WEBINAR TRANSCRIPT

Principles and Practices of Debt Management: Employing a Debt Policy
October 22, 2014

(Editor's Note: This transcript has been prepared by the California Debt and Investment Advisory Commission (CDIAC) and it believes it to be a fair and accurate reproduction of the comments of the speakers. Any errors are those of CDIAC and not the speakers.)

A debt management policy can assist a public agency to make decisions as well as support its efforts to identify conflicts, inconsistencies, and gaps in the agency's approach to project finance and debt management. Policies are also instrumental in setting a proper balance between limits on the use of debt financing and providing sufficient flexibility to respond to unforeseen circumstances and opportunities. This webinar addresses the importance of establishing a debt policy and highlights best practices for developing and maintaining a debt management policy.

Title Slide – Principles and Practices of Debt Management: Employing a Debt Policy

MARK CAMPBELL: Good morning, everyone. This is Mark Campbell, the executive director of CDIAC. I want to welcome you to this morning's webinar, Principles and Practices of Debt Management: Employing a Debt Policy. Our program today runs to 11:45 AM. Hopefully, you will have the opportunity to sit through it. We've got some great speakers speaking on a topic that we wholeheartedly believe needs to be communicated to the issuer community in the State of California. This program is in part generated by research CDIAC carried out, and we've got a speaker addressing that, but it recognizes within CDIAC, the merge – intersection between two program areas, our education and research. But certainly we undertook the research knowing how important debt policies are in the issuance process. And this seminar follows on with guidance and a discussion about the importance and purpose of debt policies in the issuers' procedures and practices.

I'm going to take a minute to cover some of the administrative issues. Your slides should recognize the fact that there are presentation slides available at the CDIAC website. MCLE credits are available to those who wish to receive those. You will email cdiac_education@treasurer.ca.gov and we will get that process set up. Finally, live captioning is available at the URL on your screen. To submit questions through the webinar program, you can do that by going to the box marked "Questions" near the bottom of the control panel. We will try and handle those through the course of the webinar, and certainly if we don't get to them, we will make every effort to address them after the webinar itself. If you need a certificate of attendance, you must be registered and logged in to the webinar under your own name. A certificate will be emailed to participants by the end of the week.

Slide 1 – Principles and Practices of Debt Management: Employing a Debt Policy (02:30)

MARK CAMPBELL: Okay. We are going to do one polling question here to begin with, and so to set the groundwork for our speakers. The question is… and it should pop up here. Okay.

Polling Question: Why Are You Participating In This Webinar? (02:45)

MARK CAMPBELL: Why are you participating in this webinar? A) We have debt policies and may update it. B) We are planning to develop a debt policy. C) Just curious-- Wanted to learn about debt policies. So take a minute, if you would, to respond.

Polling Question: Why Are You Participating In This Webinar – Results (03:16)

MARK CAMPBELL: And the results are... looks like we have got most of the audience just interested in debt policies. I know having looked at the registration list the participants seem to represent more of the issuer community. So I hope at the end of this program, you as the issuer will understand the importance of debt policies and seek to employ those on a going-forward basis.

Slide 2 – Principles and Practices of Debt Management: Employing a Debt Policy (03:48)

MARK CAMPBELL: With that I will turn it over to the moderator. Today's moderator is David Brodsly. Managing Director for KNN Public Finance. David has over 15 years of experience serving as a financial advisor to a variety of cities, counties, special districts and other agencies throughout California. Prior to joining KNN in 1999, David was vice president, senior credit officer with Moody's Investor Service in San Francisco, and a member of Moody's National Rating Committee. He began his career with the city of Los Angeles, where for 12 years he was responsible for financial planning, debt issuance, and bond administration. David, I will turn it over to you. Thanks.

DAVID BRODSLY: Hey, thank you, Mark. So I want to just begin by telling folks at CDIAC how much I appreciate your organizing of this in-depth conversation of this topic. When I first engaged with the act of trying to write debt policies in the 1980s, there were virtually no resources available. Even now, while most issuers would agree with Martha Stewart that a debt policy is indeed a good thing, the number of resources available to local agency debt managers are still pretty limited. So what I like about today's webinar is introducing a number of these resources that are available, which includes three organizations that are dedicated to improving government decision-making, and two debt issuers that have taking on the challenge of developing and maybe more interestingly, living with a debt policy. If you look into the CDIAC webinar page you will see additional resources you can go to, and you will hear about other resources that are available during the course of people's presentations.

I guess the one thing that I wanted to point out is that this webinar is not only for agencies that don't have a debt policy and wanted to consider one. I don't think I have ever met a policy that couldn't be improved. Certainly that is true of every policy I have been involved with writing. Most debt policies begin with a copy from another agency, and I'm all in favor from learning from other people's experiences and taking advantage of other people's work, but someone else's policy isn't going to fit you perfectly and needs to be adapted to local circumstances. I think personally most that I have read have some references that are irrelevant to that agency, have some vague statements that could be clarified, generalizations that can be made more specific. I don't think a debt policy should get ahead of itself, but often the hard decisions are just left for a future day and they offer generalizations. All that being said, it is a great thing to have and great thing to start with. And hopefully those who are listening today, they will get some good ideas, some fresh ideas, and hopefully CDIAC will continue to collect these ideas and make them available to the debt management community.

Slide 3 – GFOA's Best Practice: Debt Management Policy (07:01)

DAVID BRODSLY: So with that, let me begin with our panelists and get to the substance of the program. Our first speaker will be Susan Gaffney. Many of you remember Susan from her role at the GFOA (Government Finance Officers Association.) She is currently in charge of her own company and serves as the president of SG & Associates, which provides advice and marketing outreach and policy answers in terms of specialization in public finance. Prior to starting her own firm this year, she was – what was the title – the director of the Government Finance Officers Association Federal Liaison Center in Washington D.C. I have found that GFOA showing tremendous leadership in formalizing advice for a number of government agencies on a number of topics, including debt management. I know they are a resource I rely on often when I am trying to put together materials for my own clients. I steal shamelessly from the GFOA. So let's go to Susan who will walk us through some of the debt advice that they gave at the GFOA regarding debt policies. Susan.

Slide 4 – Background (08:06)

SUSAN GAFFNEY: Thanks, David and CDIAC, and good morning, everybody. I appreciate being able to speak on this important topic. GFOA developed their best practice on developing a debt management policy years ago thinking that it was a very important piece to have as a foundation for governments to use as they implemented debt programs. And also that many other items feed off of that debt policy which need attention from the government. One of the most important issues that a debt policy can help you with is not only can I issue debt, what kind of debt can I issue, how do I evaluate projects, but also the debt management. And what we like to say sometimes is a debt policy can also help you say no to a lot of people and a lot of items that come your way. If it is articulated correctly in your policy that helps set forth the charge which you can work in when you may be approached, either internally or externally, with various types of ideas. This best practice has been updated over the years. Again, like a debt policy itself, always can be improved. And there are different reasons why you may want to, as David mentioned, look to revise yours. We will talk about that in a bit. But we last revised the best practices in 2012. Of course, that came following the market crisis, just to make sure that we covered all of our bases and all the lessons learned from that crisis, and making sure that our members also were aware of that and what should be included in the policies.

GFOA has numerous best practices on a host of issues, but on the debt management, really the debt policy serves as the hub and all of our other best practices serve as the spoke, and they all feed off each other. So when we talk today about this and we talk about establishing that debt policy, you have to think about all the different sections that come part of it, some of which on their own may deserve policies and procedures, whether that's the method of sale or selecting professionals, what kind of products your government is willing to use or entertain the use of, your post-issuance compliance, your disclosure – again, feeding back and forth from each other so everything's in sync – as well as other policies within your government. You don't want to develop this debt policy in isolation. You may have investment policies on the books that obviously would make sense to make sure that they work well with this debt policy and your capital projects, etc. It sort of is a dynamic policy from that standpoint that you do need to involve and think about how it relates to other parts of your government.

One of the other really important issues is that it helps with your internal management strategy and work flow. I will talk a little bit about this later, but putting down the baseline of this debt policy is great and essential, but then from that what you can do is you can develop work flows and checklists so that you can insure that you are not only implementing the policy, but it can help you be reminded and meet those responsibilities as well.

Slide 5 – Importance of a Debt Policy (11:12)

SUSAN GAFFNEY: So when it comes to the importance of a debt policy, as Nike says, "Just do it." Think of it as something that can help you in the long run and certainly help your government in the long run. Internally, it helps all staff not only you, but your staff as well as other departments, as I mentioned, and your elected officials. It brings awareness. You have new elected officials come in and being able to show them the debt policy so they know what is currently on the books and how your government has operated and is operating now is really important.

