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The California Debt and Investment Advisory Commission (CDIAC) developed this handbook to be used as an accompanying guide to the *California Debt Issuance Primer (Primer)*. This guide will provide a starting point and “quick reference guide” to many of the general questions that arise in the issuance of debt in California, and should be used in conjunction with the Primer for comprehensive answers to your inquiries.

This handbook is structured to provide a general overview of each major area included in the Primer along with identifying specific sections within the Primer that will provide comprehensive answers on the selected subject matters.

It presents information on the following:

- Key elements of the market and structure of municipal bonds,
- Roles and responsibilities of bond market participants,
- Basics of how a bond issue is structured,
- Types of financing instruments available,
- Steps necessary to sell your bonds, and
- State and federal regulations and tax laws affecting debt.
Municipal bonds represent a promise by state or local agencies or other qualified issuers to repay to investors an amount of money borrowed, called the principal, along with interest according to a fixed payment schedule. Municipal bonds generally are repaid, or mature, anywhere from one to 40 years from the date they are issued.

THE MARKET FOR MUNICIPAL BONDS

Bonds are utilized to finance a wide variety of projects in addition to satisfying ongoing cash flow requirements. Projects range from streets and roads to low-income housing.

The municipal bond market consists of the primary market, which deals in newly issued bonds and the secondary market, where securities are bought, sold, and traded after they have been issued. There were approximately $2 trillion dollars in municipal bonds outstanding in the U.S. at year-end 2004.

The key to understanding the secondary market for municipal bonds is recognizing that it differs from other security markets. The municipal bond secondary market, unlike the corporate stock and bond markets, is not a formal market. There are no public listings of sale offerings and no institutions such as the New York Stock Exchange for these bonds to be traded. The size of the market, types of dealers and their function in the market, sources of information determining the market, and uniform regulations governing trading practices all serve to make this secondary market unique.

OVERVIEW OF CALIFORNIA’S MUNICIPAL DEBT MARKET

Debt issuance in California, as with the national market, is governed by a number of factors including the economy, public need, and the availability of funds. The following charts provide information reported to CDIAC on the major components of debt issued by public agencies in California for the year 2004.

<table>
<thead>
<tr>
<th>Debt Instrument</th>
<th>$ Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conduit revenue bond</td>
<td>$4,479</td>
</tr>
<tr>
<td>General obligation bond</td>
<td>7,228</td>
</tr>
<tr>
<td>Limited tax obligation bond</td>
<td>1,568</td>
</tr>
<tr>
<td>Other bond</td>
<td>2,948</td>
</tr>
<tr>
<td>Public enterprise revenue bond</td>
<td>6,166</td>
</tr>
<tr>
<td>Public lease revenue bond</td>
<td>927</td>
</tr>
<tr>
<td>Revenue bond (pool)</td>
<td>1,566</td>
</tr>
<tr>
<td>Sales tax revenue bond</td>
<td>416</td>
</tr>
<tr>
<td>Special assessment bond</td>
<td>439</td>
</tr>
<tr>
<td>Tax allocation bond</td>
<td>2,530</td>
</tr>
<tr>
<td>Certificates of participation/leases</td>
<td>3,303</td>
</tr>
<tr>
<td>Commercial paper</td>
<td>794</td>
</tr>
<tr>
<td>Tax and revenue anticipation notes</td>
<td>5,960</td>
</tr>
<tr>
<td>Other notes</td>
<td>266</td>
</tr>
<tr>
<td><strong>Total Local Issues</strong></td>
<td><strong>$38,590</strong></td>
</tr>
</tbody>
</table>

Source: Federal Reserve
The types and issuance of debt involves many facets—it includes both long-term and short-term debt, tax-exempt and taxable debt, as well as debt issued for the purpose of refunding existing indebtedness.

California has been a significant issuer relative to other states and continues to be a prime contributor to the growth in U.S. municipal debt markets. Total California debt issuance, including state and local agencies, normally ranges between $40-50 billion annually, but has risen sharply over the three years ending prior to 2004. The following chart describes issuance over the prior 10-year period.

**California Local Government Debt Issuance by Agency 2004**

<table>
<thead>
<tr>
<th>Government Type</th>
<th>$ Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>County Government</td>
<td>$4,684</td>
</tr>
<tr>
<td>City Government</td>
<td>5,046</td>
</tr>
<tr>
<td>City and County Government</td>
<td>442</td>
</tr>
<tr>
<td>Joint Powers Authorities</td>
<td>9,600</td>
</tr>
<tr>
<td>K-12 School Districts</td>
<td>7,874</td>
</tr>
<tr>
<td>Other</td>
<td>10,944</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$38,590</strong></td>
</tr>
</tbody>
</table>

California law allows for both competitive bidding and negotiated sale in placing debt issues. Over the ten-year period from 1994-2004, an average of 70 percent of the issues have been sold through negotiated sale.

**California Local Government Debt Issuance by Project 2004**

<table>
<thead>
<tr>
<th>Project Type</th>
<th>$ Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Improvement and Public Works</td>
<td>$13,119</td>
</tr>
<tr>
<td>Education</td>
<td>8,021</td>
</tr>
<tr>
<td>Hospital and Health Care Facilities</td>
<td>2,777</td>
</tr>
<tr>
<td>Housing</td>
<td>2,316</td>
</tr>
<tr>
<td>Interim Financing</td>
<td>6,828</td>
</tr>
<tr>
<td>Redevelopment/Multiple Purposes</td>
<td>2,858</td>
</tr>
<tr>
<td>Other</td>
<td>2,671</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$38,590</strong></td>
</tr>
</tbody>
</table>

**KEY TERMS RELATING TO MUNICIPAL BONDS**

Municipal bonds have certain key components that are described below.

**Principal.** Debt instruments typically have a “principal” component. Principal is the total amount borrowed and owed. The term principal is also referred to as the face or par value of the debt investment. Interest typically accrues based on the principal.

**Interest.** A key characteristic of a debt instrument is that it bears interest on the outstanding principal amount; the “interest” component is compensation by the debtor to the lender for the use of money for a period of time. Interest is calculated as a percentage of the principal amount borrowed over the time period of the financing. The basis of calculating is routinely a defined term of days such as a 360 day year with 30 days per month (30/360) or a 365 day year with actual days per month (actual/365).

**Maturity.** A key characteristic of a debt instrument is that principal is typically payable by a certain date. The term “maturity” means the date that the stated principal amount or face amount of the debt issuance becomes due and payable to the lender. Principal also may “mature” on multiple dates, such as with serial bond issues.
**Face Value/Par Value.** The face value, also known as the par value, is the amount of money a bondholder will receive back once a bond matures. A newly issued bond usually sells at par value. The par value is NOT the price of the bond. A bond's price fluctuates throughout its life in response to a number of variables. When a bond's price trades above the face value it is said to be selling at a premium. When a bond sells below face value, it is said to be selling at a discount.

**Denomination.** Denomination means the minimum increments by which debt investments may be sold to investors. Minimum denominations may be used for investor and seller convenience. They are also used to limit the types of entities that may be potential purchasers by limiting minimum denominations to those that would typically be purchased by “institutional investors.” Most municipal bonds are sold to investors in denominations of $5,000.

**Yield.** Yield is the annual interest rate paid by a bond, expressed as a percentage of its current market price. Yield calculations are expressed in a variety of ways depending on the investor's analytical needs. There is an inverse relationship between the yield and the price on municipal bonds. As interest rates rise, fixed income municipal bonds become less desirable and lose value, and as interest rates decline, they become more valuable. This is important to the issuer, as it dictates the cost of money at different times within the economic cycle and must be a consideration in project and debt issuance planning.

See Chapter – 1 “Credit Rating Agencies” for a complete description of the rating process.

**Bond Rating.** Municipal bond credit ratings measure the issuer's risk of paying all interest and principal back to investors. A bond rating system helps investors distinguish a company's credit risk. Municipal issuers rely on specialized rating agencies to determine the overall risk of the issue and assign a “grade” to the bond. The three major rating agencies are Moody's Investor Services, Standard and Poor's, and Fitch Ratings. Ratings have a significant affect on both the ability of the issuer to raise funds and the price the issuer will be required to pay. Investors seek high quality issues, while lower quality issues are harder to place, at a much higher interest cost.

**Bond Insurance.** Insurance may be purchased by the issuer from a bond insurer pursuant to which the insurer promises to make scheduled payments of interest, principal and the mandatory sinking fund on an issue if the issuer fails to make timely payments. When an issue is insured, the investor relies upon the creditworthiness of the insurer rather than the issuer.

**Refunding.** Generally, the purpose of a refunding is either to reduce the interest rate paid on the outstanding bonds or to remove or replace a restrictive covenant imposed by the terms of the refunded bonds. The proceeds of the refunding bonds are either deposited in escrow to pay the refunded bonds when subsequently due or applied immediately to the payment of the refunded bonds.


A detailed review of yields and the time value of money are available in Chapter 7 under “Capital Market Considerations.”
SOURCES OF INFORMATION

A significant amount of bond issuance information is available for municipal issuers. Information provided by financial institutions, government organizations, trade groups, educators, along with state and local oversight agencies is available through traditional published and electronic Internet sources. The following sources contribute significantly to the understanding of issues related to markets, credit ratings, oversight, and current trends in the industry.

