

**CDIAC**

**CALIFORNIA  
DEBT AND  
INVESTMENT  
ADVISORY  
COMMISSION**

# **DEVELOPING AND ADMINISTERING INTERNAL CONTROLS FOR BOND ACCOUNTABILITY**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Speaker Panel

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Julia Cooper, Director of Finance, City of San Jose

Sharon Erickson, City Auditor, City of San Jose

Susan Goodison, Business Services Manager, Department of  
Utilities, City of Sacramento

Scott Johnson, CPA, CGMA, Partner, State & Local  
Government Advisory Services, MGO

Nadia Sesay, Director, Office of Public Finance, Controller's  
Office, City and County of San Francisco

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# **INTERNAL CONTROLS FRAMEWORK**

**PART ONE:  
DEVELOPING THE CONTROL ENVIRONMENT AND RISK ASSESSMENT**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Session One Overview

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- The Control Environment
- Risk Assessment
- Pre-Issuance Process
- Policies, Practices & Procedures
- Disbursement of Bond Proceeds
- Construction and Expenditures
- Auditing the Internal Controls
- Testing Compliance with Bond Documents

# The Control Environment

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- Identify agency/division responsible for issuance and management of debt
  - Appropriate staffing levels
  - Qualified staff
  - On-going training
- Identify roles and responsibilities of internal participants in debt management
  - Issuing agency: Public Finance
  - Sponsor department: Public Works, Recreation & Parks, Public Health, Fire, etc.
  - Account set-up: Accounting Operations and Systems Division
  - Budgeting: Mayor's Budget Office and Budget and Analysis Division in Controller's Office
  - Independent legislative analysis: Budget Analyst to the Board of Supervisors

# The Control Environment

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- Identify oversight bodies/committees
  - Board of Supervisors
    - Legislative approval and oversight
    - Bond Accountability Reporting
  - Capital Planning Committee
    - Responsible for planning and project approval
    - Review of all long-term financing for proposed capital improvements
    - Ongoing project status updates
  - General Obligation Bond Oversight Committee
    - 0.1% of par issued from general obligation bonds allocated to oversight committee
    - Pre-issuance accountability reporting
    - Quarterly reporting of bond programs on issuances and spending
  - Commissions
    - Legislative approval and oversight

# The Control Environment

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- Identify/Establish existing policies/procedures/plans/practices
  - ▣ Debt Policy
  - ▣ Disclosure Policies and Procedures
  - ▣ Commercial Paper Policies and Procedures
  - ▣ Internal Control Activities and Best Practices for Disbursement
  - ▣ Financial Policies
  - ▣ Ten-Year Capital Plan
  - ▣ Five-Year Financial Plan (Citywide)
  - ▣ Five-Year Strategic Plan (Department specific)
- Identify all reporting requirements
  - ▣ Noticing requirements pursuant to Continuing Disclosure Certificate
  - ▣ Annual filings pursuant to Continuing Disclosure Certificate
  - ▣ Annual and ongoing reporting pursuant to voter approved bond measures
  - ▣ Annual certifications pursuant to bond covenants
  - ▣ Annual arbitrage calculation

# The Control Environment

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- Identify quantifiable measures and performance evaluation; semi-annual reporting
  - Set specific targets for:
    - Timeliness of disclosure and noticing
    - Debt service payments
    - Turnaround time of paying invoices
    - Due diligence: frequency
    - Staff and stakeholder training
    - Credit rating management
    - Refunding
    - IRS reporting
    - Updates to existing policies

# Risk Assessment: Debt Management Objectives

- Maintain access to cost-effective to capital markets through prudent debt management policies and practices
- Maintain moderate debt and debt service levels with effective long-term planning and coordination with departments
- Finance significant capital acquisitions or improvements through debt financing and, if cost effective, alternate financing mechanisms such as public/private partnerships
- Structure long-term financings to minimize transaction specific risk and total debt portfolio risk
- Support strong internal controls through support of bond oversight committees
- Maintain good investor relations through the timely dissemination of material financial information
- Maintain the highest practical credit rating to ensure efficient access to capital markets

# Risk Assessment: Debt Program Risks

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- Debt limitations
  - State law, Charter, local policies/practices
- Debt structuring – financing tools
  - Variable rate and derivative products
    - Interest rate risk
    - Counter-party risk
- Use of Bond Proceeds
  - Utilized for the purpose they are authorized
- Tax compliance matters
  - Arbitrage rebate requirements
- Fraud
  - Identify who can authorize expenditures

# Pre-Issuance

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- Prior to issuance, work with sponsor departments for project diligence:
  - Project information checklist
    - Project detail, schedule, sources and uses, etc.
  - Tax questionnaire
    - Help determine the nature of the project for any potential tax issues
  - Requisition controls
    - Encumbrance and expenditure schedules to determine timing of when bond proceeds are needed and timing of issuance
  - Preliminary typical financing schedule
    - To manage expectations of the process and schedule of a typical financing