Externally, even growing more important--I think a debt policy you all are probably getting a lot more questions about well, do you have a policy in place, certainly from credit rating agencies. They love to see debt policies and this helps you with that relationship and certainly with your ratings, and it is an extreme value to have for that alone. But, also with the professionals that you hire--You're hiring a municipal advisor, you're in a negotiated sale, you're looking at an underwriter, you have bond counsel. If they know the parameters that are already set within your government, that helps them to be able to communicate with you in a more straightforward way and as I said earlier, helps you say no perhaps to the esoteric finances that may come your way. You can easily point, "Oh, please look at page two, line six, we can't do that." And that gives you cover and ability to say yes or no when you have different types of financing options coming at you.

Unfortunately, Washington is trying to stick their nose under this tent as well. The IRS would love for you to have written policies and procedures for post-issuance tax compliance. You have seen it in the past couple of years come forward in the tax forms, check this box if you have written policies and procedures. That is something you will want to talk to your bond counsel about, whether to check yes or no on that. But when it comes to an audit that is one question they are going to ask you. May we see them? There is no law currently that says you have to have them. There is nothing in the Tax Code that says that is there. But as we will see also with the SEC, through enforcement or nudging they are trying to move the market this way to have the policies in place. And as with the SEC and with everybody else, not only do you have them, but are you practicing them? It needs to be a living document which keeps on being attended to.

The SEC also wants to see that you have disclosure practices and procedures in place, and they are being implemented. Again, not currently part of securities law, but something that they would really like to see happen. We have seen with this MCDC Initiative that one of the penalties if the SEC comes to you and says, if you have not done your disclosure correctly on this, that you will have to put policies and procedures in place. We also saw that with the San Diego pension disclosure ruling that they had to put new policies and procedures in place related to disclosure. So again, we are going to see more regulations, not less, on this so I think it is important for you to think about that as well.

And with the municipal advisor rule, again, with what an underwriter can and cannot do, maybe incorporating the use of a municipal advisor, that also can be part of your debt policy.

Slide 6 – Basics of a Debt Policy (14:58)

SUSAN GAFFNEY: So on the basics of a debt policy there are some more static more dynamic sections. It should have an overall view, what are the goals of your entity? What can you issue debt for? What is your goal in being able to provide for your citizens with your debt issuance? What can you use with those bond proceeds? All of those types of issues are the things that should be covered very generally in a debt policy. What are your debt limits and debt capacity? CDIAC has some great papers on this and the rating agencies have also commented. But how much can I issue if I issue today? Does that limit me from doing a project five years from now? And of course also, how much can I handle in debt service payments within my budgetary section as well? So those are the types of items that also need to be looked at in your debt policy.

What kinds of debt may I issue? Some of that, your GO debts, very specific, when can that be done? When can I use revenue debt? Should your government issue taxable debt or look at bank loans or look at pension obligation bonds? Being able to spell that out in your policy can help you and your entire government know when it is right to look at the debt market for these types of financing. Some of this again is a little bit more static than dynamic on whether you can or cannot issue, and that is another reason why you may want to consult – and we will talk about this later – others to develop your debt policy, again, whether that is with bond counsel or with municipal advisors. But being able to have on the books, can we issue variable rate debt? Do we only issue fixed-rate debt? What are the parameters in which we issue revenue debt? Can we do short-term debt? All of that is important as well as refunding, whether the criteria and when do we maybe look at a refunding opportunity for our government.

Slide 7 – Basics of a Debt Policy (*continued*) (16:53)

SUSAN GAFFNEY: Additionally, there's the structure of debt. How am I going to structure my debt? What are the bond terms? How do I determine the lifetime of the project and then how does that dovetail into the terms of the bond? How do I want to structure my debt service payments? That should be articulated. Also, whether I want to use credit enhancements. Of course, bond insurance as well, used prior to the 2008 crisis, is certainly coming back. So when would you want to use bond insurance? Something that you may want to cover is letters of credit. And I think now post crisis, you may want to also talk more about managing that relationship. Many times governments had bought bond insurance and never thought about it again. And I think now people want to make sure they have an ongoing relationship with that insurer. Know the terms. And so that being able to articulate your ongoing relationship with the bond insurers might be something different that existed prior to the crisis.

On the debt issuance side, how am I selecting my professionals? GFOA recommends always use an RFP process. Maybe that's articulated in your debt policy. You may want to go a step further on what are the scope of service for those professionals, and how am I paying those professionals? With the municipal advisor, am I paying them on an hourly or flat-fee basis? Are they paid out of bond proceeds? How is that done? That should be thought of as a piece of your policy. My method of sale – when would I use competitive? What factors might push me to negotiate it? Having that laid out so you know how to address that is important.

And look at your pricing. How do you know what to expect? What benchmarks you may be using and how to evaluate your final bond pricing also should be key aspects of the policy. And as I mentioned earlier, when to determine whether or not you should enter into a refunding, and what criteria needs to be met in order for a refunding to make sense?

There is also a lot more on rating agencies. Again, post-crisis, I think a lot of people are looking at ways to have stronger relationships with the rating agencies, as well as whether or not they have enough ratings. Do they need just two? Do they want three? But there's a new push to have more of an ongoing relationship. Make sure you have the communication open and sharing of information. And as with so many pieces of this on the debt policy, who is in charge of facilitating that relationship? Maybe it's the name of a person or maybe to make the document more longstanding, it's the position title. But whether it's this, or I'll say later on disclosure; who is responsible for the task so that everybody in the government knows, okay the rating agency called, we give that call to Jane or Jim. So I think that is also very important. Same with disclosure--who is developing all the information? Who is in charge of the continuing disclosure? Who is in charge of our EMMA management? How do we decide if we should voluntarily provide voluntary disclosures? Make sure that is also part of the policy, again, maybe in broad terms, and then you may want to look at a specific disclosure policy and procedures. But, who is responsible for all that is important.

Investment of bond proceeds also, what are your permissible investments? Who is supposed to help you with that? May want to address that as well and your ongoing tax monitoring. Of course we all wish there were arbitrage problems to be had. Perhaps someday we will get back to that. But once you issue the bonds, just like with the disclosure items, there are things you still have to be thinking about, whether it is the private use regulations and arbitrage. So there has to be some ongoing monitoring and that needs to also be reflected in your debt policy.

And all of these points are covered in GFOA's best practice, which you see the link to, again to provide a broad overview. And then of course, the CDIAC paper goes into greater detail and specifics about their findings from the research project that Mark commented on.

Slide 8 – Implementing the Policy (21:00)

SUSAN GAFFNEY: When you implement the policy – we need to first develop it. Develop by teams. Don't do this in isolation. Well, you may be a small government. You may be involving everyone. But it should expand past the debt management office. You may want to look at your friends over at treasury, your internal legal departments, and even those happy accountants probably have some careful and important input for you on the development of the policy. And even those that are on the team, you still may want them to review because they may have something that you want to include or maybe know something that you don't know from years ago, and it's best to have that fixed up front or placed in front, rather than to have it completed and say, oh gee, we forgot that.

It's essential to have governing body approval. This helps you fortify that document that you've worked so hard on and that you've gotten through. It means it has been blessed by the governing body and it helps them because as we will hear from others later who have been elected officials who have been very involved in developing a debt policy. Many just want to need to know, and this helps them each know because they have had to look at it, they've had to approve it. So they are more intimately involved, and that is really an important aspect out there. Make it public. Not only for the public, but again for the people that you hire, they know what the parameters are and investors know that you have this on the books. That will also help with your bond marketing and the sale of your bonds down the road.

It is a living document. So like many documents that are developed, like strategic plans, don't just say that is over with, we are done and we can stick it on the shelf. You need to keep it going. So you may want to be creating checklists. You want to know that you are really doing what you said you are doing. And again, an offshoot of the debt policy itself may be a checklist to say who is responsible for all these pieces, and when to revise. Some governments, every two years they think of that. Other governments, who may not issue very often, may do it every time they issue debt and others may want to look at it following turmoil. Again, following the 2008 and 2009 crisis, a lot of governments updated various sections like a derivative section or developed new derivatives policy after living through what happened with the crisis there.

Slide 9 – Other Observations (23:24)

SUSAN GAFFNEY: Some other observations – your peer entities are key here. Look and see what they have done here. Look at those that are similar size and type and learn from them. Also talk to your municipal advisor, talk to your counsel, look and see what they may have too. There are a lot of resources out there. I think you'd want to stay within your state due to all those specific laws etc. within California, but I think there is a lot of good out there that can be absorbed in order to help you write this and think about things when you're revising it. It sounds overwhelming, but don't think about it that way. Think about developing it section by section; take care of the low hanging fruit. What does the law say? What can we do? Build from there. And then think about whether you need to have specific things out of the debt policy for tax compliance or disclosure, as I mentioned earlier.

