Policy Type: Board

Category: Fiscal and Budget

Policy Name: Debt Policies - Board Policy 4.7

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4.7 DEBT POLICIES (Amended 9-23-03; Amended 9-26-06; Amended 9-26-17)

Since 1982, the Board of Supervisors has supported the Administration's effort to limit the issuance of short-term debt to cover cyclical cash flow needs. Every effort has been made to incorporate actions in the County's adopted annual budget that capitalize ongoing operations with existing revenues, thus avoiding or severely restricting situations where short-term deficits are financed through long-range indebtedness. Board policy does allow for the issuance of long-term debt to finance major capital improvements. However, the County historically has required a careful assessment of capital improvement priorities, capital costs, annual debt service capacities, and annual operating and maintenance costs on the scheduled improvement in advance of incurring the indebtedness. On occasion, the Board also has supported the issuance of debt when market conditions could be optimally leveraged along with arbitrable opportunities.

4.7.1 Debt Management Policy (Adopted 9-23-03; Amended 9-26-17)

This Debt Management Policy sets forth certain debt management objectives for the County and establishes overall parameters for issuing and administering the County's debt. Recognizing that cost-effective access to the capital markets depends on prudent management of the County's debt program, this policy will be incorporated into an annual debt report presented to the Finance and Government Operations Committee with ultimate recommendation to the Board of Supervisors.

4.7.1.1 Debt Management Goals and Objectives

The County's debt issuance activities and procedures shall be aligned with the County's vision and goals for providing adequate facilities and programs that support the residents. The County shall consider the overall impact of the current and future debt burden of the financing when determining the duration of the debt issue. When issuing the debt, the County shall ensure that it:

1. Maintains accountability for the fiscal health of the County, including management and transparency of the County's financing programs.

2. Attains 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.

The purpose of this Debt Management Policy is to assist the County in pursuit of the following objectives:

- Minimize debt service and issuance costs
- Maintain access to cost-effective borrowing
- Achieve the highest practical credit rating
- Full and timely repayment of debt
- Maintain full and complete financial disclosure and reporting

- Ensure financial controls are in place with respect to proceeds of debt issuances

- Ensure compliance with applicable State and Federal laws

4.7.1.2 General Provisions

(A) Scope of Application

(1) Entities Covered

These policies establish the parameters within which debt may be issued by the County of Santa Clara and the Santa Clara County Financing Authority. The County, as a member of any joint powers authority, shall take these policies into account when considering the issuance of joint powers authority debt.

Supplemental policies, tailored to the specifics of certain types of financings, may be adopted by the Board of Supervisors in the future. These supplemental policies may address, but are not limited to, any future County general obligation, enterprise, multifamily housing, and land-secured financings.

(2) Types of Debt that May be Issued

The following types of debt may be issued under this policy subject to State and Federal law, the County's Charter and County Ordinances and Policies as may be applicable. Prior to issuance of debt, a reliable revenue source shall be identified to secure repayment of the debt. Cost savings are not a revenue source for the purposes of securing debt repayment.

a. General obligation bonds

b. Bond or grant anticipation notes

c. Lease revenue bonds or notes, certificates of participation and lease-purchase transactions

d. Other revenue bonds or notes and certificates of participation (COPs)

e. Tax and revenue anticipation bonds or notes (TRANs)

f. Land-secured financings, such as special tax revenue bonds and limited obligation assessment bonds

g. Conduit financings, such as financings for affordable rental housing and qualified 501(c)(3) organizations

h. Special financing programs or structures offered by the federal or state government such as Qualified Energy Conservation Bonds (QECBs) or other tax credit obligations or obligations that provide subsidized interest payments, when the use of such programs or structures is determined to result in sufficiently lower financing costs compared to traditional bonds and/or COPs

i. Derivatives. While the County currently has one interest rate swap in its outstanding debt portfolio, no further issuance of derivatives is contemplated.

Debt may be publicly issued or privately placed and may be issued on either a long-term basis ("Long-term Borrowing") or short-term basis ("Short-term Borrowing") consistent with the provisions of this Policy.