# Pre-Issuance: Sample Debt Issuance Checklist

**Debt Issuance – Project Information Department Checklist**

Status	Description	Purpose(s)	Status	Description	Purpose(s)	Status	Description	Purpose(s)
	1. Project descriptions			e. Identification of completed and uncompleted project line items.		<input type="checkbox"/>	c. "Preferential Rights" Describe any use of the projects or the services of the projects by a non-governmental entity during the term of the bonds pursuant to any contract or other arrangement.	
<input type="checkbox"/>	a. Project description <ul style="list-style-type: none"> <li>i. project name</li> <li>ii. location/supervisory district</li> <li>iii. owner (City, hopefully)</li> <li>iv. address</li> <li>v. date of original construction</li> <li>vi. levels</li> <li>vii. size (sq. ft)</li> <li>viii. expected substantial completion date</li> <li>ix. expected final completion &amp; use/occupancy date</li> </ul>	Authorizing resolution & ordinances, staff reports, offering documents, financing structure, tax due diligence, title & property insurance		f. The status of each uncompleted project line item.		<input type="checkbox"/>	f. "Disposition of Property" Describe any intention to sell or dispose of any of the projects during the term of the bonds.	
<input type="checkbox"/>	b. Brief/broad description of existing facility or facilities (if applicable) and proposed improvements and/or replacement facility/facilities			g. Identification of any project line item not included in a proposed expenditure report.		<input type="checkbox"/>	7. Seismic Forms (Attachment 1 – not applicable for general obligation bonds) – also available in Excel	Credit ratings
<input type="checkbox"/>	c. Sources of funds for each named project <ul style="list-style-type: none"> <li>i. prior bond monies</li> <li>ii. federal &amp; state grants &amp; loans</li> <li>iii. dedicated tax revenues historic data</li> <li>iv. other non-City contributions, grants, &amp; loans</li> <li>v. other sources</li> </ul>		<input type="checkbox"/>	h. Identification of any project line item included in a proposed expenditure report for which bond proceeds will not be used.		<input type="checkbox"/>		
<input type="checkbox"/>	d. Uses of funds by project component(s) and aggregate including % of bond proceeds for each activity/phase <ul style="list-style-type: none"> <li>i. acquisition</li> <li>ii. engineering, design &amp; planning</li> <li>iii. construction</li> <li>iv. administrative, overhead, program wide costs</li> <li>v. other</li> </ul>		<input type="checkbox"/>	i. Certification that each project identified is in conformity with the voter authorization.				
<input type="checkbox"/>	e. Estimated construction start and completion date by phase and/or project components.		<input type="checkbox"/>	j. An explanation for project line items identified in paragraphs f. and g.				
<input type="checkbox"/>	f. Expenditure/cash flows schedule and reimbursement schedule by project line item		<input type="checkbox"/>	3. Environmental Review <ul style="list-style-type: none"> <li>a. Provide a schedule of milestone dates</li> <li>b. Describe issues, appeals, litigation pending or in process</li> </ul>	Authorizing resolution & ordinances, staff reports, offering documents			
<input type="checkbox"/>	2. Provide any resolutions/ordinances adopted by any oversight Board and/or Commission and any reports recently submitted to GOBOC. For GO Bonds, Bond Accountability Reports should include the following (Art. VIII 2.72 of Administrative Code):	Authorizing resolution & ordinances, staff reports, offering documents	<input type="checkbox"/>	4. Lease – lease back financings – i.e. COPs, LRBs, RBs <ul style="list-style-type: none"> <li>a. Identify existing lease-able assets as collateral</li> <li>b. Location, address, date of original construction, size (sq. ft)</li> <li>c. Determine fair market values (OPF)</li> </ul>	Authorizing resolution & ordinances, financing structure, fund deposits, title & property insurance, rating agencies			
<input type="checkbox"/>	a. A certification from an authorized officer of the governmental entity that the information contained in the accountability report is true and correct.		<input type="checkbox"/>	5. Reimbursements <ul style="list-style-type: none"> <li>a. List and describe any planned reimbursements of prior expenditures with anticipated bond proceeds                             <ul style="list-style-type: none"> <li>i. Type – capital expenditure, costs of issuance, working capital expenditures, grants, loans,</li> <li>ii. Timing of application of reimbursement</li> </ul> </li> </ul>	Authorizing resolution & ordinances, tax disclosures			
<input type="checkbox"/>	b. The cumulative amount of bond proceeds expended on the project and the cumulative amount of bond proceeds available for the project.		<input type="checkbox"/>	6. Tax due diligence items <ul style="list-style-type: none"> <li>a. "Private Use" - Description of any activity relating to the projects constituting a trade or business by persons or entities other than governmental entities. For example, leasing of a portion of a bond financed project to non-governmental entities including federal government and 501(c)3 organizations (cafeterias, stores, newsstands, concessions, garages, telecommunication towers, etc.). Include amount and % of the proceeds that will be used as described above.</li> </ul>	Tax disclosures			
<input type="checkbox"/>	c. A brief description of each project line item for which bond proceeds have been expended. Project line items shall be described in the same manner as in any proposed expenditure report or, if no proposed expenditure report was made, in as much detail as practicable.		<input type="checkbox"/>	b. "Private Loan Financing" Describe any bond proceeds and % of proceeds used to make or finance loans to any non-governmental entities.				
<input type="checkbox"/>	d. The amount of bond proceeds expended on each project line item. If applicable, such report shall also include an estimate of the amount of bond proceeds remaining to be spent on each project line item.		<input type="checkbox"/>	c. "Disproportionate or Unrelated Use" Describe of any bond proceeds and % of proceeds used for an unrelated governmental use.				
			<input type="checkbox"/>	d. "Management and Service Contracts" – Description of any contract to use, operate, manage or provide any exclusive services for any bond financed project or portion of any project.				

# Pre-Issuance

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- Work with sponsor department early in project development to identify potential issues early and work through them
- Helps determine scope of project and financing timeline
- If GO bonds, these meetings help define the project placed on the ballot
- Capital planning policies have been established from these meetings

# Policies, Practices & Procedures

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- Detailed Debt Policy
  - Specific parameters for use of various bond types, terms, disclosure reporting, administration of debt-related payments, arbitrage compliance, record keeping and training
  - Approval process
  
- Annual alignment of Debt Policy with departmental strategic planning framework
  - Integrating debt management into the larger mission of the department
  
- Develop clear set of internal controls

# Policies, Practices & Procedures

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- Coordination & Communication
  - Educating decision-makers and stakeholders
    - Trainings, Workshops, Brown Bag Lunches scheduled in partnership with other departments
    - Regularly scheduled working groups on debt-related issues
  
- Composition of finance team
  - Financial advisory, bond counsel, tax counsel, and disclosure counsel included on every transaction to supplement and backstop City's finance and legal staff

# Policies, Practices & Procedures

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- Disclosure Working Group
  - ▣ Engage outside disclosure counsel
  - ▣ Regularly scheduled meeting with City officials to update the City's organization and finances for inclusion in the Official Statement and perform due diligence – includes budget, property taxation, other City tax revenues, debt obligations, etc.
  - ▣ Review of compliance with continuing disclosure obligations
  
- Rating Agency Outreach
  - ▣ Annual in-person meetings with rating agencies and semi-annual updates upon release of financial and budgetary reports to ensure clear communication of City financial information

# Disbursement of Bond Proceeds

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## □ Preventive Controls

### ■ Documentation – Segregation of Duties

- Designate individuals with authority to initiate, submit, reconcile, view or approve different types of transactions
  - At a minimum 2 designees
  - Maintain signature cards at the city level and update from time to time
- Designate a point person for processing transactions
- Institute timely authorizations and processing of transaction
- Conduct periodic staff-level trainings for individuals in oversight and internal control functions

# Disbursement of Bond Proceeds

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## □ Preventive Controls

### ■ Format of source documents

- Establish standard forms or templates
- Establish internal tracking record of activities including but not limited to date, amount, payee information, tracking/transaction number
- Establish red flag exception reporting
  - Significant errors and discrepancies
  - Payee information varies from the pre-authorized payee information

# Disbursement of Bond Proceeds

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- Detective/Corrective Controls
  - Accuracy of activities
    - Verify that transactions and activities are for the correct purpose and amount, and allowable
    - Verify recording of transactions in a timely manner
    - Establish consistent reconciliation processes
    - Make cash confirmations part of the post-audit and/or financial audit, prepared-by-client procedures
    - Timely preparation of annual review of process narratives and cash confirmation reporting to external auditors or internal auditors
    - Maintain proper documentation for purposes of the annual audit process by the City's external auditor pursuant to City Charter and CA Government Code.

