons;
- Coupon requirements relative to the yield curve;
- Method of underwriter compensation, discount, or premium coupons;
- Use of true interest cost (TIC) versus net interest cost (NIC);

- Use of bond insurance;
- Serial bonds vs term bonds with mandatory sinking fund redemption;
- Deep discount bonds;
- Call provisions.

NEGOTIATED SALE

Favorable conditions for a negotiated method of sales include the following:

Bonds issued for the purpose of refunding and/or restructuring outstanding debt may appropriately be sold on a negotiated basis when maximum flexibility is required in order for the City to respond to day-to-day nuances in the marketplace and other complications peculiar to the issuance of refunding debt. Whenever the option exists to sell an issue on a negotiated basis, an analysis of the options shall be performed to aid in the decision-making process.

The City will actively participate in the selection of the underwriter or direct purchaser.

In negotiated sales, the City attempts to involve qualified and experienced firms which consistently submit financing plans to the City and actively participate in the City's competitive sales. The criteria to select an underwriter in a negotiated sale may include the following:

- Overall experience;
- Participation in the City's past competitive sales;
- Marketing philosophy;
- Capability;
- Previous experience as managing or co-managing partner;
- Financial statement and financing plans that are relevant and appropriate;
- Public finance team and resources;
- Breakdown of underwriter's discount, which includes management fee, underwriting fee, average takedown, and other administrative expenses.

PRIVATE PLACEMENT

When cost-beneficial, the City may privately place its debt. Since underwriting and rating agency expenses may be avoided, it may result in a lower cost of issuance. Private placement is sometimes an option for small issues. The opportunity may be identified by the municipal advisor.

INVESTMENT OF BOND PROCEEDS

STRATEGY

The City should actively monitor its investment practices to ensure maximum returns on its invested bond funds while complying with federal arbitrage guidelines. Specific investment strategies for the investment of bond proceeds are provided in the City's Investment Policy.

ARBITRAGE COMPLIANCE

The City will follow a policy of full compliance with all arbitrage rebate requirements of the federal tax code and Internal Revenue Service regulations, and will perform (internally or by contract consultants) arbitrage rebate calculations for each issue subject to rebate on an annual basis. All necessary rebates will be filed and paid when due.

ARBITRAGE LIABILITY MANAGEMENT

The Chief Financial Officer will maintain a system for tracking arbitrage rebate liability and ensuring that required calculations are performed on a timely basis. These calculations are performed no later than each five-year anniversary date of the issuance of the bonds, and at final maturity (including early redemption). Funds should be set aside in anticipation of potential rebate liabilities. Due to the complexity of the arbitrage calculations and regulations, and to the severity of the penalties for noncompliance, the advice of Bond Counsel and qualified experts will be pursued on an ongoing basis.

ARBITRAGE PROCEEDS

All bond proceeds will be separately accounted for in the financial accounting system to facilitate arbitrage tracking and reporting. The Chief Financial Officer shall include in the ACFR a report summarizing the City's arbitrage rebate liability.

DEBT POLICY GLOSSARY

Amortization

The planned reduction of a debt obligation according to a stated maturity or redemption schedule.

Arbitrage

The gain which 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.

Average Life

The average length of time debt is expected to be outstanding. Generally, a level debt service structure will limit the average life of a bond issue (i.e., a 20 year final maturity will have an approximate average life of 12 years, and a 30 year final maturity will have an approximate average life of 18 years).

Basis Point (BP)

.01 or 1/100 of 1 percent of yield. Smallest measure used in quoting yields on bonds or notes. For example, if a yield increases from 3.00 percent to 3.01 percent, the difference is referred to as a one basis point increase. Often a basis point is referred to as a "bp."

Bond Buyer Index (BBI)

Comparison of current rates for various maturities.

Bid Form

The document used by an underwriter to submit his bid at a competitive sale.

Bond

A very broad term used to describe a debt obligation. A bond may have a fixed or floating coupon rate; may be issued by the U.S. Treasury or an agency or a corporation; and may be callable or non-callable.

Bond Counsel

An attorney or law firm retained, typically by the issuer, to give a legal opinion concerning the validity of the 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 or ordinances, trust indentures, official statements, validation proceedings and litigation.

Bond Insurance

Bond insurance is a type of credit enhancement whereby a monoline insurance company indemnifies an investor against a default by the issuer to pay principal and interest in-full and on-time. Once assigned, the municipal bond issuance policy generally is irrevocable. The insurance company receives an up-front fee, or premium when the policy is issued.

Bond Years

\$1,000 of debt outstanding for one year used to compute average life and net interest cost.

Book-Entry-Only

Bonds that are issued in fully-registered form but without certificates of ownership. The ownership interest of each actual purchaser is recorded on computer.