<table>
<thead>
<tr>
<th>ORGANIZATION</th>
<th>PURPOSE</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Bond Market Association®</td>
<td>The main trade association representing firms involved in the debt markets.</td>
</tr>
<tr>
<td><a href="http://www.bondmarkets.com/">http://www.bondmarkets.com/</a></td>
<td></td>
</tr>
<tr>
<td>The Bond Buyer</td>
<td>The daily newspaper serving the municipal bond industry.</td>
</tr>
<tr>
<td><a href="http://www.bondbuyer.com/">http://www.bondbuyer.com/</a></td>
<td></td>
</tr>
<tr>
<td>The Government Finance Officers Association (GFOA)</td>
<td>Principal professional association of state and local finance officers in the United States.</td>
</tr>
<tr>
<td><a href="http://www.gfoa.org/">http://www.gfoa.org/</a></td>
<td></td>
</tr>
<tr>
<td>Fitch Ratings</td>
<td>The three largest nationally recognized credit rating agencies utilized as sources for credit ratings, research and risk analysis.</td>
</tr>
<tr>
<td><a href="http://www.fitchratings.com/">http://www.fitchratings.com/</a></td>
<td></td>
</tr>
<tr>
<td>Moody's Investor Services</td>
<td></td>
</tr>
<tr>
<td><a href="http://www.moodys.com/">http://www.moodys.com/</a></td>
<td></td>
</tr>
<tr>
<td>Standard and Poor's</td>
<td>Makes rules and regulations, along with setting standards for all municipal securities dealers.</td>
</tr>
<tr>
<td><a href="http://www.standardandpoors.com/">http://www.standardandpoors.com/</a></td>
<td></td>
</tr>
<tr>
<td>The Municipal Securities Rulemaking Board (MSRB)</td>
<td>Establishes and improves standards of state and local governmental accounting and financial reporting.</td>
</tr>
<tr>
<td><a href="http://www.msrb.org/">http://www.msrb.org/</a></td>
<td></td>
</tr>
<tr>
<td>The Governmental Accounting Standards (GASB) Board</td>
<td>Provides information, education, and technical assistance on debt issuance and public fund investment to local agencies.</td>
</tr>
<tr>
<td><a href="http://www.gasb.org/">http://www.gasb.org/</a></td>
<td></td>
</tr>
<tr>
<td>California Debt and Investment Advisory Commission</td>
<td>Provides information and technical assistance on tax law and requirements.</td>
</tr>
<tr>
<td><a href="http://www.treasurer.ca.gov/cdiac">http://www.treasurer.ca.gov/cdiac</a></td>
<td></td>
</tr>
<tr>
<td>Internal Revenue Service</td>
<td></td>
</tr>
<tr>
<td><a href="http://www.irs.gov/">http://www.irs.gov/</a></td>
<td></td>
</tr>
<tr>
<td>Securities and Exchange Commission</td>
<td>Oversees securities markets, including stock exchanges, broker-dealers, investment advisors, and mutual funds companies.</td>
</tr>
<tr>
<td><a href="http://www.sec.gov/">http://www.sec.gov/</a></td>
<td></td>
</tr>
</tbody>
</table>
The coordinated efforts of a specialized group of professionals all working in concert is required to successfully issue debt. This section provides an overview of the participants and their roles.

Please refer to Chapter 1 – “Roles and Responsibilities of Principal Participants.”

**ISSUER**
The tax-exempt status of the municipal issuer distinguishes them from other issuers of debt. A municipal debt issuer can be any entity authorized by the Internal Revenue Service (IRS) to issue tax-exempt securities. IRS code defines tax-exempt municipal issuers in a variety of ways, but the main types of municipal issuers are states, counties, cities, and school districts. In addition to these typical government units, there is a category of entities classified as “special districts”. A special district is a limited-purpose government unit with the authority to tax and includes, among others, water districts, sanitation districts, and community facilities districts.

**INVESTOR**
Three classes of investors dominate the municipal marketplace: (1) households, consisting of individuals acting directly or through investment counsel; (2) mutual funds typically classified as closed-ended funds, open-ended mutual funds, and money market funds, and (3) financial institutions (primarily commercial banks and property/casualty insurance companies). The investment market for municipal bonds is one of the world’s largest securities markets with approximately $2 trillion worth of municipal bonds in the hands of investors. There are more than 50,000 state and local entities that issue municipal securities comprising approximately two million separate bond issues outstanding. The principal characteristic of all buyers of municipal bonds is that they are in a sufficiently high tax bracket that they can benefit from the tax exemption.

**BOND COUNSEL**
Bond counsel is the attorney, firm of attorneys, or group of firms that give the legal opinion delivered with the bonds confirming that the bonds are valid and binding obligations of the issuer and that interest on the bonds is exempt from federal and state income taxes.

**DISCLOSURE COUNSEL**
Disclosure counsel is the attorney or law firm retained by the issuer to provide advice on issuer disclosure obligations and to prepare the official statement and continuing disclosure agreement.

**FINANCIAL ADVISOR**
A financial advisor is a professional consultant retained to advise and assist the issuer in formulating and/or executing a debt-financing plan to accomplish the public purposes chosen by the issuer. The role of or necessity for the financial advisor may depend upon the financial sophistication of the issuer and its staff, the workload capacity of the issuer’s staff and the division of labor among the staff and other participants in the debt financing. A financial advisor may be a consulting firm, an investment banking firm or a commercial bank.

**UNDERWRITER**
An underwriter is a firm, or group of firms, that purchases bonds directly from a bond issuer and resells them to investors. Underwriters are intermediaries between issuers and investors.
Underwriters fill the void in the marketplace by purchasing whole bond issues and then reselling them, ideally for a profit, to investors. The responsibilities and functions of the underwriter will depend primarily on whether the bonds are to be sold at competitive bid or at negotiated sale.

UNDERWRITER'S COUNSEL
Underwriter's counsel is customarily selected by the underwriter to represent the underwriter and its interests in a negotiated sale. Normally, no underwriter's counsel is retained in a competitive sale. Underwriter's counsel will customarily review, from the underwriter's perspective, the documents prepared by bond counsel, and will negotiate matters relating to those documents on behalf of the underwriter.

CREDIT RATING AGENCIES
Debt issued by governmental entities is rated to reflect the degree of risk and probability of repayment of all interest and principal to the investor. Investors use the bond ratings to determine the level of repayment risk associated with the specific issue and determine a minimum rate of return for the risk involved. If the bonds have high ratings, they are assumed to have low risk and the investor will therefore require a lower yield. Just the opposite will occur for a lower rated (riskier) bond. There are four major investment grade ratings assigned to bonds by the rating agencies – Highest (AAA/Aaa), High (AA/Aa), Above Average (A), and Medium (BBB/Baa). All long-term bonds rated below the fourth category are judged to be below investment grade (speculative grade) and are often referred to as “junk” bonds. Most financial institutions are prohibited from lending on any securities rated below (BBB/Baa).

TRUSTEE
The trustee is responsible for carrying out the administrative functions that are required under the bond documents. These functions include establishing the accounts and holding the funds relating to the debt issue, authenticating the bonds, maintaining a list of holders of the bonds, paying principal and interest on the debt, and representing the interests of the bondholders in the event of default.

CREDIT ENHANCEMENT PROVIDER
Credit enhancement provider and credit provider are terms describing any entity that guarantees or insures, in one form or another, the sufficiency of revenues to pay the bonds. The credit enhancement provider will make available, for a fee, additional security for the bonds. The credit enhancement increases the credit rating of the issue and thereby, lowers the required yield. Typical forms of credit enhancement include bond insurance and letters of credit.

INVESTMENT ADVISOR
In many cases, issuers will wish to retain an investment advisor to assist them in investing bond proceeds. Investment advisors are professionals with experience, training, and special expertise in the area of investment management.

With a few limited exceptions, investment advisors must register with the Securities and Exchange Commission (SEC) or the California Department of Corporations. However, there is no required license exam or certification for investment advisors. Investment advisors receive a fee for their service. Certain investment advisors specialize in the management of local agency funds.

NON-GOVERNMENT BORROWER
In California, various issuers are authorized to issue bonds and lend the proceeds to one or more nongovernmental borrowers to finance the development of facilities which is deemed to serve a public purpose. Such financings are often called conduit financings and the nongovernmental borrowers are often called “conduit beneficiaries”. Such facilities include, among others, single-family housing, multifamily housing, student loan programs, hospitals and other health care facilities, educational facilities, pollution control facilities, solid waste facilities, power facilities, airports, seaports, marinas, various sports facilities, and certain other types of industrial or commercial facilities.
Debt comes in many specialized forms that are tailored to the local agency’s funding needs. This chapter provides an overview of general bond structures available to the municipality.

STRUCTURING THE BOND ISSUANCE

There are many variations on the structure and security for bonds. Bonds which are general obligations are payable from general funds of the issuer. Others are limited obligations payable from only a specified source of funds. Bonds can have one maturity date or multiple maturity dates. Bonds can have a fixed interest rate or a variable interest rate. A primary consideration in any financing plan is the relationship between the term of the financing and the life of the asset being financed.

A BOND TYPICALLY SPECIFIES:
An obligation to pay a stated amount (the “principal”), at a given time (the “maturity”) with interest at a stated percent (“the rate”)

SHORT-TERM VERSUS LONG-TERM BOND ISSUANCE

Short-term borrowing is generally defined as debt maturing no later than one year after the date of its issuance. The two basic reasons for borrowing short term are to smooth out cash flows due to the timing of tax receipts and to cover start-up costs for large projects until the actual final costs are known. For example, short-term operating needs are generally financed with short-term borrowing, such as a “tax and revenue anticipation note” (TRAN), while a capital asset, such as a library building, is typically financed with a debt instrument having a longer maturity.

