

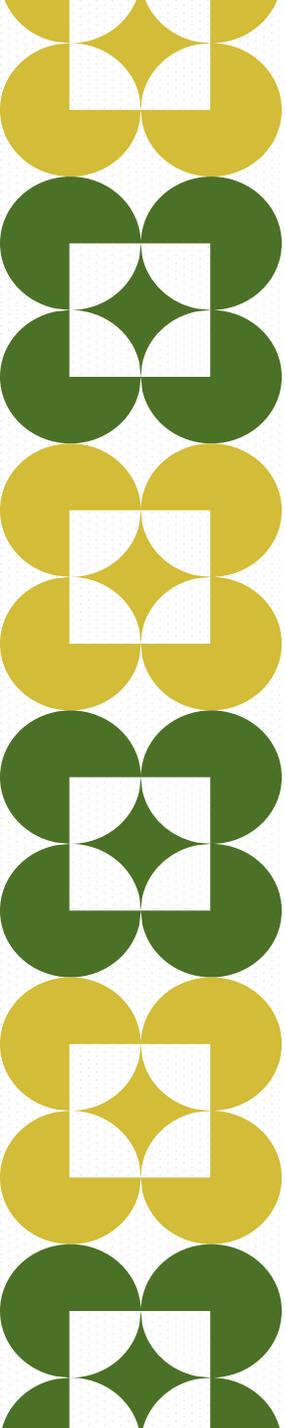
# SESSION ONE

The Issuer's Role in  
Planning a Debt Issuance

**JAY GOLDSTONE**

*Special Advisor to the Mayor*  
City of San Diego





# Topics

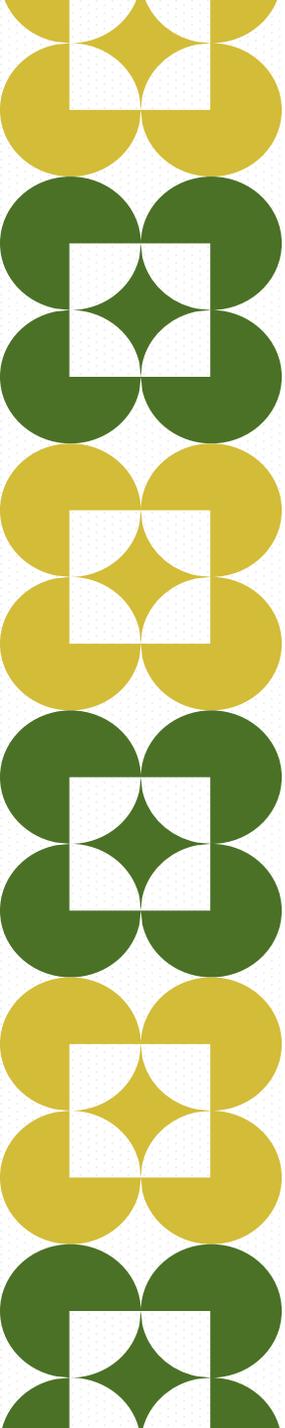
- Financial Planning
  - Multi-Year Financial (O&M) Planning
  - Multi-Year Capital Planning
- Preparing a Debt Policy
  - <https://www.sandiego.gov/sites/default/files/cosd-debt-policy.pdf>
- Capital Planning Policies
  - [https://docs.sandiego.gov/councilpolicies/cpd\\_800-14.pdf](https://docs.sandiego.gov/councilpolicies/cpd_800-14.pdf)
- Is Issuing Debt the Right Move
- Your Role as the Government's Representative
- Selecting Your Team and Understanding Their Roles

**Even Before You Decide  
To Go To Market**

Or What I Call.....

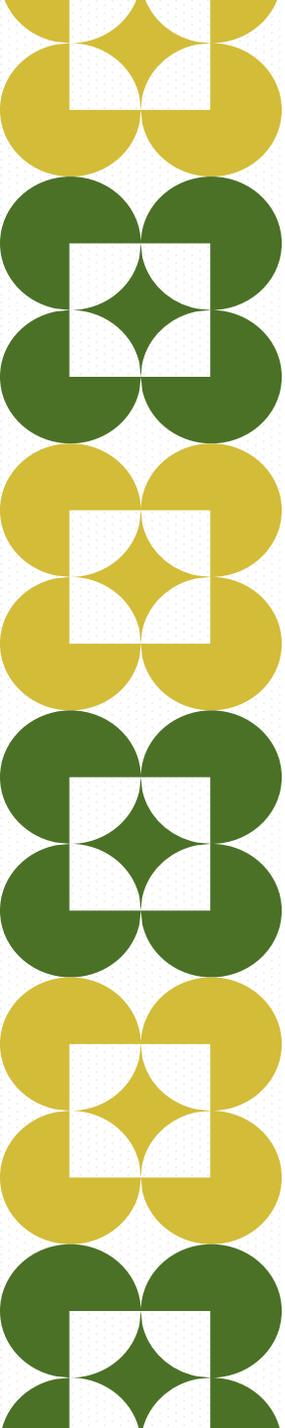
**Setting the Stage**

# Financial Planning



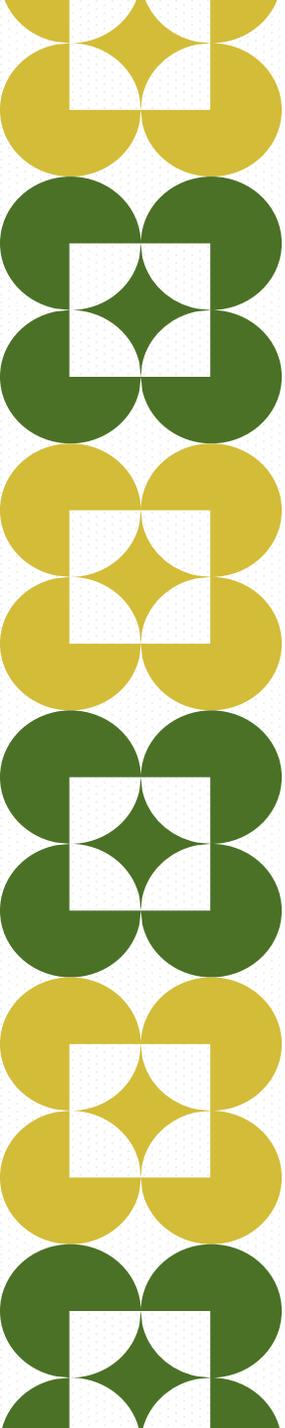
# Multi-Year Financial Planning

- Development of a Comprehensive Financial Plan
  - Governments **SHOULD** develop a viable overall multi-year financing plan covering known operating revenues and expenses and anticipated revenues and expenses.
  - Build into your Financial Plan your approved and proposed capital plan and how you propose to pay for it to ensure that the proposed capital plan is achievable within expected available resources.
  - Include O&M related to your capital project.
  - Prepare a separate Plan for each of your significant funds.



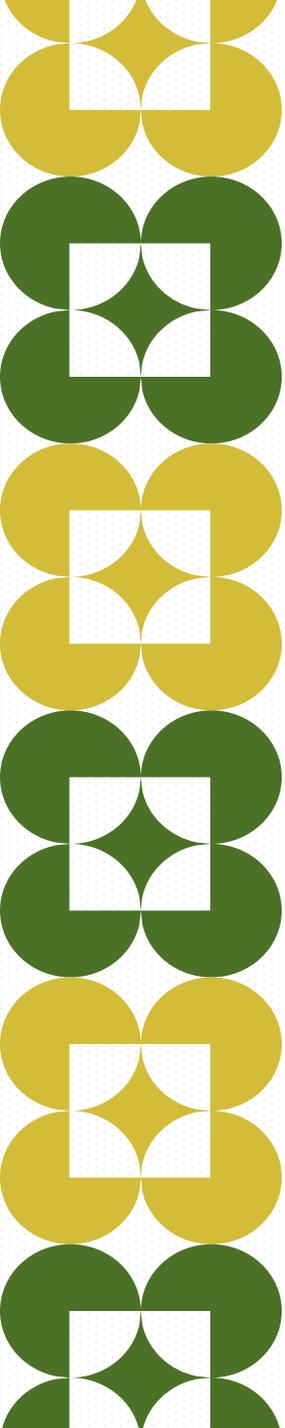
# Debt Issuance Integration with Capital Improvement Plan

- Governments should develop and adopt capital planning policies
  - Policy serves as a framework for stakeholders to know their roles and responsibilities and process expectations. A plan should:
    - Promote sound, long term operational and capital financing strategies
    - Describe approach to capital planning
    - Determine what is a capital improvement project
    - Identify how decisions and prioritizations of projects occur
    - Require assessment of entity's fiscal capacity
    - Link funding strategies with useful life of asset
    - Require multi-year CIP that includes long term financing considerations and strategies
    - Develop a process to ensure compliance with legal requirements for capital project funding
    - Include significant capital maintenance projects
    - Have a process for monitoring and oversight of the CIP program



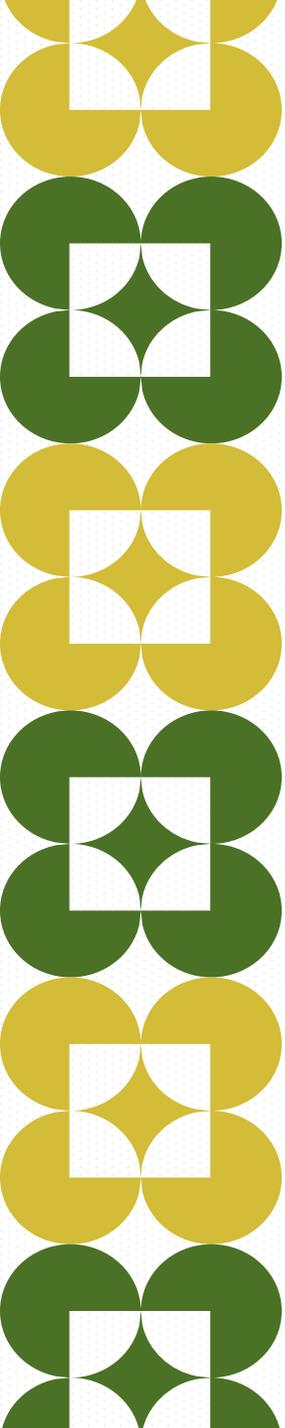
# Capital Improvement Plan

- *Best Practice – Multi-Year Capital Planning*
  - GFOA recommends that governments adopt comprehensive, fiscally sustainable, multi-year capital improvement plans (CIP) to ensure effective management of capital assets
  - CIP should cover five years or more
  - Reviewed/updated annually



# Capital Improvement Plan – (cont. 2 of 7)

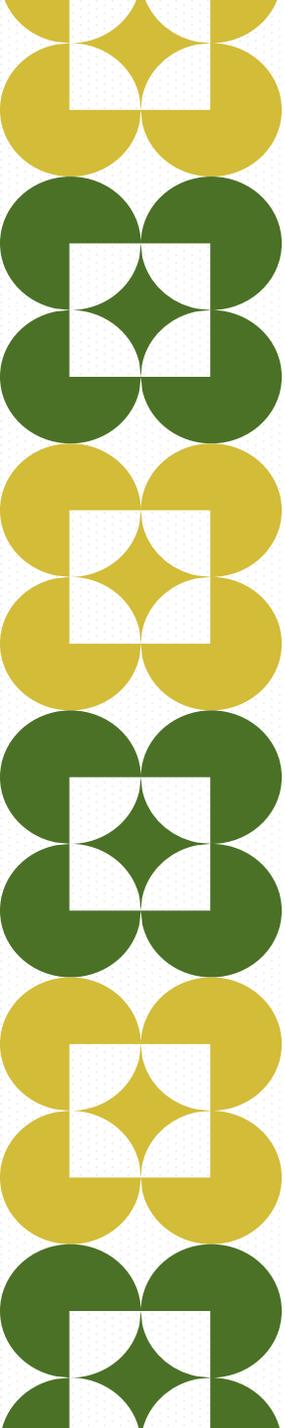
- Prudent Capital Improvement Plans do the following:
  - Identify needs
  - Determine financial impacts
  - Prioritize capital requests
  - Integrate into your comprehensive long range financial plan



# Capital Improvement Plan – (cont. 3 of 7)

## ■ Identify Needs:

- Using information such as development projections, strategic plans, comprehensive plans, facility master plans, and regional plans
- Governments should identify present and future service needs that require capital infrastructure or equipment
- Develop a capital asset life cycle for major capital assets
- Break out by fund (general, enterprise, etc.)