Things can change that aren't in your control, and that is with everything, a headache, but you need to think about that when it relates to your debt policy as well. There may be state-level decisions, there might be laws passed that ultimately affect what you can and cannot do, and that needs to be reflected in your debt policy. And of course the federal government may also make some changes that could also affect that and the way practice. So while you just need to stay informed on these items because a lot of these issues are more static than dynamic, they can change. So just keep an eye on things and make sure you are aware of what is happening both on the state and national level.

And lastly, bonds last a long time, probably longer than you may serve in your government or your elected officials may serve. And so this is a document that is a gift that keeps on giving. You want to make sure that you have everything documented; you have everything written; you have the policy in place. Again, you have the procedures on how you implemented that because it helps those who come after you. I'm sure many of you wish there had been more when you walked into your office and took on these responsibilities, and you want to make sure there is a continuum to keep going. There was an example of, there was a small government in New England a few years ago, and they got a new mayor and he got all new staff, and so there was nobody there from previous administrations and well a very small government. And no one knew they had to make bond payments, so they didn't make bond payments. And that seems pretty trivial, and of course we do that, but making sure those types of things are documented, part of a policy, part of your debt policy, so you know and those that come after you know what is supposed to happen, is very essential. Of course, that is sort of an extreme example, but whether it is your disclosure items or how you select professionals, or what kind of debt you can issue, having this document helps you and especially those that come after you. So with that, I will hand it back to David. Thank you.

Slide 10 – Employing A Debt Management Policy: Practices among Local Agencies(26:30)

DAVID BRODSLY: That was great, Susan. I do commend the best practices paper that I'm sure your fingerprints are all over, Susan, that is on the GFOA website. It's not that long, but it provides not only kind of a checklist, but it gives you some insight as to what you are trying to accomplish in the various sections. I have a couple takeaways just from what you said that kind of caught my attention. One of them was how much of this document is for, if you will, internal management? I love that term – an internal marketing management strategy – because much of what the debt professional has to do is try to coordinate activities and keep the train from going off the tracks. The fact that it becomes a way of saying no, I think, is something that I hadn't thought about, but that is great. It helps to have somebody say no. We all look to external parties like the rating agencies to be the parent, but with a debt policy you can be the parent.

And the other thing I like was the notion of this being a dynamic process. I made reference to it in my opening, but the fact that there is opportunity for conversation about your values, what matters and, if you will, to create your permanent culture around the topic of debt management. That is why I want to emphasize the revisions. You are just never done with this stuff. If nothing else, you learn from your own experiences, and those experiences should be recorded so that those that follow get some benefit from those experiences. And finally, I wanted to say with debt capacity. I know I have worked on it through the life of my career. It is a difficult area to get your arms around and the capacity for a voter-approved obligation versus a general fund obligation versus a revenue obligation are so, so different. So I wanted to appreciate that you made the point that there are real distinctions there, and it was always well done in the paper from GFOA.

So I also wanted to point out that there is a place on the web page for questions. And please submit them through this. And we will get to them. I got my first one, which I am going to defer for a while because it is going to come up in the course of the conversation. But if you would, anyone who is listening who wants to lob something over the transoms, please do so. So with that, we already heard about the CDIAC study that sort of kicked off the thinking about this seminar. And I think everybody who is on this call knows what an extraordinary actor CDIAC's been in the research and publications in the area for local debt management. I don't think there is another organization in the country except perhaps the GFOA that has put so many resources into helping public officials stay informed. And one of the folks doing that is Robert Berry, who is the Deputy Executive Director at CDIAC, and he led the research team that looked at the local agency debt policies, which he will tell us about in a second. Robert's been with CDIAC since 2010, and prior to that he had a career in real estate finance for both private equity firms and for the State of California. With that, Robert, why don't you take us through your research.

ROBERT BERRY: Thank you, David. And good morning, everyone. My job here this morning is to give you a brief overview of a study that is also available on our website that CDIAC conducted last year on the preparedness of California municipal issuers to make good sound debt management decisions by virtue of the policies that they have in place, or in some cases the lack thereof.

Slide 11 – Study Setting (30:32)

ROBERT BERRY: Just as background, the setting for our study – some of the conditions in municipal finance at the time of our study and many which persist today – there was unprecedented physical stress with agencies experiencing service-level solvency issues where debt service and other obligations were impeding the delivery of customary public services. We had municipal bankruptcies where debt service obligations were at least cited as a root cause, a regulatory environment that was not only strengthening, but holding issuers more accountable, and then lastly on my list here, through some of our research projects here at CDIAC, we saw evidence that many issuers were not fully aware of the risks associated with some of the debt structures they were taking on and the downstream implications to tax and ratepayers.

Slide 12 – Study Premise (31:22)

ROBERT BERRY: In conducting – Mark kind of mentioned this in his opening comments – but in conducting our study, CDIAC was operating from a very basic premise in industry standard guidance. That is that a debt management policy is an essential element of an agency debt program and not just for frequent issuers. There essentially is a risk baseline regardless of issuance frequency, and that baseline has really increased because of many of the conditions that I just mentioned and that Susan mentioned in the prior presentation. Some of the supporting rationale for debt policy among those already discussed: first and foremost, there is a wealth of policy development and guidance already available from GFOA. We've already talked about that. Guidance on the development of the policy itself and really guidance on virtually every policy element CDIAC evaluated in its study. Kind of the hub-and-spoke comment that Susan mentioned. There are also numerous examples from peer agencies that can be adapted. And we will hear from some of your peer agencies in a few minutes. And we found that the policies were very readily available on websites and easy to access.

Next, rating agencies, as has already been mentioned, give consideration to an agency's management structure and to the existence of a debt management policy. Having a debt management policy will have a positive effect on the issuer's rating and ultimately the cost of debt. And it would seem the risk of not having policies in place to guide compliance with SEC, MSRB, IRS regulations on disclosure and arbitrage are really reason enough to have a policy. The IRS has even indicated that noncompliance issues are dealt with less harshly when an agency has policies and procedures in place. It sounds as though it is one of the first things they look for in an audit.

Lastly, a policy will assist agencies to issue debt at the lowest cost and burden on taxpayers. This is a pretty simple consideration made all the more important in an era of increased transparency and accountability.

Slide 13 – Study Methods (33:44)

ROBERT BERRY: So, given the conditions and premise that we operated from, CDIAC set out to gauge issuers' preparedness with their debt policies. So, how did we go about this study? I will quickly go through our methodology. We pulled a data set from our debt issuance database that all municipal issuers report to, of all county, city and school districts issuance for a ten-year period. There were over a thousand issuers in the data set, mainly school districts, and they issued $172 billion during that period of time. That's new money and refunding. From the population of issuers that we pulled out of the database, we randomly selected 230 to create a statistically significant sample for each of the issuer types. And as you can see, the volume in that final column there issued by the sample was still quite large. That was because we happened to pick up some of the larger issuers in our sample.

Slide 14 – Study Methods *(continued)* (34:50)

ROBERT BERRY: We then went down the random list of sample issuers and gathered debt management policies. As I mentioned, we found them available on websites quite readily. We gathered those documents that were clearly identified as debt management policies. If there was no policy online or if there was any ambiguity as to whether a document was a policy, we contacted the agency directly. In surveying the sample, we counted the policy if the agency identified it as a policy. And believe me, it was not always easy to tell just from looking at the document. So in the most basic measurement of preparedness, whether you had or did not have a debt policy, that fourth column there, issuers with policies, more than half the county issuers had policies, about half the cities had policies, and less than a quarter of the school districts issuers had policies in place. The good news is at least in terms of the sample agencies, over 80 percent of the volume that was issued by sample agencies, was issued by agencies with policies. Again, this was a result of our sample including some large issuers.

Slide 15 – Study Methods *(continued)* (36:00)

ROBERT BERRY: The next step in our process was to do a content evaluation of the debt policies. And we based it on GFOA standards and best practices. We reviewed each of the 84 policies in our sample and looked for 30 different policy elements and four different policy categories: debt limitations, debt structuring, debt issuance and debt management. And then we simply scored each policy on a 1-to-30 scale based solely on whether the element was mentioned. We didn't give any weight to any one element over another, and we made no adjustment for how well the element was addressed. So just whether it was mentioned or included. And as you can see, we also established some protocols to reduce subjectivity in our review process and reconcile differences in scoring among our reviewers.