# Disbursement of Bond Proceeds

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- Resolution of errors and discrepancies
  - ▣ Notify interested parties on extent of error and/or discrepancy
  - ▣ Establish expectations for timeliness of error correction or recovery of unallowable funds disbursed

# Construction and Expenditures

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- Bond Accountability Reporting
  - Finance staff and legal counsel participation in project development process, review of expenditure plans
    - Documentation before issuance allows for accountability post-issuance
- Maintain records identifying the assets or portion of assets that are being financed
- Consult with Bond Counsel and other legal counsel in the review of any contracts or arrangements
- Maintain records for any contracts or arrangements
- Conduct site visits and document results

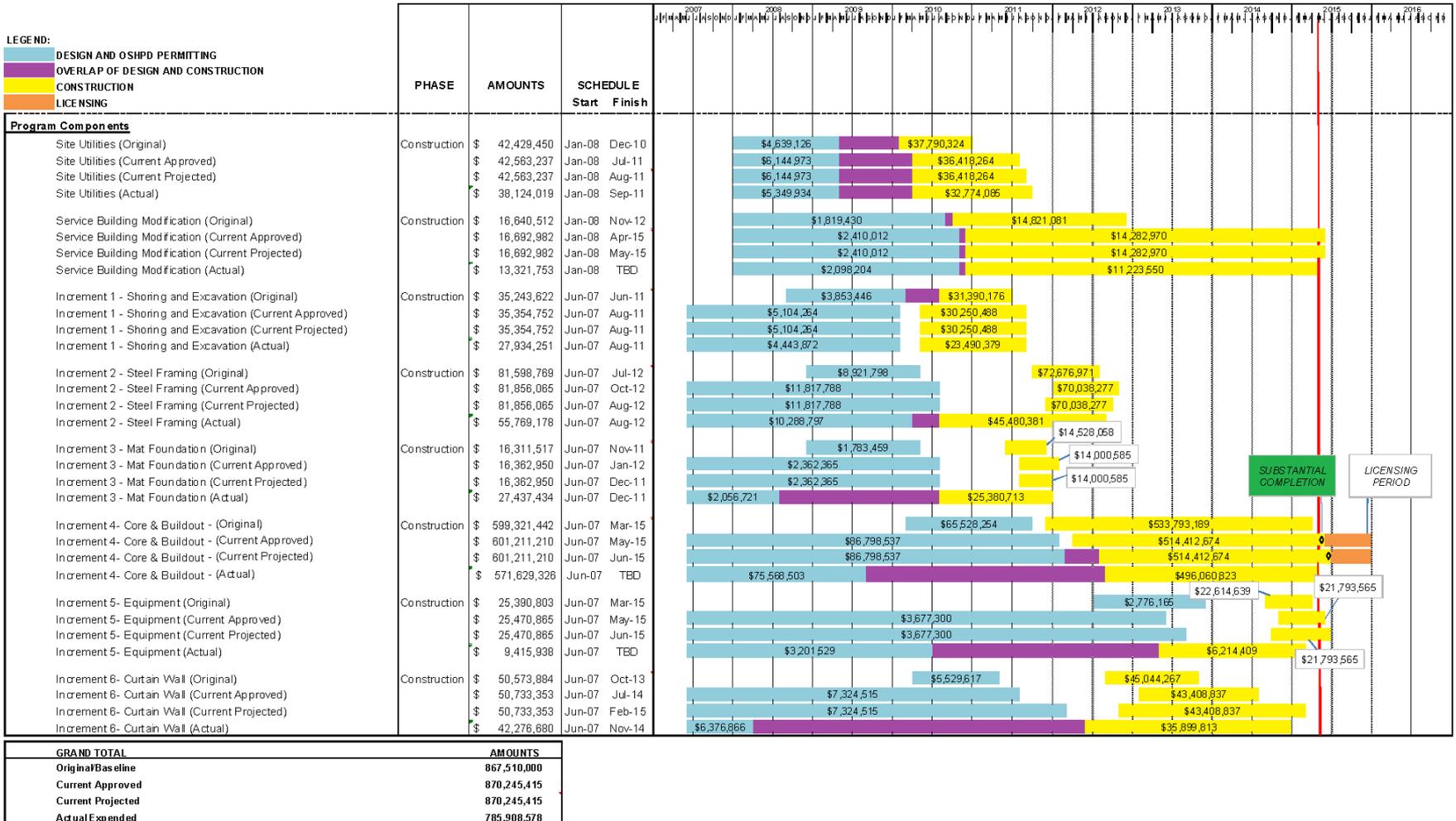
# Construction and Expenditures

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- Require regular budget and schedule progress updates built into debt management process
  - Finance staff coordinate regularly with project managers to track the status of debt-funded projects, both for accountability as well as planning
- Periodic status reporting to oversight committee
  - Expected versus actual expenditures
  - Expected versus actual encumbrances
  - Expected versus current status of project budget and schedule
  - Reasons for delay and related mitigation strategies

# Construction and Expenditures: Sample Project Progress Monitoring

## PROGRAM TIMELINE AND SCHEDULE



# Auditing the Internal Controls

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- Periodic review of internal controls
- On going monitoring of the effectiveness of internal control
- Effective information and communication
- Frequent evaluation that internal controls are performed
- Mandatory staff training

# Testing Compliance with Bond Documents

- Integrate compliance into performance measures and performance evaluations
- Integrate as part of policies, procedures, practices, etc.
- Consult with bond counsel and other legal counsel and advisors following issuance of bonds to ensure that all applicable post issuance requirements are in fact met
- Maintain records, including but not limited to material documents relating to capital expenditures financed, construction contracts, invoices, payment records, assets or portion of assets financed, etc.
- Confer at least annually with personnel responsible of bond-financed project to ensure uses are consistent with all covenants and restrictions