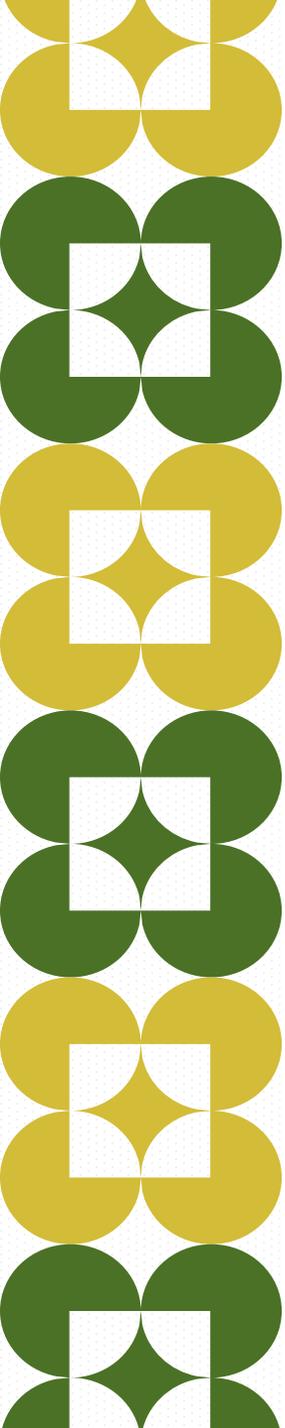
# Capital Improvement Plan – (cont. 4 of 7)

- Determine Financial Impacts
  - Capital asset life cycle should include costs to operate, maintain, administer and renew or replace the capital asset
  - A clear estimate of all major components required to implement a project should be outlined, including land acquisition needs, design, construction, contingency, and post-construction costs
  - The impact on operating budget impacts resulting from capital projects

# Capital Improvement Plan – (cont. 5 of 7)

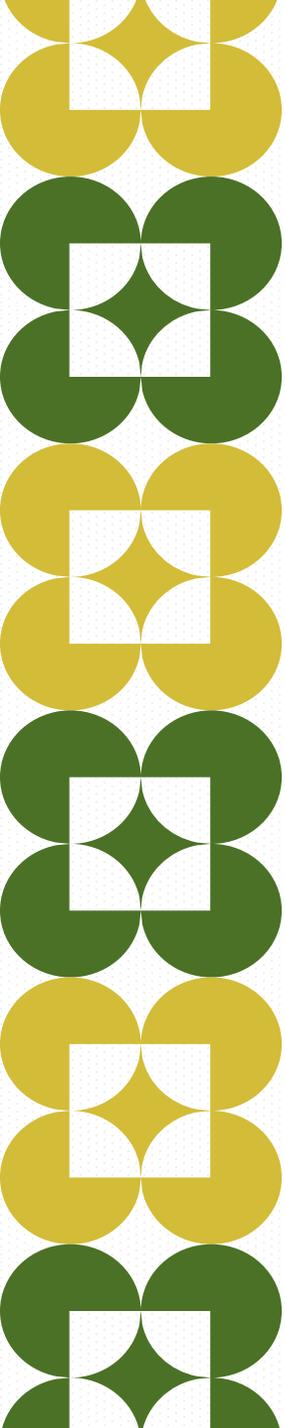
## ■ Prioritize Capital projects:

- Prioritize expected needs based on a strategic plan
- The scope and timing of a planned project should be well defined in the early stages of the planning process
- When evaluating capital requests, governments should first prioritize based on:
  - Health and Safety - Priority should be given to high-risk safety issues that require a capital project to correct
  - Asset Preservation - Capital assets that require renewal or replacement based on capital asset life cycle
  - Service/Asset Expansion/Addition - Infrastructure improvements needed to support government's policies, plans, and studies



# Capital Improvement Plan – (cont. 6 of 7)

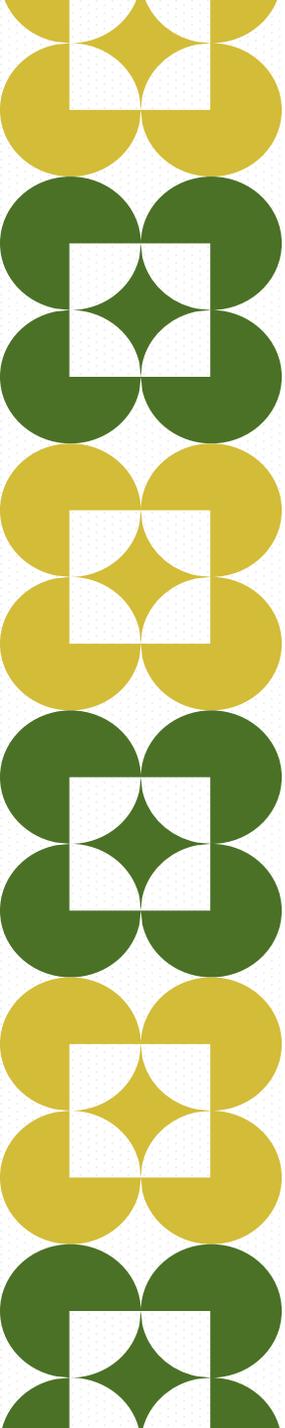
- Prioritize Capital Projects (continued)
  - In this prioritization process, attention should be given to:
    - Coordination with related entities
    - Allow submitting dept. to provide an initial prioritization
    - Incorporate input and participation from major stakeholders and the general public
    - Apply analytical techniques, as appropriate, for evaluating potential projects (e.g., net present value, payback period, cost-benefit analysis, life cycle costing, cash flow modeling)
    - Use a rating system to facilitate objective decision-making



# Capital Improvement Plan – (cont. 7 of 7)

- **Governments Undertaking a Capital Financing Plan Should:**
  - Anticipate expected revenue and expenditure trends including their relationship to multi-year financial plans and ongoing impacts to the operating budget due to the capital plan
  - Prepare cash flow projections of the amount and timing of the capital financing
  - Specify funding sources (PAYGO, debt, mix, etc.)
  - Continue compliance with all established financial policies
  - Recognize appropriate legal constraints

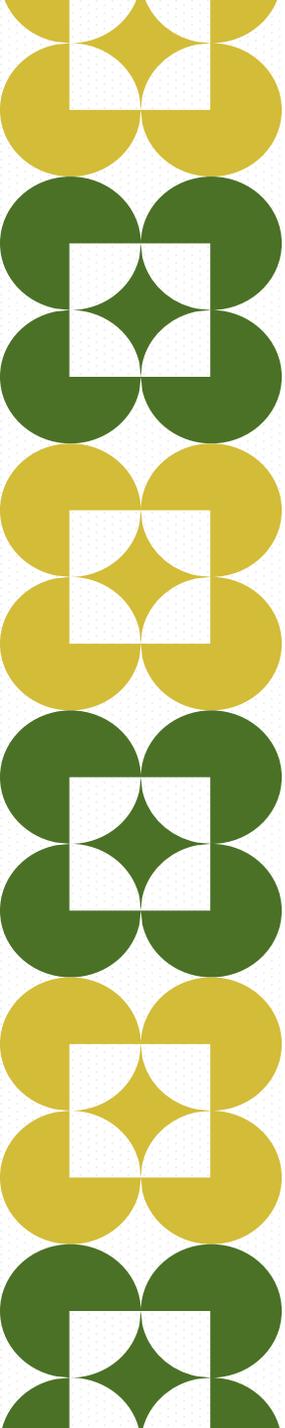
# **Developing and Maintaining a Debt Policy**



# Debt Policy

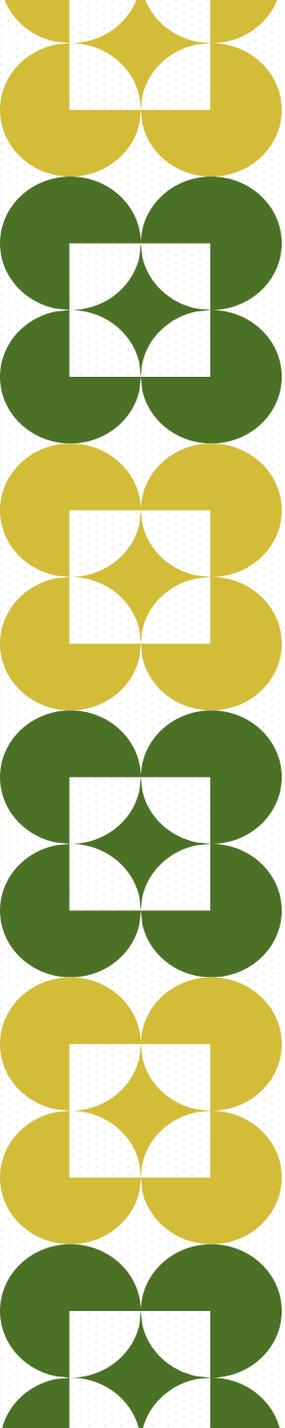
## ■ Having a Debt Policy is Vital

- Guides the debt issuance practices of state or local governments
- Improves the quality of decisions
- Articulates policy goals to internal and external parties
- Provides guidelines for the structure of debt issuance
- Demonstrates a commitment to long-term capital and financial planning and enhances intergenerational equity
- Displays commitment to adhere to local, state, and federal laws
- Provides information and guidance to staff and elected officials



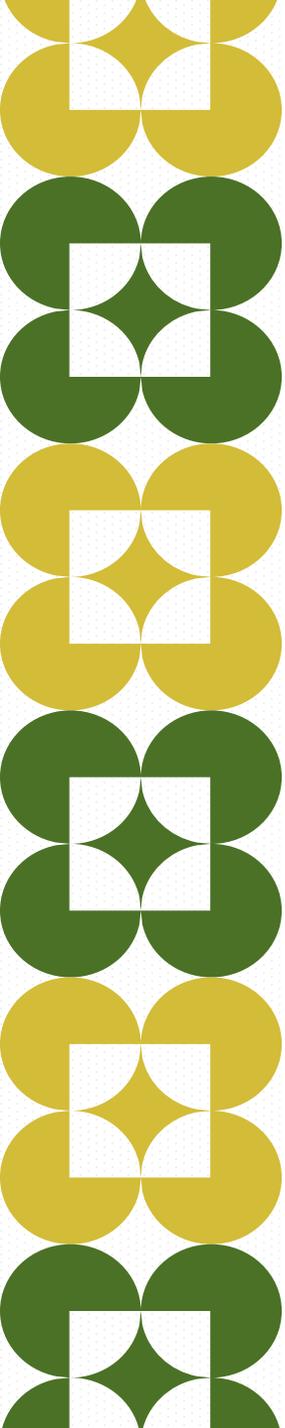
# Importance of a Debt Policy

- Enhances Internal Management Practices
- External Recognition and Transparency
  - Credit rating agencies
  - Investors and the public know the entity's parameters
- Regulators Asking For Evidence Of Policies And Procedures
  - IRS Form 8038
  - IRS in audits
  - SEC investigations
- Establishes a Road Map of Procedures to Stay Out of Trouble