Long-term debt is usually defined as bonds or other obligations with maturity of 10 years or longer. Most “long-term” assets such as public buildings and major infrastructure are financed over 25 or 30 years. On the other hand, equipment, which typically has a much shorter economic useful life, is usually financed over an intermediate term of 3 to 10 years.

FIXED AND VARIABLE-RATE BONDS

FIXED-RATE BONDS

Most municipal bonds are issued as fixed-rate bonds, which means that the rate of interest to be paid is “fixed” at the time of issuance and never changes over the life of the bond.

VARIABLE-RATE BONDS

In recent years, a significant proportion of municipal bonds have been issued as variable-rate bonds, which do not have a fixed rate of interest. Instead, the interest rate is re-set periodically to match current market conditions, often daily, weekly or monthly. The re-setting can be based upon an index of interest rates, such as a U.S. Treasury Index, Bond Market Association (BMA) Index, or the London Interbank Offered Rate (LIBOR). Using this mechanism, issuers can borrow long term at lower short-term rates if the rate environment is favorable.

Key types of variable-rate bonds:

- Variable-Rate Demand Obligations (VRDO)
  A variable-rate demand obligation (VRDO) is a security for which the interest rate is reset periodically according to a specified index.
The bond's demand feature permits the bondholder to require the purchase of the bonds by the issuer or by a specified third party, either periodically, at a certain time prior to maturity, or upon the occurrence of specified events or conditions. This process is often referred to as “putting” a bond or exercising a “tender option.” Interest rates generally are based on market conditions and the length of time until the bondholder can exercise the put option. VRDOs typically have a 1-day or 7-day put option where the investor receives the par value plus accrued interest. The minimum denomination is $100,000.

Almost all VRDOs carry credit enhancement, either a Letter of Credit (LOC), or Stand-by Purchase Agreement (SBPA).

The market for VRDOs is large, with many issuers and investors. Issuers include state and local governments and municipal service providers such as water and sewer districts healthcare entities and colleges. Investors include money market funds (VRDOs qualify for purchase under SEC rule 2a-7), corporations, and high net worth individuals.

- **Auction Rate Securities (ARS)**

Auction Rate Securities (ARS) are long-term, variable-rate bonds tied to short-term interest rates. ARS have a long term nominal maturity with interest rates reset through a modified Dutch auction process, at predetermined short-term intervals, usually 7, 28, or 35 days. They trade at par and are callable at par on any interest payment date at the option of the issuer. Interest is paid at the current period based on the interest rate determined in the prior auction period. Although ARS are issued and rated as long-term bonds (20 to 30 years), they are priced and traded as short-term instruments because of the liquidity provided through the interest-rate reset mechanism.

- **Tax-exempt Commercial Paper (TXCP)**

TXCP notes are usually unsecured obligations payable from a specified source of funds. Exempt from SEC registration, TXCP generally matures in a short period of time and usually does not exist for more than 270 days. The average maturity of TXCP is between 30 and 35 days. The average investment is about $100,000, but some investors like TXCP because they are able to negotiate note amounts and maturities that fit their investment objectives and portfolio needs. Major investors in commercial paper include money market mutual funds and commercial bank trust departments. These large institutional investors often prefer the cost savings inherent in using commercial paper instead of traditional bank loans.

Although commercial paper is occasionally issued as an interest-bearing note, it typically trades at a discount to its par value. In other words, investors usually purchase TXCP below par and then receive its face value at maturity. The discount, or the difference between the purchase price and the face value of the note, is the interest received on the investment. All TXCP interest rates are quoted on a discounted basis.

One attractive feature is that TXCP notes can generate quick cash; investors pay for notes on the day notes are sold. Another attractive feature is that TXCP interest rates are typically lower than long-term fixed rates. A third attractive feature is simplicity of documentation in that TXCP notes can be sold without an Official Statement or other issuer-prepared disclosure document, although, as explained below, TXCP dealers have been pressing issuers to take responsibility for disclosure.

Dealers are generally unwilling to undertake a TXCP program unless a minimum amount (say $25 million) of notes will be outstanding. Consequently, smaller borrowers do not have access to the TXCP market and small programs are generally not cost effective.

1. A CDIAC “Issue Brief” on Auction Rate Securities is available at the CDIAC website.
In order to undertake a TXCP program, an issuer must have statutory authority to issue notes in an unlimited principal amount and sell notes in a negotiated sale.

**INTEREST RATE SWAPS AND CAPS**

*Interest rate swaps* are contracts that allow a debt issuer to “swap” the interest rate it currently pays on an outstanding debt issue. For instance, an issuer with variable-rate debt outstanding may want to lock in a fixed-rate of interest. To do this, the issuer enters into a floating-to-fixed rate swap, whereby the issuer will now pay a fixed interest rate. The counterparty to this swap is then obligated to pay a floating rate of interest as determined by some benchmark, such as LIBOR or the BMA Index. Neither the principal nor the actual interest payments change hands. Instead, the net difference between the two interest rates is determined - monthly, semiannually, or annually - and is paid by the party whose payment obligation exceeds that of the other.

A CDIAC “Issue Brief” on Interest Rate Swaps is available at the CDIAC website.

Under an *interest rate cap*, an issuer enters into a contract with a counterparty who, upon receipt of a one-time premium from the bond issuer, agrees to pay the issuer if a specified interest rate index rises above a certain percentage rate, known as the cap or strike rate. The main advantage of caps is the protection they offer against rising interest rates. They can provide an issuer the stability associated with fixed rate debt, while allowing the issuer to take advantage of the lower interest rates often associated with variable rate debt.

**SERIAL BONDS AND TERM BONDS**

There are two approaches to structuring the maturity of bonds. A *serial bond* issue consists of a series of bonds that mature in a regular pattern, usually annually over the entire life of the issue. The interest on each series is paid at regular intervals until that particular bond matures. Serial bonds allow the investor a variety of maturities to fit his or her specific needs. Usually, a single bond issue will consist of a series of bonds with different maturities.

The further away the maturity of a bond, generally the higher the risk of the investment and the higher the interest rate associated with the bond.

A *term bond* issue has a single maturity date when the entire principal will be repaid for all the bonds in the issue. A term bond is usually financed through the use of a sinking fund. A sinking fund is a fund into which the issuer makes payments so that when the maturity date of the term bond arrives there will be sufficient funds available to repay the bonds.

**CREDIT ENHANCEMENT**

Credit enhancements generally provide a source of repayment funds that may be relied upon if the primary source of repayment becomes unavailable. Common types of credit enhancement include (1) bond insurance, which insures the timely payment of scheduled principal and interest on the bonds, (2) a letter of credit, which is a standby obligation of a bank to make payments with respect to debt service on bonds if the issuer fails to do so, and (3) a liquidity facility, which is often used with variable rate issues to provide the issuer the amount necessary to purchase the bonds if the investor exercises the option to “put” the bonds back to the issuer.

**CALL PROVISIONS**

Most sizable tax-exempt bonds contain provisions that allow the issuer to redeem all or a portion of its bonds prior to maturity at specific prices. Issuers frequently want the option to refund previously issued bonds to obtain interest-rate savings in lower interest-rate environments than when the bonds were issued. On the other hand, investors normally prefer the certainty of a fixed maturity with no possibility of a call.

Callable bonds typically will carry a higher interest rate (10 to 50 basis points in the current environment) to offset the risk to the bondholders of having their investment cashed out. Often the bond includes a call protection period of five to ten years after the sale date. During this period, the bonds cannot be called. After the call protection period has expired, the issuer must decide if it is in its best interest to call the debt. Most call
provisions require the issuer to pay a call premium to compensate the investor for an early retirement of the debt. The call premium is usually 2 percent to 5 percent above the par value of a bond and will often decrease as the bond ages.

REFUNDING

A substantial amount of long-term debt issuance consists of debt issued to refund other existing outstanding debt. In simple terms, new debt is issued to pay off old debt, normally to achieve cost savings associated with lower interest rates.

A current refunding is a transaction where the outstanding bonds to be refunded are called and paid off within 90 days of the date of issuance of the refunding bonds. There is no federal limitation on the number of current refundings that an issuer may conduct. In an advance refunding, the issuer sells new bonds and places the proceeds into an escrow account. These proceeds, along with the interest earnings that result from their investment, are used to pay off the bonds at their scheduled maturity or first call date (which is more than 90 days after the date of issuance of the refunding bonds). Federal tax law generally provides that a bond issue may be advance refunded only once (although bonds issued prior to 1986 may be advance refunded twice). Issuers should believe that the savings to be generated by the advance refunding if it is done now significantly exceed the potential savings that could be generated if it is done later in a more favorable interest rate environment.

**ARBITRAGE**

Arbitrage in the municipal bond market is the difference in the interest paid on an issuer’s tax-exempt bonds and the interest earned by investing the bond proceeds in taxable securities. Proceeds from a bond issue are usually put into short-term investments until either they are spent on their intended use or, in the case of a refunding issue, used to call the original bonds. Both of these situations can generate arbitrage earnings. If interest rates on investments are below the interest rates on the bonds, then there is “negative arbitrage.” If interest rates on investments are higher than interest on the bonds, then there is “positive” arbitrage.

