CITY OF SEATTLE

DEBT MANAGEMENT POLICIES

Introduction

The following policies are enacted to maintain standard and rational practices for the issuance and management of debt by the City of Seattle. Their primary objective is to establish conditions for the use of debt and to create procedures and policies that minimize the City's debt service and issuance costs, retain the highest practical credit rating, and maintain full and complete financial disclosure and reporting. The policies apply to all general obligation debt issued by the City of Seattle, including leases, debt guaranteed by the City, and any other forms of obligation or indebtedness. Debt policies for revenue bonds issued by the City's utilities shall be detailed separately in utility financial policies, except as noted in this document.

Standard and up-to-date debt policies are an important tool for ensuring that the City's resources are responsibly managed. These policies are therefore guidelines for general use, and allow for exceptions in extraordinary conditions.

These policies have been approved by the Debt Management Policy Advisory Committee (DMPAC) and have been adopted by the City Council by resolution. The Debt Management Policies of the City can be adjusted at any time by resolution of the City Council following review and comment by the DMPAC and the Executive. They will be reviewed and updated as needed on a five-year cycle, with the next update scheduled for 2006.

Creditworthiness Objectives

Policy 1. **Credit Ratings:** The City of Seattle seeks to maintain the highest possible credit ratings for all categories of short- and long-term General Obligation debt that can be achieved without compromising delivery of basic City services and achievement of adopted City policy objectives.

The City recognizes that external economic, natural, or other events may from time to time affect the creditworthiness of its debt. Nevertheless, the Mayor and City Council are committed to ensuring that actions within their control are prudent and consistent with the highest standards of public financial management, and supportive of the creditworthiness objectives defined herein.

Policy 2. **Financial Disclosure:** The City is committed to full and complete financial disclosure, and to cooperating fully with rating agencies, institutional and individual investors, City departments and agencies, other levels of government, and the general public to share clear, comprehensible, and accurate financial information. The City is committed to meeting disclosure requirements on a timely and comprehensive basis.

Official statements accompanying debt issues, Comprehensive Annual Financial Reports, and continuing disclosure statements will meet (at a minimum) the standards articulated by the Municipal Standards Rulemaking Board (MSRB), the Government Accounting Standards Board (GASB), the National Federation of Municipal Analysts, the Securities and Exchange Commission (SEC), and Generally Accepted Accounting Principles (GAAP). The Department of Finance shall be responsible for ongoing disclosure to established national information repositories (NRMSRs) and for maintaining compliance with disclosure standards promulgated by state and national regulatory bodies.

Policy 3. **Capital Planning:** To enhance creditworthiness and prudent financial management, the City of Seattle is committed to systematic capital planning, intergovernmental cooperation and coordination, and long-term financial planning. Evidence of this commitment to systematic capital planning will be demonstrated through adoption and periodic adjustment of a Comprehensive Plan pursuant to the Growth Management Act and the adoption of a six-year capital improvement program (CIP).

Policy 4. **Councilmanic Debt Capacity and Reserve:** The City will keep outstanding debt within the limits prescribed by State statute and at levels consistent with its creditworthiness objectives. The City will reserve $100 million of legal limited tax (councilmanic) general obligation debt capacity, or twelve (12) percent of the total legal limit (which is one and a half (1.5) percent of total city-wide assessed value), whichever is larger, for emergencies, such as responses to major natural disasters or other significant threats to public health or safety.

Policy 5. **Net Debt Service:** The City will monitor and limit the net debt service being paid from the General Fund. "Net debt service" is defined as the total annual debt service on limited tax general obligation (councilmanic) debt minus any revenues generated by the debt-financed projects to pay this debt service. Except in emergencies, net debt service paid from the General Subfund will not exceed 9% of the total General Fund budget.[1] In the long run, the City will seek to keep net debt service at 7% or less of the General Fund budget.

Policy 6. **Annual Debt Report:** The Department of Finance shall prepare an annual report on City debt and present it to the Council at the time the Mayor submits his or her Proposed Budget. This report will describe any bond issues planned for the coming year and will describe bonds issued during the current year. The report shall also provide historical and projected information on debt, including debt capacity and debt service analyses. The report will cover all forms of City debt, including utility debt, and debt guarantees.