# QUESTIONS

# BREAK

We will reconvene at 10:00 AM

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# **INTERNAL CONTROLS FRAMEWORK**

**PART TWO:  
DEVELOPING CONTROL ACTIVITIES, INFORMATION AND  
COMMUNICATIONS, AND MONITORING**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Session Two Overview

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- Control Activities
  - ▣ Objectives
  - ▣ Examples – Bond Reporting & Closeout Phase
  - ▣ Single Issuer v. Conduit Issuer
  
- Information and Communication
  - ▣ Internal Staff
  - ▣ External Audiences
  - ▣ Options for Dissemination of Information
  
- Monitoring
  - ▣ Annual Audits
  - ▣ Whistleblower Hotline

# Control Activities

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- Recommended practices to help account for, manage and safeguard bond funds
- Policies, procedures, and practices to ensure management objectives are achieved
- Mitigate assessed risk
- Provide reasonable assurance agency will meet objectives of their bond program
- Same system of controls as applies to all other governmental funds

# Control Activities Examples

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- Development of bond closing procedures
- Select Trustee for custody and control of bond funds
- Select compliance staff
- Establish procedures for ongoing bond administration activities
- Establish target dates/deadlines for closing down the bond program
- Determine disposition of remaining bond funds
- Conduct and document final inspection/closeout of the projects

# Control Activities

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- What is meant by a conduit issuer?
- Internal control obligations for conduit borrowers
  - Conduit borrower responsible for ensuring internal controls over bond disbursements
  - Conduit borrower ensures access to financial information
  - May include fund account statements to track payments, balances and cash flows
  - City of Sacramento Utilities as example of “conduit” issuer

# Information & Communication

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- Internal Staff
  - Tone at the top critical to meaningful program
  - Train agency board members, management and staff responsible for administration and compliance
  - May require documented completion of biennial ethics training
  - Develop annual checklist to determine compliance obligations

# Information & Communication

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- Internal Staff cont'd.
  - Resources for bond issuance and administration training
    - CDIAC Seminars
    - GFOA Trainings
    - Bond Buyer Conferences
    - Disclosure Counsel
    - State of CA Ethics Training
    - CA Debt Primer

# Information & Communication

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- Internal Staff cont'd.
  - Establish fund and account structure to record and report use of proceeds
  - Establish process to periodically evaluate changed risks, legislative or legal actions or events requiring changes to control system
  - Ensure process in place to communicate to responsible staff changes in reporting, disclosure or other requirements

# Information & Communication

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- External Audiences
  - Establish accountability and level of trust with public and interested parties
  - Annual reports
    - Highlight purpose and use of proceeds
    - Provide milestones of success toward meeting objectives
    - Account for bond expenditures
    - Provide status of bond funds

# Information and Communication

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- To be effective, information needs to be reliable and timely
- Options for Dissemination of Information
  - Presentation at governing body meeting
  - Posting on dedicated website
    - Creatively display bond program accomplishments
    - Establish deadlines for periodic reporting and updating
    - Be cognizant of securities laws governing disclosure
  - Electronic delivery of FAQ's focused on bond program information

# Monitoring

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- Provide reasonable assurance bond proceeds used for legal and intended purposes
- Provide reasonable assurance bond funds are properly accounted for, managed and safeguarded
- Perform annual audits designed to ensure compliance with legal requirements, best practices and internal controls
- Monitoring of conduit financings requires testing of control functions of the conduit borrower

# Monitoring

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- Establish Whistleblower or Fraud Hotlines
  - Website or Telephonic
  - Anonymous tips provide another layer of oversight
  
- Monitoring of conduit financings should include provision of whistleblower or fraud hotlines for the conduit borrower

# Control Activities in Practice

## City of Sacramento

Pre-Issuance	Project Expenditure Period	Post Expenditure Period
<b>Adoption of Rate Proposal</b> <ul style="list-style-type: none"> <li>Capital plan</li> <li>Financing plan</li> <li>City Council</li> <li>URAC</li> </ul>	<b>Accountability Updates</b> <ul style="list-style-type: none"> <li>URAC</li> <li>Council</li> </ul>	<b>Celebration meeting</b> <ul style="list-style-type: none"> <li>85% 3-year milestone</li> <li>Projects completed</li> </ul>
<b>Bond Resolutions to Council</b> <ul style="list-style-type: none"> <li>Resolution of Intent</li> <li>Authorization to issue</li> </ul>	<b>CIP Dashboard on website</b>	<b>Reports to stakeholder groups</b> <ul style="list-style-type: none"> <li>Expenditure of funds</li> <li>Tax compliance</li> <li>Investment in infrastructure</li> </ul>
<b>CTO Leads Financing Team</b> <ul style="list-style-type: none"> <li>DOU</li> <li>Finance</li> <li>CAO</li> <li>External Team Members</li> </ul>	<b>Budget to actual monitoring for proposed expenditures</b> <ul style="list-style-type: none"> <li>DOU</li> <li>Finance</li> <li>CTO                             <ul style="list-style-type: none"> <li>Eligible expenditures</li> <li>Tracking for tax counsel</li> <li>Multiple levels of approval prior to release of funds</li> </ul> </li> </ul>	<b>Bond administration</b> <ul style="list-style-type: none"> <li>DOU working with CTO                             <ul style="list-style-type: none"> <li>Re: debt service payments</li> </ul> </li> <li>Continuing disclosure filings</li> <li>Ratings surveillance</li> </ul>
<b>Accountability updates to URAC &amp; Council</b> <ul style="list-style-type: none"> <li>Plan of finance</li> <li>Capital project dashboards</li> <li>Expected expenditure of funds</li> </ul>	<b>Closing transcript on shared drive</b> <ul style="list-style-type: none"> <li>Creation of calculations to ensure tax compliance (see tax certificate)</li> </ul>	<b>Monitor fraud hotline</b> <ul style="list-style-type: none"> <li>Establishment and communication of whistleblower hotline</li> </ul>
	<b>Focus on 85% expenditure date &amp; progress toward it</b>	<b>Annual monitoring to maintain debt service coverage ratio as covenanted (budget development)</b>
	<b>Continuing Disclosure Agreement &amp; filing</b> <ul style="list-style-type: none"> <li>Work with CTO</li> </ul>	<b>Independent oversight of bond program</b> <ul style="list-style-type: none"> <li>City Council</li> </ul>
	<b>Payment of debt service – departmental budget</b> CTO Works with Trustee Department monitors budget to actual	