During the 1980s, the federal government became concerned that municipal governments were abusing their power to issue bonds by issuing bonds unnecessarily in order to try to take advantage of positive arbitrage. The 1986 Tax Reform Act put into place a variety of restrictions and regulations designed to prevent such abuse.

**A detailed discussion of federal arbitrage restrictions also is contained in Chapter 4 of the CDIAC California Public Fund Investment Primer.**
Chapter 6 presents a full description of types of instruments including legal authority and allowable projects.

Appendix E – provides a quick reference table summarizing all the instruments described in the Primer.

ASSESSMENT BONDS
Assessment bonds are repaid from taxes collected from those who benefit from the project. An assessment is any levy or charge imposed upon real property by a local agency for a special benefit conferred upon the real property from a public improvement.

Assessment bonds are issued upon the security of the assessments and are payable from either (a) scheduled installments of assessments, collected either by a direct billing to the property owner or by posting to the secured property tax roll of the county in which the real property is located or (b) proceeds of prepayments of assessments made by property owners to discharge the lien of the unpaid assessment on a specific parcel.

GENERAL OBLIGATION BONDS
General obligation (GO) bonds are bonds secured either by a pledge of the full faith and credit of the issuer and/or by a promise to levy taxes in an unlimited amount as necessary to pay debt service. The State of California’s GO bonds are full faith and credit bonds, to which the state’s general fund, rather than any particular tax revenue, is pledged.

With very few exceptions, local agencies are not authorized to issue “full faith and credit” bonds. The GO bonds of such agencies are typically payable only from ad valorem property taxes, which are required to be levied in an amount sufficient to pay interest and principal on the bonds maturing in each year.

While GO bonds typically are the least expensive debt available to a government, there are drawbacks to using GO debt in certain situations. GO bonds require voter approval, which may delay the financing of a project. If the voters do not approve the bonds, then officials must find another way to finance the project, or cancel the project outright. Furthermore, the ability to issue GO bonds may be constrained by legal debt limits for entities with such restrictions.

REVENUE BONDS
Revenue bonds are long-term debt instruments retired by specific dedicated revenues, often revenues generated by a project funded out of bond proceeds. Revenue bonds are designed to be self-supporting through user fees or other special earmarked receipts; the general taxing powers of the jurisdiction are not pledged. The debt created through the issuance of revenue bonds is to be repaid by the earnings from the operations of a revenue-producing enterprise (an enterprise revenue bond), from special taxes (a special revenue bond), or from contract leases or rental agreements (a lease revenue bond).

MARKS – ROOS BONDS
The Marks-Roos Local Bond Pooling Act of 1985 provides Joint Powers Authorities (JPAs) with broad powers to issue bonds for a wide variety of purposes. As the name of the Act implies, the law was originally enacted to facilitate local bond pooling efforts, which allowed local agencies to achieve lower costs of issuance through spreading fixed costs across a number of small issues.
**MELLO-ROOS BONDS**

The Mello-Roos Community Facilities Act of 1982 authorizes a public entity to form a Community Facilities District (a “CFD” or “district”), otherwise known as a Mello-Roos district. Once formed, the district can finance facilities and provide services. Upon approval by a two-thirds vote of the registered voters or landowners within the district, the district may issue bonds secured by the levy of special taxes. The special taxes are not assessments, and there is no requirement that the special tax be apportioned on the basis of benefit to property. A special tax levied by a district is not an ad valorem property tax, however the lien of the special taxes has the same priority as property taxes.

**PRIVATE ACTIVITY (CONDUIT) BONDS**

Private activity bonds are used either entirely or partially for private purposes and are given tax-exempt status. Section 141 of the Internal Revenue Code qualifies a bond as tax-exempt if it meets the private business test and falls within certain categories.

A bond issue is categorized as a private-activity, tax-exempt bond if it meets the following criteria; (1) more than ten percent of the proceeds of the issue are to be used in the trade or business of any person other than a governmental unit, (2) more than ten percent of the payment of principal or interest on the issue is, directly or indirectly, secured by property used in a trade or business, or derived from payments related to property used in a trade or business, or (3) the amount of the proceeds of the issue to be used to make or finance loans to persons other than governmental units exceeds the lesser of five percent of such proceeds, or $5,000,000.

**TAX AND REVENUE ANTICIPATION NOTES**

Tax and revenue anticipation notes (TRANs) are issued by public agencies to fund cash flow deficits in a fiscal year. Typically, they would be issued at the beginning of the fiscal year and mature at the end of such fiscal year. Similarly, grant anticipation notes (GANs) are issued by a public agency to cover anticipated shortfalls in project funds pending receipt of federal or state grant monies. A bond anticipation note (BAN) is a short-term debt instrument that is issued by a municipality or a state to fund the start-up costs for a project prior to the actual long-term debt issuance. At maturity, the debt is paid from the proceeds of a new bond issue.

**FINANCING LEASES AND CERTIFICATES OF PARTICIPATION (COPS)**

In a lease-purchase agreement, a government seeking to acquire an asset makes a series of lease payments that are considered installments toward the purchase of the asset. The participants in a lease-purchase agreement are (1) the lessee, which is a government, (2) the lessor, which may be a private firm, vendor, or another governmental entity, and (3) investors. Often the lessor, after arranging an agreement, will assign the rights to the lease payments to a number of investors.

Certificates of participation, (COPs), are a widely used type of lease-purchase financing mechanism. Each certificate signifies that the investor owns a proportional interest in the lease payments to be made by the governmental entity. In a typical COP transaction, the lessor assigns the lease and lease payments along with its rights and obligations to a trustee, who executes the certificates. The tax-exempt status will be passed through to the owners of the COP to whom the interest component is distributed.

**PENSION OBLIGATION BONDS**

Pension obligation bonds (POBs) are financing instruments typically used to pay some or all of the pension plan’s unfunded pension liability. In order to achieve the expected financial relief, the issuer hopes to invest the bond proceeds at a rate higher than the total cost of borrowing. POBs were originally tax-exempt borrowings. Currently, pension obligation bonds must be issued on a taxable basis because federal law restricts the use of tax-exempt proceeds for investment in higher yielding taxable securities.
California Debt Issuance Primer – Summary of Financial Instruments

<table>
<thead>
<tr>
<th>INSTRUMENT</th>
<th>ISSUER</th>
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<th>RESTRICTIONS</th>
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<tbody>
<tr>
<td><strong>DIRECT BONDS</strong></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Assessment Bonds</td>
<td>Multiple Entities (see reference table D-1-2 for listing)</td>
<td>Assessments on Property / Fees</td>
<td>Improvement Bond Act of 1911 and 1915 (see reference Table D-1-1 for list of statutes) State Constitution – Proposition 218.</td>
<td>State Constitution – Proposition 218 and Special Assessment, Investigation, Limitation and Majority Protest Act of 1931 for detailed requirements.</td>
<td>Projects must distinguish between and identify parcels being assessed and specific benefits received.</td>
</tr>
</tbody>
</table>

**Typical Projects:** Works of a “local nature”. Improvements authorized by the Bond Acts of 1911 and 1915.

**Project Examples:** Streets, roads, parks, sewer, lighting, water, drains, transportation, water, gas, electric power.

| Local Agency General Obligation Bonds | Multiple Entities (see reference Table D-2-1 for listing of special districts authorized to issue general obligation bonds) | Ad Valorem Tax | Improvement Bond Act of 1911 and 1915 (See Tables D-1-2 and D-2-1 for listings). Article XVI, Section 1B and Article XIII A Section 1(b) of the California Constitution. Cities, Counties, School districts and Special districts each have specific requirements. | Article XVI, Section 18 and Article XIII A Section 1(b) of the California Constitution. Cities (GC 43600), Counties (GC 29900), School Districts (Ed Code 15100) and Special districts (see D–2–1 for listings) each have specific requirements. | 2/3 majority approval of voters in specified area (with some exceptions). |

**Typical Projects:** Projects are classified by City, County, School District and Special District.

**Project Examples:** Schools, parks, highways, bridges, airports. (See tables in Local Agency General Obligation Bonds section for a comprehensive description of projects financed categorized (by county, city and school district).

| Mello-Roos Bonds | Community Facilities District(CFD) | Parcel Taxes | Mello-Roos Facilities Act of 1982. | See “Mello-Roos” bond section for the establishment of a CFD and approval process. | 2/3 majority voter approval of landowners in district. Must be sold using competitive bid unless negotiated bid cost is proven lower. |

**Typical Projects:** the CFD.

**Project Examples:** Local parks, recreation, open-space, schools, libraries, child care centers, water/power/gas facilities. Services such as police, fire, recreation, and park maintenance.

| Pension Obligation Bonds | Local Agencies | General Fund | Structured as refunding bonds issued pursuant to the Local Agency Refunding Law (GC Section 53580) Article XVI, Section 18. Qualify for exception of “obligations imposed by law” No 2/3 majority needed. | Resolution of issuance, validation procedures. | Must be bond issuance refunding. Cannot exceed Unfunded Accrued Actuarial Pension Liability(UAAL). |

**Typical Projects:** Refunding of UAAL.

**Project Examples:** Restricted to UAAL.
# California Debt Issuance Primer – Summary of Financial Instruments

## DIRECT BONDS

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<tr>
<th>INSTRUMENT</th>
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<th>ADMINISTRATIVE PROCEEDINGS</th>
<th>RESTRICTIONS</th>
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</thead>
<tbody>
<tr>
<td>Sales Tax Bonds</td>
<td>Special sales tax districts</td>
<td>Sales and use tax revenues</td>
<td>Revenue Bond Act of 1941. See Table D-6-1 for listing of statutory authorizations.</td>
<td>Revenue Bond Act of 1941.</td>
<td>California Constitution, Article XVI Sec 18 for issuing. Community Redevelopment Act of 1993 (AB1290) for restrictions.</td>
</tr>
</tbody>
</table>

**Typical Projects:** Transportation infrastructure.

**Project Examples:** Highway improvement, expansion, and maintenance. Public transit systems.

## Tax Allocation / Redevelopment Bonds

<table>
<thead>
<tr>
<th>INSTRUMENT</th>
<th>ISSUER</th>
<th>SECURITY</th>
<th>LEGAL AUTHORITY</th>
<th>ADMINISTRATIVE PROCEEDINGS</th>
<th>RESTRICTIONS</th>
</tr>
</thead>
</table>

**Typical Projects:** Activities that reduce or eliminate blight within a project area not expected to be improved by private or government action.