# Components of a Debt Policy

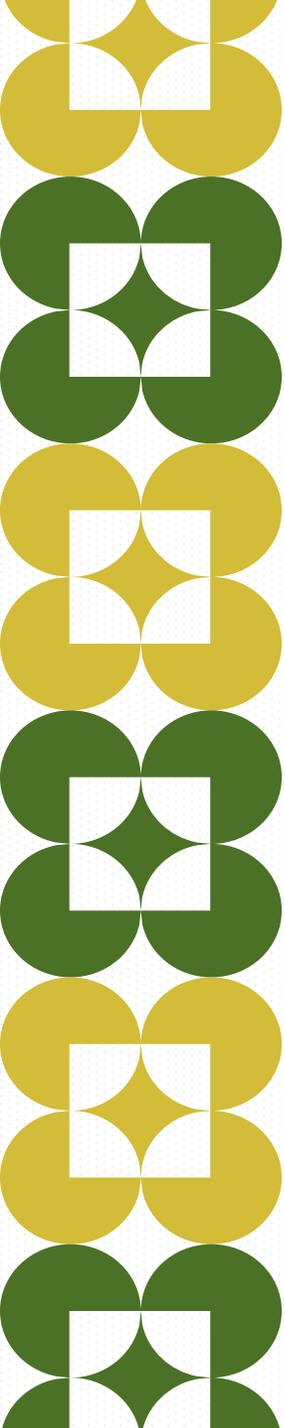
- Authority to Issue Debt
- Entity's Debt Limits
  - Legal restrictions (e.g., state constitution, bond referenda)
  - Public policies (purposes, tied to CIP, economic development)
  - Financial restrictions (debt limits and debt capacity)
    - Debt per capita
    - Debt to personal income
    - Debt to personal property
    - Debt service payments as % of general fund revenues/expenditures



# Components of a Debt Policy – (cont. 2 of 3)

## ■ Debt Structuring

- Types of Debt Allowed to be Issued
  - General Obligation and parameters of that pledge
  - Revenue
  - Taxable (including tax-credit and subsidy)
  - Fixed or Variable Rate
  - Direct Purchase (bank loan or private placement)
  - Refundings
  - Other Products: Pension bonds, OPEB, Swaps, and Derivatives
- Debt Structuring
  - Maximum term
  - Average maturity
  - Debt repayment structure
  - Use of optional redemption features
  - Other features such as bond insurance and reserve accounts



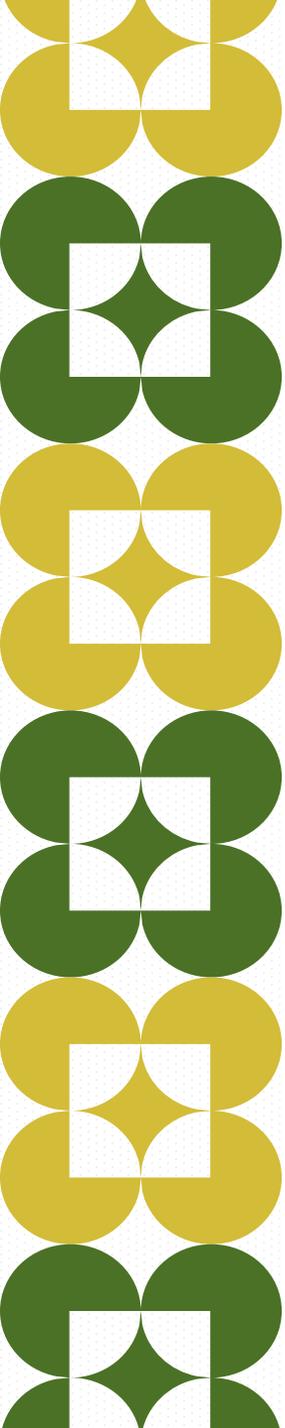
# Components of a Debt Policy – (cont. 3 of 3)

## ■ Debt Issuance Practices

- Selection of external professionals
- Criteria for determining method of sale
- Evaluating bond pricing
- Use of credit rating agencies
- Primary disclosure practices and procedures

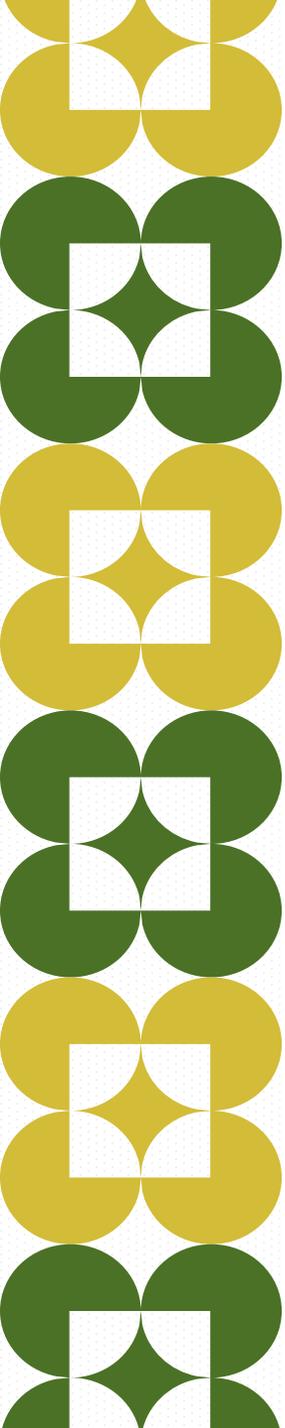
## ■ Debt Management Practices

- Investment of bond proceeds
- Budgeting for and making debt service payments
- Continuing disclosure practices
- Federal tax law compliance (arbitrage private use)
- Monitoring refunding opportunities
- Investor relations



# Implementing the Policy

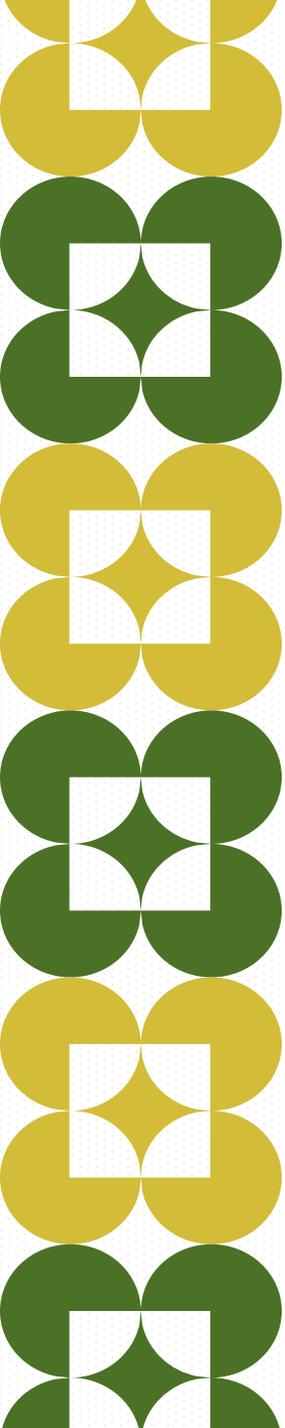
- Development By Team (With A Leader!)
- Internal Staff Sign Off
- Approval From Governing Body
- Disseminating to Team (Internal And External)
- Compliance Procedures for the Policy
  - Are we doing what we said we would do?
  - Developing checklists to ensure compliance
- Periodically Reviewing and Amending Debt Policy in Response to Changing Market and Regulatory Requirements (review at least annually)



# Other Observations

- If Starting From Scratch, Review Policies From Peer Governments
- Develop Section By Section
- Have Separate Policies Where Needed – e.g., Disclosure And Investment of Proceeds
- Stay Alert for Changing State and Federal Laws and Regulations
- Debt Policy Provides Cover in Certain Situations
  - Outside Professionals
    - "Have I got an idea for you!" "Sorry, we can't!"
  - Elected Officials
    - "Let's do a swap!" "Sorry, we can't!"
  - The Media

# Issuing Debt for Capital Projects



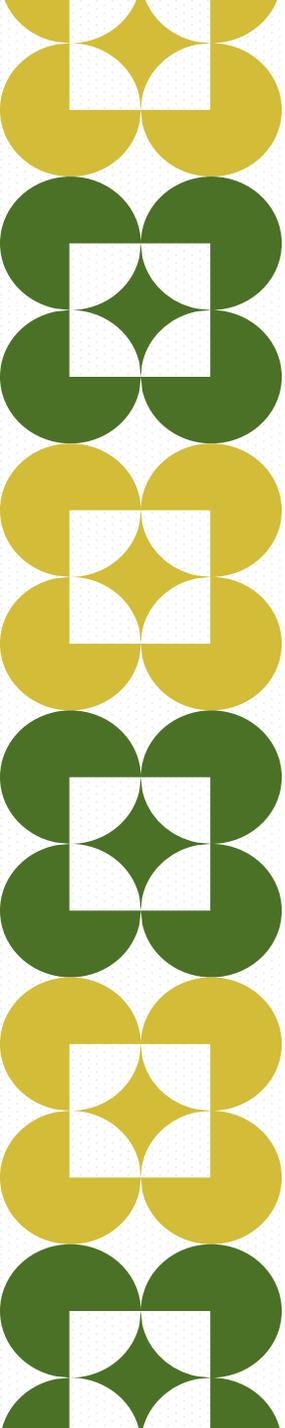
# Confirm Debt is the Right Path for Your Project

- What is the Project ?

- Expected lifetime of asset (capital vs operating costs)

- What Are Your Financing Strategies?

- Cash flow projections
- Consider all funding alternatives, including cash funding or “Pay-as-you-go”
- Reliability and stability of funding sources
- Affordability of strategies
- What financing tools are available in the current market at reasonable cost?
- What is permissible by state and local laws?
- What is allowable per your debt management policy?



# Understanding Debt Limits

## ■ Legal Limits – Debt Capacity

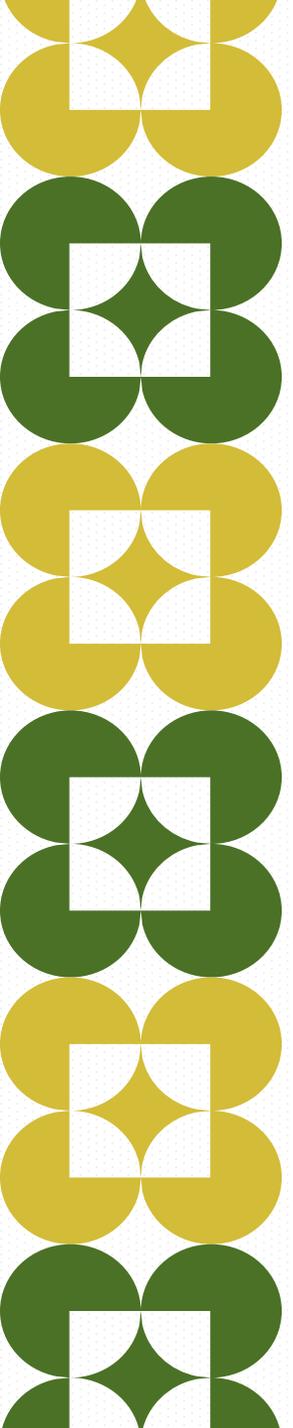
- Most states impose legal limits on how much debt can be issued
- Typically based on market value of property within jurisdiction
- Most often applicable only to general obligation debt

## ■ Financial Limits – Based on Revenue Sources

- Revenue bond capacity may depend on ability and willingness to raise rates and to maintain debt service coverage factors over time