# QUESTIONS

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# **ENHANCING AN AGENCY'S INTERNAL CONTROL ACTIVITIES**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Session Three Overview

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- Debt Management Policies
- Internal Controls
- Intersection of Policies, Procedures & Internal Controls
- Training – Post Issuance Compliance
- Continuance Review and Improvement

# Debt Management Policies

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- Government Finance Officers Association of US & Canada (GFOA) important resource for Best Practices across broad spectrum of government financial disciplines (<http://gfoa.org/best-practices>)
- Debt Issuance should be closely integrated with Capital Improvement Plan and Debt Management Policy assists in establishing parameters
- Debt Capacity is finite resource and Debt Management Policy and Capital Improvement Plan assist in managing capacity

# Debt Management Policy Importance

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- Enhances Internal Management Practices
- External Recognition and Transparency
  - ▣ Credit Rating Agencies
  - ▣ Outside Professionals/Public Know Entity's Parameters
- IRS Asking for Policies and Procedures
  - ▣ Investment of Bond Proceeds
  - ▣ Use of Proceeds
- SEC Encouraging Use of Disclosure Policies and Procedures
  - ▣ More Aggressive Stance Over Past Few Years
  - ▣ MCDC Initiative
- Evolving Federal Regulatory Landscape
  - ▣ MA Rule
  - ▣ IRS/Issue Price Regulations

# Basics of a Debt Management Policy

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- Authority to Issue Debt – Who Are You?
- When Debt May be Used to Finance Capital Projects
  - ▣ Including Use of P3s and TIFs
- Entity's Debt Limits/Debt Capacity
- Types of Debt Allowed to Be Issued
  - ▣ General Obligation
  - ▣ Revenue
  - ▣ Taxable (including tax-credit, subsidy)
  - ▣ Fixed or Variable Rate
  - ▣ Other Products: POB, OPEB, Derivatives, Notes and Loans
  - ▣ Refundings (current and advanced)

# Basics of a Debt Management Policy

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- Structuring Debt
- Hiring, Scope of Services, and Fee Structures for Outside Professionals
- Method of Sale
- Bond Ratings and Enhancements
- Pricing Evaluation
- Investment of Bond Proceeds
- Compliance with Federal Tax & Securities Laws
  - Disclosure, Including Posting Information on EMMA
  - Arbitrage

# Implementing Debt Management Policy

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- Development by Team (with a leader!)
- Internal/Staff Sign Off
- Approval From Governing Body
- Disseminating to Team (internal and external)
- Compliance Procedures
  - ▣ Are We Doing What We Said We'd Do?
  - ▣ Developing Checklists to Ensure Compliance
- Schedule to Review and if Needed, Revise

# Other Debt Policy Observations

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- Look at Peer Entities
- Develop Section by Section
- Know Which Issues are More Static and Others That Are More Dynamic, and Don't be Afraid to Revise
- Stay Alert for Changing State and Federal Laws and Regulations
- Help Those That Come After You!
  - ▣ Professional Staff
  - ▣ Elected Officials

# Internal Controls

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- Voter approved bond measures frequently include “bond oversight committees”
  - ▣ Citizen oversight
  - ▣ Roles and responsibilities often left to local agency to define after bond sale
- San Jose – three voter authorized GO bonds subject to annual independent audit and citizen’s oversight committee
  - ▣ Parks - <http://www.sanjoseca.gov/DocumentCenter/View/62636>
  - ▣ Library - <http://www.sanjoseca.gov/DocumentCenter/View/62635>
  - ▣ Public Safety - <http://www.sanjoseca.gov/DocumentCenter/View/62628>

# Sample Ballot Language

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## **SAN JOSE NEIGHBORHOOD LIBRARIES BOND**

*To improve San Jose's neighborhood libraries and expand literacy and learning opportunities for children, families and seniors by: expanding and improving aging branch libraries to reduce noise, add parking, and add space for more books and computers; and building new libraries in neighborhoods throughout the City, shall the City issue \$211,790,000 in bonds, at the best .rates possible, with **guaranteed annual audits, a citizen's oversight committee**<sup>\*</sup>, and no money for library administrators' salaries?*

*<sup>\*</sup>emphasis added*

# Internal Controls

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- Public Works Department – generally responsible for bidding, awarding and management of construction project
- “User” Department, i.e. Library may be charged with review of bond expenditures within guidelines of permitted expenditures and project delivery
- Finance Department/Accounts Payable responsible for payment of invoices
- Finance Department/Debt Management responsible for review of requisitions of reimbursement of project expenditures from bond proceeds

# External Controls

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- Annual Independent Financial Audit
- Specific Independent Financial Audit and report of the bond expenditures
- Citizen's Oversight Committee review of Annual Independent Audit and expenditure/delivery of public projects/facilities

# Intersection of Policies, Procedures and Internal Controls

- GFOA Best Practices in Accounting & Financial Reporting provide guidance for managing government agency's day-to-day payment processing and financial reporting
- Bond proceeds change the “character” of the funds given the additional accounting/restrictions associated with tax-exempt funds
- No change in fundamentals of good internal controls
- Added controls associated with tax-exempt bonds and voter approval requirements for review of expenditures

# Training for Post Issuance Compliance

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- Contract Management
- Budget Actions
- Post-Issuance Compliance
  - Tax Law Requirements
  - Disclosure Requirements
  - Bond Covenants and Agreements
- Disbursement of Bond Proceeds
- Investment of Bond Proceeds
- Facility Use Monitoring

# Training for Post Issuance Compliance – Contract Management

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- Consultants and Service Providers
  - ▣ Establish contract procedures
  - ▣ Track payments and encumbrances
  - ▣ Contract payment process

# Training for Post Issuance Compliance – Budgeting for Debt Service Payments

- Annual budget actions necessary to appropriate debt service and related payments
  - ▣ Who in your organization is responsible for debt service payment activities?
  - ▣ How are reserve fund earnings treated?
  - ▣ How are you going to annually “clean out” your debt service payment funds
- Require Trustee/Fiscal Agent to send debt service invoice
- Ensure sufficient time for internal wire/check processing
- Work with investment/cash management staff, debt service critical component of any cash flow analysis

