

Kern County Policy and Administrative Procedures Manual

CHAPTER 18

DEBT MANAGEMENT

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1801. Introduction. The County is committed to long-term financial planning, maintaining appropriate reserve levels and employing prudent practices in governance, management and budget administration. Debt will be issued for the purposes stated in this policy and to implement policy decisions incorporated in the County's annual operations budget. It is the County's goal to protect taxpayers, ratepayers and constituents by utilizing conservative financing methods and techniques so as to obtain the highest practical credit ratings (if applicable) and the lowest practical borrowing costs.

This Policy shall provide guidance for the issuance and management of all debt and lease financings of the County, together with credit, liquidity and other ancillary instruments and agreements secured or executed in connection with such transactions. While adherence to this Debt Policy is recommended in applicable circumstances, the County recognizes that changes in the capital markets, County programs and other unforeseen circumstances may produce situations that are not covered by the Policy or require modifications or exceptions to achieve Debt Policy goals. In these cases, management flexibility is appropriate, provided specific authorization from the Board is obtained. The County may approve bonds and other related agreements the terms or provisions of which deviate from this Debt Policy, upon the recommendation and approval of the County Administrative Office or his designee, as circumstances warrant. The failure by the County to comply with any provision of this Policy shall not affect the validity of any debt that is otherwise duly authorized and executed.

Financial management policies are commonly developed by local governments to serve as a blueprint to achieve the fiscal stability required to accomplish the County's goals and objectives. It is a mechanism to ensure that the County is financially able to meet its immediate and long term service objectives. It also enhances financial planning and internal financial management for the County.

Kern County issues bonds and other forms of indebtedness to finance capital improvement projects, equipment acquisitions, and other enhancements for the County. While issuing debt is an appropriate method of financing, careful monitoring of such issuances is required to preserve the County's credit rating and budget flexibility. This policy will address the circumstances and methods of issuing debt and guidelines to be followed.

1802. Goals. The County's debt issuance activities and procedures shall be aligned with the County's vision and goals for providing adequate facilities and programs for the citizens of the County. When issuing debt, the County shall ensure that it:

- .1 Maintains accountability for the fiscal health of the County, including prudent management and transparency of the County's financing programs
- .2 If applicable, pursue the best possible credit rating for each debt issue in order to reduce interest costs, within the context of preserving financial flexibility and meeting capital funding requirements
- .3 Takes all practical precautions and proactive measures to avoid financial decisions that will negatively impact current credit ratings on existing or future debt issues
- .4 Maintains effective communication with rating agencies and, as appropriate, credit enhancers such as bond insurers or other providers of credit or liquidity instruments in order to enhance the creditworthiness, liquidity, or marketability of the debt
- .5 When determining the timing of debt issuance, considers market conditions, cash flows associated with repayment, and the County's ability to expend the obtained funds in a timely, efficient, and economical manner consistent with federal tax laws
- .6 Determines the amortization (maturity) schedule which will fit best within the overall debt structure of the County at the time the new debt is issued
- .7 Considers the useful lives of assets funded by the debt issue, as well as repair and replacement costs of those assets to be incurred in the future

.8 Preserves the availability of the County's general fund for operating purposes and other purposes that cannot be funded by the issuance of voter-approved debt

.9 Meets the ongoing obligations and accountability requirements associated with the issuance and management of debt under state and federal tax and securities laws

1803. Financing Team. The County financing team includes staff from the County Administrative Office, the Treasurer-Tax Collector, the Auditor-Controller, and County Counsel. The County shall also retain the services of an Independent Registered Municipal Advisor and/or Special Counsel to assist with County financings, as needed.

1804. Management Practices. The County Administrative Office is responsible for issuing debt and administering the ongoing debt management of all County Funds. Forms of debt include, but are not limited to, Tax and Revenue Anticipation Notes, Pension Obligation Bonds, Certificates of Participation, Lease Revenue Bonds, Enterprise Revenue Bonds, Privately Placed Obligations, and Capital Leases. Should the County Administrative Office find other forms of debt that would be beneficial to the County's public purpose, a request can be made to the Board of Supervisors to approve such form of debt without requiring an amendment of this policy.

1805. Uses of Long-Term Obligations. In order to maintain fiscally prudent practices, long-term financial obligations will not be used to finance current operations, for recurring needs, or circumstances when the sole purpose of such debt financing is to reduce annual budgetary expenditures. The term of the long-term obligation will not exceed the useful life or the average life of the project or projects to be financed. Projects to be financed must be prioritized and the level of relative need for the project or equipment to be financed is an extremely important factor in making the decision to issue long-term debt. Projects that are deemed critically needed to mitigate a serious health and safety hazard or maintain critical operations, are time sensitive due to legal mandate, or will provide matching funds for State and federal grants will be considered for long-term financing. The County Administrative Office must determine that sufficient revenues will be available to service debt through its maturity and that the issuance of the debt will comply with applicable state and federal law.

1806. Uses of Short-Term Obligations. Short-term debt, such as Tax and Revenue Anticipation Notes (TRAN), may be used to provide financing for operational cash flows in order to maintain a steady and even cash flow balance. Short-term debt may also be used to finance short-lived capital projects for example, lease-purchase financing for equipment.

1807. Long-Term Debt Structuring Practices. The structure of any long-term debt issuance must be financially and economically prudent. The County's debt portfolio shall be reviewed annually to initiate any type of restructuring, refunding, or refinancing beneficial to the County.

.1 *Variable rate.* It is often appropriate to issue variable rate debt to diversify the debt portfolio. Variable rate obligations shall not exceed 15% of the County's outstanding long-term obligations. Variable rate debt should be reviewed annually to determine advisability of conversion to fixed rate debt. Derivative products, such as interest rate swaps, will be considered only if they meet the economic goals and objectives of the County.