Purposes and Uses of Debt

Policy 7. **Capital Financing:** The City will normally rely on existing funds, project revenues, and grants from other governments to finance capital projects such as major maintenance, equipment acquisition, and small development projects. Debt may be used for capital projects only when a project generates revenues over time that are used to retire the debt, when debt is an appropriate means to achieve a fair allocation of costs between current and future

[1] For this purpose, the "General Fund budget" is the budget of the General Subfund of the General Fund and does not include the budgets of other subfunds such as the Emergency Subfund or Health Care Subfund.

beneficiaries, or in emergencies. Debt may be used for non-capital purposes only in emergencies.

Policy 8. **Asset Life:** The City will consider the use of debt for the acquisition, development, replacement, maintenance, or expansion of an asset only if it has a useful life of at least five years. Debt will not be issued for periods exceeding the useful life or average useful lives of the project or projects to be financed.

Policy 9. **Project Financing:** In general, the City expects to make a cash contribution to any project with an expected useful life of less than 10 years, rather than relying on 100% debt financing.

Policy 10. **Debt Guarantees:** The City may consider, on a case-by-case basis, the use of its debt capacity for legally allowable capital projects by public development authorities or other special purpose units of government, so long as total City debt guarantees do not exceed 15% of the City's total legal authority for non-voted general obligation debt and so long as the guarantees do not infringe on the debt capacity reserve established in Policy 4. A City guarantee of debt service coverage will be made only: (1) after the prior commitment of the full assets and resources of the development authority to debt coverage; (2) if project revenues, or development authority revenues pledged to debt service, are at least equal to debt service (average coverage of 1.0 during the term of the debt); (3) if debt service reserves are provided by the development authority's own resources and are equal to at least six months' debt service; (4) if all other viable means of financing have been examined, including, but not limited to, revenue debt, letters and lines of credit, and extension of credit by other governmental agencies; and (5) after completion of a fiscal note, as defined in the most recent Council adopted capital funding policies.

Policy 11. **Use of LTGO Debt:** Before issuing limited tax general obligation (LTGO) debt, the City will consider all other financing alternatives or funding sources, including non-debt financing. The City shall only use limited tax general obligation debt:

- under catastrophic or emergency conditions; or
- if the project to be financed is expected to generate positive net revenues after debt service. Net revenues after debt service must not only be positive over the life of the debt, but must be expected to become positive on an annual basis within the first five years after completion of the project; or
- if the debt service will be payable from a specific new revenue source, such as a voter-approved levy lid lift, which is expected to be sufficient to pay the debt service; or
- if the project is expected to significantly reduce City operating costs within the first five years; or
- if an equal or greater amount of non-City matching funds will be lost if City LTGO funds are not applied in a timely manner; or
- if the project to be financed is less than $10,000,000; or
- if the project to be financed provides essential City services or would so advance core City policy objectives that its value overrides the value of seeking voter approval.

Debt Standards and Structure

Policy 12. **Length of Debt:** Debt will be structured for the shortest period consistent with a fair allocation of costs to current and future beneficiaries or users.

Policy 13. **Debt Structure:** Debt will be structured to achieve the lowest possible net cost to the City given market conditions, the urgency of the capital project, net revenues expected from the project (if any), and the nature and type of security provided. Moreover, to the extent possible, the City will design the repayment of its overall debt so as to recapture rapidly its credit capacity for future use. The City shall strive to repay at least 18 percent of the principal amount of its total general obligation debt within five years and at least 35 percent within ten years.

Policy 14. **Backloading:** The City will seek to structure debt with level principal and interest costs over the life of the debt. "Backloading" of costs will be considered only when natural disasters or extraordinary or unanticipated external factors make the short-term cost of the debt prohibitive, when the benefits derived from the debt issuance can clearly be demonstrated to be greater in the future than in the present, when such structuring is beneficial to the City's overall amortization schedule, or when such structuring will allow debt service to more closely match project revenues during the early years of the project's operation.