Slide 16 – Results: At a Glance (37:01)

ROBERT BERRY: So what did we find? Well, first of all, there was a statistical significance to our findings on whether the issuer population had policies in place or not. The content analysis that we conducted really can only be projected upon the policies that we reviewed, not the entire population of agencies, but we think the results are informative. We found that some of the sample policies in our group were very strong and comprehensive. And in reading them, their practicality in guiding debt management practices was apparent, clearly apparent, and that's the good news. But as a group, adherence to the GFOA standards was fairly poor. The chart shows in the slide how the policy scored against an arbitrary break point of 15 of 30 elements. County scored fairly well as a group, but there was a significant drop-off among cities and another quite large drop-off for school districts. Not only did less than a quarter of the school districts have policies, but the ones that did, failed to include more than just a handful of elements.

So I'm going to run through the different elements we looked at. A quick scoring note: a score of four percent in the school district column likely means that Los Angeles Unified School District, one of our samples – one of the districts in our sample – covered the element.

Slide 17 – Results: Debt Limits Category (38:30)

ROBERT BERRY: So the first elements that we looked at were those in the debt limits category. These are the elements that really set the high-level policy guidance on the appropriateness of debt. They established the broad parameters under which debt should be considered for an asset or cash flow financing. Specifically, in the elements under the purpose of issue section, this is where an agency discusses what they will not finance. We talked about that with Susan. Also the characteristics of the assets that are acceptable, integration and financing decisions with a capital improvement plan or capital improvement budget, and also circumstances under which PAYGO financing is preferred to debt.

The next category – debt limits subcategory – provides visibility to the statutory limitations and establishes financial guidance for outstanding debt and debt service in relation to general fund, assessed values, revenue sources and security metrics. The type and criteria subcategory – it provides policy guidance for the selection of term length and circumstances for selecting fixed or variable rates. The subcategory also discusses the conditions under which specific debt types – COPs, leases, TRANs, Mello-Roos, etc. – are more or less appropriate. Generally, the policies we reviewed covered these elements – the elements in this category the best. Counties in particular were careful to include the higher level policy elements in this category. The policies of school districts were very often simply a citation of government and education code for the issuance of general obligation bonds. And that code specifically addresses uses, uses of debt, and some of the terms of issuance. The school district's inclusion of an element directly related to whether that element was in statute. And as you can see, it is reflected in the scores as we go along.

Slide 18 – Results: Debt Structuring Category (40:40)

ROBERT BERRY: The next category is the debt structuring category. This includes the elements that address the conditions and circumstances under which specific features of debt should be considered and evaluated. The policies included elements that range in their level of guidance from very general guidance to specific operative guidance. For instance, some of the policies discuss the use of credit enhancement to achieve minimum credit ratings. Others had very detailed or even separate interest rate swap policies. Susan mentioned how several of these elements warrant separate policy documents themselves. That swap policy was an example of that. A number of city and county policies set maximum debt maturities below statute. The statutes covering the issuance of school general obligation bonds include maximum maturities. So many school districts were given credit for the maturity element. The others district elements in this category were covered by the Los Angeles Unified School District.

Slide 19 – Results: Debt Issuance Category (42:52)

ROBERT BERRY: The next category we evaluated was debt issuance. Perhaps the knowledge that rating agencies look for debt policies and the direct connection between ratings and interest rates caused more cities and counties to address policies around ratings maintenance. The next section – method of sale, competitive versus negotiated sale – was addressed with general statements about preference up to specific guidance about the conditions for choosing one or the other. Policies rarely included the topics of direct lending or private placements. These are expanding methods of financing that CDIAC hopes will be addressed as policies are developed and updated in the future.

One surprising subcategory here, the results – the process for selecting professionals was rarely addressed. It was much more common for the policies to generally list financing team members, their roles and responsibilities, almost like a glossary, but did not provide guidance for how they are selected. And as we heard from Susan that was a very important element. Lastly, a discussion of the acceptable conditions for refunding was frequently covered by counties and a fewer cities. And then a common feature with these elements was the all-in net present value savings target.

Slide 20 – Results: Debt Management Category (43:23)

ROBERT BERRY: The last category that we looked at was the category of debt management. And as discussed before, the elements addressed in the debt management category are probably reason enough to develop and maintain a debt management policy. These are the high-risk elements that, if not properly addressed over the entire term of the debt, can have serious consequences of an agency and its ability to debt finance in the future. More than half the counties we reviewed address these critical elements. Cities did not perform nearly as well. And as much as schools were apt to cite legal code as the basis for their debt policies, they very rarely covered these legal and regulatory elements. It was also very uncommon for a policy to include a connection to an agency's operative investment policy for investing bond proceeds.

Slide 21 – Results: Review and Approval (44:23)

ROBERT BERRY: So in addition to the 30 policy elements that we derived from the GFOA best practices, we took a look at some of the characteristics that may give an indication as to whether the policies were adapting to changing conditions, whether they were maintained, and how operative and practical they might be. I can't say that we came away with really anything conclusive in this area, but we did find the cities usually included their debt policies as a section in a broader set of administrative financial policies. And I think there are some advantages to that.

The policies of counties and schools were normally standalone, although the schools were, as I said before, were generally a citation of statutory authority for general obligation bond issuance. The standalone nature of the county debt policies may have caused the counties to address more elements because they were simply unobstructed by other non-debt policy considerations. Seems like it may be plausible, but as I mentioned before, it may also be valuable to integrate the debt management policy with other financial and administrative policies because of their connections.

Most of the policies were dated and showed some evidence of running an approval process through a legislative body, an important element. The ladder of course, demonstrating the commitment to the policies beyond the staff levels throughout the organization. Very few of the policies included provisions or procedures for updates. While this is not necessarily a GFOA standard provision for policy maintenance in the policy itself, it was included in a few we reviewed and may be of value for updating policies and developing new policies.

Slide 22 – End Notes (46:09)

ROBERT BERRY: So in conclusion, wrapping up the discussion of our findings, I would just like to reiterate the CDIAC's position that low issuance frequency is not a good reason for not having a comprehensive debt policy. At the same time, we realize that not every element applies to every issuer, but the policy should recognize the inapplicability of an element and not simply ignore it. A policy element may not be relevant today but may become more relevant and applicable in the future. And then we also want to recognize that our sampling method surely missed out on some great policies. We didn't review everyone. So perhaps there are many of you on the webinar that have policies that are very effective and very comprehensive.

So I think now I'm going to shift away from this clinical discussion of elements and scores to more practical information from some of the peer agencies. But before I do, up on the screen is a chart that shows 14 agencies in our sample that scored well on our content analysis, and point out that these policies may be helpful examples to you to get started, in addition to the GFOA guidelines and developing your process for debt management policy development. David, that really concludes the overview of the study. I will kick it back to you.

DAVID BRODSLY: Thanks, Robert. One of the things that, as I look at the study, it certainly gives a sense of who is comprehensive, whether or not being that comprehensive is that important or not really depends I think on the individual entity. And certainly there is a part of me that thinks it is not better to say something than to say something that is not particularly meaningful. But I guess does CDIAC have a library of these good policies? And maybe this is as much a request to CDIAC as it is a question. But I think I wouldn't expect CDIAC to make a judgment that somebody's debt capacity discussion got an A- and somebody else got a B+, but it would be helpful for these templates to be available for others to review. And I don't know. Obviously you can go on the websites for most of these entities and find their debt policy. But has there been any thought on your front, Robert, to try to collect a library, if you will, of good debt policies?

ROBERT BERRY: Well, like I said, we found that the policies were quite readily available on websites. So there's the issue of making sure you have the most up-to-date policy, making sure that the agency that you are looking at, that the policy that you are looking at, is comparable to you and your circumstances. So it is not a one-size-fits-all, as has already been mentioned. There is also the maintenance issue of keeping a library of policies. It's not something that we have done. And that's why I wanted to put up the chart there to show some of those that at least a year and a half ago when we did the review, hit on a lot of the different elements. Again, we did not get to the quality of how well they were dealt with, but they did hit quite a few – 20 or plus – of the elements in their policies. And you can see too there's a range of different entities: rural, north, south, large and small agencies there, too. So we are hoping that list and a lot of the other reference points that we put on the website might be helpful for our webinar participants.

DAVID BRODSLY: Yeah, I think that's a good point. And what prompted my question, I know of some robust policies that just aren't on – where it didn't make it to the sample, which makes sense. But the City of San Diego comes to mind, L.A. County Metropolitan Transportation Authority comes to mind. I don't think L.A. County is on here. So anyway, I guess I would encourage folks to look broadly, but this is a great place to start.

I have a question for the group that was raised by someone in the audience. Maybe it's a good time to take one of these. Susan mentioned the importance of rating agency relationships. It's certainly part of the checklist, probably in most of the policies I have looked at. And the question from the audience is: How do you develop a relationship with rating agencies with staff turnover at the rating agencies? And I would add to that, their new regulatory schema, which seems designed to make them less useful to issuers in the desire to keep them from "structuring debt." I would be curious if anybody on the panel has an answer in how you approach rating agency relationships specifically.