## ■ Internal Policy Limits – Debt Affordability

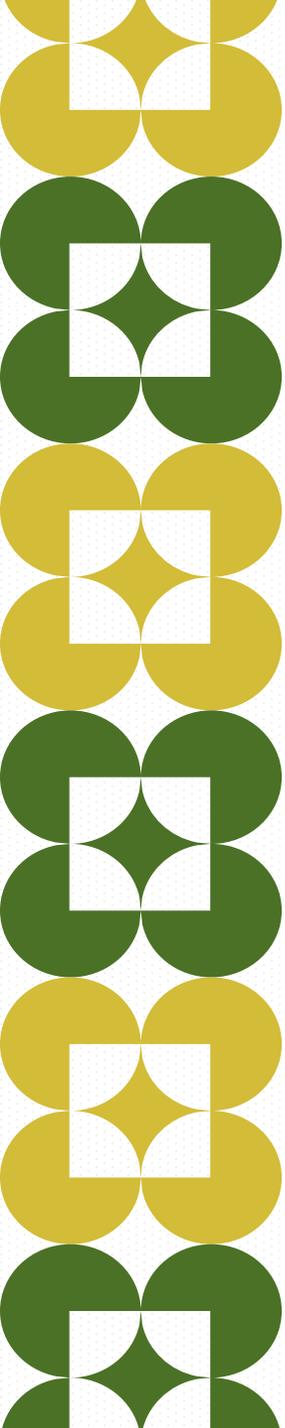
- Internal debt policies may provide additional limitations on how much debt may be issued



# Assessing Debt Capacity

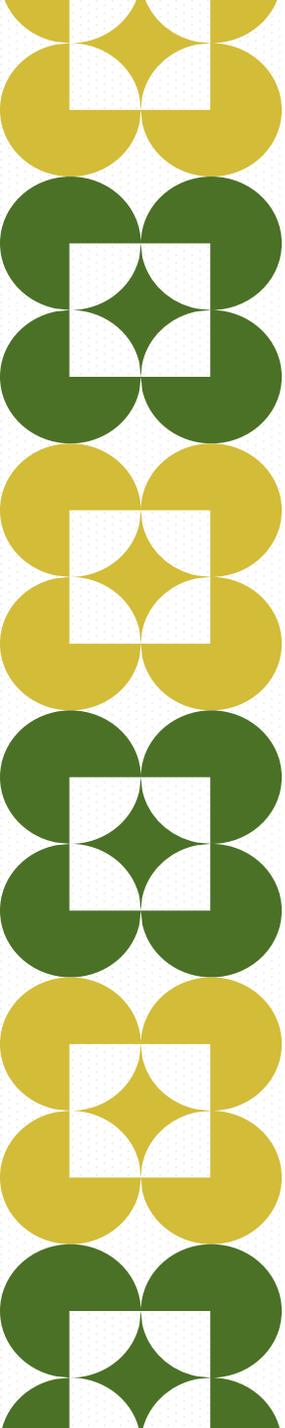
- Future principal and interest payments
- How much debt are you legally allowed to issue?
- Debt covenant restrictions
- Overlapping debt

**Structure debt to fit within available capacity**



# Debt Affordability Ratios

- Determining “Affordability” is an Art, Not a Science
- Ratios to Assess Affordability of General Obligation Debt
  - Debt per capita
  - Debt service as % of revenues or expenditures
  - Debt Coverage Ratio
    - Net operating income/debt service
- Affordability Ratios Should Also Consider Any Future Borrowing Plans

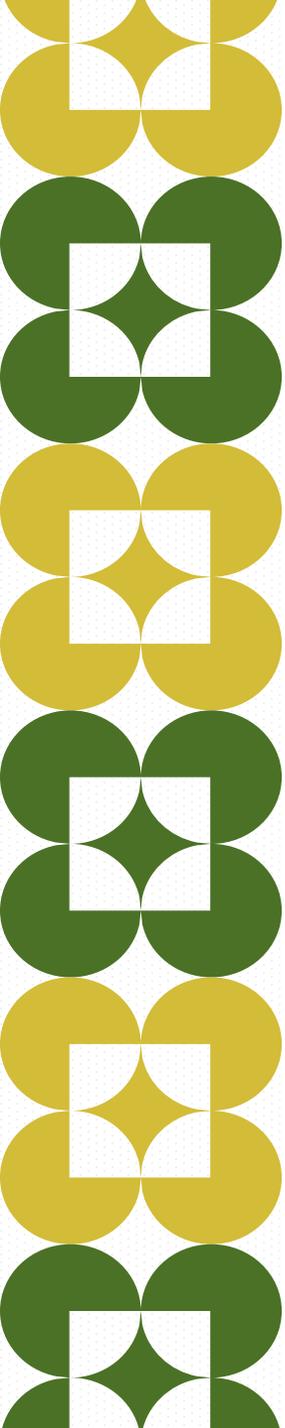


# Debt Affordability Considerations

- Excessive debt service as a percentage of operating expenses can serve to constrain future opportunities
  - Maximum Annual Debt Service (MADS) as % of projected revenues/expenditures
- However, debt issued for projects also grows strategic programs, increases the organizations revenue and operating expense base, and provides additional prudent borrowing capacity in future years
- Be mindful of rating agency analysis

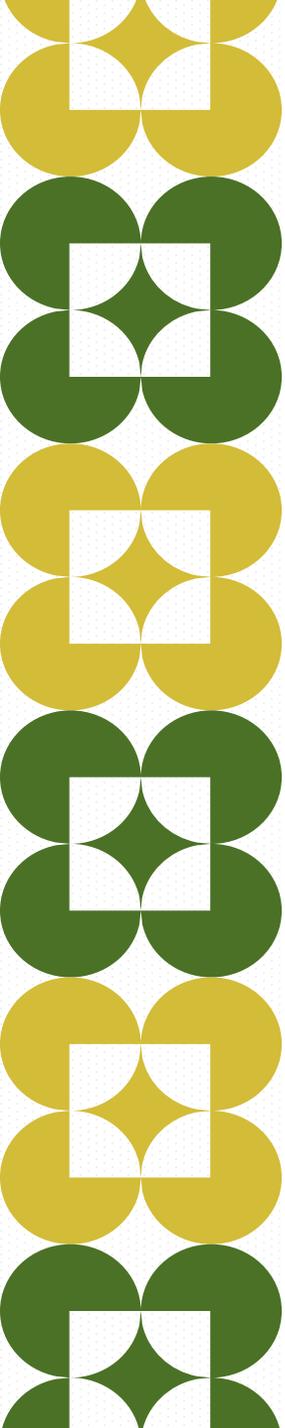
**So, Now You Are Ready To  
Proceed**

**You Are The Quarterback**



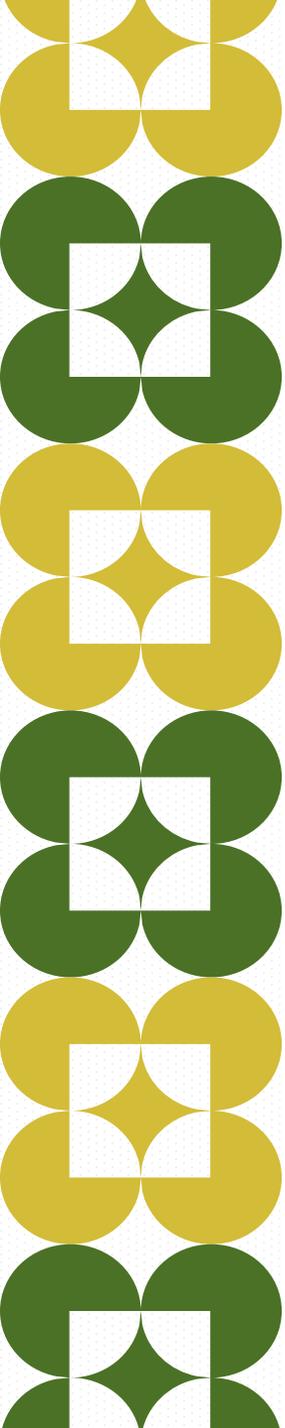
# Understanding Your Responsibilities

- Debt Issuance is **NOT** a Casual Assignment
- This Is Your Agency's Transaction
- You Are the Agency's Representative, But Not the Only One With Responsibilities
- When the Bonds Are Closed and Documents Executed, Your Organization May Have To Live with the Obligations and Commitments for the Next 20 to 30 Years
- If Anything Goes Wrong (i.e., default, audit, etc.), the Regulators/Enforcers Will Come Knocking On Your Door
- Potential For Personal Liability and Reputational Damage



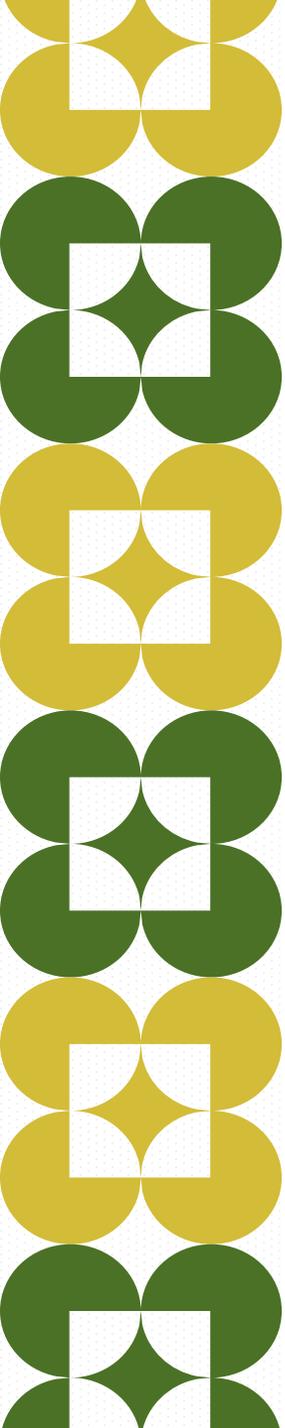
# Role of the Finance Officer

- Your role extends past administration of debt program
- Understand your responsibilities as they relate to:
  - Federal Securities Law
  - Federal Tax Law
  - State Law
  - Your Entity Ordinances, etc.
- Have documented policies and procedures related to elected officials' responsibilities and do's/don'ts
- Be aware of your roles and responsibilities PRIOR to starting the debt issuance process, not after
- Finance officer's responsibility is to taxpayers and ratepayers to ensure costs of debt repayment are most favorable in short and long-term



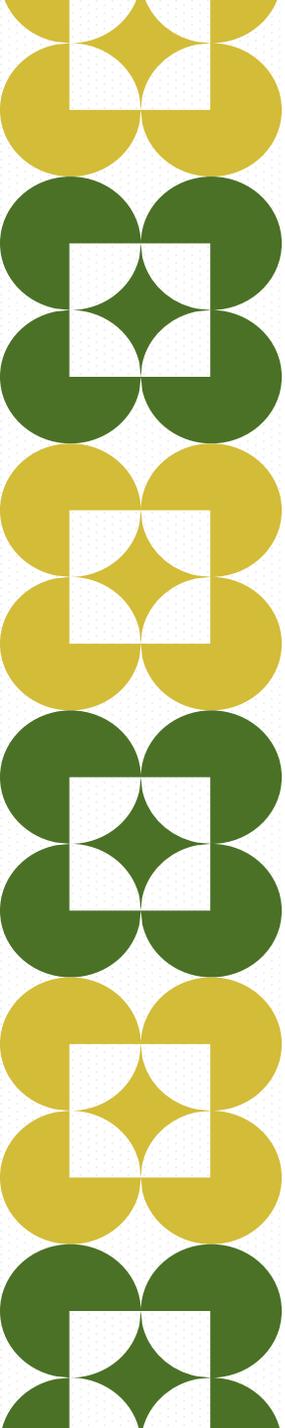
# Role of the Finance Officer – (cont. 2 of 4)

- Be an active participant
  - Attend every meeting
  - Read all the documents
  - Don't be afraid to ask questions
  - Be prepared to present the deal to your governing board
  - If you don't understand the transaction, do not present it to the governing body
- Make sure your internal team understands their responsibilities
  - Offer bond training courses



# Role of the Finance Officer – (cont. 3 of 4)

- Coordinate internal team members (finance staff, city/county/special district attorneys, project managers, etc.)
- Work with “partner” departments/agencies/bureaus by providing direction, leadership, oversight, and guidance
- Select and assign duties to outside finance team participants and manage performance
- Manage the financing project and timeline
- Structure financing within parameters of state and local law and legislatively adopted policy