Policy 15. **Variable Rate Debt:** The City may choose to issue securities that pay a rate of interest that varies according to pre-determined formula or results from a periodic remarketing of the securities, consistent with state law and covenants of pre-existing bonds, and depending on market conditions. The City will have no more than 15% of its outstanding general obligation debt in variable rate form.

Policy 16. **Second Lien Debt:** The City shall issue second lien debt only if it is financially beneficial to the City or consistent with creditworthiness objectives.

Policy 17. **Derivatives:** The City will consider the use of derivative products on a case by case basis and consistent with state statutes and financial prudence.

Policy 18. **Refundings:** Periodic reviews of all outstanding debt will be undertaken to determine refunding opportunities. Refunding will be considered (within federal tax law constraints) if and when there is a net economic benefit of the refunding or the refunding is essential in order to modernize covenants to thereby improve operations and management.

In general, advance refundings for economic savings may be undertaken when a net present value savings of at least five percent (5%) of the refunded debt can be achieved. Current refundings which produce a net present value savings of less than five percent will be considered on a case-by-case basis. When reviewing potential refunding candidates, the City may utilize the following analytical tools: net present value savings as a percent of refunded par, graduated net present value savings as a percent of refunded par, opportunity cost indexing, and refunding efficiency. Refundings with negative savings will not be considered unless there is a compelling public policy objective. When refunding an entire bond series or a large portion of a bond series, relatively small negative savings for individual maturities may be acceptable if these individual maturities are refunded together with the larger bond series or portion of a bond series, for the purpose of administrative convenience, as long as the overall refunding of the bond series or large share of the bond series meets the refunding targets.

Policy 19. **BANs:** Use of short-term borrowing, such as bond anticipation notes (BANs) and tax-exempt commercial paper, will be undertaken only if the transaction costs plus interest of the debt are less than the cost of internal financing, or available cash is insufficient to meet working capital requirements.

Policy 20. **Credit Enhancements:** Credit enhancement (letters of credit, bond insurance, etc.) may be used, but only when net debt service on the bonds is reduced by more than the costs of the enhancement.

Policy 21. **Other Facilities:** The Department of Finance shall maintain a special facility that will allow for borrowing on short notice, in the form of short-term notes, long-term bonds or internal financing, for small amounts not economical to finance through regular full bond sales. This facility may also be used as an interim financing mechanism when cost effective.

Debt Administration and Process

The following policies apply to all City debt issuance and to debt guaranteed by the City, including all General Obligation and Revenue debt (including utility debt), except where specifically noted.

Policy 22. **DMPAC:** Pursuant to Seattle Municipal Code Section 3.76, the City will maintain a Debt Management Policy Advisory Committee (DMPAC). The DMPAC consists of the City's Director of Finance, who shall be its Chair; the Chair of the City Council Finance Committee or an alternate designated by the Council President; the Superintendent of Seattle City Light or his/her designee; the Director of Seattle Public Utilities or his/her designee; and one other City official designated annually by the Mayor. The DMPAC will be advised by the City Attorney or his/her designee.

The DMPAC is authorized to provide advice to the Mayor, City Council, and Director of Finance in all matters pertaining to the incurrence of debt, including the borrowing of money. The DMPAC also has oversight of these Debt Policies, and will recommend amendments from time to time to the Mayor and City Council.

No City Department, agency, or subunit shall incur indebtedness of more than $50,000 without the approval of the DMPAC. All requests to incur indebtedness of more than $50,000 will be presented by memo from the requesting Department, through the Director of Finance, to the DMPAC. The memo shall specify the purpose of the borrowing, any options for financing the project without borrowing, and specific sources of payment of debt service. It shall include, as specified by the Director of Finance, a detailed project budget, specifying all sources and uses and a detailed project cashflow showing all project expenses and revenues, including anticipated interest earnings. The cashflow will be shown on a quarterly basis for the first two years of the project (or until the project is completed, if less than two years are required) and on an annual basis thereafter. The utilities may submit all of the standard financial tables as prepared and updated for the Official Statement in lieu of the project budget and cashflow.