SUSAN GAFFNEY: This is Susan. I mean, I think you are right. There is an even more extreme firewall post Dodd-Frank regarding the business office versus the analysts' office. But, I think that it is important, just as with disclosure, as you are developing information, as you have interim information, reaching out to that analyst and making sure they are aware of the information you are putting out. I think that that's key. They are not the ones that can talk to you about contracts or pricing or the cost of a rating, but maintaining that analyst relationship. I know there is a lot of turnover, but doing your part so that you feel good about that and giving them more information rather than less, I think is one way to approach it.

DAVID BRODSLY: Thanks. I will tell you from my experience as a financial advisor as part of the city of L.A. team, they do a very good job of whenever there is a report of significance, just shooting an email to the rating analyst. And part of that is making sure they have the information. Part of that is developing a sense that the rating analyst can trust the issuer to keep them in the loop. And of course, it is probably more important to share information that is a little more unfavorable than the things that just tell you how wonderful you are doing. And that's a balance.

SUSAN GAFFNEY: Right. You'd rather have them learn from it you than reading it in a newspaper.

DAVID BRODSLY: Exactly

SUSAN GAFFNEY: Because it is public either way. So get ahead of it.

DAVID BRODSLY: Exactly. If nothing else, it builds credibility. So we will be turning to a couple of practitioners who developed and lived with debt policies over the past few years to get a sense of their experiences. We are going to start with Butte County, who, despite its relatively small size, has a particularly robust debt policy, which in a way is a great case study of how you don't have to be in the market every day and be a seasoned debt issuer to be able to come up with a valuable policy to help guide you.

Joanne Wilson's going to review their Debt Management Guidelines and Procedures. She is a financial analyst for the county. Responsible for debt management and was responsible for implementing the debt policy. And before joining the county, she was a loan officer for several federal lending agencies. If anybody else on the phone has had bad experiences with the agencies, it is not Joanne's fault. With that, Joanne, why don't you take it over.

Slide 23 – Debt Management Guidelines and Procedures (54:30)

JOANNE WILSON: Good morning. And I would like to thank CDIAC for inviting me to participate in today's program.

Slide 24 – Table of Contents (54:38)

JOANNE WILSON: First of all, let's go to the slide that just follows the table of contents. One more. The next slide would be perfect.

Slide 25 – Plans Are Good (54:48)

JOANNE WILSON: First, some background. Prior to the adoption of the County Debt Management Guidelines and Procedures, a thorough financial analysis of the issuance was performed by the Treasurer's office, and the proposed financing was evaluated by Administration and the Auditor's office.

But the County lacked the formal transparent review process. The County gives a lot of credit to CDIAC and GFOA for promoting the benefits of having a written debt management policy in place.

In 2006, representatives from the Treasurer's office attended a CDIAC workshop which included a section entitled “Developing a Debt Management Policy.” Convincing support for the substantial benefits derived from adopting a clear debt management policy was presented. One of the many lasting impressions left with the employees who attended the training is demonstrated on the first slide. The chart provides an example of the power of having policies in place. It clearly shows that the cities with policies were more financially sound. Having specific written guidelines which were followed undoubtedly benefitted the cities with policies. The chart communicated such a powerful message to the employees, they returned to work advocating for a written debt management policy. Development of concurrent policies was also encouraged at that same workshop. Butte County adopted its general fund debt policy in 2010.

Slide 26 – Objectives (56:11)

JOANNE WILSON: The County's initial considerations and objectives included documenting the County's goals for the use of debt for financing County needs. For example, the documents provides that the County recognizes that although long-term financing usually requires higher total expenditures than a cash purchase, it has the benefit of allowing immediate completion of the project, so those paying for the project are also those benefitting and utilizing the project. And this was an important consideration to the County. Additionally, we point out in the documents that during times of rapidly increasing construction costs, the costs related to financing a project are sometimes less than the construction cost increases caused by delaying the project until adequate cash is available.

The types and purposes of debt are thoroughly discussed in the document, including short-term financing options such as TRANs and bond participation notes as cash management tools. We wanted the County's debt issuance values to be clear prior to encountering pressures. In the event of time pressures to analyze a project financing, having written specific guidelines in place, allows for an organized, efficient, and thoughtful analysis, thereby preventing hasty decisions which may not have been made with thoughtful deliberations.

We also wanted the guidelines and procedures document to have an educational component for all readers. We chose not to simply include a glossary of terms at the end of the document. It was important the body of the document was clear and educational for the board of supervisors, as well as County staff and the public. Therefore, terms were defined and discussed within the document. The document provides continuity with staff changes. The guidelines and procedures are concise and thorough, and provide new staff with an excellent educational foundation with regard to types of debt, the issuance process, and the County's debt issuance values and procedures.

It was important the guidelines and procedures address long-term capital improvement cost. The County developed and implemented a ten-year capital improvement program in 2006, and the document is updated annually. The close coordination of capital planning and debt management ensures the County achieves maximum benefit from available capital funds, and it minimizes the potential for inappropriate or avoidable spending. The guidelines and procedures discuss the process of determining the feasibility of a proposed project and its funding with long-term debt. Operating and maintenance costs were always a part of that analysis. Each debt issuance proposal will be evaluated by comparing it with competing proposals on the basis of the benefits derived, the prioritized need for the County, and the limits of debt that can be legally absorbed by the County.

The document addresses the County's intention to minimize the County's debt service and issuance cost. The County seeks to minimize borrowing costs by taking advantage of favorable economic conditions. Timing debt issuance to accommodate market interest rates and investor sentiment is an important means of minimizing the cost of debt.

Maintaining the highest practical credit rating is an important objective. By maximizing the County's credit ratings by the primary bond rating agencies, the County can issue its debt at lower interest rates than entities with lower ratings. Accordingly, each proposal for additional debt will be analyzed for its impact on the County's credit rating. Credit enhancement will be considered if the minimum rating requirement of investment grade or higher cannot be met. When analyzing the appropriateness of a debt issuance, the guidelines and procedures incorporate current accepted measures of affordability used by the credit rating agencies. We compare those to the current value for the County. These measures include the ratios overall debt per capita, overall debt as a percentage of the assessed valuation, and total governmental funds debt service as a percentage of total governmental funds expenditures. Adherence to these measures is important even if the current issuance will not be receiving a credit rating.

In order to maintain full and complete financial disclosure and reporting, the guidelines and procedures clearly list the County’s financial disclosures, monitoring and record keeping obligations. The Debt Management Guidelines and Procedures provide structure and consistency to debt evaluation. The use of a financing proposal form, which is included as an appendix to the guidelines and procedures, gives structure to debt evaluation and helps avoid oversight of pertinent factors. We also wanted to ensure the responsibilities for debt administration were clearly understood. Next slide, please.

Slide 27 – Initial Draft (01:01:00)

JOANNE WILSON: An initial draft of the guidelines was completed in 2006 after the CDIAC workshop. Our Treasurer-Tax Collector, Assistant Treasurer-Tax Collector, and Manager of Finance and Investment in the Treasurer's office took the lead in drafting the guidelines. The first draft incorporated the guidelines from the policies of other successful municipalities. It provided us an excellent framework. We knew what we wanted to cover. The table of contents is listed on this page. The objectives of the guidelines and procedures are discussed first. Many of those I just discussed in the previous slide.

A debt advisory committee was formed. All debt issuance proposals analyzed and approved for escalation by County administration and the department with the authority and responsibility are communicated to and reviewed by a debt advisory committee. The committee is comprised of our Chief Administrative Officer, County Treasurer, the County Auditor and Controller and the Chief Financial Officer. Two of the members are elected positions. This was done intentionally to avoid any abuse of power by a CAO. The committee reviews all financing requests to determine if they comply with the guidelines and procedures. At least three members must be present at the meeting and at least three must concur. If the committee determines the guidelines and procedures have been followed, the Chief Administrative Officer shall present a certification of compliance and any justifications for recommended exceptions together with the detailed financial proposal document to the board of supervisors for their authorization and direction to proceed with the issuance.

Additionally, the document includes the authority and responsibility for debt issuances which had not been previously defined. Under the guidelines and procedures, the Chief Administrative Officer is responsible for coordinating the issuance and administration and coordination of long-term debt, and the Treasurer, in cooperation with the Auditor, is responsible for coordinating the issuance and administration of short-term debt, all of course, with the approval of the Board of Supervisors.

The credit issuance guidelines include the debt ratio targets discussed previously, as was the capital planning. The County addresses in detail the types and purposes of debt, methods of sale and issuance, the selection of financial consultants and service providers, term and structure of the County long-term debt, credit ratings, investment of bond proceeds, refunding the long-term debt, derivatives and conduit financings, annual audited financial statements, financial disclosures, monitoring and record keeping and ethics and conflict of interest issues. The Appendix A is the proposed financing form which functions as the feasibility analysis. So the County attempted to cover all aspects of the debt issuance process and the factors to be considered when evaluating a debt issuance. The next slide, please.