**Project Examples:** Buildings, housing, freeway interchange, sewer systems.

## Public Enterprise Revenue Bonds

<table>
<thead>
<tr>
<th>INSTRUMENT</th>
<th>ISSUER</th>
<th>SECURITY</th>
<th>LEGAL AUTHORITY</th>
<th>ADMINISTRATIVE PROCEEDINGS</th>
<th>RESTRICTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Enterprise Revenue Bonds</td>
<td>Cities, Counties, Joint Powers Authorities</td>
<td>Revenue from the enterprise</td>
<td>Revenue Bond Act of 1941. See Table D-3-1 for listing of statutory authorizations.</td>
<td>Revenue Bond Act of 1941. See Table D-3-1 for specific codes relating to issuance requirements.</td>
<td>California Constitution Article XVI Sec 16, Health and Safety Code Sections 33640,33204.</td>
</tr>
</tbody>
</table>

**Typical Projects:** Revenue producing enterprises. See “Public Enterprise Revenue Bond” section for examples.

**Project Examples:** Public buildings, stadiums, electric utilities, water and sewer treatment, airports, police stations, libraries, low-income housing, police and fire vehicles, computers.

## Public Lease Revenue Bonds

<table>
<thead>
<tr>
<th>INSTRUMENT</th>
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<th>SECURITY</th>
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<th>RESTRICTIONS</th>
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</thead>
<tbody>
<tr>
<td>Public Lease Revenue Bonds</td>
<td>Joint Powers Authorities, Non Profits, Redevelopment Agencies, Parking Authorities, Public Works Departments</td>
<td>Lease Payments</td>
<td>Instruments structured as leases, not classified as debt for purposes of debt limit and voter approval. See Table D-4-1 for codes addressing authorization for specific issuers.</td>
<td>See Table D-4-1 for codes addressing approval procedures for specific issuers.</td>
<td>Maturity cannot be longer than useful life of project. A legally enforceable lease must be created.</td>
</tr>
</tbody>
</table>

**Typical Projects:** Capital improvements to be leased by a public agency.

**Project Examples:** Stadiums, parking facilities, convention centers, school buildings, airports, entire water or sewer systems.
## Conduit Bonds

### Conduit Revenue Bonds – Economic Development
- **Issuer**: CEDFA, CPCFA, Joint Powers Authorities, Industrial Development Agencies
- **Security**: Revenue derived from project
- **Legal Authority**: Various – See Table D-B-1 for specific issuers.
- **Administrative Proceedings**: Various – See Table D-B-1 for specific issuers.
- **Restrictions**: CDLAC Volume Cap, CEDFAC Approval, CPCFA Approval.

**Typical Projects**: Small manufacturing facilities, pollution control facilities, specific narrowly defined projects.

**Project Examples**: Manufacturing, assembly fabrication, renovation or processing plants for goods or agriculture. Hazardous waste disposal and processing facilities, waste collection/treatment facilities.

### Conduit Revenue Bonds – Educational Facility
- **Issuer**: CEFA, Joint Powers Authorities, Charter Cities
- **Security**: Payments from Educational Facility
- **Legal Authority**: California Educational Facilities Act – Education Code Section 94100.
- **Restrictions**: CDLAC Volume Cap, CPPFA Approval.

**Typical Projects**: Educational facilities.

**Project Examples**: Dormitories, administration buildings, dining halls, student unions, school libraries, research facilities, student loan programs.

### Conduit Revenue Bonds – Hospital and Health Care
- **Issuer**: CHFFA, County Health Care Districts, Charter Cities, Joint Powers Authorities
- **Security**: Payments from Health Care Facility
- **Legal Authority**: California Health Care Facilities Financing Authority Act – GC Section 15430.
- **Restrictions**: TEFRA hearing required.

**Typical Projects**: Construction, renovation, expansion of health care facilities.

**Project Examples**: Acute care hospitals, psychiatric care hospitals, skilled nursing facilities, community clinics, outpatient hospitals.

### Conduit Revenue Bonds – Multifamily Housing
- **Issuer**: Cities, Counties, Joint Powers Authorities, Housing Authorities, Redevelopment Agencies (described in Table D-9-1)
- **Security**: Revenue derived from project or lending program
- **Legal Authority**: See Code Sections described in Table D-9-1.
- **Restrictions**: CDLAC Volume Cap, Various rent and income limitations.

**Typical Projects**: Financing and/or refinancing construction, renovation, rental housing developments for private developers.

**Project Examples**: Multi-family projects, including apartment buildings.

### Marks-Roos Bonds
- **Issuer**: Joint Powers Authorities
- **Security**: General Fund or revenue derived from participating local agency
- **Legal Authority**: Marks-Roos Local Bond Pooling Act of 1985 – GC Section 6584. See “Marks-Roos” bond section for complete discussion.
- **Restrictions**: CDLAC Volume Cap, Various rent and income limitations.

**Typical Projects**: Assisting local agencies with financing needs. Capital improvement bonds, bond pooling and working capital or insurance programs.

**Project Examples**: Public buildings, stadiums, electric utilities, water and sewer treatment, airports, police stations, libraries, low-income housing, mass transit, telecommunications.

### Single Family Mortgage Revenue Bonds
- **Issuer**: Cities, Counties, Joint Powers Authorities, Housing Authorities
- **Security**: Revenue from project
- **Legal Authority**: Authorized through CA Health and Safety Code. See Table D-7-1 for specific issuers.
- **Restrictions**: Authorized through CA Health and Safety Code. For codes related to issuance procedure, see table D-7-1.

**Typical Projects**: Below market loan programs for low to moderate income families, acquisition, rehabilitation and improvement of single family homes.

**Project Examples**: Purchase mortgage loans originated by one or more lenders participating in the program.
### California Debt Issuance Primer – Summary of Financial Instruments

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<tbody>
<tr>
<td><strong>LEASES</strong></td>
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<tr>
<td>Certificates of Participation / Financial Leases</td>
<td>Joint Powers Authority, Non-Profit Corporation, Leasing Company, Bank or Other Lessor</td>
<td>Rent</td>
<td>Instruments structured as lease, not classified as debt for purposes of debt limit and voter approval. See Table D-5-1 for codes addressing approval procedures for specific issuers.</td>
<td>May be used for land and depreciable property.</td>
<td></td>
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</table>

**Typical Projects:** Public buildings. Only land and depreciable property that a public agency has statutory authorization to lease.

**Project Examples:** Educational facilities; irrigation, water, sewer, police and fire facilities; transportation equipment.

<table>
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<tr>
<th>SHORT TERM DEBT /OTHER</th>
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</thead>
<tbody>
<tr>
<td>Commercial Paper</td>
<td>State, Local Agencies</td>
<td>General Fund</td>
<td>Issuer must have statutory authority to issue notes in an unlimited principal amount and sell in negotiated sale.</td>
<td>Governing body adopts resolution authorizing the issuance.</td>
<td>Denominations of $25 Million</td>
</tr>
</tbody>
</table>

**Typical Projects:** Provide short term working capital.

**Project Examples:** Operating expenses or capital project start-up costs.

| Taxes and Revenue Anticipation Notes (TRANS) | Public Agencies | General Fund | General and individual entity authorizations detailed in GC Sections 53820 thru 53859.08. | General and individual entity authorizations detailed in GC Sections 53820 thru 53859.08. | 15 month maturity, 85% of estimated uncollected taxes, income, revenue or other sources needed to repay notes. |

**Typical Projects:** Fund cash flow deficits in a fiscal year.

**Project Examples:** Provide funds to cover operating expenses (salaries, miscellaneous expenses) for a school districts


**Types of Projects:** County financing of local agency’s delinquent property taxes fines and penalties.

**Project Examples:** County acts as “bank” to local agencies and loans on delinquent property taxes and penalties.
Most local governments do not have the expertise or resources to find investors for their proposed bond offerings and will require the services of a specialized municipal securities dealer, underwriter or a syndicate of underwriters to sell the bonds for them.

The legally required procedural steps vary widely among the different types of public debt financing. For example, some types of debt require voter approval; some require approval by ordinance subject to referendum; and others may be approved by simple resolution of the governing body of the issuer. Some types of debt require action by official bodies other than the issuer; others need only be approved by the issuer.

Nevertheless, much of the process is common to virtually all types of public debt. Broadly speaking, the issuer must undertake the above steps before and after the debt is issued.