From time to time, the Board of Supervisors may find that other forms of debt, or that an exception to the revenue requirement, consistent with the Objectives and Goals of this Policy, would further its public purposes and may approve the issuance of such debt without an amendment of this Policy.

(B) Responsibility for Debt Management Activities

The Finance Agency shall be responsible for managing and coordinating all activities related to the issuance and administration of debt, including the implementation of internal control procedures to ensure that the proceeds of debt are directed to the intended use. The Director of Finance is appointed by the County Executive and is subject to his or her direction and supervision. In accordance with the County Charter and the County Ordinance Code, the Director of Finance is charged with responsibility for the conduct of all Finance functions.

Departments implementing debt-financed capital programs will work in partnership with the Finance Agency to provide information and otherwise facilitate the issuance and administration of debt.

(1) Debt Management Policy Review and Approval

This policy shall be presented to the Finance and Government Operations Committee as part of the annual debt report and reviewed annually by the Finance Agency to ensure its consistency with respect to the County's debt management objectives. Any modifications to this policy shall be presented to the Finance and Government Operations Committee with ultimate approval by the Board of Supervisors.

(2) Debt Administration Activities

The Finance Agency is responsible for the County's debt administration activities, particularly the timely payment of debt, investment of bond proceeds, monitoring compliance with bond covenants, continuing disclosure, and arbitrage compliance for tax-exempt debt. The Finance Agency is also responsible for implementing internal control procedures to ensure that bond proceeds or other debt is directed to the intended use.

(3) Annual Debt Report

The Finance Agency shall prepare an annual debt report for review by the Finance and Government Operations Committee containing the following:

- Description of currently outstanding debt portfolio
- Refunding and restructuring opportunities
- Future financings
- Debt administration

4.7.1.3 Purposes For Which Debt May Be Issued

(A) Long-term Borrowing

Long-term borrowing may be used to finance the acquisition or improvement of land, facilities, or equipment for which it is appropriate to spread these costs over multiple budget years, attempting to match the useful life of the assets acquired by the financing. Long-term borrowing may also be used to fund capitalized interest, costs of issuance, required reserves, and any other financing related costs which may be legally capitalized. Long-term borrowing shall not be used to fund operating costs.

(B) Short-term Borrowing

Short-term borrowing, such as TRANs (tax and revenue anticipation notes) and lines of credit, will be considered as an interim source of funding to be utilized when appropriate. Short-term debt may be issued for any purpose for which long-term debt may be issued, including capitalized interest and other financing related costs.

(C) Refunding and Restructuring

Periodic reviews of outstanding debt will be undertaken to identify refunding and restructuring opportunities. Refunding will be considered (within federal tax law constraints) if and when there is a net economic benefit of the refunding. Refundings which are non-economic may be undertaken to achieve objectives relating to changes in covenants, call provisions, operational flexibility, tax status, issuer or the debt service profile.

In general, refundings which produce a net present value savings of at least three percent (3%) of the refunded debt are considered economically viable. Refundings which produce a net present value savings of less than three percent (3%) will be considered on a case by case basis. Refundings with negative savings will not be considered unless there is a compelling public policy objective that is accomplished by retiring the debt.

Restructuring may be undertaken with the objective of minimizing long-term volatility and the exposure to future market conditions on the overall debt portfolio.

4.7.1.4 Debt Issuance

(A) Relationship to County's Budget

The County will keep outstanding debt within the practical limits of the County's debt rating and any applicable law.

The County shall assess the impact of new debt issuance on the short-term and long-term affordability of all outstanding and planned debt issuance, including additional operating costs. Such analysis recognizes that the County has limited capacity for debt service in its budget, and that each newly issued financing will obligate the County to a series of payments until the bonds are repaid. Tools include, but are not limited to, the County's Debt Affordability Model which helps evaluate the impact of proposed debt on the operating budget as well as on the County's credit ratings.

(B) Credit Quality

The County seeks to obtain and maintain the highest possible credit ratings for all categories of short and long-term debt. If appropriate from a cost-benefit standpoint, and appropriate from a sale structure, the County will consider the issuance of bonds that do not carry investment grade ratings.

