

**DEBT MANAGEMENT POLICY
CITY OF GALVESTON
APRIL 2019**

Overview

The City of Galveston is authorized by federal law, Texas law and City Charter to issue long-term debt to finance the cost of public improvements over a period not to exceed the life of each improvement. The process of issuing debt, making debt payments, and reporting results is heavily regulated by state and federal law. The management of debt proceeds, including investment, appropriation, and spending is also heavily regulated and must be addressed to ensure transparency to the public, responsiveness to oversight and reporting agencies, as well as compliance with internal controls, records requirements and security for cash proceeds.

Purpose

The purpose of the City's Debt Management Policy is to establish and maintain well-defined guidelines for issuing new debt, as well as managing outstanding debt. This Policy will ensure the City sustains a strong debt management program, achieves manageable borrowing costs, and maintains the greatest flexibility to meet the City's needs.

Definitions

Long-Term debt may be issued to finance major capital improvements: i.e. to purchase facility/venue sites, to finance infrastructure improvements, construction of new facilities, significant expansions of existing facilities, extensive remodeling of existing structures and the equipping thereof. Depending upon the location of the facilities, one or more of the following options may apply:

1. **Public Improvement Bonds** – Also known as General Obligation bonds or GO's; Used for the construction, acquisition, and equipping of buildings, and the purchase of necessary sites for buildings; Public Improvement bonds (GO's) are intended to provide long-term financing for facilities payable by the City's ad valorem taxes. GO bonds issued for refunding of existing bonds (see Debt Refunding below) do not require voter approval. Authority to issue GO bonds for new projects and repay the bonds using ad valorem (property) taxes must be approved by the voters prior to issuance.
2. **Certificates of Obligation** – Certificates of Obligation (CO's) may be used to fund projects where both property taxes and revenues are pledged repayment sources for the same projects as GO bonds as well as equipment, including vehicles, computers, radios and major equipment and machinery that is not a part of a facility rebuild project. The use of CO's may occur when a credit rating upgrade will be the result of the dual pledge of revenues. Certificates of Obligation may be approved by City Council after meeting special public notice requirements under State law regarding the sale.
3. **Revenue Bonds (Senior Lien and Junior Lien)** – Capital requirements for the construction, acquisition, and equipping of projects that are supported by revenues other than property tax revenues, such as Utility System, Wharves and Terminal Revenue Bonds, or Hotel Occupancy Taxes.
4. **Self-Supporting debt** – Bonds issued with an underlying property tax pledge that are planned and administered so as pay all debt service with reliable revenues streams other than property taxes, including sales taxes, water and sewer revenue, special district assessments, tax increment reinvestment zones (TIRZs).

4. **Debt Refunding** – The refinancing and/or restructuring of existing debt is used in order to take advantage of lower interest rates and/or provide debt relief. Refunding transactions are usually considered practical if they produce a minimum amount of savings to the City.
5. **Variable Rate Bonds** – Variable rate debt is a bond issue that includes provisions by which interest rates can be adjusted after the time of sale using an agreed upon market based index at regular periodic intervals.
6. **Private Placement Loans (Bank Notes/Loans)** – Private placements are sold directly to financial institutions. These may be short-, medium- or long-term, fixed or floating rate. Private placements may be used in lieu of the preferred methods of sale for financing specific assets or programs or refunding of existing debt.
7. **Capital Lease** - A capital lease is a contract entitling a renter to the temporary use of an asset, and such a lease has the economic characteristics of asset ownership for accounting purposes. The capital lease requires a renter to book assets and liabilities associated with the lease if the rental contract meets specific requirements. In essence, a capital lease is considered a purchase of an asset, while an operating lease is handled as a true lease under generally accepted accounting principles (GAAP).

Scope

The City's Debt Management Policy applies to all debt instruments directly or indirectly issued by the City regardless of the purpose for which issued or the funding source for repayment.

1. These instruments include but are not limited to Public Improvement Bonds, Certificates of Obligation, Utility System Revenue Bonds, Hotel Occupancy Tax Revenue Bonds, Wharves and Terminal Revenue Bonds, Sales Tax Revenue Bonds, Emergency Notes, as well as,, equipment leasing where appropriate. Also included are refunding bonds of any of the above debt instruments, as well as, debt such as bank notes and loans that are privately placed with financial institutions.
2. This policy applies to all debt where such debt issuance or allocation of bond proceeds requires formal approval of City Council, requires or includes a primary or underlying pledge of city tax revenues (i.e. property, sales, franchise or hotel occupancy taxes), or might involve the city as guarantor in the event of insufficiency of revenues involved in the primary or original pledge.
3. This policy is applicable to the City and/or its component units including but not limited to:
 - a. The City of Galveston,
 - b. The Park Board,
 - c. The Industrial Development Corporation,
 - d. The Galveston Wharves,
 - e. The Galveston Port Facilities Corporation,
 - f. The Galveston Housing Finance Corporation,
 - g. The Galveston Property Finance Corporation, and, where applicable
 - h. The Galveston Island Redevelopment Authority, Tax Increment Revitalization Zones, and Public Improvement Districts.