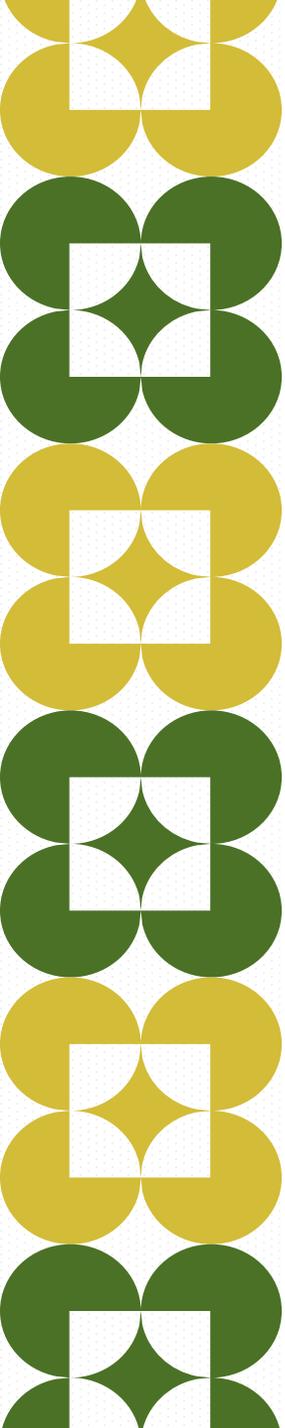


# Role of the Finance Officer – (cont. 4 of 4)

- Select The Method Of Sale In Consultation With Municipal Advisor and be Consistent with Debt Policy
- Negotiate Business Points and Structure of the Transaction
- Ensure Consistent, Accurate, and Complete Disclosure to the Marketplace
- Ensure Continuing Disclosure, Monitoring, and Compliance
- Oversee Disbursement of Project Funds
- Oversee Debt Service Payment Process
- Ensure Tax And Disclosure Compliance
- Your Job Doesn't End When The Bonds Are Issued
  - **Now Comes the Real Work!**

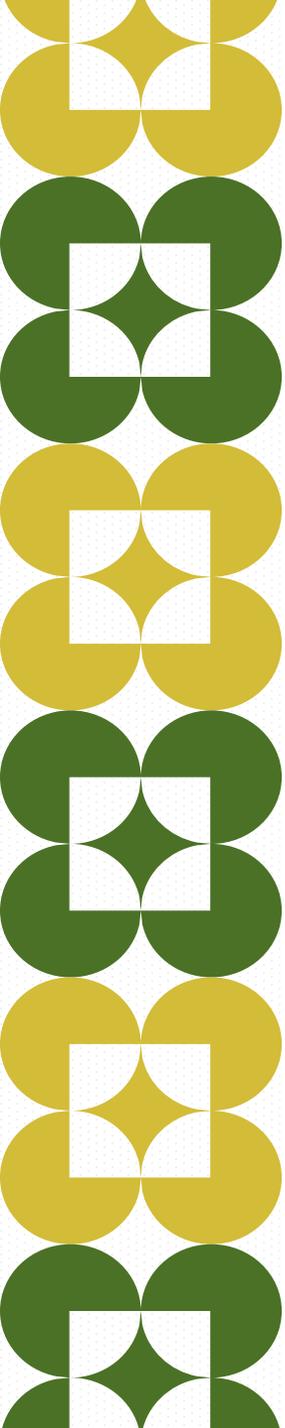
# **The Supporting Cast**

**(Know the Players & Their Roles)**



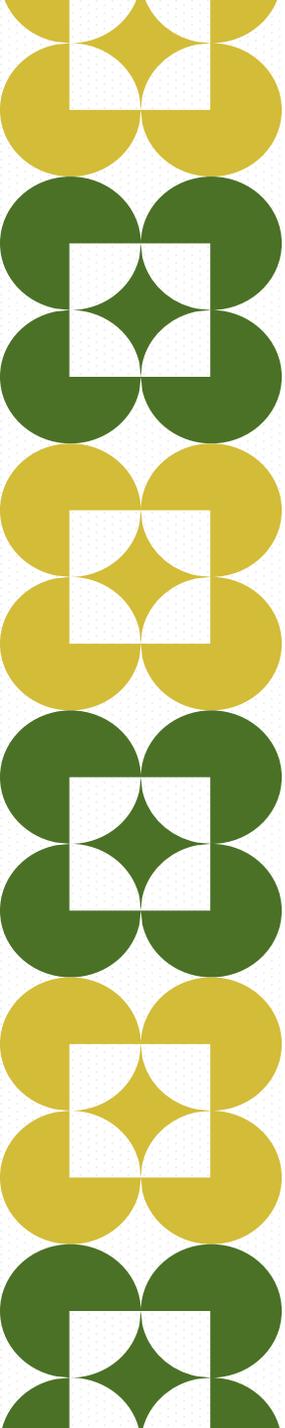
# The External Team

- Municipal Advisor
- Bond Counsel
  - Disclosure Counsel
  - Special Tax Counsel
- Underwriter (if negotiated sale)
- Underwriter's Counsel (if negotiated sale)
- Placement Agent (if direct placement)
- Paying Agent/Trustee
- Verification Agent (if refunding)
- Bidding Agent (if open market escrow refunding)
- Feasibility Consultant (revenue bonds)
- Others



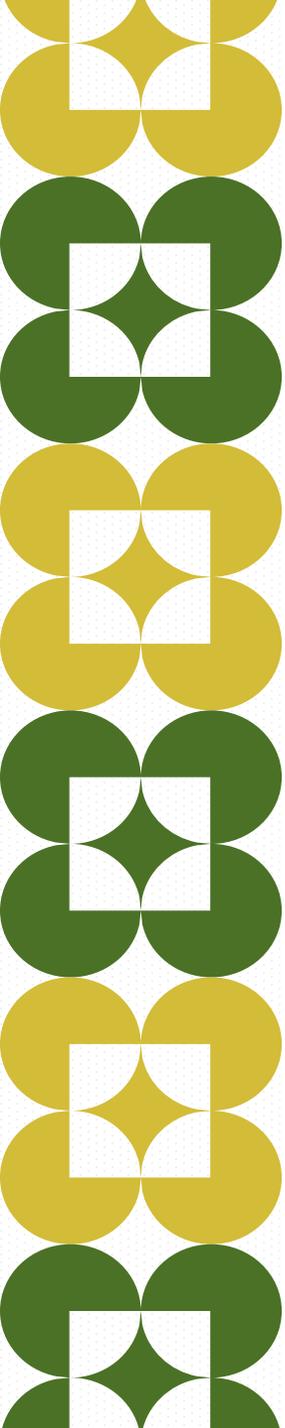
# Selecting the Financing Method and Financing Team

- Selecting Municipal Advisors
- Selecting Bond/Legal Counsel
- Selecting and Managing the Method of Sale of State and Local Government Bonds
- Selecting Underwriters for Negotiated Bond Sales
- Selecting Underwriters Counsel
- **KNOW YOUR ENTITY'S PROCUREMENT POLICIES!**



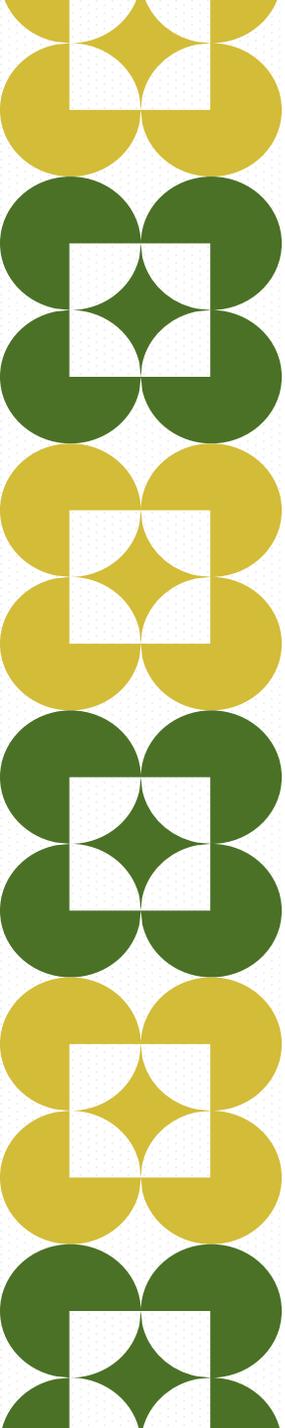
# Who Should I Hire First?

- Unless the issuer has sufficient in-house expertise and access to market information, it should hire a municipal advisor prior to undertaking a debt financing”
- MA has a federal fiduciary responsibility to represent the issuer, and only the issuer, in debt financings
- Select MA through an RFP process
- Issuer establishes MA scope of services
- **MAKE SURE MA FIRM AND INDIVIDUAL MA ARE REGISTERED WITH THE MSRB**
  - <http://msrb.org/MARegistrants.aspx>



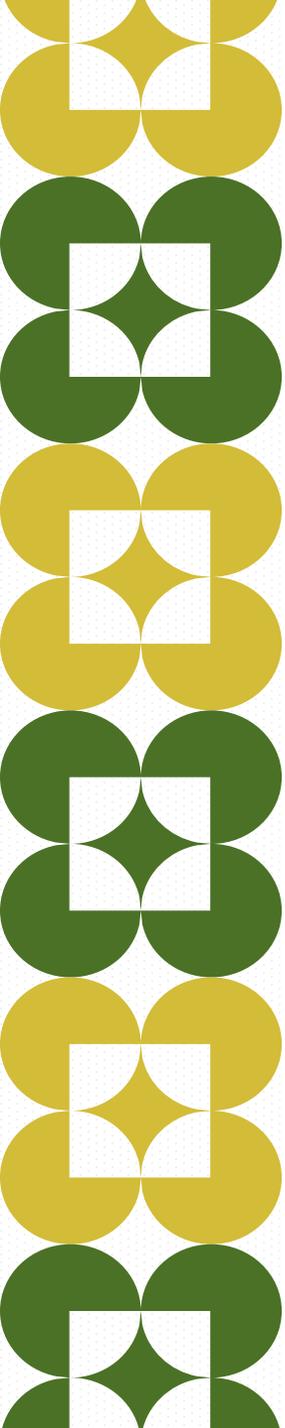
# Role of the Municipal Advisor

- Municipal Advisor Should Assist With:
  - Assessing the objectives of the project
  - Identifying financing strategies and priorities
  - Selecting the method of sale that best fits the financing
  - Evaluating other members of the external financing team
  - Assist selecting (through RFP) the underwriting team
  - Ratings presentations
  - Credit enhancement assessment
  - Providing expert advice regarding the bond sale
  - Other services



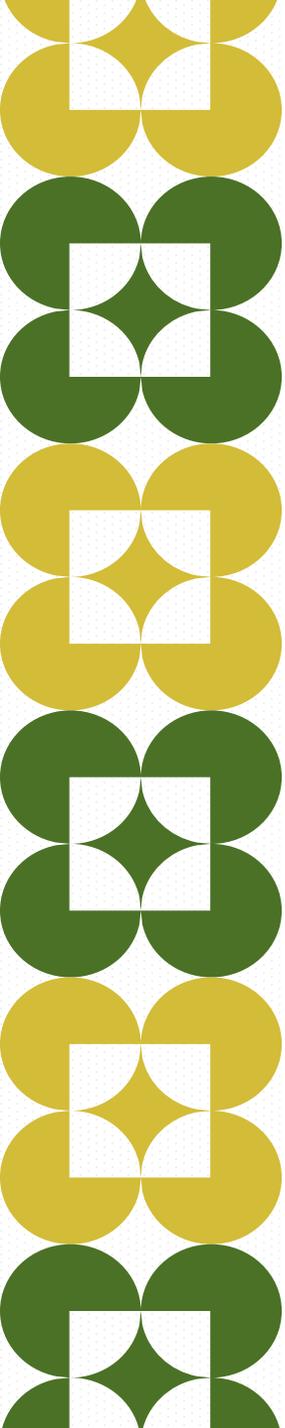
# Role of the Municipal Advisor: Competitive Sale