COMPETITIVE SALE VERSUS NEGOTIATED BID PROCESS

The decision of how to market municipal bonds should be based on the characteristics of the issuer, the bond issue, and the market. Governmental entities usually issue bonds through competitive bid or a negotiated sale. The goal of an issuer undertaking a bond issue should be the proper administration of the bond issue at the least possible issuance cost and interest rate. Both methods are used frequently in bringing municipal bonds to market. The overriding concern of many issuers is the minimization of interest rates and issuance costs; however, there currently is disagreement in the industry regarding which types of sale results in the lowest costs.

Competitive bidding is appropriate when the issuer is well known, good demand for the bonds is predicted, and the market is stable. A negotiated sale is more appropriate when the issuer is less known, the market instrument is complex and less well understood by investors, and/or the market is less stable.

Competitive Bid Process. In a competitive bid sale, the issuer conducts all of the tasks necessary to offer bonds for sale including structuring the maturity schedule, preparing the official statement, verifying legal documents, obtaining a bond rating, securing credit enhancement, if advantageous, and timing the sale. These tasks are normally done with the assistance of outside consultants, including a financial advisor and bond counsel. Once the issue is structured, the public sale begins with the publication of an official notice of sale that delineates the size, maturities, purpose, and structure of the proposed issue, along with instructions for submitting bids.

Underwriters submit closed bids to the issuer on the day and time designated in the official notice of sale. The bonds are awarded to the underwriter that has submitted the best bid, i.e. the lowest true interest cost bid. No structural aspects of the bonds...
are changed regardless of the success or failure of
the underwriter/underwriting syndicate to sell the
bonds. Any unsold bonds remain the responsibility
of the underwriter.

**Negotiated Sale Process.** In a negotiated sale, the
bond issue is not structured before an underwriter
is chosen. If the issuer has not retained a separate
financial advisor, the underwriter may assist the
issuer in determining what is to be financed, the
method of financing and the financing structure.
The underwriter is chosen based on expertise,
financial resources, compatibility, and experience.
After the underwriter is selected, the issuer and the
underwriter will begin the process of structuring
the bond issue and completing the other origination
tasks. The underwriter starts the marketing process
and develops an interest rate to be negotiated with
the issuer. The issuer often employs a financial
advisor not associated with the underwriting firm to
represent the issuer’s interests in the process.

### THE COSTS OF ISSUANCE

Borrowing costs money, in addition to the interest
on the amount borrowed. Additional costs include
expenses for:

- Bond Counsel Services,
- Publishing Bond Documentation,
- Determining Credit Ratings,
- Trustee/Paying Agent Services,
- Financial Advisor Consulting Fees, and
- Underwriter Commission.

The profits made by underwriters are referred to as
the spread. The spread is the difference between
the price the underwriter pays the issuer for the
bonds and the price the underwriter receives from
the resale of those bonds to investors. The spread
can be calculated by basis points. One percent of
the bond issuance equals 100 basis points. For
example, an underwriting spread of 100 basis
points or $10 per $1000 bond would equal one
percent of the principal amount of the bonds.

For both competitive and negotiated bids, the
spread is made up of four separate components: the
management fee, expenses, the underwriting fee
and the takedown.

- **The Management Fee** - The management fee
  compensates the underwriters for their efforts
  in creating and implementing the financing
  package. The amount of the management fee
  depends on the complexity of the issuance.

- **Underwriting Fee** - The underwriting fee, also
  known as the “risk” component of the spread,
  is designed to compensate the underwriter for
  the risk incurred by buying the entire issuance
  before it has received orders from investors for
  all the bonds.

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<table>
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<tr>
<th>PRIOR TO ISSUING DEBT</th>
<th>AFTER DEBT IS ISSUED AND CLOSED</th>
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<tbody>
<tr>
<td>Determine that a project or program to be financed is necessary or desirable</td>
<td>Ensure that continuing disclosure undertakings are fulfilled</td>
</tr>
<tr>
<td>Select the financing team</td>
<td>Respond to investor inquiries</td>
</tr>
<tr>
<td>Structure the financing</td>
<td>Calculate and file arbitrage rebate returns</td>
</tr>
<tr>
<td>Obtain formal approval by the governing body of the issuer and, if applicable, conduit borrower</td>
<td>Administer any assessments or special taxes securing the issue</td>
</tr>
<tr>
<td>Administering any construction or acquisition program</td>
<td>Deal with any workout-related issues</td>
</tr>
</tbody>
</table>

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A CDIAC "Issue Brief" on the Underwriter’s Spread is available at the CDIAC website.

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• **Takedown** - The takedown is usually the largest part of the underwriter’s spread. It represents the discount at which the firm or members of the syndicate buy or “take down” bonds from the overall underwriting account. The amount of the takedown depends on how difficult the bond issuance is to sell to investors.

• **Expenses** - The issuer must also reimburse the underwriter for expenses incurred during the development of the financing package and the actual sale of the bonds. The expenses portion represents the physical costs incurred in the course of the bond sale including travel, printing costs, and the underwriter’s counsel fees.

Bond counsel fees comprise the next largest portion of the costs of issuance, but are a significantly smaller portion compared to the underwriter’s spread. Other fees, such as the costs of procuring bond ratings, preparing independent financial audits, and producing disclosure documents, are less than two percent of the total costs.

Internal costs also add up. Often forgotten and uncounted are the numerous hours incurred by both the executive and the legislative bodies in initiating, analyzing, and approving the borrowing.

**THE UNDERWRITING PROCESS**

**Steps and Timetable**

The following is a general description of the steps and timetable in a typical bond issuance.

1. **Chapter 2 – “Checklist of Steps in a Debt Financing”** contains a detailed description of the steps, timeframes and participant roles in undertaking a financing.

**Step 1 – Preliminary discussion.**

In a negotiated sale, the issuer starts preliminary discussions with the underwriter, bond counsel, and underwriter’s counsel.

In a competitive sale, the issuer consults with a financial advisor to arrange the bond sale instead of an underwriter.

Bond counsel analyzes applicable local, state and federal laws to determine the extent the financing is affected and what, if any, approvals are necessary.

**Step 2 – Issuer adopts resolution stating intention to proceed with a bond financing.**

- Underwriter is chosen
- Bond counsel is employed
- Preliminary drafts of bond documentation are produced and reviewed by bond counsel and underwriter (if a negotiated sale). Credit enhancement, if any, is coordinated.

**Step 3 – Preliminary Official Statement drafted.**

- A draft of the Preliminary Official Statement (POS) is produced and adjustments to the preliminary bond documents are received from the interested parties.
- A series of revisions based on comments from the interested parties are distributed, reviewed and subsequent drafts of the basic documents are circulated. The POS is revised based on the revised documents that have been negotiated and agreed upon by the responsible parties.

**Step 4 – Public hearings.**

- After a 14-day notice, the issuer initiates a public hearing on the new financing.
- Underwriter (negotiated offering) or financial advisor (competitive sale) distributes POS to prospective investors. Issuer starts printing of bond documents and bond resolution.

**Step 5 – Approvals**

- The issuer adopts the bond resolution, in which it agrees to sell the bonds to the underwriter, approves the documents and authorizes execution of the bonds.
- The purchase agreement is signed.
- The final Official Statement (OS) is printed. Bond counsel circulates drafts of closing documents. All parties complete and assemble the remaining documents for the closing.
**Step 6 - Closing**

All documents are executed and delivered. Bond counsel delivers its opinion that the bonds are valid and the interest on them is exempt from federal income taxes. The issuer delivers the bonds to the underwriter, and the underwriter transfers money to the trustee.

**BOND ISSUE DOCUMENTS**

The following are some of the key documents in a bond issuance:

- **Bond/Trust Indenture.** The bond/trust indenture is a contract between a trustee, usually a bank, the bondholders, and the issuer. The bond/trust indenture is the most important of the bond documents and includes the form of the bonds. It establishes the security, interest rate, maturity, bondholder rights and remedies in case of a default. The issuer and the trustee each are bound by the terms of the bond/trust indenture. The issuer promises to pay principal and interest on the bonds. The trustee holds all funds under the bond/trust indenture; pays principal and interest to bondholders; and acts for the bondholders in the event of a default.

- **Official Statement.** The Official Statement (OS) contains the final terms of the bonds. Under federal securities laws, the issuer is obligated to disclose in this document all information that a “reasonable investor” would consider important in deciding whether to purchase a bond. A Preliminarily Official Statement (POS), complete except for interest rates and maturities, is used to market and pre-sell the bonds.

- **Purchase Contract.** This is the agreement between the issuer and the underwriter in which the issuer agrees to sell the bonds to the underwriter, and the underwriter agrees to purchase the bonds from the issuer at a specified purchase price, typically principal plus accrued interest from the date of the bonds to the date of closing. The purchase contract sets forth the terms and conditions under which the underwriter will purchase the bonds. These provisions include provisions for various documents and opinions to be provided by parties to the financing at the closing, including any expected bond rating.

- **Credit Enhancement Agreement.** In many financings, there may be a credit enhancement agreement that a third party insures or guarantees either the bonds or the issuer’s mortgage repayment obligation. Often there are two documents, the guaranty or insurance agreement, which runs to the trustee, and the agreement of the issuer to repay the insurer/guarantor.

- **Disclosure Agreement.** Another common document is the disclosure agreement, in which the issuer, or the borrower in a conduit financing, agrees to provide ongoing disclosure as required by Securities and Exchange Commission Rule 15c2-12.