Responsibilities

The City Manager and/or the Manager's designee will be responsible to present for approval and implement debt issuances in accordance with budgets and long-term plans approved by the City Council as well as the City Charter, State law, Federal law, and this policy.

Policy Statements

1. All bond sales will be conducted in accordance with the City Charter, State and federal law.
 - a. Article VII, Section 14 of the charter states as follows:

“**Section 14. General Obligation Bonds.** The City shall have the power to borrow money on the credit of the City and to issue general obligation bonds for permanent public improvements or for any other public purpose not prohibited by the Constitution and Laws of the State of Texas, and to issue refunding bonds to refund outstanding bonds of the City previously issued. All such bonds shall be authorized and issued in conformity with the Laws of the State of Texas.”
 - b. As required by Chapter 1331 of the State of Texas Government Code, the authority to issue tax supported bonds to construct and/or purchase permanent improvements (i.e. streets, drainage lines, buildings) shall be approved by a majority of the qualified voters of the city.
 - c. Chapter 1251 of the Government Code specifies the form of the ballot by which tax supported bonds are to be authorized and the means of publicizing the election as well as the maximum length of the repayment period, currently set at forty years;
 - d. The required bond election shall be conducted in accordance with provisions of the State of Texas Election Code: Chapter 41 (days, times and places of the election), Chapter 3 (means of ordering an election).
 - e. Refunding bonds are issued when (1) net present value savings is three percent or more of the par value of the refunded bonds as confirmed by the City’s Municipal Advisor and be based upon the same repayment schedule as the refunded bonds, or (2) the City Council approves of a restructuring of existing debt for purposes of debt relief.
2. Bond sales shall be based on specific projects:
 - a. Taken from the five-year Capital Improvements Plan (CIP) and the operating budget as approved by City Council through the annual financial planning process, generally including funds needed to cover actual scheduled contract awards, in house design and inspection costs, also considering available cash on hand;
 - b. Using funding amounts needed for specific CIP projects, including but not limited to design, engineering, site or right of way acquisition, construction, equipment and project management;
 - c. Providing funding for non-CIP projects that may be required for interlocal cooperation, public private partnerships or special districts, based on a complete project plan that includes all of the elements required for CIP projects;
 - d. Providing Certificate of Obligation sales shall be based on specific listings of vehicles, equipment and technology purchases required for City operations;
 - e. Providing Capital Leases are compared with COs to determine the most advantageous financing alternative for vehicles, equipment and technology.
 - f. Considering availability of funds to achieve a balance between adequate maintenance and operations, replacement or renewal of infrastructure, as well as, adequate future funding for debt service;
 - g. Limited by prior authorization of the voters for General Obligation bonds as required by State law and the City Charter; and
 - h. A limit on total general obligation debt payable from ad valorem taxes shall not exceed 1.5 percent of total taxable assessed valuation except in the event of an emergency requiring the use of an Emergency Note.
3. Bond sales shall be structured to:

- a. Consider all possible structures for principal and interest payments which, allow for flexibility in meeting current and future needs, efficiently utilize available debt capacity, continue to emphasize credit considerations, and match well with the useful life of the assets for which debt is incurred;
 - b. Smooth and/or restructure the City's total debt to accommodate financial administration as deemed necessary by City Council;
 - c. Provide for regular repayment of annual principal amounts and semi-annual interest amounts considering the revenue source or sources utilized to make payments, the timing of revenue receipts, and other cash flow needs financed with the same sources;
 - d. Incorporate payment schedules that provide for level payments (annual totals of principal and interest are equal throughout the life of the repayment period), level principal payments (annual principal payments are equal throughout the repayment period); a combination of the two aforementioned amortization approaches (level principal and level payments); and/or aggregation of scheduled payments over as much as a five year period for term bonds payable to bond holders but with annual payments by the bond issuer; and/or
 - e. Inclining payments or deferred principal payments for facility revenue bonds, Emergency Notes issued for disaster recovery, and or where a dedicated revenue stream has been guaranteed by a third party other than the City of Galveston.
4. Bond sales will be scheduled taking into consideration:
 - a. The need to include new property tax supported debt service payments in the subsequent fiscal year's budget through adjusting the debt service property tax rate to include new debt service payments; and
 - b. Projected cash needs for at least a twelve month period sufficient to fund planned contracts for approved and/or planned projects and equipment.
 5. Bonds may be sold by the City to achieve savings as required by the financial market and allowed by State law including:
 - a. Competitive sales where sealed bids are accepted for the purchase of all of the bonds included in a sale, and the low overall bid using an agreed upon measure of total cost is accepted by a six vote supermajority of City Council;
 - b. Negotiated sales where a group of bond underwriting firms are selected by the City, and bonds are priced using the current market, sold by each of the participating underwriting firms, with the results accepted on a preliminary basis by city officials as designated by City Council, and then accepted by a six vote supermajority of City Council; or
 - c. Parameter sales by which bonds are refunded and the City Manager is designated by City Council to pick the most advantageous day in the financial markets within a time frame, dollar amount and interest savings as approved by City Council.
 6. The City may consider issuing variable rate bonds during periods when variable short-term interest rates are historically lower than long-term fixed rates.
 - a. As a general rule, the City will adhere to the bond rating agencies' recommendation that variable rate debt not exceed 20 percent of total bonds outstanding.
 - b. The City or its component units will issue variable rate debt to lower the cost of borrowing and provide a hedge against interest rate risk.
 - c. Total variable debt will not exceed 20 percent of the City's outstanding debt for each revenue source, including that issued by its component units.
 - d. The City shall not pledge ad valorem (property) taxes for repayment of variable rate debt.