- Helps determine timing of offering
- Assists in structuring the bond issue
- May assist in preparing the preliminary official statement (POS)
- May assist with obtaining ratings and preparing rating presentation
- Ensures bidders/UW are aware of upcoming sale



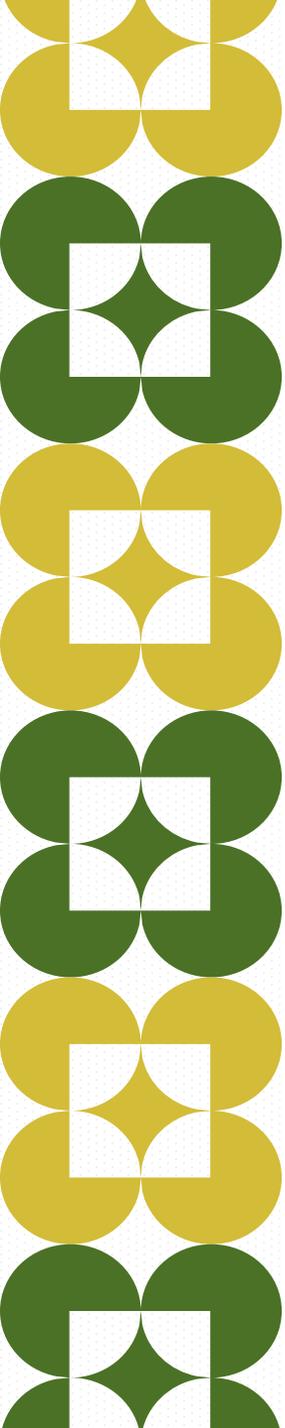
# Role of the Municipal Advisor: Competitive Sale – (cont. 2 of 2)

- Supports general marketing to the investor community
- Puts out Notice of Sale
- Verifies accuracy of all bids received
- Makes a recommendation to issuer to accept or reject the bid



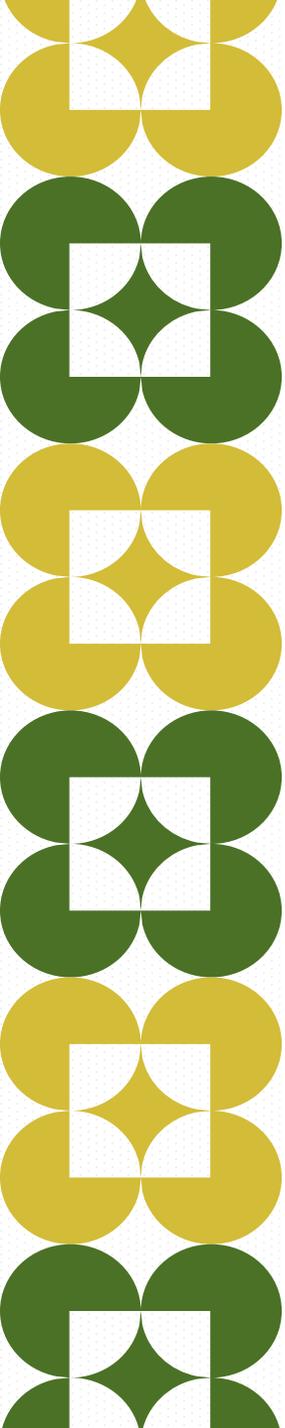
# Role of the *Municipal Advisor:* *Negotiated Sale*

- Assists with Underwriter RFP and Selection Process
- Assists Issuer In Structuring the Bond Issue
- Assists In Preparing the Preliminary Official Statement (POS)
- May Assist In Publicizing Upcoming Bond Sale to Investor Community



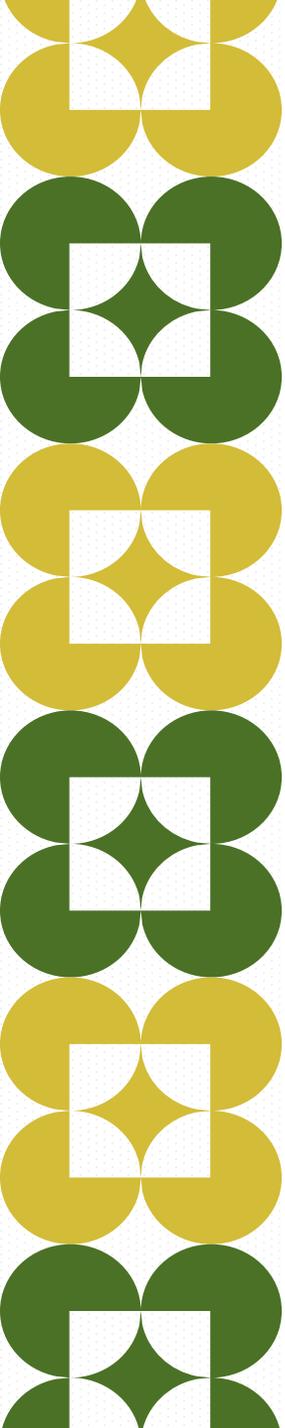
# Role of the Municipal Advisor: Negotiated Sale – (cont. 2 of 2)

- Advises Issuer with Redemption Provisions and Other Terms with Respect to Negotiation Of Coupon Yields. MA Should Provide Independent Pricing Views.
- Advises Issuer On Day Of Pricing With Respect To Final Negotiation Of Terms (Pricing Changes, Call Features, Discounts, Premiums, Etc.)



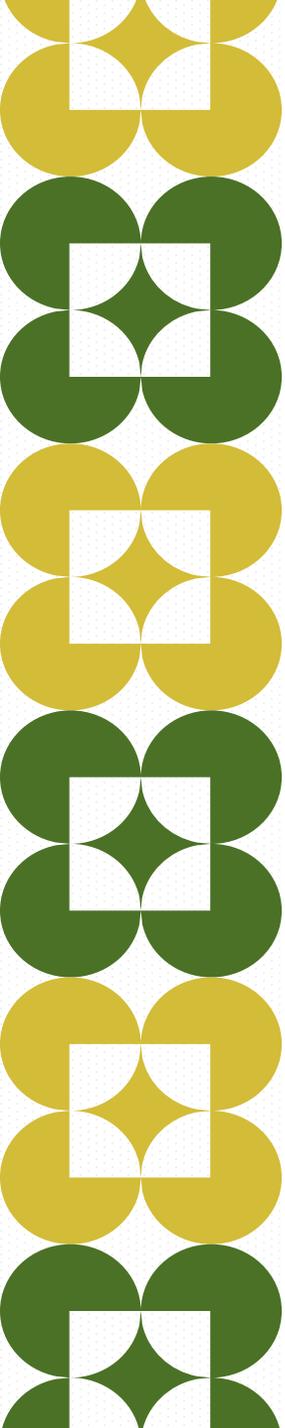
# Managing Your Municipal Advisor Relationship

- Ongoing Communication of Priorities, Objectives, And Expectations
  - Match to specific issuer project/financing needs
    - For example, swap advisor
  - Active vs. Passive
  - Continuity of MA staff
  - Written scope of services from issuer assists with this
- Use of Multiple MAs
  - Project or task-specific
  - Pricing and/or post-pricing specialists



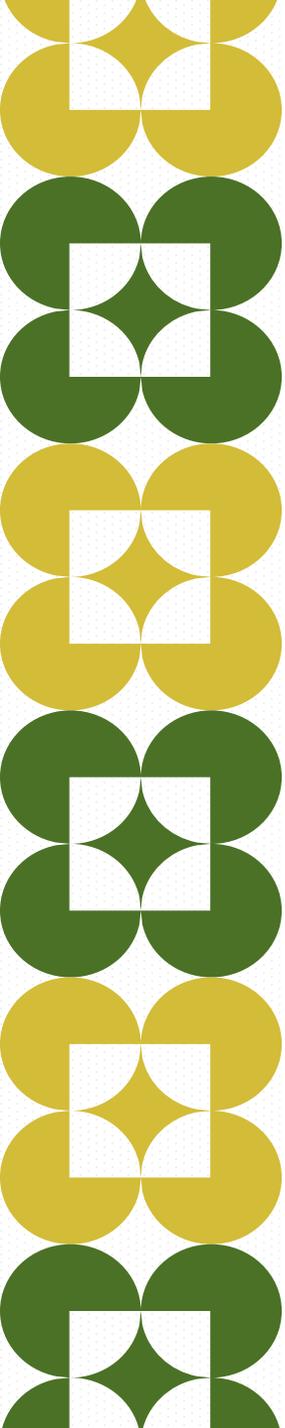
# Selecting and Managing MAs

- Hire MA prior to undertaking a debt financing
- Select MA through an RFP process, based on merit
- Determine if MA is for a specific transaction or a period of time
  - Pool of MAs
- Issuer sets scope of work, be specific
- Determine basis for compensation (e.g., bond proceeds)
- Make sure MA is registered with SEC and MSRB
- Develop selection criteria
  - Experience
  - Knowledge of market
  - Knowledge of issuer



# MSRB Rules For MAs to Protect Issuers/Overview

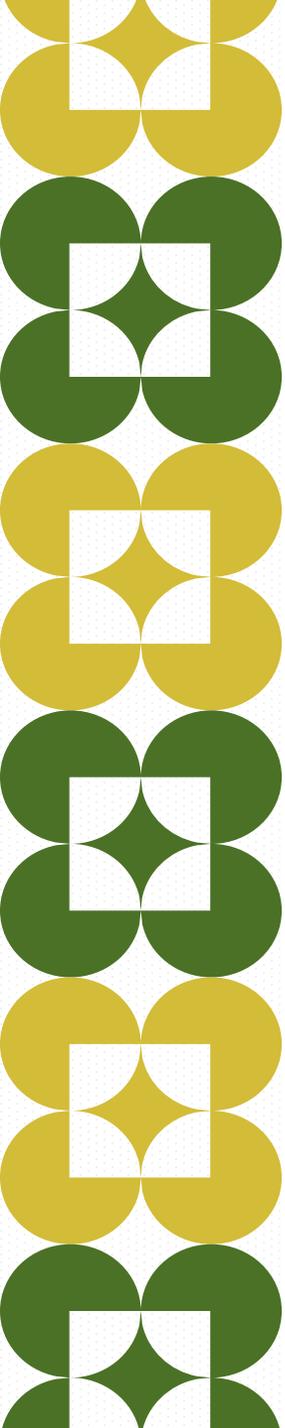
- Rule G-42
  - Fiduciary Duty
  - Scope of Services in Writing
  - Method of Payment in Writing
  - Disclosure of Conflicts
  - Have the Basis to Provide Advice/Recommendations
  - Suitability and Know Your Client Standards
- Rule G-10
  - Information About How to File a Complaint
- Rule G-37
  - Restricts Political Contributions/Pay to Play Practices for Underwriters and MAs



