SAMPLE DEBT POLICY

Introduction

The following is a sample debt policy based on different municipalities' policies throughout the United States. The following sample debt policy statements are offered as useful working material by the Municipal Debt Advisory Commission for use by local municipalities in creating their own formal debt policy. Many items listed may not be appropriate. The following are intended to be only ideas that may be evaluated, altered, and used if appropriate.

No recommendations of ratios, percentages, or numbers are included in these sample statements; these are determined by the municipality. Blank areas may be filled-in by local governmental units in accordance with desired policy limits, local resolutions, or the Oregon Revised Statutes as appropriate.

Sample Municipal Debt Policy Statements

Accounting Policy

1. Establish and maintain accounting systems according to Generally Accepted Accounting Principles [GAAP], standards of the Government Finance Officers Association [GFOA], and the National Committee on Governmental Accounting.

2. An annual audit will be performed by an independent public accounting firm that will issue an official opinion on the annual financial statements detailing areas that need improvement.

   Target debt ratios will be annually calculated and included in the review of financial trends:

   a. Net debt as a percentage of Real Market Value of taxable property should not exceed X.X percent.

   b. The ratio of debt service expenditures as a percent of governmental fund expenditures should not exceed XX.X percent.

   Total indebtedness including direct and overlapping debt will be analyzed in determining financial condition.

3. Full disclosure will be provided in the financial statements and bond representations.

4. Financial systems will be maintained to monitor expenditures and revenues on a monthly basis with thorough analysis and adjustment (if required) at mid-year.

5. All revenue collections will be consolidated under finance and be audited at least annually.

6. Annually seek the GFOA Certificate of Achievement for Excellence in Financial Reporting and the GFOA Distinguished Budget Presentation Award.

7. Reports shall be made to rating agencies on a regular basis and at such other times as may be deemed appropriate in order to maintain effective relations.

8. Refunding

    a. Outstanding debt will be refunded when advantageous, legally permissible, prudent, and net present value savings greater than X.X percent are available through refunding.

    b. Outstanding indebtedness shall be refunded for the benefit of management goals when debt covenants and structures exist which are not consistent with prudent financial management.

    c. A record keeping system to meet the information requirements of the Tax Reform Act of 1986 shall be maintained. Specifically, the system will monitor earnings on bond proceeds and rebate excess earnings above the allowable level to the U.S. Treasury in a timely manner in order to avoid the loss of tax-exempt status of debt issues.

Capital Budget Policy

1. All capital improvements will be made in accordance with an adopted Capital Improvements Program. A five-year capital improvement program that details each capital project, the estimated cost, description, and funding source will be prepared annually. The debt issuances that are a part of the capital improvement program will be structured to meet debt policy and debt ratio targets.

2. Operating expenditures will be programmed to include the cost of implementing the capital improvement program and providing all labor, operating costs, and capital outlay required.

3. The total cost for each potential financing method for capital project proposals will be determined.

4. Identify cash flow needs for all new projects and determine which financing method best meets the cash flow needs of the project.

5. Current revenues will be used to finance ongoing maintenance needs and to provide reserves at a level adequate to protect capital investment and to minimize future maintenance and replacement cost. The size of such reserves shall be dependent on the economic nature of the facility and policy considerations regarding its future use and ultimate disposition. As a general rule, the annual contribution to such reserves shall be approximately X to X.X percent of a facilities replacement value depending on useful life.

Debt Issuance Policy

1. Generally

    a. General and Non-general obligation debt financings may be sold on a negotiated basis if it is found that the sale by negotiation provides significant cost or other advantages.

    b. The right to reject any or all bids is reserved for competitively bid issues.

    c. Increasingly rely on current revenue to finance capital improvements; a "pay as you go" basis. Strive to increase each year the percentage of capital improvements financed by current revenues.

    d. Excess balances in completed project funds should be used as a substitute for new issues to fund projects that have been approved in the normal evaluation process and priority system. Surplus balances should not be used for projects that have not been so evaluated.

    e. Agreements with commercial banks or other financial entities may be entered into for purposes of acquiring lines of credit that will provide access to credit under terms and conditions judged prudent and advantageous.

2. Short-Term Financings

    a. Tax or Revenue Anticipation Notes will not *normally* be issued to fund operations. Cash will be managed in a fashion that will lessen the need for borrowing to meet working capital needs.