# Training for Post-Compliance – Budgeting for Variable Rate Debt

- Objective: minimize program impact by making a reasonable interest rate assumption
- Create a methodology and use consistently
- Involves a programmatic budgetary trade-offs
- Assume average rate in effect through next budget period and monitor throughout the budget year
- Annual debt service = principal x interest rate
  - Future interest rates are unknown for variable rate debt

# Training for Post Issuance Compliance – Tax Law Compliance

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- Tax Law Requirements
  - ▣ General Matters
  - ▣ Use of Proceeds
  - ▣ Private Activity Bonds
  - ▣ Arbitrage
  - ▣ Pool Bonds
  - ▣ Record Retention

# Training for Post Issuance Compliance – Disclosure Compliance

60

- Disclosure Requirements
  - SEC Rule 15c2-12
  - Use of EMMA mandated since July 1, 2009
  - Notification to Underwriters of Bonds
  - Info Requirements to Other Entities
  - Create universal e-mail address for reporting and noticing  
Example: [debt.management@sanjoseca.gov](mailto:debt.management@sanjoseca.gov)
  
- Miscellaneous Requirements
  - Security
  - Insurance
  - Financial Covenants
  - Transfer of Property
  - Investments
  - Derivatives

# Training for Post Issuance Compliance

## Bond Covenants and Agreements Compliance

61

- For variable rate bonds include credit/liquidity provider administration
- Develop internal tickler system from beginning
- Keep up-to-date
- Don't reinvent the wheel with every deal; similar reporting requirements are okay and always preferred
- Keep as simple as possible
  - ▣ Consider providing multiple parties to deal the same compliance reports

# Training for Post Issuance Compliance – Disbursement of Bond Proceeds

62

- Establish Procedures for Disbursement of Bond Proceeds and Train Staff
  - ▣ Project staff
  - ▣ Finance staff
- Understand eligible expenditures
  - ▣ Working capital limits
  - ▣ Private Activity limits/restrictions
  - ▣ Use of proceeds
  - ▣ Develop procedures for allocation expenditures of bond proceeds to Projects
- Bond Project Monitoring

# Training for Post Issuance Compliance – Investment of Bond Proceeds

- Principals of good investment management and understanding of inherent risks in investing bond proceeds critical
  - ▣ Establish good guidelines for permitted investments to reduce credit risk – **SAFETY**
  - ▣ Good cash flow estimates mitigate market risk – **LIQUIDITY**
  - ▣ Integration of knowledge of expected and future market conditions with other cash flows to reduce opportunity risk – **YIELD**

# Training for Post Issuance Compliance – Investment of Bond Proceeds

- Initial investment – generally “*easier part*”
  - Project cash flows
  - Capitalized Interest
  - Debt Service Reserve Fund
  - Cost of Issuance
- Reinvestment – generally “*really hard part*”
  - Develop process to monitor and make reinvestment decisions
  - Use of cash flow expectations v. reality

# Training for Post Issuance Compliance – Facility/Project Use

65

- Maintain records of facility use
  - ▣ Follow Record Retention Requirements
  
- Review all agreements for facility use
  - ▣ Potential impact on tax-exemption
  
- Everything must be reviewed by bond/tax counsel
  - ▣ Solar panels on roof top or cellular phone receiver on roof top could negatively impact tax-exemption
  - ▣ Operator Agreements for facilities can also impact tax-exemption

# Internal Control Activities

66

- Continual Review
- Updates to Policies and Procedures necessary to reflect changes in federal and state law
- Updates to reflect changes in internal processes and procedures
- Documentation critical in era where
  - ▣ Constrained staffing resources
  - ▣ Staff organizational tenure declining
- Institutional memory needs and must be documented!

## Internal Control System Checklist

The Internal Control System Checklist is a tool to allow public agencies to assess their internal control system for the management of bond funds. For additional information on how to evaluate internal controls, refer to the U.S. Government Accountability Office (GAO) Internal Control Management and Evaluation Tool.<sup>58</sup>

Internal Control Checklist for Bond Requirements		
Task/Deliverable	Completed? ( <input type="checkbox"/> )	Comments/Remarks
<b>Part 1. Control Environment:</b>		
1. Do you have a designated compliance officer? <sup>59</sup> (Identify a compliance officer or establish a compliance team to verify internal controls and bond requirements.)		The designated compliance officer should be a staff person that, with respect to their regular duties, are not responsible for processing invoice payments, but may be a member of the governing body of the public agency.
2. Compliance officer and compliance team members have participated in training on internal control and bond administration requirements.		
3. Establish an inventory of outstanding bonds and obtain or prepare a list of bond requirements, including covenants in the following controlling bond documents: <sup>60</sup> <ul style="list-style-type: none"> <li>a. Indenture</li> <li>b. Loan or Lease Agreement</li> <li>c. Tax Certificate and Continuing Disclosure Agreement</li> </ul>		<i>(Refer to Part 3. Control Activities of this checklist for examples of bond requirements)</i>
4. Establish written procedures for bond administration processes and bond requirements that support the agency's internal control system.		
5. Adopt a debt policy with objectives and		Debt policy and procedures are

<sup>58</sup> This tool can be accessed at <http://www.gao.gov/products/GAO-01-1008G>.

<sup>59</sup> If practicable, an agency may utilize a compliance team that represents a cross-section of bond administration roles and responsibilities throughout its program operations and organizational structure. If a compliance team is utilized, a single point of contact should be identified by the agency to coordinate compliance activities.