Slide 28 – Resources and Experience (01:04:00)

JOANNE WILSON: Work on the draft Debt Management Guidelines and Procedures were submitted for several years due to the recession and the absence of capital projects. Additionally, an internal restructuring involving the transfer of debt management responsibilities from the Treasurer's office to Administration occurred prior to finalizing the compliance and procedures. In 2011, the County focused on expanding and finalizing the Debt Management Guidelines and Procedures, which was formally adopted in May 2013.

The final version incorporated the answer to IRS Form 14002, which is a Government Bond Financing Compliance Questionnaire. This was our initial starting point when we expanded. We understand the form is randomly sent to municipalities to determine their post-issuance bond compliance and record retention practices. We attempted to address each question in the guidelines and procedures.

We wanted to include an exhaustive list of financial disclosure, monitoring, and record keeping responsibilities which included annually applying the private use test and maintaining a system of monitoring, reporting, and record keeping to meet the arbitrage rebate compliance requirements of the federal tax code. Complete and accurate disclosure supports the taxable or tax-exempt status of bonds issued by the County and provides transparency regarding County finances and operations.

The following are some of the valuable resources we used to develop the guidelines and procedures: CDIAC Debt Issuance Primer, the GFOA "A Guide for Preparing a Debt Policy", GFOA "Debt Issuance Management, A Guide for Smaller Governments", the Government Finance Review Article from October 1997 entitled "Elements of a Comprehensive Local Government Debt Policy," and Standard & Poor's methodologies and criteria. We actually telephoned both agencies and discussed what the methodologies were.

We've analyzed and approved one large capital project since the adoption of our Debt Management Guidelines and Procedures. The process of evaluating the debt issuance proposal was extremely thorough. We systematically followed all the requirements in our written guidelines, and the written financing proposal discussed in the next slide clearly lays out for any to readers the key elements of analysis.

Slide 29 – Additional Comments (01:06:19)

JOANNE WILSON: Next slide please. Actually, we are a slide ahead, stay put. The County elected not to refer to the document as policy. We did not want the document to be viewed as the law of the land. As stated in the GFOA publication, sometimes policies become so restrictive or are followed so rigidly that they interfere with the government's legitimate efforts to provide public services and facilities. We wanted our written guidelines and procedures to establish clear methods of addressing long term capital improvement cost and short- and long-term cash management strategies, but the county recognizes that deviations in the document may be appropriate from time to time to address, for example, changing financial goals, emerging financial products and debt structures, and unique market opportunities. We found the financing proposal document, which includes the information on this page, to be highly effective in performing and presenting the analysis. Next page, please.

Slide 30 – What Next? (01:07:20)

JOANNE WILSON: So what's next? The County will be developing a separate written continuing disclosure policy as a companion to the Debt Management Guidelines and Procedures. This, too, will serve as an educational document for any reader and will be invaluable with staff changes. The guidelines and procedures require the debt advisory committee to meet annually. The annual agenda include the discussion of specific issues which have arisen over the year and whether they should be addressed in the debt management guidelines and procedures. If necessary, the guidelines and procedures will be amended with board approval. It is imperative we keep our document current. This completes my presentation. Thank you.

DAVID BRODSLY: Joanne, how did you start? Did you start by looking at policy documents? Did you start by just doing a collection of other people's policies?

JOANNE WILSON: That's what we did. We reviewed the policies of a couple other municipalities and used that as our basic framework and structure. And then when we returned to the document to expand upon it, we referred to many of the resources and what was unique to our county, and expanded upon it. But that was the framework, yes. We used other municipalities.

DAVID BRODSLY: And I assume just knowing that you haven't – I just know how much I learned with every new bond issue, and I am particularly slow but I have been doing this a long time, so I have sort of caught up – that it is a steep learning curve. So I have to assume this was a project that took a fair amount of intellectual capital and intellectual energy on your part.

JOANNE WILSON: Right. And then obviously our Treasurer's office has had a lot of input into it. They had previously handled the debt issuances prior to my joining the County. And then our Chief Financial Officer also was very involved with his wealth of knowledge from years and years of working for the County.

DAVID BRODSLY: Well, I suspect that when you were done, the working relationships in this area were only strengthened amongst the principal officials, which was another benefit.

JOANNE WILSON: Absolutely.

DAVID BRODSLY: Great. I do. I really am impressed, knowing how hard it is to do this. That you both had the courage to do it and the result is so strong.

JOANNE WILSON: Thank you.

DAVID BRODSLY: Robert, there was a question for you that I got after I let you go. On your slide, you had a reference to whether our debt policy was standalone or embedded in other document. Do you have an opinion as to how important it is and how this is done?

ROBERT BERRY: Well, my only comment was it appeared that the standalone documents, particularly of the counties, may have been a reason why they hit on so many more elements. But then I go back to what Susan commented on in her hub-and-spoke analogy and how the debt policy really needs to be integrated with other financial and administrative policies within the municipality. So I guess I don't really have an opinion as to which way is best. We clearly saw some very good policies that were integrated and we saw some very good policies that were standalone.

DAVID BRODSLY: I guess that goes back to the observation that it kind of – the better it fits the place the more useful it is going to be.

Slide 31 – City of Fresno (01:11:12)

DAVID BRODSLY: Well, let's turn to a city – City of Fresno, who is an interesting case study in the area of debt management. Fresno went on a bit of a shopping spree with their municipal credit card. And as a result there was a desire to adopt a set of policies where they can learn from their own experience, so that some of the mistakes or what looks like mistakes or misjudgments in retrospect wouldn't be repeated. We are going to get two presenters from the City. One is a council member, Lee Brand, who has been a council member for five and a half years. And this is one of only two instances I am aware of where the elected official rather than – I shouldn't say elected official – but a representative elected official, or board member or council member took the lead in a debt management project. And, besides serving – so just to introduce Lee – besides serving on the City Council he has been the President and Co-founder of a property management construction firm for the past 27 years. And Fresno as a council member is pretty much a full-time job. I don't know how you do that.

Lee will be joined by the City's debt manager, Phil Hardcastle, who has been serving in the role for the past 16 years. And I have done a bit of work with the City of Fresno, arguably the enabler of the credit card, I suppose. And Phil is one of my secret weapons out there, a resource in the area of debt management when I need to talk to somebody who actually does stuff and has hands-on experience as a practitioner. So with that, let me hand it over to the City of Fresno and their presentation about their policies.

Slide 32 – Why a Debt Management Policy? (01:12:54)

LEE BRAND: Good morning, David. Lee Brand. Thank you for the invitation to participate on the panel. And let me start out by saying that briefly my background as you mentioned was in private finance. I've crunched numbers for 30 years on small and very large construction projects, different properties. So it was a change to come in 2009, to come into public finance and learn all the complex nuances, and it was done by necessity. But for the fundamentals, why do you need a debt policy? I think you need a rational policy guideline restrictions to make your debt decision making. You send a message not only to credit agencies, but I think to the private sector and to the public at large that you want to provide credibility, transparency, and really faith in your local government, which I thought was lacking at one time. And also you want to encourage private investment to know that if you have your own house in order financially, that there's a confidence that whether it is an existing employer or somebody coming to Fresno, that they know that you are a sound city and you take pride in what you do.

On our own open specific policy, we had at the time that I came in only informal policies. There was no debt limit on the general fund. The only thing I found in the city charter was a limitation on the general obligation bonds, which we hardly issued in 50 years, of five percent of the total assets which were well beyond the capability of the City of Fresno to even do that. There was no requirement for annual evaluation. And the most important thing you touched on was that most debt issuances were very political. I would call it the legacy builders. I'm going to build a park or a stadium or a bridge. I don't know. We had quite a bit of that. So when we started, what really got the whole thing started for me, it was borne out of necessity. It was like a confluence of excessive debt issuance from the previous eight or ten years with the oncoming great recession. So these two forces put City finances in peril, and for the next six years to keep the City financially solvent and manage debt we had to have, in my opinion, really strict policies: 1) to manage the existing debt and 2) to prevent future debt.

So in my pre-council – I was elected in June in the primary and didn't have to do a runoff so I had six months to prepare myself. And part of my preparation was learning all the aspects of city government, including finances. I had several former city officials come to me and say privately, "Lee, there's major problems there. There's big debt issues. So I didn't know. So early on, I went to Karen Bradley, our then-acting Controller and asked her for a list of all the debt, and Karen provided that. And when I saw it, I realized there was a lot of debt that was issued. And in fact in the previous ten years, they had issued millions and millions of dollars of lease revenue bonds. Based on what I saw there was no rational basis for what they were doing, and there certainly was no formal debt policy. That is how I got my motivation. And when I talked to Phil and Karen and others, they all said, "Lee, we want debt policies. We are not getting that signal. We have not got that signal in the past. In fact, just the opposite."