# Types of Legal Counsel in Bond Transactions

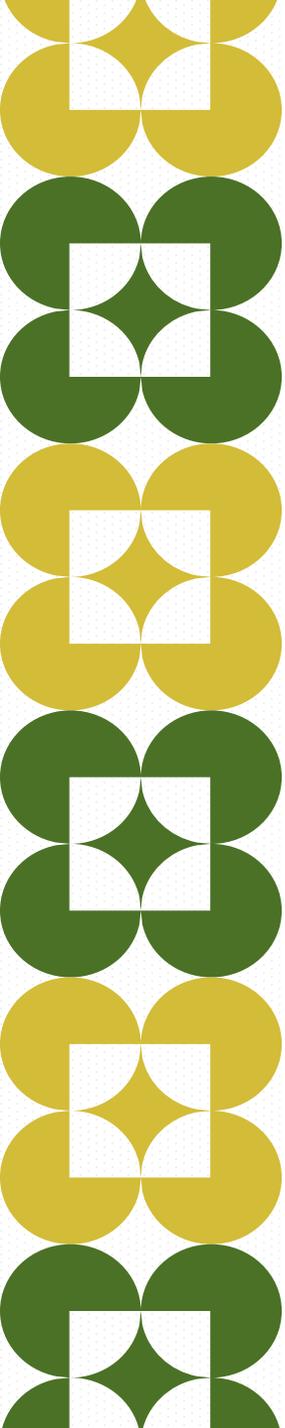
Not all types of counsel are needed on every transaction. Will depend on type of bonds, method of selling bonds, and issuer preferences

- **Issuer Counsel:** Issuers own internal counsel that focuses on ensuring compliance with local ordinances, codes, and policies
- **Bond Counsel:** Provides legal opinion that 1) bonds are legally issued; and 2) meet IRS tax-exemption standards. Bond counsel is a part of all public transactions and most bank loans



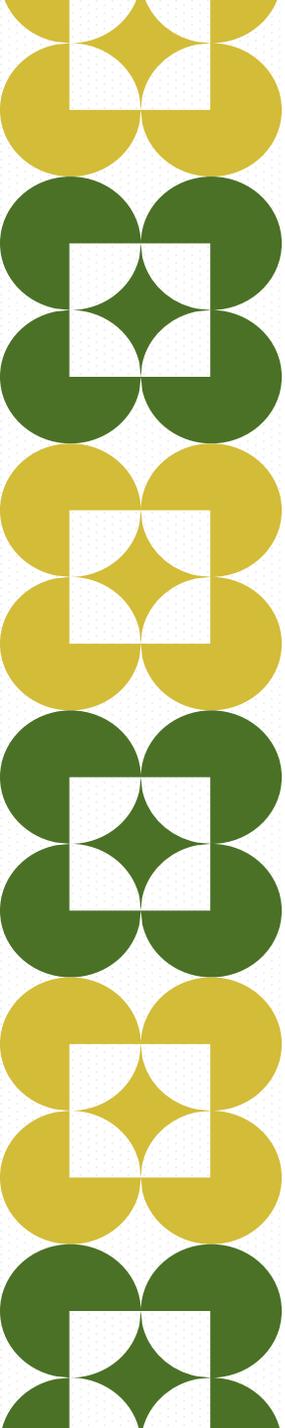
# Types of Legal Counsel in Bond Transactions – (cont. 2 of 2)

- **Underwriter's Counsel:** represents underwriter in a negotiated bond sale
- **Disclosure Counsel:** law firm that assists issuers in meeting its primary disclosure obligations. Use of disclosure counsel by issuers is growing.
- **Special Tax Counsel:** provides special tax related opinions on certain complex transactions
- **Bank Counsel:** similar to underwriter's counsel, bank counsel represents banks direct purchases, bank loans, etc.



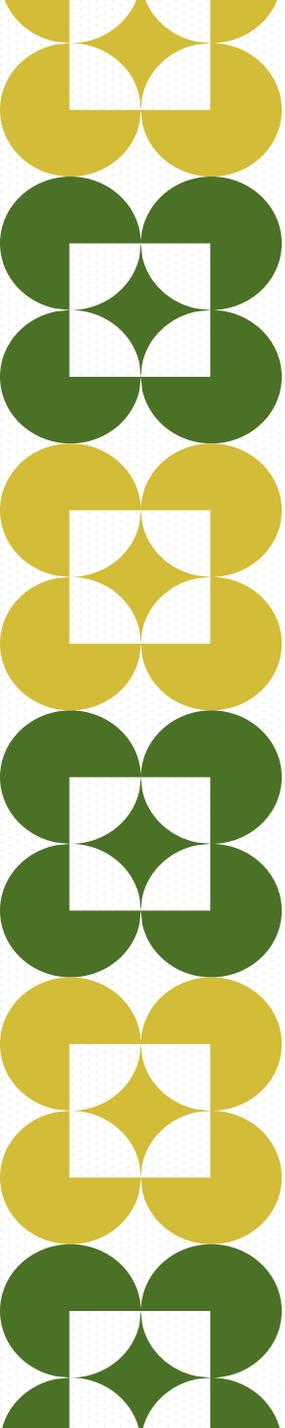
# Selecting Bond Counsel

- Provides opinion that (1) the bonds are legally authorized and issued and (2) if applicable, interest is excluded from gross income (Federal/State/Local)
- Often handles disclosure related items (drafting or reviewing documents) and may also assist with due diligence process leading up to issuance of the bonds
- Selection of bond counsel should be based on merit and generally done through a Request for Proposals (RFP) process
- RFP should address scope of services, term of contract, evaluation criteria, and the selection process
  - May be managed by Finance Office and/or City Attorney



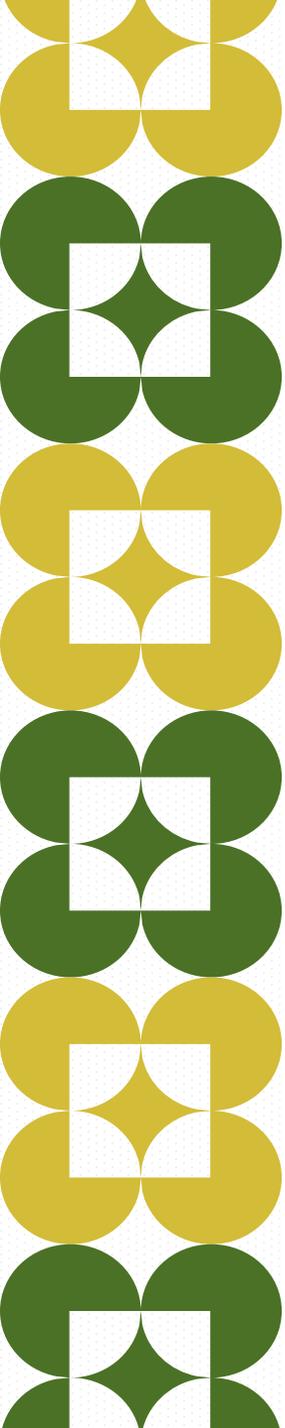
# Selecting Bond Counsel – (cont. 2 of 3)

- Key qualifications of Bond Counsel include:
  - Experience with similar financings: type, size, structure, and state law
  - Specialized tax advice beyond normal bond counsel services
  - Expertise in federal securities laws and regulations
  - Be aware of relationships that might pose conflict of interest
- Determine if other ‘specialty counsel’ is needed, due to nature of transaction or potential conflict of interest.
  - Disclosure Counsel
  - Special Tax Counsel



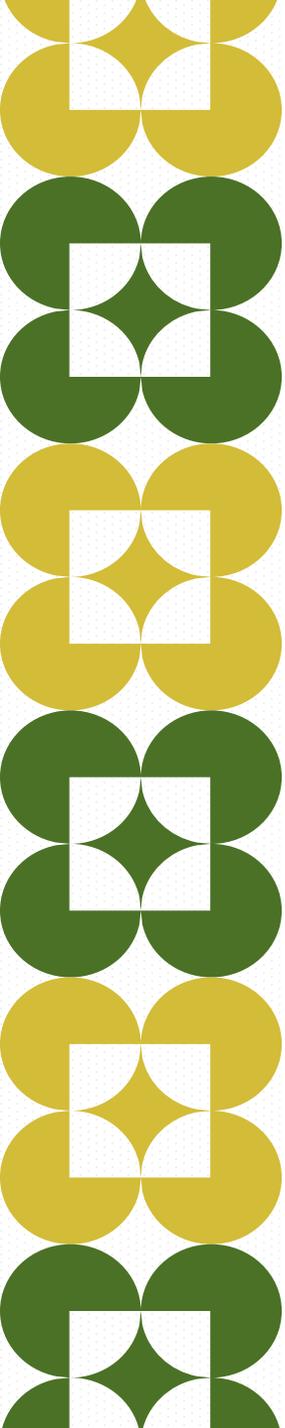
# Selecting Bond Counsel – (cont. 3 of 3)

- Determine if other ‘specialty counsel’ is needed, due to nature of transaction or potential conflict of interest.
  - Disclosure Counsel
  - Special Tax Counsel
- Same firm as Bond Counsel?
- Seeking Counsel’s Advice When Issuers Receive an IRS Letter/Audit Inquiry



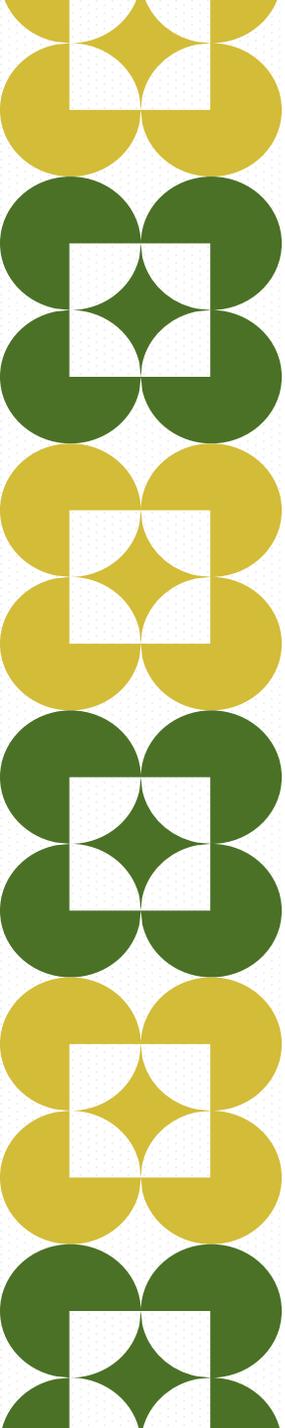
# Underwriter's Counsel

- May prepare the investor disclosure document (official statement), bond purchase agreement, agreement among underwriters, and related documents
- Conducts due diligence on behalf of the Underwriter
- Selected by the Underwriter, cannot be same firm as Bond Counsel



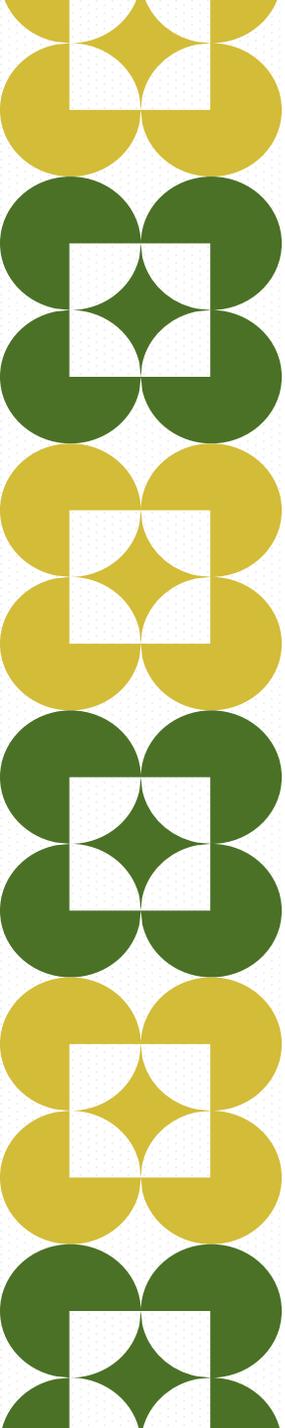
# Issuer's Role in Selecting Underwriter's Counsel

- Issuers should minimize their involvement with underwriter's counsel selection
- If desired, develop list of general criteria and qualifications
- If warranted, prepare list of acceptable firms
- Review Underwriter Counsel's scope of services
- You are paying for underwriter's counsel, set appropriate fee arrangement – “not to exceed”.
- Have policies and procedures in place to minimize conflicts of interest