Call Option

The right to redeem a bond prior to its slated maturity, either on a given date or continuously. The call option is also referred to as the optional redemption provision.

Capital Appreciation Bond

A bond without current interest coupons that is sold at a substantial discount from par. Investors are provided with a return based upon the accretion of value in the bond through maturity.

Capital Lease

The acquisition of a capital asset over time rather than merely paying a rental fee for temporary use. A lease-purchase agreement, in which provision is made for transfer of ownership of the property for a nominal price at the scheduled termination of the lease, is referred to as a capital lease.

Certificates of Obligation

A type of debt authorized to be issued pursuant to the Certificated of Obligation Act of 1971 (Subchapter C of Chapter 271, Texas Government Code).

Closing

When bonds are exchanged for money (a/k/a delivery or settlement).

Commercial Paper (CP)

Unsecured, short-term obligations with maturities ranging from 1 to 270 days issued by banks, corporations and other borrowers to investors with large temporary cash positions. This type of security is usually issued at a discount and carries a zero coupon. The accounting process is identical to a T-bill. Prime commercial paper carries a short-term rating of A1 P1 or equivalent.

Competitive Sale

A sale of securities in which the securities are awarded to the bidder who offers to purchase the issue at the best price or lowest cost.

Coupon Rate

The interest rate on specific maturities of a bond issue. While the term "coupon" derives from the days when virtually all municipal bonds were in bearer form with coupons attached, the term is still frequently used to refer to the interest rate on different maturities of bonds in registered form.

Cover Bid

The runner-up in a competitive bond sale.

Credit Enhancements

Credit enhancements are mechanism which guarantee principal and interest payments. They include bond insurance and a line or letter of credit. A credit enhancement, while costly, will usually bring a lower interest rate on debt and a higher rating from agencies, thus lowering overall costs. Cost effectiveness of credit enhancement will be evaluated for each debt issue.

CUSIP

The term CUSIP is an acronym for the **Committee on Uniform Securities Identification Procedures**. An identification number is assigned to each maturity of an issue, and is usually printed on the face of each individual certificate of the issue. The CUSIP numbers are intended to help facilitate the identification and clearance of municipal securities. As the municipal market has evolved, and new derivative products are devised, the importance of the CUSIP system for identification purposes has increased.

Dated Date

Date at which interest begins accruing on a newly issued security. The dated date can sometimes differ from the issue date potentially causing accrual discrepancies.

Debt Burden

The ratio of outstanding tax-supported debt to the market value of property within a jurisdiction. The overall debt burden included a jurisdiction's proportionate share of overlapping debt as well as the municipality's direct net debt.

Debt Limitation

The maximum amount of debt is legally permitted by a jurisdiction's charter, constitution, or statutory requirements.

Debt Service

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

Debt Service Reserve Fund

The fund into which moneys are placed which may be used to pay debt service if pledged revenues are insufficient to satisfy the debt service requirements. The debt service reserve fund may be entirely funded with bond proceeds, or it may only be partly funded at the time of the issuance and allowed to reach its full funding requirement over time, due to the accumulation of pledged revenues. If the debt service reserve fund is used in whole or part to pay debt service, the issuer usually is required to replenish the funds from the first available funds or revenues. A typical reserve requirement might be the maximum, aggregate annual debt service requirement for any year remaining until bonds reach maturity. The size of the reserve fund, and the manner in which it is invested, may be subject to arbitrage regulations.

Default

The failure to pay principal or interest in full or on time. An actual default should be distinguished from technical default. The latter refers to a failure by an issuer to abide by certain covenants but does not necessarily result in a failure to pay principal or interest when due.

Defeasance

Providing for payment of principal of premium, if any, and interest on debt through the first call date or scheduled principal maturity in accordance with the terms and requirements of the instrument pursuant to which the debt was issued. A legal defeasance usually involves establishing an irrevocable escrow funded with only cash and U.S. government obligations.

Depository Trust Company (DTC)

A firm through which members can use a computer to arrange for securities to be delivered to other members without physical delivery of the certificates. The DTC uses computerized debit and credit entries. The system mirrors the FedWire system and was designed to reduce its load. When settling an investment that is DTC eligible, the delivering dealer will request the DTC number of the safekeeping agent.

Downgrade

A reduction in credit rating.

Enterprise Activity

A revenue-generating project or business. The project often provides funds necessary to pay debt service on securities issued to finance the facility. The debts of such projects are self-liquidating when the projects earn sufficient monies to cover all debt service and other requirements imposed under the bond contract. Common examples include water and sewer treatment facilities and utility facilities.

Electronic Municipal Market Access (EMMA)

Effective July 1, 2009, the SEC implemented amendments to SEC Rule 15c2-12 which approved the establishment by the MSRB of EMMA, the sole successor to the nationally recognized municipal securities information repositories with respect to filings made in connection with disclosure undertakings. Access to filings are made free of charge to the general public by the MSRB.