    [Realizing that expenditure cycles may not follow the cycle of tax receipts and may not follow the cycle of revenues generated by the enterprise funds, short-term debt in the form of Tax or Revenue Anticipation Notes to meet cash flow requirements may be issued as required].

   b. When financing a project, Bond Anticipation Notes may be issued if such notes will result in a financial benefit. Bond Anticipation Notes will not be issued for a period of longer than X years.

   c. Tax-exempt commercial paper or variable rate demand notes may be issued when their use is judged prudent and advantageous.

3. Long-term debt will be self-supporting whenever possible. Revenue Bonds, Certificates of Participation, Limited Tax Obligations, General Obligation (Self-Supporting), and Tax Increment Bonds may be issued as best fits the financing objectives.

4. Contract interest rates on loans made from the proceeds of General Obligation (Self-Supporting) bonds shall be equal to the effective interest rate paid on the bonds sold to finance such loans plus X.X percent for servicing and self-insurance. All GO(S) indebtedness shall be self-supporting. Prior to the issuance, there shall be a review of projected cash flows, based on assessment payments, prepayments and possible defaults, to assure that all future GO(S) bonds shall be self-supporting.

5. Revenue bonds, whether solely revenue backed or backed with a General Obligation or Limited Tax pledge, will be used whenever possible to finance public improvements which can be shown to be self-supported by dedicated revenue sources, and needed for the infrastructure and economic development.

   a. Revenue supported bonds are to be used to limit dependence on property taxes for those projects with available revenue sources, whether self-generated or dedicated from other sources.

   b. Adequate financial feasibility studies are to be performed for each project to provide assurances as to the self-liquidating nature of the project or adequacy of dedicated revenue sources. Assurances are to be obtained that persons primarily benefiting from the project will provide the maximum financial support allowable.

6. General Obligation Bonds will be used to finance only those capital construction or improvements which have been determined to be essential to the maintenance or development of the municipality. For self-supporting projects, GO bonding may be used in order to obtain the lowest possible interest costs.

   a. Capital improvement projects will be analyzed, prioritized and designated as to essential characteristics through the capital improvement program process. This process should distinguish and separately rank GO bonding and self-supporting projects.

   b. Use GO bonding only after considering alternative funding sources, such as Federal and State grants and project revenues.

7. Use Tax Increment supported bonds only where projects can be shown to be self-supporting from tax increments to avoid the use of general property tax revenues. Tax Increment supported debt should be managed to achieve improvement in the ratio of property tax base supported debt per dollar of Real Market Value (RMV) over time.

8. Conduit Revenue Bonds, for which no financial or moral obligation is incurred, should only be issued if the associated development projects can be shown to be financially feasible and contributing substantially to citizen welfare and/or economic development.

    a. Assurances should be received that the proposed project will contribute to economic goals.

    b. Adequate financial feasibility studies should be performed for each project to provide assurances as to the financial viability of the project.

    c. Adequate assurance should be obtained that the users of the project are financially viable, financially committed to the project, and the property will be used for its intended purpose for an extended period.

9. Variable rate debt instruments may be issued to provide flexibility and/or attempt to achieve interest savings.

    a. Economic and cash flow projections for variable rate issues shall be calculated at the then applicable fixed rate.

    b. Total variable rate debt shall be limited to X.X percent of total debt outstanding, and in no event exceed X.X percent of RMV.

    c. At least twice each year, an analysis of each outstanding variable rate bond issue shall be undertaken to determine the advisability of converting the issue to fixed-rate debt.

    d. Variable rate bonds shall be structured to protect to the greatest extent possible, against cyclical interest rate fluctuations.

Debt Policy

1. Property Tax-Supported bonded indebtedness will promote a balanced relationship between expenditures for debt service and current municipal costs and assist in minimizing the overall property tax burden.

2. The amount of annual debt service of non-self-supporting GO debt outstanding at any time (except for leases) shall not exceed XX.X percent of the total annual budgeted expenditures.

3. The amount of annual debt service of non-self supporting GO debt outstanding at any time (except for leases) shall not exceed XX.X percent of the Real Market Value of property.

4. The total outstanding amount of debt that has been incurred to acquire equipment and furnishings on an installment lease purchase basis shall not exceed, at any time, XX.X percent of Real Market Value. Individual items with a cost of less than $XX,XXX shall be paid from current cash revenues.

5. The total outstanding Bancroft Bond indebtedness shall not exceed XX.X percent of Real Market Value.

6. Current operations will not be funded from the proceeds of borrowed funds.

7. Capital projects, financed through the issuance of bonds, shall be financed for a period not to exceed the expected useful life of the project.