<sup>60</sup> A thorough review and understanding of covenants or provisions in controlling bond documents is necessary to prepare a list of bond requirements for compliance purposes. If necessary, an agency should seek advice or assistance from bond counsel and/or a financial advisor regarding the development of its list of bond requirements. Lists of post-issuance requirements for the specific purpose of compliance with federal tax law regarding arbitrage rebate, yield restriction, and private use and legal or regulatory requirements for continuing disclosure are available from the IRS or organizations such as the National Association of Bond Lawyers (NABL) and the Government Finance Officers Association (GFOA).

specifications for bond administration and integrate into the agency's organizational policies, procedures, and long-term plans. <i>(Refer to Part 2. Risk Assessment of this checklist for additional information)</i>		maintained in the agency's policy and procedures manual.
6. Establish an audit committee to review compliance with testing of bond requirements. <sup>61</sup>		<i>(Refer to Part 4. Monitoring of this checklist for additional information on compliance tests for bond requirements)</i>
<b>Part 2. Risk Assessment:</b>		
1. Clearly define the objectives <sup>62</sup> of the bond administration program related to: <ul style="list-style-type: none"> <li>a. Operations (related performance measures are effectiveness and efficiency)</li> <li>b. Reporting (related performance measures are accuracy and precision)</li> <li>c. Compliance</li> </ul>		Objectives are clearly measurable and easily understood at all levels of the agency. Objectives relate to activities within all stages of the debt lifecycle.
2. Include objectives of the bond administration program in a debt policy and integrate risk assessment for all stages of the debt lifecycle into the agency's decision-making and planning process.		The agency's objectives in its strategic plan include elements of bond administration and define strategies the agency uses to manage risk.
3. Establish performance measurements <sup>63</sup> to monitor how successfully the agency achieves its objectives for the bond administration program.		Performance measurements for the bond administration program are defined and included in a strategic plan.
4. Establish risk tolerance relative to each of the objectives of the bond administration program. Risk tolerance is equal to the variation of performance or condition that the agency has determined to be within its risk appetite.		A debt policy defines the level of risk that is deemed reasonable for an agency to accept in the achievement of its objectives (risk appetite) and identifies the conditional elements of the bond administration program that are monitored within the agency's internal control system.
5. Identify and analyze risks (including potential fraud and misuse) related to the objectives		Risk analysis estimates the significance of each risk, assesses

<sup>61</sup> Such tests commonly include procedures that validate statutory authority to borrow, legal requirements of debt sales, tracing authorized debt to accounting records, and confirming compliance with bond documents, covenants, and other legal requirements.

<sup>62</sup> Objectives of the bond administration program may reflect issuer responsibilities specified in controlling bond documents as well as specifications required by laws, regulations, or an agency's policies and procedures.

<sup>63</sup> Performance measurements relate to elements of bond administration objectives and are used to evaluate variances of performance (levels of risk) for each element on a conditional basis, i.e., Is the objective achieved in a manner that is effective, efficient, accurate, precise, or in compliance?

and conditional elements of the bond administration program. (Refer to the Task Force Guidelines in Part 3 – Control Activities for additional information on appropriate responses an agency may deploy to manage risks)		the likelihood of occurrence, and forms the basis for the types of control activities that are used to prevent and detect risks, including remedies that management may use to immediately respond to risk events.
<b>Part 3. Control Activities:</b>		
1. At a minimum, the agency applies the same system of internal control activities to bond funds as it does to all other governmental funds.		Based on bond requirements and risk assessment findings, control activities provide a reasonable assurance of internal control for bond funds applicable to all stages of the debt lifecycle.
2. Review and update inventory of outstanding bonds and related bond requirements.		Review official bond transcripts.
3. Review and update bond administration procedures.		
4. Review and update debt policy for changes to legal requirements, new debt and revised objectives, strategies, and procedures.		The debt policy is reviewed on a periodic basis for approval by the governing body.
5. Confirm compliance with policies, covenants, and bond administration procedures that support the agency's internal control system (all control activities).		All control activities sufficiently evaluate risk factors of fraud and misuse of bond proceeds.
<b>Control Activities for Legal and Financial Requirements:</b>		
6. Confirm legal requirements of debt sales (new issues and refunding transactions) are met.		
<ul style="list-style-type: none"> <li>Receive copies of approvals, authorizations, and controlling bond documents (official bond transcripts) and maintain in a safe and secure but accessible location.</li> </ul>		
<ul style="list-style-type: none"> <li>Monitor/track bond authorizations to debt issuances and refunding transactions.</li> </ul>		Update inventory of outstanding bonds.
<ul style="list-style-type: none"> <li>Bond documents and amendments are appropriately approved pursuant to the agency's administrative or legal policies and procedures.</li> </ul>		
<ul style="list-style-type: none"> <li>Confirm bond projects and related expenditures are consistent with approvals, authorizations, and controlling bond documents.</li> </ul>		Conduct site visits to confirm work is performed as reflected in progress estimates submitted by contractors.

7. Confirm compliance with financial covenants and other restrictions.		
<ul style="list-style-type: none"> <li>Confirm funds and accounts are established in the agency's accounting system to record the receipt of proceeds and account for bonds payable.</li> </ul>		<p>Applies to new issues and refunding transactions at the time of closing. For tax-exempt borrowing, proceeds include investment earnings.</p>
<ul style="list-style-type: none"> <li>Confirm funds and accounts established by the trustee and deposits of bond proceeds reconcile with controlling bond documents.</li> </ul>		
<ul style="list-style-type: none"> <li>Monitor trustee funds and accounts and perform periodic reconciliations of trustee statements with agency records for bond expenditures, including costs of issuance for new issues or refunding transactions.</li> </ul>		<p>Officer certificates or requisitions match trustee records and statement activity.</p>
<ul style="list-style-type: none"> <li>Confirm expenditures for bond proceeds are processed pursuant to appropriate segregation of duties and practicable checks and balances (three-way matching) or, alternatively, by appropriate compensating controls.</li> </ul>		<p>Officer certificates or requisitions have required agency authorizations supported by audit trail documents that support the reconciliation of expenditures with capital budget and agency records.</p>
<ul style="list-style-type: none"> <li>Confirm deposit of funds with trustee for debt service and maintenance of reserve funds or other accounts, including the rebate account and monitor cash flow activity on a periodic basis.</li> </ul>		<p>Confirm any excess funds at the trustee are applied pursuant to the terms of the indenture or other controlling bond document.</p>
<ul style="list-style-type: none"> <li>Confirm trustee is performing compliance activities for financial covenants required by indenture, loan or lease agreements, or other bond documents.</li> </ul>		<p>Trustee is correctly following procedures contained in bond documents including the maintenance of funds and accounts, insurance and credit rating filings, monitoring and adherence to debt coverage ratios and additional bonds tests, distribution of notices and corporate actions, and mandatory or optional redemption instructions.</p>
<ul style="list-style-type: none"> <li>Confirm compliance with debt policy provisions regarding financial performance measurements for conditional elements of the bond administration program. <i>(For</i></li> </ul>		<p>Conditional elements of a debt policy are consistent with the agency's objectives and strategies in the strategic plan or other long-term planning report.</p>