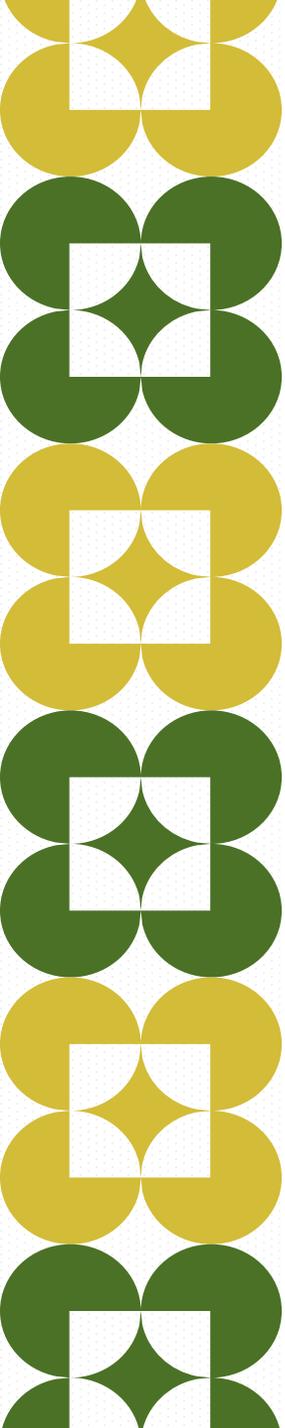
# The Role of the Underwriter in Competitive vs. Negotiated Sale

- **Competitive Sale**: sale in which multiple underwriters submit bids to purchase the bonds at a specified date and time. The Underwriter that submits the lowest purchase price (true interest cost or TIC) is awarded the bonds for sale to investors.
- **Negotiated Sale**: sale in which the Underwriter is selected before the sale, optimally through a competitive RFP process. Underwriter assists MA and Issuer in structuring the bonds and preparing the bonds to be sold.



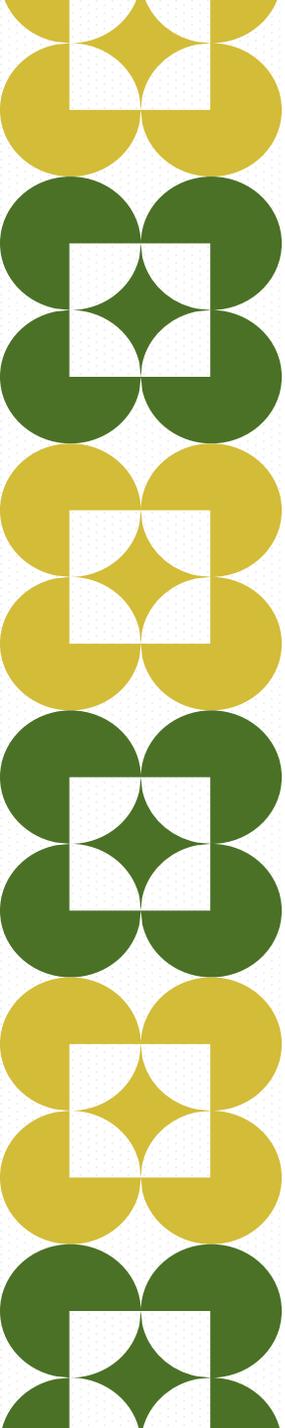
# Selecting Underwriters

- If a negotiated sale is deemed appropriate:
  - Select Underwriters through an RFP that rewards firms with demonstrated experience underwriting the types of bonds the issuer proposes to sell. RFP promotes fairness, objectivity and transparency.
  - Recognize that the role of the Underwriter and the MA are separate roles and **cannot be provided by same party**. The underwriter is not your municipal advisor.
  - Look at past transactions and their performance vs. competitive sales.



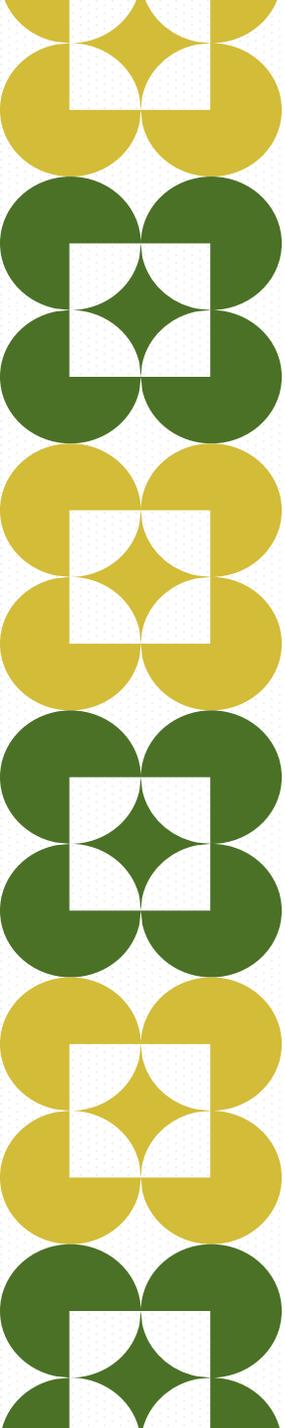
# Selecting Underwriters – (cont. 2 of 3)

- Key Underwriter selection criteria may include:
  - **Relevant experience** with type of bonds being proposed. Experience should include both the firm's investment bankers and underwriters (“the desk.”)
  - The firm's **distribution capabilities**. Can the Underwriter access institutional and retail buyers?
  - **Understanding of the Issuer's financial situation** and how to approach financing issues such as bond structure, rating strategies and investor marketing



# Selecting Underwriters – (cont. 3 of 3)

- Key Underwriter selection criteria may include:
  - **Documentation of the Underwriter's participation** in the issuer's recent competitive sales or the competitive sales of other issuers in the same state
  - The proposed “**spread**”, or **underwriter's discount**, should be requested in the RFP, but should rarely be the primary decision criterion. Proposed spread is most useful in pricing negotiations, but not as a basis for selecting the Underwriter.



# MSRB Underwriter Rules to Protect Issuers Overview

## ■ MSRB Rule G-17

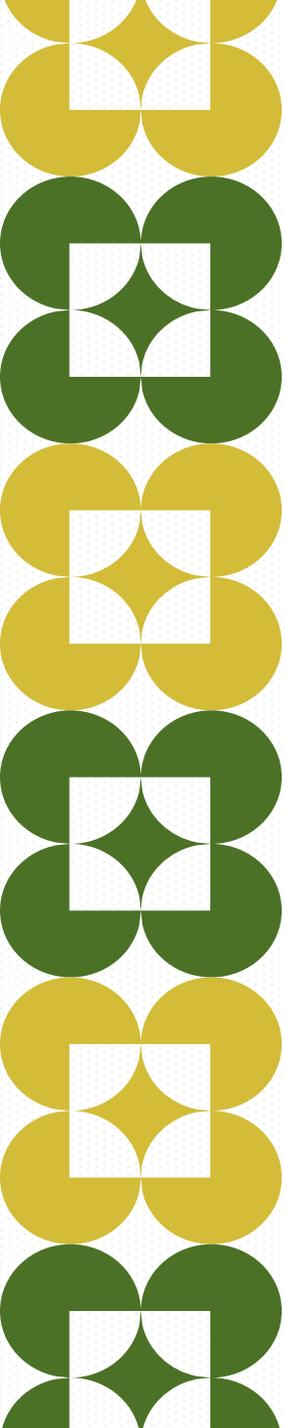
- Underwriters must disclose their role in a transaction to Issuer
- Underwriter **does not** have a fiduciary duty to Issuer
- Underwriter must disclose general and special risks of transaction
- Underwriter must disclose any conflicts they have within the transaction
- Must not suggest that issuer not use an MA
- Must seek Issuer acknowledgement of the above

## ■ Rule G-10

- Information about how to file a complaint

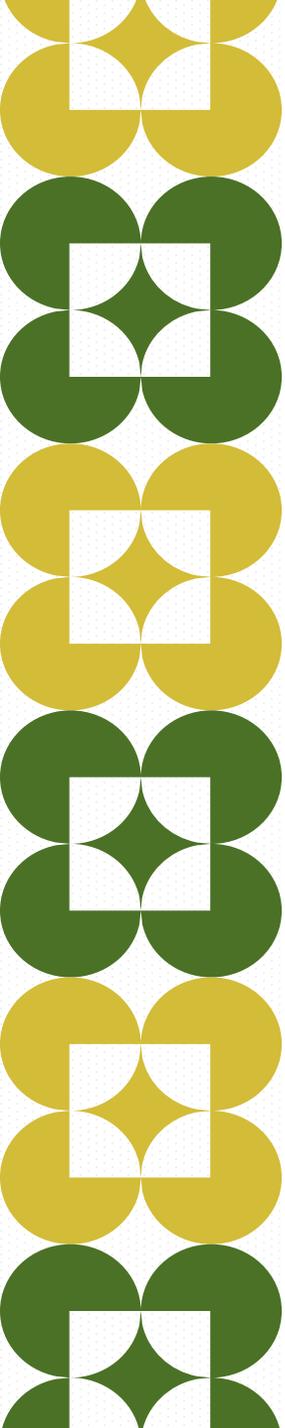
## ■ MSRB Rule G-37

- Restricts Political Contributions/Pay to Play Practices for Underwriters and MAs



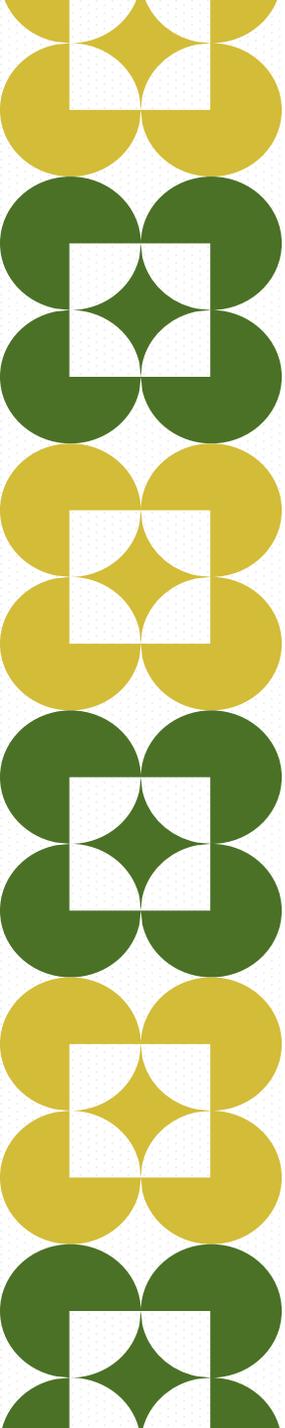
# Placement Agent

- Placement agent finds investor(s) for direct placement
  - Registered broker/dealer
- MA can not serve as placement agent
- MA can help Issuer review RFPs and bids from placement agents but can not solicit to find investors
- Know what you need to know



# Trustee or Paying Agent

- Typically, a commercial bank
- Purpose to hold/administer funds for benefit of bondholders
- Monitors compliance with the terms of the authorizing ordinance or bond indenture
- Often acts as paying agent and registrar
- May act as dissemination agent for continuing disclosure
- Consider customer service history from references as well as costs
- Selection based on “lowest bid” not always best criteria; look for services provided, such as on-line access and ease of use



# Other Financing Team Participants

- Bond Insurer or Credit Enhancement Provider
- Surety Bond
- Liquidity or Credit Providers (variable rate debt)
- Investment Advisor
- Escrow Verification Agent (in case of refunding)
- Bidding Agent (in case of refunding with open market escrow)
- Independent ESG Verifier (in case of ESG/Green bonds)

# QUESTIONS?

**JAY GOLDSTONE**

*Special Advisor to the Mayor*  
City of San Diego