The County has traditionally benefited from strong ratings and shall take any necessary steps to maintain favorable ratings.

(C) Structural Features

The Director of Finance shall be responsible for determining the appropriate structure for the debt financing considering factors including, but not limited to, the inter-generational benefit of the financing and current market conditions.

(1) Debt Repayment

Debt will be structured for a period consistent with a fair allocation of costs to current and future beneficiaries of the financed capital project. The County shall structure its debt issues so that the maturity of the debt issue is consistent with the economic or useful life of the capital project to be financed.

(2) Variable-rate Debt

The County may choose to issue securities that pay a rate of interest that varies according to a pre-determined formula or results from a periodic remarketing of the securities. Such issuance must be consistent with applicable law and covenants of pre-existing bonds, and in an aggregate amount consistent with the County's creditworthiness objectives. When making the determination to issue bonds in a variable rate mode, consideration will be given in regards to the useful life of the project or facility being finance or refinanced or the term of the project requiring the funding, market conditions, and the overall debt portfolio structure. The Director of Finance shall evaluate the use of variable-rate debt on a case by case basis to determine whether the potential benefits are sufficient to offset any potential costs.

(3) Tax Structure

The County may choose to issue securities on a taxable or tax-exempt basis. The Director of Finance shall evaluate the use of taxable versus tax-exempt bonds on a case by case basis to determine which structure will be most effective and beneficial.

(D) Professional Assistance

The County shall utilize the services of bond counsel on all debt financings. The County shall utilize the services of independent financial/municipal advisors when deemed appropriate by the Director of Finance. The Director of Finance shall have the authority to periodically select service providers as necessary to meet legal requirements and minimize net County debt costs. Such services, depending on the type of financing, may include financial advisory, underwriting, trustee, verification agent, escrow agent, arbitrage consulting, and special tax consulting. The goal in selecting service providers, whether through a competitive process or sole-source selection, is to achieve an appropriate balance between service and cost.

(E) Method of Sale

Except to the extent a competitive process is required by law, the Director of Finance shall be responsible for determining the appropriate manner in which to offer any securities to investors. The County has used competitive bid, negotiated sale, and private placement to sell its bonds. On a case by case basis the Director of Finance will make a determination as to the most effective method of sale.

4.7.1.5 Debt Administration

(A) Investment of Bond Proceeds

Investment of bond proceeds or other forms of debt shall be consistent with federal tax requirements, the County's Investment Policy as modified from time to time, and with requirements contained in the governing bond documents.

(B) Disclosure Practices and Arbitrage Compliance

(1) Financial Disclosure

The County is committed to full and complete primary and secondary market financial disclosure in accordance with disclosure requirements established by the Securities and Exchange Commission and the Municipal Securities Rulemaking Board, as may be amended from time to time. The County is also committed to cooperating fully with rating agencies, institutional and individual investors, other levels of government, and the general public to share clear, timely, and accurate financial information.

(2) Arbitrage Compliance

The Finance Agency shall maintain a system of record keeping and reporting to meet the arbitrage compliance requirements of federal tax law.

4.7.1.6 Compliance with Internal Control Procedures

The Finance Director 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 proceeds, complying with all laws and regulations, preventing fraud and avoiding conflict of interest.

The County shall be vigilant in ensuring that bond or other proceeds are only expended in accordance with the stated purposes at the time such debt was incurred as defined in the text of the voter-approved bond measure or other governing document. This includes maintaining records of draws on said proceeds which identify the purpose and payee of said draw.

Proceeds of debt will be held either by (a) the County, to be held and accounted for in a separate fund or account, the expenditure of which will be carefully documented by the County; or (b) by a third-party trustee or fiscal agent, which will disburse such proceeds to or upon the order of the County upon submission of one or more written requisitions by the Finance Director or designee.

The policy of the County is to comply with all federal tax and securities law which may be applicable to its debt, which may include requirements relating to arbitrage, rebate and continuing disclosure. Reviews of such requirements in connection with prior and new debt issues may be conducted by County Counsel or bond counsel. Any county personnel involved in conducting such reviews may receive periodic training regarding their responsibilities as needed.