So what I did to start out the process – really from someone who is a layman in public finance – was I did extensive internet research for probably two or three months. I must have looked at least 25 plus cities. I looked at counties. I looked at even cities in Canada, cities in California and across the United States, and my goal was to try to pick those best practices and policies – particularly even if it was outside of California – that would fit within California law and our governing authority, and then ultimately put all of these pieces together on our unique situation in the City of Fresno.

So after I had completed this analysis in a rough draft, roughly about 25, 35 pages of policy that I thought was pretty thorough, I then took it out in the private sector. What do you think? Am I in the right spot? Do I need to add, delete? And got some input from the private sector. And the next step, I brought the policy and draft form to the city manager, to the mayor, and of course Karen Bradley and Phil Hardcastle were part of that. Joe Gray, the former Controller, was part of that. And of course, David you were part of that, too, in putting this together. About a couple months, we worked together from my draft and came up what we all felt in the end was a really sound policy that covered all the stuff that you talked about earlier, all the major areas. And at that point in time I had learned, if you wanted to get a major policy passed in the City of Fresno, just don't take it blindly take it out to the elected officials and hope you don't have any unforeseen opposition.

So I went out to the city stakeholders, like the Chamber of Commerce, the Business Council, labor groups, and other really important bodies to get their approval and come in with a lot of momentum, having the full support of the administration, all the City finance people, private sector people and private stakeholders. So it went well and the City Council adopted the policy as I recall in a unanimous vote in early 2010.

At that point in time I was also concerned about in just my brief time in city government, that city councils have very short memories. So what I did now under these great financial stresses may not be around ten years from now and there will be a temptation to abandon some of the policies. So I felt the only way to really make sure this policy and some other policies – I have written many others that were similar fiscal reform policies – was to try to put this on the city charter, which meant I had to take it to the ballot.

So myself and Councilmember Borgeas, who co-authored everything, we had a series of issues of charter reform that we wanted to have a council review and the mayor review, and ultimately vote on to be placed on the November ballot. And in the end from about a list of twenty, three items survived to go on to the ballot and they were the debt management policies, reserve policies I had also written, as well as what I called the Better Business Act, which was a policy to provide due diligence – when the City, which we did get a lot of requests for private financing on different projects and invariably we lost money on them. So if the City was going to be a bank, they should act like a bank and do all their own due diligence.

So these three items were approved by the Council and they went to the voters in November 2012. And we didn't do any formal campaign. I wrote op-eds, interviewed with the editorial board, did the speaking tour, went out to all the rotaries, myself and Andreas, and it was successful because in November 2012, seventy percent of the voters approved the charter amendment. So these policies are now institutionalized within our city charter. And what that did is it put a threshold for changing at a much higher level instead of a simple majority vote of the Council to say we don't want these policies, we want to go back and spend our money again. It will take a vote of the people on the city charter to overcome that.

And in the roughly two or three years since this was passed, we have had instances where we have utilized these policies. And we had at least two or three refinancing policies that were subject to this policy. There were limitations on debt issuances particularly in the general fund that were put in here. And luckily, nobody had any plans to do any further issuance of general fund debt. Another important thing was outside of the budget cycle, the policy was written to have a supermajority vote to approve any bonds. And that also came out. So I think so far it has been a success. I think we worked with the City, who had a legacy of making a lot of bad decisions and being overly, in my opinion, unfairly criticized. This was a huge step of several steps – we successfully avoided bankruptcy. We've actually paid off $36 million in internal loans. We've started to fund a reserve fund. Our credit ratings are starting to improve.

This was the start of an overall process that lifted Fresno from really almost the depth of bankruptcy into – we have our head above water and we have a ways to go. And I think this would serve other cities well who have been in similar circumstances in California. You mentioned other cities like Vallejo and Stockton and others, and San Bernardino who had filed bankruptcy. And I know in part it wasn't just labor contracts. It was excessive bond debt. I think in the case of Stockton it was under the pension obligation bond where they really rolled the dice and came out wrong in the deal. So I want to thank everybody that was part of the team who did that and pass onto Phil Hardcastle for the rest of our portion.

PHIL HARDCASTLE: Thank you, this is Phil Hardcastle. And as Councilmember Brand had stated, we as the City had gotten in such a habit of issuing debt. I was sitting here listening and put down some information just to get some perspective. I have been administering the debt since 1999 here at the City of Fresno. And when I first took over the debt, our total outstanding debt was $760 million citywide. That included over half of that being enterprise revenue bonds. But within the first ten years of my career here, we had issued enough debt to surpass the $1 billion mark for the first time in the City's history. And that was troubling for me because it was growing so quickly in a time where the economy was doing well, but anybody with a financial background and understanding of economics knows that the level of economic improvement over the course of the decade of the 2000s was not sustainable. And at some point it would have to level off.

Of course, none of us would have ever thought that it would level off and turn around to the level that it did in 2008 through 2010. But at the same time, we got ourselves into such a financial situation that as long as things were going fine or going as good as they were, we would be doing fine. But we knew in the finance department that that was not sustainable and were trying to rein in on that and were not having a whole lot of success. So what we did was, we had asked for a debt policy, which we were not able to get until Councilmember Brand had come into the picture, and we are very grateful for his lead in this task because I don't think we would have a debt policy today if it weren't for his efforts.

Slides 33-36 skipped

Slide 37 – Brief Overview of Policy (01:25:25)

PHIL HARDCASTLE: That said our debt policy covers several different things. It covers the legal restrictions. And one of the things that I think would be great for the group to know is that he had mentioned the only legal restriction that we had was a charter section that said that we could not exceed general obligation debt – that's voter-approved debt – of more than five percent of our assessed valuation of the City of Fresno. I did that calculation when I first came in and realized that is just an absolutely ridiculous goal to shoot for because at that time, back I think in 2000, that equated to over $3 billion of voter-approved debt, and we don't have any voter-approved debt. All of our debt is lease revenue bonds and enterprise revenue bonds. So it was a ludicrous amount. And when I started looking at our financials I knew there was no way the City could afford that level of debt. So there had to be something else to rein in. So the legal restrictions, although are important, are stated in our legal documentation, but they were minor with respect to the debt policy because there was no way to achieve that level anyway.

But what was really the contributing factor and what I felt was the best purpose of the debt policy was to rein in on the financial restrictions. What could the city afford? Too many times I had council members and other staff members come to me and say, “What is our debt limit?” Well, it depends on what bond you are issuing or what department you were issuing for. There was no limit. So this provides us with a financial restriction that keeps us well within our means. So I think it is a great tool for that.

It also defines our internal standards. The reasons why we have a debt policy, our objectives and things like that. The types of debt instruments that are available to us, the relationship to our capital improvement program. Basically, what can we reasonably expect to finance versus what can we reasonably expect to pay as we go. Those types of things are built into our debt policy and help us to make the decisions more ready available.

Economic development and revenue streams were a critical factor in determining whether we can afford to issue new debt or things like that. It also provided us with a documented – although we had an undocumented informal policy as to refinancing and what constituted when we could refinance – this actually formalized those restrictions into the document so that, as Susan pointed out in her presentation, so that our successors have an idea of what is going in. When I took over the debt in 1998, I had nobody to teach me how to do this, and I came in not knowing anything about debt issuance. So I had to learn as I went, and I don't want my successor to have to do that. I want them to have the resources to carry on as if I wasn't there.

Slide 38 – Brief Overview of Policy *(continued)* (01:29:10)

PHIL HARDCASTLE: So we structured our practices, how we do things, we actually documented those in the debt policy so that it would help us out; Created maximums so that we could stay under the threshold of our financial limits and be able to do things. Unfortunately, this was all adopted after the spending spree, as David so aptly put it, in the decade of the 2000s. So we have had some catch-up to do over the last few years. And fortunately for us we have not issued any debt. And so as I said, our outstanding debt that surpassed $1 billion back in 2008 is now back down to just a little bit over $800,000, which is a lot more manageable and our city is much doing better financially than we were between 2009 and 2012.

Slide 39 – Brief Overview of Policy *(continued)* (01:30:30)

PHIL HARDCASTLE: So the policies that we put in place help us to be able to stay under control. And so that's pretty much all I had to say. Thank you for participating and allowing me to participate.

DAVID BRODSLY: Thanks, Phil and Lee. It has been an interesting experience and interesting ride and I think it goes back to Susan's statement about being able to say no. And I know that the City attempted to get interest in a debt policy, but that was inconvenient to the politics at the time. So I think you guys really are a poster child of recovery in a way that did not make it into the newspapers. So kudos there.