**DISCLOSURE REQUIREMENTS**

The SEC has set forth rules that place regulatory responsibility on the underwriters to ensure that the issuers whose securities are being underwritten have fully committed to provide current and ongoing disclosure of financial details and material events that may impact their ability to meet debt service requirements. They have also given authority to the Municipal Securities Rulemaking Board (MSRB) to write rules related to the conduct of municipal securities dealers and their trading practices.

See Chapter 10 “Continuing Disclosure and Investor Relations Programs.” Additional publications and information are available on the CDIAC website, keyword: “disclosure.”

SEC Rules 10b-5 and 15c2-12 provide the general basis for municipal securities disclosure. SEC Rule 10b-5 makes it unlawful for a person to make untrue statements or omit material facts in
connection with the purchase or sale of a security. SEC Rule 15c2-12 requires two forms of disclosure: initial (or primary) and continuing (or secondary), unless an issue is exempted.

**Initial Disclosure** requires the underwriter to obtain the POS and OS from an issuer. In turn, the underwriter is required to send the POS to any potential customer until the OS is available. The OS is required to be sent to customers until 90 days after the underwriting period or, if the OS is available from a nationally recognized municipal securities information repository (NRMSIR), 25 days after the underwriting period.

**Continuing Disclosure** regulations require the underwriter to obtain a written agreement (the continuing disclosure agreement) from the issuer to provide certain information to each NRMSIR, state information depositories, or, in some cases, the Municipal Securities Rulemaking Board (MSRB). Information to be provided to the market includes, annual financial information or audited financial statements, material event notices (when applicable), and notices of failure to provide annual financial information (also when applicable).

There are 11 defined material events requiring disclosure. They include such major negative occurrences as principal and interest payment delinquencies, non-payment related defaults, unscheduled draws on debt service reserves or credit enhancements, and failure to provide annual financial information as required. There are also a variety of other events, such as bond calls, defeasances, release, substitution, or sale of property securing repayment, and rating changes that are not necessarily negative events.

Material misstatements or omission in the POS, OS, annual financial information, or event notices may be the basis for claims of securities fraud under Rule 10b-5 and other federal or state securities laws. This could result in action taken by the SEC or private plaintiffs (bondholders or other investors) with substantial potential liability for issuers or other obligated persons.
Under the Internal Revenue Code of 1986, bonds issued by states and local governmental units generally bear interest that is excluded from gross income for federal income tax purposes. Municipal bonds are taxable if the bonds do not meet the Internal Revenue Code definitions or violate various other prohibitions contained in the tax code.

Chapter 3 – “General Federal Tax Requirements” provides a comprehensive review of federal tax requirements related to municipal debt.

The term “bond” includes any evidence of indebtedness, including notes, installment sale agreements, or financing leases. Although exempt from federal income tax, interest on bonds may be taken into account in determining other federal income tax consequences, such as personal or corporate alternative minimum tax, interest expense deductions, taxation of social security benefits, etc.

In order to be tax exempt, bonds must be issued by or on behalf of a state or a political subdivision of a state. Political subdivisions are public agencies that can independently exercise a substantial amount of one or more of the following governmental powers: eminent domain, police power or taxing power.

DEFINITIONS

The following definitions are crucial to an understanding of how the tax law applies to public finance.

Bond Issue. In general, federal tax requirements apply to an “issue” of bonds rather than individual bonds. Bonds are part of the same issue if the bonds are sold at substantially the same time (i.e., less than 15 days apart), are reasonably expected to be paid from substantially the same source of funds and are sold pursuant to the same financing plan. Typically, all of the bonds that are sold pursuant to the same official statement are part of the same issue.

Bond Proceeds. Just as federal tax rules primarily apply to an issue of bonds, the application of federal tax rules requires an analysis of the investment and ultimate use of the “proceeds” of a bond issue.

Gross Proceeds. Understanding whether funds held by an issuer are “proceeds” at any given time requires an understanding of how funds related to a bond issue are treated as having been spent.

PRIVATE ACTIVITY BONDS

If a bond is a “private activity bond,” it is not tax-exempt unless it meets the requirements for one of the categories of “qualified” private activity bonds. The requirements are listed below:

Private Business Use Test
More than 10 percent of the proceeds of the issue are to be used for any private business use.

Private Payment or Security Test
The payment of principal or interest on more than 10 percent of the issue is to be secured by or derived from payments in respect of property used for a private business use.

Private Loan Test. Even if the Private Business Tests are not satisfied, an issue will nevertheless be an issue of private activity bonds if the lesser of 5 percent of the proceeds or $5 million are used to make or finance loans to persons other than governmental units.
**Volume Cap**

In general, the aggregate amount of all tax-exempt qualified private activity bonds issued by all issuers in a state may not exceed the so-called “volume cap.” The volume cap for each state is calculated annually and is equal to $50 multiplied by the population of the state (approximately $2.8 billion for California in 2005). In order to issue tax-exempt qualified private activity bonds, every issuer must apply to the California Debt Limit Allocation Committee (CDLAC) to be assigned a portion of this state ceiling.

**TEFRA Public Hearing**

The Tax and Equity Fiscal Responsibility Act of 1982 (TEFRA) hearing process is a public accountability procedure involving the legislative body of the local agency in which the proposed project is located. During such process, the legislative body conducts a public hearing providing members of the community the opportunity to speak on behalf of or against the nature and location of the proposed project to be financed with tax-exempt bonds.

**REBATE REQUIREMENT**

Generally, the tax code requires that, to the extent gross bond proceeds are invested, on an aggregate, blended basis, in non-purpose investments at a yield in excess of the bond yield, such excess, often referred to as “arbitrage earnings”, must be rebated to the federal government.

**SIMPLIFIED REBATE EXAMPLE:**

<table>
<thead>
<tr>
<th>Bond yield = 6%</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100,000 (proceeds invested at 6.5% for 5 years)</td>
</tr>
<tr>
<td>$32,500 (investment earnings)</td>
</tr>
<tr>
<td>$30,000 (bond interest)</td>
</tr>
<tr>
<td>$2,500 (rebate to federal government)</td>
</tr>
</tbody>
</table>

**Arbitrage Yield Restriction**

The tax code generally prohibits municipalities from issuing tax-exempt bonds if the issuer reasonably expects to use the proceeds of such bonds, directly or indirectly:

- To acquire securities or obligations with a yield materially higher than the yield on such bonds, or
- To replace funds used to acquire such higher yielding securities or obligations

Thus, the tax code generally restricts the rate of return on investments purchased with gross bond proceeds to a yield that is not materially higher than the yield on the bonds.

**REBATE EXCEPTIONS**

There are four important exceptions to the rebate requirement that should be carefully considered by the issuer and bond counsel when structuring a bond issue. They are the “Small Issuer Exception” which exempts small issues under $5,000,000 from the rebate requirement and three time limit exemptions the (Six Month, Eighteen Month and Two Year Expenditure Exceptions), which allow for an exemption if the proceeds are spent within certain time constraints.

**FAIR MARKET VALUE RULES**

One fundamental requirement of all yield related limitations (e.g., the arbitrage yield restriction and the rebate requirement) is that non-purpose investments must be purchased by issuers at a fair market value. Without this fair market value requirement, issuers could simply direct excess profits paid to the federal government to entities other than the United States. The process of purchasing investments at an inflated price, known as “yield burning,” has received significant attention and enforcement efforts from federal authorities.

**HEDGE BOND RESTRICTIONS**

The tax code generally prohibits tax-exempt bonds from being issued far in advance of the time money is required to construct or acquire the assets to be financed. In general, bonds will be considered
“hedge bonds” and will not be tax-exempt unless the issuer reasonably expects either to spend a minimum percent of the proceeds during a defined period of time.

REFUNDING BONDS/ADVANCE REFUNDING BONDS

Refunding bonds are bonds that refinance currently outstanding issues. Refunding bonds often involve complex federal tax issues and invoke a number of very technical requirements. In general, issuers are limited to only one advance refunding of any particular bond issue. This is one of the main reasons that issuer’s should be concerned about the total savings they are receiving in a refunding. For bonds originally issued prior to January 1, 1986, an issuer gets up to two advance refundings, and for this purpose, all advance refundings issued prior to March 15, 1986 are counted as one. There are no limitations on the number of current refundings. In general, qualified private activity bonds may not be advance refunded at all.

FOR FEDERAL TAX PURPOSES, THERE ARE TWO IMPORTANT CATEGORIES OF REFUNDING BONDS:

- **Advance Refunding** – bonds issued more than 90 days before the bonds being refunded will be retired
- **Current Refunding** – bonds issued within 90 days of the date the bonds being refunded will be retired

ARBITRAGE YIELD RESTRICTION

When a municipality issues advance refunding bonds to refinance a current issue, the proceeds of the refinancing held in escrow are prohibited from being invested at a yield that exceeds the yield on the new advance refunding bonds. Often, however, the yield of investments purchased in the open market at fair market value will exceed the yield of the advance refunding bonds because the investments are typically taxable, while the advance refunding bonds are tax-exempt. As mentioned earlier, tax-exempt yields have a competitive advantage over taxable yields.

LIMITATION ON REFUNDING NON-CALLABLE BONDS

In an advance refunding, federal tax law generally does not permit refunding any portion of the issue being refunded which is not callable prior to maturity. This is because, except for savings resulting from exploiting the difference between taxable and tax-exempt interest rates, there can be no economic savings from refunding non-callable bonds, since the higher rate of interest they bear will have to be paid to their full maturity.