The Department of Finance will recover budgeted DMPAC expenditures via the six fund allocation methodology described in Resolution 30384, or the then-most-current successor resolution to Resolution 30384. Any DMPAC expenditures incurred on behalf of an issuing agency outside of the City of Seattle (for example, Public Development Authorities) will be billed directly to the issuing agency, and will not be included in the allocated charges.

Policy 23. **Bond Sales:** After obtaining approval by the DMPAC, the requesting Department shall, in conjunction with the City's Bond Counsel, Office of the City Attorney, and Director of Finance, produce appropriate ordinance(s) and, if needed, resolutions for consideration by the City Council.

Before the sale of general obligation bonds (not revenue bonds), the requesting Department will submit a "Sources, Uses, and Payment" memo, to the Director of Finance identifying source and use of bond proceeds, Funds and/or Sub-Funds and/or other accounting units for deposit of all bond proceeds, and Funds and/or Sub-Funds and/or other accounting units for payment of debt service. No bonds or other forms of general obligation indebtedness shall be incurred by the City without submission of a "Sources, Uses, and Payment" memo.

Policy 24. **Bond Fund:** All payment of general obligation debt service shall be from the General Bond Interest and Redemption Fund (the "Bond Fund"). The Bond Fund shall act as a clearing account for debt service and will not itself be used as a final source of debt payment. The Department of Finance shall make debt service payments out of the Bond Fund by transferring the amounts from the accounts specified in the "Sources, Uses, and Payments" memo. Fund Balance in the Bond Fund should be maintained at levels that retain the Bond Fund's status as a legitimate debt service fund under IRS regulations.

Policy 25. **Accrued Interest:** Accrued interest on general obligation bonds shall be deposited into the Bond Fund and applied to pay interest on or principal of those bonds unless otherwise specified or authorized by or pursuant to an ordinance authorizing or a resolution confirming the sale of the debt issue. For purposes of this section, "accrued interest" is the interest for the period between the dated date of bonds and the settlement date.

Policy 26. **Net Premium - Unlimited Tax General Obligation Bonds:** Any net premium resulting from the sale of an unlimited tax general obligation bond issue shall be used first to pay the costs of issuance of that bond issue; and to the extent the net premium exceeds those costs of issuance, the remaining net premium shall be deposited into the Bond Fund and applied to pay interest on or principal of that bond issue unless otherwise specified or authorized by or pursuant to an ordinance authorizing or a resolution confirming the sale of the debt issue.

Policy 27. **Net Premium and Re-Sizing**: The City may re-size a bond issue at pricing in order to ensure that projects receive the appropriate amount of overall bond proceeds from the sale of limited tax general obligation bonds, if it is practical to do so. In such circumstances, net premium may be allocated to individual projects, but only to the extent necessary to provide the amount of bond proceeds designated for those projects. Any residual net premium, above what is designated for projects, will be deposited in the Bond Fund and applied to pay interest on or principal of that bond issue unless otherwise specified or authorized by or pursuant to an ordinance authorizing or a resolution confirming the sale of the debt issue.

Policy 28. **Investment of Bond Proceeds:** All general obligation and revenue bond proceeds shall be invested as part of the City's consolidated cash pool, unless otherwise specified by the bond legislation, by other ordinance, or by the lead Department or project manager and approved by the Director of Finance. Investments will be consistent with those authorized by existing city and state law and by the City's investment policies.

Policy 29. **Costs and Fees:** All costs and fees related to issuance of bonds will be paid out of bond proceeds or by the project lead Department.

Policy 30. **Competitive Sale:** In general, City debt will be issued through a competitive bidding process. Bids will be awarded on a true interest cost basis (TIC), providing other bidding requirements are satisfied. In the event that the City receives more than one bid with identical TICs, the tie may be broken by a flip of a coin. In instances where the City in a competitive bidding deems the bids received unsatisfactory, the Director of Finance may enter into negotiation for sale of the securities if authorized by the City Council.

Policy 31. **Negotiated Sale:** Negotiated sales of debt will be considered in those circumstances when the complexity of the issue requires specialized expertise, when a change of underwriter may result in losses (for example, changing the remarketing agent in mid-program for variable rate debt), when the negotiated sale would result in substantial savings in time or money, or when market conditions or City credit are unusually volatile or uncertain.