In addition, the Finance Director 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.

4.7.2.1 Purposes for Interest Rate Risk Mitigation Products

The purposes for which the County may utilize Interest Rate Risk Mitigation Products are specified in Section 5922(a) of the California Government Code. The Director of Finance shall evaluate the use of such products on a case-by-case basis to determine whether the potential benefits are sufficient to offset any potential costs.

As required by the Government Code, no local agency may enter into any contracts or arrangements unless its governing body first determines that the contract, arrangement or program of contracts is designed to reduce the amount or duration of payment, currency, rate, spread, or similar risk or result in a lower cost of borrowing when used in combination with the issuance of bonds or enhance the relationship between risk and return with respect to the investment or program of investment in connection with, or incident to, the contract or arrangement which is to be entered into. When the Director of Finance recommends the use of such derivatives, the Director of Finance shall provide information to the County Executive and Board of Supervisors (Board) necessary to make the determination required by the Government Code.

4.7.2.2 No Speculation

Swaps will not be used for speculative purposes.

4.7.2.3 Form of Swap Agreements

To the extent possible, the swap agreements entered into by the County will contain the terms and conditions set forth in the International Swap and Derivatives Association, Inc. (ISDA) Master Agreement, including any schedules and confirmation. However, the County reserves the right to amend these terms and conditions, including the remedies and obligations, and any other section of such agreement, as appropriate to benefit the County.

4.7.2.4 Professional Assistance

The County shall utilize the services of independent financial advisors when deemed appropriate by the Director of Finance. The County shall utilize the services of bond counsel on all debt financings. The Director of Finance shall have the authority to periodically select service providers as necessary to meet legal requirements and minimize net County debt costs. Such services, depending on the type of financing, may include financial advisory, underwriting, trustee, verification agent, escrow agent, bond counsel, disclosure counsel, arbitrage consulting, and special tax consulting. The goal in selecting service providers, whether through a competitive process or negotiated sale, is to achieve an appropriate balance between service and cost.

4.7.2.5 Method of Sale

Except to the extent a competitive process is required by law, the Director of Finance shall be responsible for determining the appropriate manner in which to offer any securities to investors. The County has used competitive bid, negotiated sale, and private placement to sell its bonds. On a case-by-case basis, the Director of Finance will make a recommendation as to the most effective method of sale to the Finance and Government Operations Committee (FGOC).

4.7.2.6 Aspects of Risk Exposure

Before entering into a swap agreement, the Director of Finance will evaluate risks inherent in the transaction. The risks to be evaluated may include, but are not limited to, the following: amortization risk; basis risk; credit risk; counterparty risk; interest rate risk; rollover risk; tax event risk; and termination risk. Important consideration will be given to diversifying counterparty risk by having separate swap issuances with different counterparties as much as prudently possible.

Identification of the risks and discussion of the means, if any, employed to mitigate the risks will be contained in the Director of Finance report recommending to the County Executive and Board approval of the swap agreement.

4.7.2.7 Counterparty Credit Standards

To protect the County's interests in the event of a credit problem, the Director of Finance will recommend entering into a swap agreement with a counterparty only if it meets the following standards:

(A) At least two of the counterparty's credit ratings are rated at least "Aa3" or "AA-", or equivalent, by any two of the nationally recognized rating agencies (i.e. Moody's, Standard and Poor's, or Fitch); or

(B) The payment obligations of the counterparty are unconditionally guaranteed by an entity with such a credit rating.

4.7.2.8 Collateralization on Downgrade

In the event of a downgrade, the obligations of the counterparty will be collateralized at levels and with securities acceptable to the Director of Finance, as set forth in the swap agreements, should the rating:

(A) of the counterparty, if its payment obligations are not unconditionally guaranteed by another entity, or

(B) of the entity that unconditionally guarantees its payment obligations, if so secured, does not satisfy the requirements set forth in Section 4.7.2.7 Counterparty Credit Standards above.