Slide 40 – School Services of California Inc. (01:31:10)

DAVID BRODSLY: We are going to move on to talk a little bit about schools. And to do that we are going to hear from Ron Bennett, who is the CEO of School Services California (SSC). SSC serves as a business financial management and advocacy resource for educational agencies in California. They are a tremendous resource both to the school district community and to folks like my firm in working in the industry and trying to follow the business of running schools. Before Ron took over SSC in 1999, he was a chief business officer at several school districts in Southern California.

And, Ron, I'm going to start you off with a question which is a little bit out of order, but somebody asked if the CSBA (California School Boards Association) or anybody else was formulating sample board policies on the subject of debt management. As the CDIAC study reported, this is an area where the number of debt management policies are pretty limited, and my guess is that what is necessary for the multibillion dollar issuing LAUSD (Los Angeles Unified School District) may not be so on point for the smaller school districts. So with that Ron, I will hand it over to you and you can take it away.

Slide 41 – Why School Agencies Should Have Debt Policies? (01:32:29)

RON BENNETT: Thanks very much, David. There's an advantage and disadvantage to going last. Going last means you are going to have to get to the point before you run out of time, and I will do that. And it also means that when we condense our message, I'm really going to condense it down into two pieces. One is we see that school districts didn't score very well. And I'm going to talk about why in the past school districts were likely to not score very well in their debt policies. CSBA, the California School Boards Association, has lots of policies. They have a system they call Gamut that has hundreds of policies. I'm not aware that any of them that would qualify for the standards that I would say are necessary for a debt management policy.

So at the end of this discussion David and I are going to make a little commitment to all of you. But before we do that, let me get to kind of how we got here. So over the past 40 years, school districts have received money under a revenue limit that has virtually nothing to do with their tax collections or their debt obligations. They receive the money in advance of when they needed it in most years until the recession, where all of a sudden money was being slowed down from the state. They received a large portion of their capital funds from statewide bonds. Nobody does statewide bonds to put in local city parks, but they do them for school districts and for building high schools and other grade levels of schools.

So school districts have been the beneficiary of early receipt of their cash for the operating budget and a lot of their capital needs being covered by the State. All of those things have changed now. And over the past seven years, the school districts have found that when the state was delaying the receipt of their operating budget, they had to go to the markets for short-term debt. When the state stopped issuing statewide school bonds, they had to go to the longer-term markets and conduct local elections and pass bonds. And we are going to talk about this. If we can go to the next slide.

Slide 42 – Why School Agencies Should Have Debt Policies? *(continued)* (01:34:57)

RON BENNETT: We have debt policies now that I think have to be considered differently than they have been considered over the last 40 years. And I think that the involvement of CDIAC has brought that to a fine point in my mind. And we work with every school district in the state virtually every community college district. And we are going to be pushing hard. And we also write policies for CSBA. So we will be pushing hard to make this a featured issue.

The time you want to do that is not when you are in the heat of battle in issuing debt. You want to do it during a time when you can consider the policies carefully, take advantage of the work that has already been done by the people on this call and others. The debt advisory commission has already given us a lot of information about why we need this. I'm not going to repeat that. But if we are going to make good capital funding decisions, we need to adopt best practices and you're hearing some of those today. We can go to the next slide.

Slide 43 – Future Needs for Borrowing (01:35:57)

RON BENNETT: When the budgets got cut, all of a sudden we are going to short-term markets, when the bonds stopped we're going into long-term markets. We will see more of that, not less, in the future. Los Angeles Unified is a multi-billion-dollar organization. They are going to the markets all the time. Necessarily, they have very good policies. And Megan Riley is very, very good, very seasoned and knows about debt management policy, knows how important they are, and she's put that in place in Los Angeles Unified. Not everybody goes to the markets as often as they do, not everybody has the variety of debt, but all of us should have the same principles that we use when we issue debt and when we consider debt.

What we think about debt is a lot different than how we think about. How we think about it is what belongs in the policy. And so I think over the next few years we're going to need to focus on the policies. Next slide, please.

Slide 44 – Local School Bonds on the Ballot for November 2014 (01:36:57)

RON BENNETT: So when the state stopped issuing long-term bonds, all of a sudden we have school districts that are going out to the local bond market. And at an eight-three percent pass rate in 2012, local school districts put out $15.3 billion of debt for capital facilities. That is a very high pass rate even during the middle of a recession. Voters were still voting for schools for their kids. So, next slide.

Slide 45 – Local School Bonds on the Ballot for November 2014 (continued) (01:37:28)

RON BENNETT: On the '14 election two weeks from now, 2014 election, we have another $11.5 billion. One hundred and thirteen school agencies that are asking voters to approve $11.5 billion. I say the over-and-under is $10 billion. We are likely to get about $10 billion in approvals. So that's $10 billion in school facilities money that districts will be going to the capital markets for. This is a time for them to have good policies. Most of them don't have good policies. I've explained why they thought it was less important in the past. I certainly thought it was less important when I was in the school district, and I was getting the money in advance for my needs from somebody else. But we are not getting it in advance of our needs now. And we are not going to get it from somebody else. We are going to have to be as good as cities and counties and Los Angeles Unified and other agencies that go to the market regularly. Next slide, please.

Slide 46 – Now is the Time to Review Debt Policies (01:38:25)

RON BENNETT: We are going to be recommending that school districts do use this calm before the next storm to get their debt house in order. I think that the development of a policy often leads to refundings and the leveling of debt, and the discovery of some bad policies in the past that have come together in a conglomeration that hurts for the future--and, a need to restructure some of the debt. So, just the act of looking at the policy, I think will help some districts to manage better. David, do you want to talk a little bit about our commitment or would you like me to do it?

DAVID BRODSLY: Why don't you start and then I will finish and make that the wrap.

RON BENNETT: Okay, so David and I have talked about KNN and School Services, since we have access to so much knowledge, and so many districts doing a template that would serve as a starting point. And as was pointed out earlier, you cannot go buy a policy. It has to be developed for your agency; it has to be customized for your agency. But we can give you a template that conforms with the GFOA standards that gets you started for the kinds of things that you should think about in your policy. And as you develop it, you may put high emphasis on some and lower emphasis on others, but we will give you the elements that we think you need to work with.

David, that concludes my presentation, do you want to do the wrap and maybe talk a lit bit more about the template?

Slide 47 – Questions (01:39:56)

DAVID BRODSLY: Sure, thanks. While we were working on this presentation, it was really clear there was this need. And we got a question through the webinar site about-- what does a small district do that has one business officer? How are they supposed to handle this? And I think that's a real challenge. So seems like there is a void there. And Ron and I are willing to step up and try to at least get the ball rolling in a direction.

One thing I would say is that if you're a small district and you haven't done a bond issue, maybe the time to finish the policy is when you start working on the bond issue. Though I would do it early in the process before you go to the voters so that you incorporate in the policy the planning, and that dialogue will help you do better planning and bring a more coherent measure to the bondholders and position you that if you get approved for a bond issue, you are not making promises that you subsequently can't keep, which has been a problem with a number of school districts that had tax rate expectations that for a variety of reasons they were unable to keep.

With that, I don't think I have any more questions. And I know we are at the time of cutoff. There was one more question that was to go to the group, and I don't know if the folks in CDIAC want to send that out. There they go. So the final question is: Now that you have participated in the webinar, are you motivated to review the best practices to develop and improve your policy? And you can do your vote. I feel like I should be humming the Jeopardy theme during this, but that would be cruel and unusual punishment. And oh, good, well thank you. That means this seems to have been worth not only the investment of the people on the panel but hopefully for the people who are on the phone. And thanks to CDIAC for creating this conversation, which I don't think I have ever heard such a thorough job of exploring in my career. And with they will hand it back to Mark.

Slide 48 – Thank You for Your Participation (01:42:30)

MARK CAMPBELL: David, thank you very much for facilitating our discussion. And I want to thank all of the speakers for their participation. I think it goes without saying that along with GFOA, CDIAC absolutely supports the need to undertake the analytic deliberative process that goes into developing policies with the regard to the use of debt. Whether or not you are a frequent or infrequent issuer that the analysis itself and the guidelines that result help to resolve issues and direct the organization on an ongoing basis. So again, it goes without saying that we encourage the public agencies that are in the debt markets to undertake this process.

We are here to support that effort, and we will continue to try and develop both educational programs and research on the topic of debt policies and hope to contribute to your efforts to develop them. Again, thank you for participating. Thank you to all the speakers. Please look forward to our next educational program, which will be sometime in the spring. All right. Continue to monitor our website and look for our List-Serv notifications on our education programs. And, again, thank you and have a good day.