Final Official Statement (FOS)

A document published by the issuer which generally discloses material information on a new issue of municipal securities including the purposes of the issue, how the securities will be repaid, and the financial, economic and social characteristics of the issuing government. Investors may use this information to evaluate the credit quality of the securities.

Flow of Funds

The order in which pledged revenues must be disbursed, as set forth in the trust indenture or bond resolution. In most instances, the pledged revenues are deposited into a general collection account or revenue fund as they are received and subsequently transferred into the other accounts established by the bond resolution or trust indenture. The other accounts provide for payment of the costs of debt service, debt service reserve deposits, operation and maintenance costs, renewal and replacement, and other requirements.

General Obligation Debt

Debt that is secured by a pledge of the ad valorem taxing power of the issuer. Also known as a full faith and credit obligation.

Good Faith Deposit

A sum of money given by the Underwriter to assure his bid.

Institutional Buyer

Banks, financial institutions, insurance companies, and bond funds.

Issuance Costs

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

Junior Lien Bonds

Bonds which have a subordinate claim against pledged revenues.

Letter of Credit

Bank credit facility whereby a bank will honor the payment of an issuer's debt, in the event that an issuer is unable to do so, thereby providing an additional source of security for bondholders for a predetermined period of time. A letter of credit often is referred to as an L/C or an LOC. Letter of Credit can be issued on a "stand-by" or "direct pay" basis.

Level Debt Service

When annual payments are substantially the same each year.

Line of Credit

Bank credit facility wherein the bank agrees to lend up to a maximum amount of funds at some date in the future in return for a commitment fee.

Manager

The member (or members) of an underwriting syndicate charged with the primary responsibility for conducting the affairs of the syndicate. The managers take the largest underwriting commitment.

Lead Manager or Service Manager

The underwriter serving as head of the syndicate. The lead manager generally handle negotiations in a negotiated underwriting of a new issue of municipal securities or directs the process by which a bid is determined for a competitive underwriting. The lead manager also is charged with allocating securities among the members of the syndicate in accordance with the terms of the syndicate agreement among underwriters.

Join Manager or Co-Manager

Any member of the management group

Municipal Advisory Council of Texas (MAC)

The designated State of Texas Information Depository as approved by the SEC with respect to filings made in connection with undertakings.

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. New Board members are selected by the MSRB pursuant to the method set forth in Board rules.

Negotiated Sale

A sale of securities in which the terms of sale are determined through negotiation between the issuer and the purchaser, typically an underwriter, without competitive bidding.

Net Interest Cost

The average interest cost of a bond issue calculated on the basis of simple interest.

Paying Agent

An agent of the issuer with responsibility for timely payment of principal and interest to bond holders.

Preliminary Official Statement (POS)

The POS is a preliminary version of the official statement which is used by an issuer or underwriters to describe the proposed issue of municipal securities prior to the determination of the interest rate(s) and offering price(s). The preliminary official statement, also called a "red herring", often is examined by potential purchasers prior to making an investment decision.

Present Value

The value of a future amount or stream of revenues or expenditures in current dollars.

Refunding

An advance refunding is a refunding that occurs more than 90 days before a call date of the refunded bonds. A current refunding is a process of selling new issue of securities to obtain funds needed to retire existing securities. Debt refunding is prone to extend maturity and/or to reduce debt service cost.

Retail Buyer

Individual investors.

Revenue Bond

A bond which is payable from a specific source of revenue and to which the full faith and credit of an issuer with taxing power 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 activity. Generally, no voter approval is required prior to issuance of such obligations.

Secondary Market

A market existing for the purchase and sale of securities that were originally sold to investors days or even years earlier.

Senior Lien Bonds

Bonds having a prior or first claim on pledged revenues.

Serial Bonds

A bond issue in which the principal is repaid in periodic installments over the issue's life.

Split Ratings

Different rating levels from different rating agencies.

Surety Bond

A bond guaranteeing performance of a contract or obligations.

Term Bonds

Term Bonds usually refer to a particularly large maturity of a bond issue that is created by aggregating a series of maturities. A provision is often made for the mandatory redemption of specified amounts of principal during several years prior to the stated maturity, which effectively simulates serial bonds.

True Interest Cost (TIC)

An expression of the average interest cost in present value terms. The true interest cost is a more accurate measurement of the bond issue's effective interest cost and should be used to ascertain the best bid in a competitive sale.

Variable Rate Bonds

A bond on which the interest rate is reset periodically, usually no less often than semi-annually. The interest rate is reset either by means of an auction or through an index.

Upgrade

An increase in credit rating.