7. The City may consider issuing private placement loans (bank notes/loans) provided:
 - a. The private placement provides reasonably comparable terms, has a reasonably acceptable risk structure, and project and financing circumstances warrant,
 - b. It is understood that private placements have a variety of risks not associated with bonds, such as termination and debt acceleration risk due to force majeure (acts of God) and covenant breaches, as well as counterparty risks.
 - c. Private placements do not constitute more than 20 percent for each revenue source.

8. The City shall retain the services of professionals chosen through competitive processes to provide advice and consent on debt issuances including:
 - a. The Municipal Advisor (e.g. Financial Advisor) to:
 - Ensure that the City's bonds are issued at the lowest possible interest cost and are structured in accordance with the City's financing guidelines;
 - Assist with credit enhancements;
 - Evaluate the bids submitted and recommend that they be accepted or rejected;
 - Review draft closing documents and monitor the closing process;
 - Assist in the preparation of and submit the City's Annual Disclosure Report in accordance with SEC Rule 15c2-12; and
 - Assist in establishing repayment schedules that complement existing requirements and maintain a repayment pace acceptable to credit rating agencies.
 - b. The Bond Counsel to:
 - Certify that the City has the legal authority to issue bonds;
 - Prepare required orders, resolutions, and tax certificates;
 - Work with the U.S. Department of Justice-Voting Rights Section to obtain approval of all elections if required;
 - Work with the Attorney General to obtain approval of the bond issue;
 - Provide a legal opinion as to the enforceability and the federal income tax implications of the bonds;
 - Represent the City in negotiations related to the issuance of debt; and
 - Coordinate the closing transactions.
 - c. The Disclosure Counsel to:
 - Compile information necessary to prepare offering documents, including but not limited to the Preliminary Official Statement prior to sale, the Official Statement after sale, and all necessary disclosure documentation required by federal law;
 - Provide independent verification of the City's financial records and project information necessary to support the sale.
 - i. Paying Agent/Trustee to:
 - Authenticate the bonds;
 - Send/receive transfers of money at closing;
 - Maintain a listing of bondholders and applicable addresses;
 - Receive principal and interest payments from the City and remit to bondholders; and
 - The Trustee may represent bondholders in case of default.
 - j. Bond underwriters to:
 - Purchase negotiated or private placement debt and resell the debt to investors.

8. City issued bond proceeds shall be:
 - a. Deposited in the City's main bank account, and accounted for in the City's financial accounting system through a separate fund or funds for each sale;

- b. Invested as a part of the City's investment pool according to the City's Investment Policy as provided for by the Texas Public Funds Investment Act;
 - c. Presented for City Council appropriation on a first in/first out basis (e.g. oldest bond proceeds used first) for contracted work on eligible projects according to the general purpose named in the Official Statement for the bond sale; and
 - d. Tracked and reported in annual and quarterly budget and financial reports.
9. Debt administration by the City and its component units will include the following considerations:
- a. Designated reserves and/or unreserved fund balances will be maintained so as to cover scheduled debt service payments until dedicated revenue is available for deposit in the appropriate debt service fund for payment of the principal and interest scheduled to be paid.
 - b. The City's General Debt Service fund balance will not exceed thirteen months of debt service payments as required by the Internal Revenue Service.
 - c. Project schedules and costs provided as the basis for an individual bond sale shall be based on the CIP and will not constitute the basis for continued commitment of bond proceeds for any specific project, contract or cost past the end of a fiscal year.
 - d. Capital project funds, including bond proceeds, that are unencumbered in a contract awarded by City Council as of the end of a fiscal year must be presented for contract awards in the subsequent fiscal year by City Council as eligible CIP projects are brought forward and before new bond sales are conducted.
 - e. The Finance Director is responsible for coordinating and analyzing the debt requirements as part of the annual budget and capital improvement plan preparation. This will include timing of debt, calculation of outstanding debt, debt limitation calculations and compliance, impact on future debt burdens, and current/future revenue requirements.
 - f. The Infrastructure and Debt Service Fund may be used through the annual Budget process to provide funds for debt service payments within the parameters outlined in 5(d).
10. The City shall maintain an emergency line of credit under the provisions of the Texas Government Code section 1431 and other state law provisions as applicable:
- a. To provide emergency cash funding for operating, recovery and rebuilding costs necessitated by a federally or state declared disaster; and
 - b. Including options that allow for repayment of the emergency loan over a period of time and at such terms deemed beneficial to the City of Galveston and its residents by the Mayor and City Council.