FIRST CALL DATE RULE

For advance refundings issued for the purpose of debt service savings, the refunded bonds must be paid off with the proceeds of the refunding bonds no later than the first date that they may be redeemed at the option of the issuer. The policy behind this rule is to have tax-exempt bonds (in this case the refunded bonds) in the market for the least amount of time possible.
CONSIDERATIONS FOR THE INVESTMENT OF PUBLIC FUNDS

The fundamental considerations for the investment of public funds are safety, liquidity and yield.

SAFETY

Preservation of principal (or safety) is the first and most important consideration of public investment. Public agencies address the safety consideration through the implementation of an investment program that controls exposure to many risks, including risk of principal loss through excess exposure to market or credit risk. The public investment program must provide for third party custody of the agency’s assets to avoid the possibility of principal loss through theft or collusion, and must avoid strategies that may provide higher yield, but hold risk that is inappropriate for the public agency.

In the context of public fund investment, safety relates to preserving the principal of an investment in an investment portfolio; local agencies address the concerns of safety by controlling exposure to risks.

Interest Rate Risk (Market Risk)

Interest rate risk, also known as market risk, means the potential risk that the value of securities will decline as the general level of interest rates rises. For example, given a fixed coupon rate, the value (price) of an investment is inversely related to interest rates. As interest rates rise, price falls.

Credit Risk

Credit risk means the risk that the financial performance or status of an issuer will fall during the time a security remains outstanding. In the context of a debt security, credit risk means the possibility that the issuer will be unable to make scheduled payments of principal and interest. A more common concern for investors is that the market’s perception of an issuer’s credit will cause the market value of a security to decline, even if default is not expected.

LIQUIDITY

The second consideration of public fund investment (after safety concerns are addressed) is liquidity. Public agencies invest funds that are intended to meet their ongoing demands for cash for operations and capital spending. One of the agency’s objectives must be to structure a portfolio that ensures adequate cash flow to meet both anticipated and unanticipated expenditures when needed. Beyond projected cash flow needs, the agency must be prepared for the unexpected, such as when actual revenues fall short of projections due to a weakening economy. The agency can meet this need with additional short-term investments or securities that can readily be sold without the risk of a significant loss of principal risk to meet unexpected cash flow needs.

In the context of public fund investing, liquidity can have different meanings. Liquidity can mean the measure of the ability to convert an instrument to cash on a given date. Another definition of liquidity is the ability of an agency to pay its expenditures with cash equivalent investments, or with investments that mature on the date cash is needed.
YIELD
The third consideration of public fund investment (after safety and liquidity needs are met) is yield. Investment income and portfolio growth are important to public agencies to provide necessary funds for budgetary purposes. With preservation of principal and liquidity accounted for, public agencies must seek reasonable rates of return on their investments.

Yield is a measure that describes the income from a security as a percentage of the value of the security. Yield calculations are complex for securities that have more than one interest payment, and are quite difficult to calculate manually. There are many different variations on the definition including:

**Yield to Maturity.** Yield to maturity means the constant discount (interest) rate that makes the net present value of future principal and interest cash flows equal the current market price of the security. On the initial purchase date, yield to maturity at cost and yield to maturity at market will be identical since cost is equal to market value on the purchase date. After the initial purchase date, the yield to maturity at market reflects current market conditions, and may be higher or lower than the yield to maturity at cost.

**Yield to Call.** Yield to call means the constant discount (interest) rate that makes the net present value of future principal and interest cash flows equal the cost or market value of the security at the first call date; this yield is valid only if the security is called.

**Current Yield.** Current yield means the annual income of a security divided by its market value.

THE SPECTRUM OF AVAILABLE INVESTMENTS
There are three major classes (and many sub-categories) of financial products available for the investment of bond proceeds:

**Individual Securities or a Structured Portfolio Comprised of Individual Securities.** Generally, these securities are limited to direct obligations of the United States Treasury, obligations of federal agencies that are directly or indirectly guaranteed by the United States, and debt obligations of other entities, including corporate, for profit entities, that are of exceedingly high credit quality and relatively short duration. It is important to remember, however, that while these securities generally contain little credit risk, they can be subject to substantial market value volatility if purchased with an inappropriately long remaining time period to maturity.

In addition, in most circumstances “equity” or stock investments are prohibited for municipal issuers under Article XVI, Section 6 of the California Constitution.

As with the other financial products available as investment alternatives, individual securities work better or worse according to the fund in which they are contained and other circumstance specific factors. However, combining several types of securities with varying maturity and interest payment dates can often provide almost perfect credit safety with minimal liquidity risk and adequate yield performance.

**Mutual, or Pooled, Investment Funds.** Pooled investment funds available for local agency bond proceeds include commercial, for-profit mutual funds and public sector, not-for-profit pools. Both types of pooled investment funds attempt to leverage economies of scale in professional management, purchasing power, transaction costs, credit risk diversification, and liquidity requirements to improve upon what a smaller or less experienced investor could accomplish through individual securities purchases.

POOLED INVESTMENT PROVIDERS
Local Agency Investment Fund (LAIF)
County Treasurer Pooled Investment Funds
JPA pooled programs
Bond insurer-sponsored pools
Bank-sponsored pools
Pooled investment funds sponsored or managed by counties, large cities, and the State Treasurer's Office have widely varying characteristics. While they often offer an administratively simple option for smaller local agencies, it is important to understand the credit, liquidity and yield characteristics of each fund. Because these funds are not highly regulated, their managers may have very different philosophies which impact net asset value, liquidity, and, ultimately, safety. Before investing in such pools, local agencies should study the type and average life of underlying investments and fully understand deposit, withdrawal, interest payment, and interest allocation provisions. There are many types of pooled investment programs available (see box). Local agencies should not assume that a pooled investment fund is managed in a manner consistent with the local agency’s specific investment policies simply because it is sponsored by a larger, more sophisticated public agency.

**Investment Agreements.** An investment agreement (IA) is a contract providing for the lending of issuer funds to a financial institution, which agrees to repay the funds with interest under predetermined specifications. Under favorable market conditions, IAs can offer a fixed interest rate in excess of otherwise appropriate individual securities, daily or otherwise appropriate liquidity, virtual elimination of reinvestment risk and administrative and brokerage costs, and high credit quality.

**Security Provisions.** Because an investment agreement is essentially a promise to repay funds at specified times and rates of interest, the single most important consideration with respect to purchasing an IA is the provider's ability to make good on these promises. Most IA providers, especially those qualifying under the permitted investments section of a bond indenture, are insurance companies, banks, or primary U.S. government securities dealers with repayment ability for both short-term and long-term obligations that are rated by firms such as Moody's Investor Services, Standard & Poor's or Fitch Ratings.

**Providers.** Insurance Companies were among the first institutions to make IAs available for bond proceeds investment. Often referred to as guaranteed investment contracts (GICs), these securities are typically “guaranteed” only by the repayment ability of the insurance company. Banks sell bank investment contracts (BICs) can be thought of as a flexible series of CDs. They may or may not be collateralized and are typically issued only by the largest and most creditworthy banking institutions.

**PROCEEDS AVAILABLE FOR INVESTMENT**

Typically, proceeds, which are to be used for distinctly different purposes, are segregated into separate accounts, or funds, for financial, accounting and general administrative purposes. The required amount deposited at issuance in any particular fund is usually less than the total costs expected to be paid from that fund. The remaining expenditure requirements are expected to be met by investment earnings realized in the fund.

**A Project or Construction Fund** generally receives the lion’s share of bond proceeds deposits in all but refunding transactions. As the names suggest, monies in these funds are used to pay primary project costs such as land and equipment acquisitions, architectural and other planning costs, site preparation, and construction costs.

**A Debt Service Reserve Fund (DSRF)** is common in the municipal market for all but general obligation bonds, variable rate obligations secured by a direct pay letter of credit, and obligations which utilize a surety instrument (a form of insurance policy). DSRFs are designed to address temporary financial difficulties on the part of the obligor and, consequently, usually contain amounts equal to maximum annual debt service.

**The Capitalized Interest Fund** that is the primary source of repayment to bond holders when revenues from income generating project will not be available until some time after project construction is completed. A common solution is to borrow as part of the original financing an amount
that, together with interest earnings thereon, will be sufficient to pay interest during the construction phase.

**Refunding Escrow Funds** are designed to pay debt service on prior obligations that cannot be redeemed immediately. Because most municipal issues are not subject to voluntary redemption, or “call,” by the issuer prior to an agreed upon number of years (usually 10) from the issue date, refunding escrows are necessary to take advantage of interest rate reductions and to otherwise effectuate a refinancing of “call protected” obligations. Refunding escrows are also subject to especially complex and restrictive federal tax law limitations. For all of these reasons, they are almost always structured by professional investment bankers, financial advisors, and tax lawyers and then verified for tax law compliance and cash flow sufficiency by an independent certified public accountant.

**A Debt Service Fund (DSF)** is typically composed of interest, principal and/or redemption accounts, and is intended to facilitate proper matching of revenues and debt service obligations. DSFs are usually required to be funded in advance of actual principal and interest payment dates - typically on a monthly basis. The predictability of when monies will be needed to make debt service payments suggests that issuers purchase, or instruct their trustee to purchase, securities with DSF deposits that mature on or about the debt service requirement date.

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CDIAC’s *California Public Fund Investment Primer* provides an all-inclusive review of information pertinent to the investment of bond proceeds.
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