8. Long-term borrowing shall be confined to capital improvements or projects that cannot be financed from current revenues.

9. The general obligation debt will not exceed X.X percent of the Real Market Value of property.

10. The total general obligation debt will not exceed XX.X percent of the total annual operating revenue.

11. Annual general obligation debt service shall not exceed XX.X percent of the total, non-enterprise activities and will be strictly limited to those expenses incurred prior to actual operation of the facilities.

12. The municipality will attempt to use lease purchase agreements when the terms of the lease purchase agreement are lower than the average 90-day certificate of deposit rate.

13. Borrowing shall be of a duration that does not exceed the economic or useful life of the improvement that it finances and where feasible shall be shorter. To the extent possible repayment shall be designed so as to recapture credit capacity for future use as soon as possible.

Debt Ratios

1. Strive to maintain the highest possible debt service coverage ratio consistent with long-term financial objectives. Coverage ratios should be consistent with maintenance of the highest possible rating while preserving user charge equity and affordability.

2. Closely monitor the absolute amounts and year-to-year trends of key financial ratios.

3. There are several key debt ratios that investors and financial analyst's use when reviewing municipalities credit worthiness. The following threshold and target numbers have been established which are to be used when reviewing the key debt ratios. The threshold number is the absolute minimum or maximum ratio the municipal administration will permit. The target number is the ratio intended to achieve by XX/XX/XX through a planned program of debt management. Contingent liabilities secured by revenue or tax pledges are included as debt within the appropriate ratios. Debt issued in anticipation of taxes in the process of being collected, or grants for which a contractual commitment exists are not to be included within the debt ratios.

Sample Ratios

Current		Threshold	Target
XX.X%	G.O. debt as a percent of RMV[1]	XX.X%	XX.X%
$XXX.X	Debt per capita[2]	$X,XXX.X	$XXX.X
XX.X%	Debt per capita as a percent of per[3] capita income	XX.X%	XX.X%
XX.X%	Debt service as a percent of general[4] governmental expenditures	XX.X%	XX.X%
XX.X%	Percent of total debt to be retired[5] after ten years.	XX.X%	XX.X%
XX.X%	Unreserved General Fund Balance as[6] a percent of General Fund Revenue	XX.X%	XX.X%
XX:X	Dedicated revenues to debt service[7] for Revenue Supported bonds.	XX:X	XX:X

Footnotes

[1] Debt to Real Market Value [RMV] indicates ability to repay debt. A small ratio is an indication of the ability to withstand possible future economic downturns and continue to meet debt obligations.

[2] Debt per capita is a general indicator of debt burden. The smaller the ratio - the better.

[3] Debt per capita as a percent of per capita income is a measure of the capacity of citizens to finance tax-supported debt. A low ratio means that taxes required to repay debt represent a smaller portion of the average citizen's income.

[4] Debt service as a percent of general governmental expenditures is a measure of the ability to repay debt without hampering other services. A small ratio indicates a lesser burden on the operating budget.

[5] A high ratio indicates a conservative structure on the debt portfolio allowing (among other things) more flexibility on future debt issuance and shorter repayment schedule.

[6] Unreserved General Fund balances as a percent of General Fund revenue indicates the ability to cope with unexpected financial problems or emergencies. The larger the balance, the greater the ability to cope with financial emergencies and fluctuations in revenue.

[7] Dedicated revenues to debt service for Revenue-Supported bonds ratio indicates the ability to service debt on revenue supported bonds. The higher the ratio the better.

Goals

1. Maintain ability to incur present and future debt at minimal interest rates in amounts needed for infrastructure and economic development without endangering the ability to finance essential services.

2. Establish reasonable debt level targets that recognize projected inflation and planned capital needs for each unit of government.

3. Seek opportunities to finance capital projects with revenues other than general obligation bonding.

4. Seek opportunities to finance debt service for general obligation bonds with revenues other than property taxes.

5. Structure debt retirement to relate closely to those who benefit.

6. Produce a debt policy that will help maintain and improve credit ratings.

7. Consider opportunities such as refinancing, restructuring, or defeasance of general obligation debt, which reduce existing debt service.

8. Pay all recurring expenditures with recurring revenues and to use nonrecurring revenues for nonrecurring expenditures.

9. Maintain a positive undesignated fund balance and a positive cash balance in all governmental funds at the end of the fiscal year.

10. Try not to increase current tax rates.

11. Financial management policies should be oriented to maintain a balanced relationship between debt service requirements and current operation costs, encourage growth of the tax base, actively seek alternative funding sources, minimize interest costs and maximize investment returns.