Policy 32: **Underwriters:** For all competitive and negotiated sales, underwriters will be required to demonstrate sufficient capitalization and experience related to the debt issuance.

Policy 33. **W/MBE Participation:** For all negotiated sales, the Director of Finance shall make affirmative efforts to ensure that all qualified parties have equal opportunities to compete and participate, consistent with City non-discrimination policies. The City shall encourage women and minority owned businesses (W/MBEs) to submit their credentials to serve as lead manager, co-senior manager, or co-manager. The City also shall encourage underwriters to include W/MBE participation in syndicates for competitive sales.

Policy 34. **Bond Counsel:** The City will retain external bond counsel for all debt issues. No debt will be issued by the City without a written opinion by bond counsel affirming that the City is authorized to issue the debt, stating that the City has met all state constitutional and statutory requirements necessary for issuance, and determining the debt's federal income tax status. Bond counsel will be selected for a term of up to four years through a competitive process administered by the City's Department of Finance. The selection process will require comprehensive municipal debt experience. Upon expiration of a four year contract, the City has the option, after a full competitive process, of signing a new contract with its existing bond counsel. Bond counsel will be encouraged to maintain a diverse work force and provide subcontracting opportunities to women and minority owned businesses.

Policy 35. **Underwriter's Counsel:** City payments for underwriter's counsel will be authorized for negotiated sales by the Department of Finance on a case by case basis depending on the nature and complexity of the transaction and the needs expressed by the underwriters.

Policy 36: **Financial Advisor:** The City will retain an external financial advisor, to be selected for a term of up to four years, through a competitive process administered by the City's Department of Finance. The utilization of the financial advisor for particular bond sales will be at the discretion of the Director of Finance on a case by case basis and pursuant to the financial advisory services contract. The selection process for financial advisors will require comprehensive municipal debt experience and experience with diverse financial structuring requirements and pricing of municipal securities. Upon expiration of a four year contract, the City has the option, after a full competitive process, of signing a new contract with the existing financial advisor. For each City bond sale the financial advisor will provide the City with information on pricing and underwriting fees for comparable sales by other issuers. The Financial Advisor will be encouraged to maintain a diverse work force and provide subcontracting opportunities to women and minority owned businesses.

Policy 37. **Fiscal Agents:** The Department of Finance will utilize a fiscal agent on all City indebtedness.

Policy 38. **Compensation for Services:** Compensation for bond counsel, underwriter's counsel, financial advisors, and other financial services will be as low as possible, given desired qualification levels, and consistent with industry standards.

Policy 39. **RFP Process:** The Director of Finance shall make all final determinations of selection for underwriters, bond counsel, and financial advisors. The determination will be made following an independent review of competitive bids or responses to requests for proposals (RFPs) or requests for qualifications (RFQs). The bids and responses to RFPs and RFQs will be reviewed by at least three City financial professionals. All underwriter bids will also be reviewed by the City's financial advisors.

Policy 40: **Other Service Providers:** The Director of Finance shall have the authority to periodically select other service providers (e.g., escrow agents, verification agents, trustees, arbitrage consultants, etc.) as necessary to meet legal requirements and minimize net City debt costs. These services can include debt restructuring services and security or escrow purchases. The Director of Finance may select firm(s) to provide such financial services related to debt without a RFP or RFQ, consistent with City and State legal requirements.

Policy 41. **Arbitrage Compliance:** The Director of Finance shall maintain a system of record keeping and reporting to meet the arbitrage rebate compliance requirements of federal tax code.

Policy 42. **Financing Proposals:** Any capital financing proposal to a City Division, Agency, or Utility involving pledge or other extension of the City's credit through sale of securities, execution of loans or leases, marketing guarantees, or otherwise involving directly or indirectly the lending or pledging of the City's credit, shall be referred to the Director of Finance for review.

Policy 43. **LIDs*:*** The Director of Finance shall issue notes, interfund certificates, or other financial instruments as necessary to finance Local Improvement Districts (LIDs) as authorized by the City Council.