4.7.2.9 Refunding

While the adopted County Debt Policy threshold for a standard refunding is 3 percent net present value (NPV) savings, the criteria for a swap structured refunding threshold will be 5 percent NPV savings to compensate for the inherent higher risk factor of a swap financing. The Director of Finance shall be responsible for determining the appropriate type of swap structure to be used in the refunding. Additionally, any swap structured refunding analysis will also take into account the percentage amount of swaps in the overall debt portfolio with the goal of having a balanced portfolio.

4.7.2.10 Debt Portfolio Distribution

Aggregate net (including offsetting reverse swaps) notional amount of all County swaps should not exceed 40 percent of the County's overall debt, assuming that the swaps have an average life of 20 years. If the life of the swaps are longer or shorter than 20 years, percentages may be adjusted accordingly, e.g. the percentage would be reduced for longer life since risk increases.

4.7.2.11 Termination

A termination payment to or from the County may be required in the event of termination of a swap agreement due to default of either the County or the counterparty, certain additional termination events or optional termination by the County. Prior to making any termination payment due to default of the counterparty, the Director of Finance will evaluate whether it is financially advantageous for the County to obtain a replacement counterparty to avoid making such termination payment.

4.7.2.12 Legality

The County shall receive appropriate legal opinion that swap agreements entered into by the County are legal, valid and binding obligations of the County.

4.7.2.13 Responsibilities

The Director of Finance is responsible for determining the appropriate uses for derivatives in conjunction with the County's debt financing and programmatic needs and making recommendations to the County Executive and the Board of Supervisors.

The Board is responsible for approving all debt issuances and approval of all official documents related to such issuance. County Counsel is responsible for approving all documents in any such issuance.

The County Controller is responsible for monitoring and reporting on all County debt obligations and reporting on such debt to the County Executive and Board. In this capacity, the County Controller will review and report on the activities and assumptions related to the various swap transactions. In addition, the Controller is responsible for reflecting the use of interest rate swap agreements and other financing transactions on the County's financial statements in accordance with Generally Accepted Accounting Principles (GAAP) and with rules promulgated by the General Accounting Standards Board (GASB).

4.7.2.14 Monitoring and Reporting

The Director of Finance will issue a report to the County Executive and Board as deemed appropriate during the term of the interest rate swap agreement. One such report that will be issued is a quarterly report on portfolio balance to the Finance and Operations Committee. Additionally, the Director of Finance will include, in an Annual Debt Report, the following information, to the extent applicable:

(A) Highlights of material changes to interest rate swap agreements including counter-party downgrades and/or terminations;

(B) A summary of new interest rate swap agreements entered into by the County since the last report;

(C) A summary of planned interest rate swap transactions and the impact of such transactions on the County;

(D) A description of each outstanding interest rate swap agreement, including a summary of its terms and conditions, the notional amount, rates, maturity, the estimated market value of each agreement, the method of procurement (competitive or negotiated), and the full name, description and credit ratings of the agreement's counterparty and, if necessary, its applicable guarantor;

(E) Amounts which were required to be paid and received, and any amounts which actually were paid and received under each outstanding interest rate swap agreement;

(F) Credit enhancement, liquidity facility or reserves associated with the swaps including an accounting of all costs and expenses incurred, whether or not in conjunction with the procurement of credit enhancement or liquidity facilities under each outstanding interest rate swap agreement; and

(G) An assessment of the counterparty risk, termination risk, and other risks associated therewith, which will include the aggregate mark-to-market value for each counterparty and relative exposure compared to other counterparties and a calculation of the County's Value at Risk for each counterparty.

This report will also include a copy of this Policy in the quarter after it is adopted or subsequently modified. The Director of Finance, with the assistance of the Counsel, and the County Controller, will periodically review this Policy for changes in best practices (i.e. GFOA Recommended Practices) and recommend modifications to this Policy to the County Executive and Board.

Related Policies

None.

Related Forms and Information

None.

History

Date	Changes Made
9/26/2017	Policy Amended. View legislative file.
1/30/2014	Policy Uploaded. (Kyle Larson)
9/26/2006	Policy Amended. View legislative file.
9/23/2003	Policy Amended. View legislative file.