Investment Policy

1. Investment policy will be based on the GFOA Model Investment Policy and consistent with ORS 294.040 and ORS 294.135 to ORS 294.155 approved investments. See ORS 294.035 for local government summary of approved investments for details.

2. Analyze annual cash flow needs. Disbursements, collections, and deposits of all funds will be scheduled to ensure maximum cash availability and investment potential.

3. When permitted by law, pool cash from its various funds for investment purposes.

4. Obtain the best possible return on all investments commensurate with appropriate risk.

5. Annually review contractual consolidated banking services.

Operating Budget Policy

1. General

    a. The budget is a plan for allocating resources. The objective is to enable service delivery with allocated resources. Services must be delivered to the citizens at a level which will meet real needs as efficiently and effectively as possible.

    b. The goal is to pay for all recurring expenditures with recurring revenues and to use nonrecurring revenues for nonrecurring expenditures. It is important that a positive appropriated fund balance (surplus) and a positive cash balance is shown in all governmental funds at the end of each fiscal year.

c. When deficits appear to be forthcoming within a fiscal year, spending during the fiscal year must be reduced sufficiently to create a positive undesignated fund balance and a positive cash balance.

2. Current operating revenue should be sufficient to support current operating expenditures.

3. Debt or bond financing will not be used to finance current expenditures.

4. Annually recurring revenue will not be less than annually recurring operating budget expenditures (operating budget minus capital outlay).

5. Prepare a five-year operating budget that includes projections of annual growth plus allowances for operating costs of new capital facilities.

6. Develop a program to integrate performance measures and productivity indicators within the budget.

7. Structure the budget so that the relationship between expenditures and the achievement of service objectives can be readily established.

8. Establish a risk management program to provide for protection against loss and a reduction in exposure to liability. Self-insure when possible to provide protection against major loss in excess of $XXX,XXX. Excess coverage may be purchased to cover catastrophic loss to $X million. Establish a safety program to minimize exposure to liability and thereby reduce the number of claims against the fund.

9. The budget will provide for adequate maintenance of capital plant and equipment and for its orderly replacement. Establish an equipment reserve fund to replace capital outlay items with a life of more than two years and a value of $X,XXX or more. Annualize replacement costs using a sinking fund factor pegged to the estimated market rate of interest plus salvage value.

Reserve Policy

1. Maintain an unallocated fund balance of XX.X percent of the general operating budget (excluding capital outlay). These funds will be used to avoid cash flow interruptions, generate interest income, reduce need for short-term borrowing and assist in maintaining an investment-grade bond rating.

2. Establish a contingency reserve to provide for unanticipated expenditures of a nonrecurring nature, or to meet unexpected increases in service delivery costs. This reserve will be budgeted at XX.X percent of the general fund revenue estimated for that fiscal year.

3. Maintain a two-to-one [2:1] ratio of total current assets over total current liabilities in the Water and Sewer Utility Fund.

4. Maintain sufficient self-insurance reserves as established by professional judgment based on the funding techniques used and loss records.

Revenue Policy

1. Maintain a diversified and stable revenue structure to be protected short-run fluctuations in any one-revenue source.

2. Estimate annual revenues by an objective, analytical process. Prepare each year, a five-year projection of revenues and expenditures to improve financial planning and decisions.

3. Aggressively collect tax revenues. The annual level of uncollected current property taxes should not exceed XX.X percent.

4. Identify and assess merits of intergovernmental aid funding possibilities.

5. Cumulative increases in revenue from the levy of property tax will not exceed XX.X percent from the preceding fiscal year:

    - excluding taxable value gained through annexation or consolidation;
    - excluding the taxable value gained through new construction;
    - excluding millage increases mandated by the voters or courts.

6. Where and when possible, institute user fees and charges for specialized programs and services. Rates should be established to recover operational and capital or debt service costs. For example:
    a. User fees in lieu of ad valorem taxes are to be used to the maximum extent possible for services that can be individually identified and where the costs are directly related to the level of service:
        - Recreational programs will be funded from user charges for all programs in which it is practical to charge.
        - The user charge fees for water and sewer will be sufficient to finance all operating, capital, and debt service costs.
        - Connection fees are to reflect the cost of water and sewer improvements to service the additional increments of growth.
        - Building and code enforcement activities should be funded through a user charge in the form of building permits, inspections and plan-checking fees.

    b. Regularly review user fee charges and related expenditures to determine if goals are being met.