.2 *Fixed Rate.* Fixed Rate obligations should be used to finance capital asset improvements, lease financing and other essential capital assets. The form of disbursement for the debt service payments shall come mainly from the fund receiving the benefit.

1808. Issuing Debt. There are three methods of issuing debt obligations: a competitive sale, a negotiated sale, and a direct purchase/private placement. In a competitive sale, underwriters submit sealed bids and the underwriter or underwriting syndicate with the lowest True Interest Cost (TIC) is awarded the sale. In a negotiated sale, the underwriter or underwriting syndicate is selected through a Request for Proposal (RFP) process. In a direct purchase/private placement, the County would select a financing partner via a RFP process. Depending on the market conditions and the advice of financial advisor staff, the County may utilize any of the three methods of debt issuance.

1809. Refinancing Outstanding Debt.

.1 *Potential Savings.* The County Administrative Office will monitor the potential savings available by refinancing outstanding debt. Savings will be analyzed on a percentage value basis, all costs and benefits of refinancing will be taken into account.

.2 *Target Savings.* Analysis must be prepared to identify the economic effect of any proposed debt refunding. When determining whether to refund, the County Administrative Office will use one of two options. The first being that the net present value savings as a percentage of the refunded par amount is a minimum of 5% net savings for any one current or advance refunding transaction. The second option is to redeem the obligations in order to achieve other goals that may be determined by the County Board of Supervisors.

1810. Relationship of Debt to County Capital Improvements and Budget. Decisions regarding the issuance of debt for the purpose of financing capital improvement shall be aligned with current needs for acquisition, development, and/or improvement of County property and facilities as identified by the Board of Supervisors, the projected costs and schedules for the projects, and the expected resources.

The County may enter into credit enhancement agreements such as municipal bond insurance, surety bonds, letters of credit, and lines of credit with commercial banks, municipal bond insurance companies, or other financial entities when their use is judged to lower borrowing costs, eliminate restrictive covenants, or have a net economic benefit to the financing.

To the extent practicable, the County shall also consider credit issues, market factors, and tax law when sizing the County's bond issuance. The sizing of refunding bonds shall be determined by the amount of money that will be required to cover the principal of, any accrued interest on, and any redemption premium for the debt to be paid on the call date and to cover appropriate financing costs.

The County will not use interest rate swaps in connection with its debt program unless a separate swap policy is prepared and approved by the Board. The County may use derivative-like investment products to invest bond funds, but only upon staff's analysis of the investment as part of the staff report transmitting the financing and specific approval as part of the Board action.

The County may consider refunding or restructuring outstanding debt if it will be financially advantageous or beneficial for debt repayment and/or structuring flexibility. When doing so, the County shall consider the maximization of the County's expected net present value savings over the life of the debt.

1811. Disclosure. The County is required to prepare and file appropriate continuing disclosure for each bond issuance in a timely manner. The County reports all continuing disclosure to the Electronic Municipal Market Access (EMMA) where it is made available to all interested parties.

.1 *Requirements.* The County will continue to comply with all on-going disclosure conditions as stated in Rule 15(c)2-12 of the Securities and Exchange Commission. In summary, Rule 15(c)12-2 is the reporting of significant events to the bond holders that they receive notice of any event in relation to the securities of the holder. This rule also prohibits a broker or dealer of municipal securities to recommend the purchase or sale of a security for which adequate information is not available. The County will continue to comply with federal tax compliance requirements, including without limitation arbitrage and rebate compliance, related to any prior bond issues. The County provides the Audited Financial Statements and for specific obligations, the County reports the adopted budget. The County Administrative Office will periodically review these debt policies to ensure they remain in compliance with federal and state regulations.

1812. Internal Controls. The County Administrative Officer or designee shall establish internal control procedures to ensure that the proceeds of any debt issuance are directed to the intended use. Such procedures shall assist the County in maintaining the effectiveness and efficiency of operations, properly expending funds, reliably reporting debt incurred by

the County and the use of the proceeds, complying with all laws and regulations, preventing fraud, and avoiding conflict of interest.

In addition, the County Administrative Officer or designee shall ensure that the County completes, as applicable, all performance and financial audits that may be required for any debt issued by the County, including disclosure requirements applicable to a particular transaction.

On or before January 31 of each year, the County Administrative Officer or designee shall submit a report to the CDIAC regarding the debt authorized, the debt outstanding, and the use of proceeds during the reporting period from July 1 to June 30 of the prior fiscal year for debt issued on or after January 21, 2017.

The County Administrative Officer or designee shall provide initial and any annual or ongoing disclosures required by any continuing disclosure undertakings, and shall ensure that the County's disclosure filings are updated as needed.

The County shall comply with all ongoing responsibilities associated with being an issuer of tax-exempt debt, such as arbitrage rebate requirements and appropriate retention of documents. The County shall maintain or cause to be maintained an appropriate system of accounting to calculate bond investment arbitrage earnings in accordance with the Tax Reform Act of 1986, as amended or supplemented, and applicable United States Treasury regulations related thereto.

1813. Exclusions.

- .1 *Derivatives*. This policy excludes derivative products, such as interest rate swaps. Should it be determined that derivative instruments would meet the economic goals and objectives of the County, they will be addressed in a separate policy.
- .2 *Other Land and Non-Land Secured Financing*. This policy excludes issuances that are required to be heard by the County's Debt Advisory Committee per the Kern County Debt Financing Policies (Policy on Land Secured and Non-Land Secured Financing), including those covered by the Mellow-Roos Community Facility District Act of 1982 and the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA). Such financings include Assessment Districts, Industrial Development Revenue Bonds, Mortgage Revenue Bonds, and Mortgage Credit Certificates which can found on the Kern County Treasurer-Tax Collector's website.