<p><i>examples of conditional elements refer to the GFOA model debt policy at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a></i></p>		
<p><b>Control Activities for Non-Financial Requirements:</b></p>		
<p>8. Confirm compliance with agency oversight requirements for bond administration activities.</p>		
<p>9. Confirm compliance with staffing plans for the bond administration program.</p>		
<p>10. Confirm compliance with agency records retention policy and procedures.</p>		<p>Records retention for bond related material is maintained pursuant to federal treasury regulations and tax law requirements. <i>(Refer to Other Control Activities in this checklist below)</i></p>
<p><b>Other Control Activities:</b></p>		
<p>11. Confirm compliance with tax certificate covenants, i.e., post-issuance tax compliance requirements for bonds. <i>(For detailed information on tax compliance for bonds refer to the IRS Compliance Guide at <a href="http://www.irs.gov/pub/irs-pdf/p4079.pdf">www.irs.gov/pub/irs-pdf/p4079.pdf</a>)</i></p>		<p>Pursuant to IRS guidelines, in order to comply with post-issuance federal tax rules, issuers ensure that the rules are met both at the time the bonds are issued and throughout the term of the bonds.</p>
<ul style="list-style-type: none"> <li>• Do you have a post-issuance tax compliance procedure similar to that referenced in IRS form 8038?</li> </ul>		
<ul style="list-style-type: none"> <li>• Do you have an arbitrage rebate consultant? (Consult with arbitrage rebate consultant and/or bond/tax counsel as necessary to ensure compliance with post-issuance tax requirements for tax-exempt bonds.)</li> </ul>		<p>Implement procedures that will enable adequate safeguards against post-issuance violations that result in loss of the tax-exempt status of bonds.</p>
<ul style="list-style-type: none"> <li>• Maintain copies of filings with the Internal Revenue Service (IRS) for each bond issuance, i.e., Information Return Form 8038-G and arbitrage rebate reports.</li> </ul>		<p>8038-G is included in official bond transcripts.</p>
<ul style="list-style-type: none"> <li>• Confirm due dates for arbitrage rebate and yield restriction filing requirements with the IRS.</li> </ul>		<p>First installment due on fifth bond year of bond issuance plus 60 days. Tax certificate provides the bond year to determining due date for tax filings.</p>
<ul style="list-style-type: none"> <li>• Monitor compliance with expenditure spend-down targets, use of proceeds, private use, and disposition of bond-financed</li> </ul>		<p>Maintain a separate list of compliance requirements for tax compliance and continuing disclosure, i.e., post-issuance</p>

facilities.		requirements for tax-exempt bonds. Request a compliance checklist from consultant or tax counsel or refer to the checklist developed by the National Association of Bond Lawyers (NABL) and the GFOA at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a> .
<ul style="list-style-type: none"> <li>Monitor compliance with records retention requirements for bond related records, pursuant to federal treasury regulations and tax laws.</li> </ul>		
12. Confirm compliance with continuing disclosure agreement covenants, i.e., post-issuance disclosure requirements.		
<ul style="list-style-type: none"> <li>Confirm annual filing on the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Marketplace Access (EMMA) website due dates for annual reports and other financial reports applicable to each outstanding bond issuance.</li> </ul>		Continuing disclosure agreement for bond issue specifies filing due date.
<ul style="list-style-type: none"> <li>Update information in the agency's annual report required by the continuing disclosure agreement for the bond issue and file with EMMA no later than the required due date. If the agency utilizes a dissemination agent to file the annual report with EMMA, the compliance officer should locate the filing on EMMA and confirm the annual report has been filed prior to the due date and verify correct CUSIPs were used in the filing.</li> </ul>		Maintain a separate list of compliance requirements for tax compliance and continuing disclosure, i.e., post-issuance requirements for tax-exempt bonds. Request a compliance checklist from consultant or bond/disclosure counsel or refer to the checklist developed by NABL and the GFOA at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a> .
<ul style="list-style-type: none"> <li>Monitor outstanding debt for events that are listed in the continuing disclosure as a material or listed event and file or arrange to file a notice of material event on EMMA for an occurrence within 10 business days of the event.</li> </ul>		Consult with bond/disclosure counsel as necessary to ensure compliance with post-issuance disclosure requirements
<b>Part 4. Information and Communications:</b>		
1. Establish process to alert personnel to changes in policies and procedures for internal controls and bond requirements.		
2. Establish an official structure of communication within the agency based on roles and responsibilities in the bond		Job descriptions define roles and responsibilities for essential bond administration functions. (Refer to

administration program.		<i>Control Activities for Non-Financial Requirements, Item 9.)</i>
3. Confirm that staff with internal control and/or bond administration responsibilities, including compliance, received or are scheduled to receive periodic training.		
<b>Part 5. Monitoring:</b>		
1. Perform period review of bond activities and report results to the governing body.		
2. Complete Internal Control Checklist and immediately report findings to management.		

# QUESTIONS

# LUNCHEON

We will reconvene at 1:30 PM

**CDIAC**

**CALIFORNIA  
DEBT AND  
INVESTMENT  
ADVISORY  
COMMISSION**

# **A DIVE INTO THE CONTROLLING DOCUMENTS:**

**BOND DOCUMENTS TO BOND ACCOUNTABILITY**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Session 4 Overview

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- Documents Containing Financial, Administrative and Reporting Direction
- Indenture
- Trustee Agreement
- Tax Certificate
- Continuing Disclosure Agreement
- Tying Documents to Procedures

# Documents Containing Financial, Administrative and Reporting Direction

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- Certain bond documents are key to bond administration
- Documents contained in the closing transcript should be a focus pre, during and post issuance
- Documents govern supervising, investing and administering proceeds in compliance with Federal and State laws
- Documents contain requirements for filing required reports with regulators

# Documents Containing Financial, Administrative and Reporting Direction

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- Primary Documents
  - Indenture or Resolution
  - Trustee Agreement
  - Tax Certificate
  - Continuing Disclosure Agreement
  - Agreements with Credit Enhancers
- Other Documents
  - Acquisition or Funding Agreement (Mello-Roos)
  - Loan Agreement (Conduit Issuance)

# Indenture

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- ❑ Establishment of subaccounts
- ❑ Waterfall of revenues and payments
- ❑ Covenant Restrictions
- ❑ Maintenance of Security Interests
- ❑ Compliance and documentation procedures
- ❑ Permitted Investments
- ❑ Requirements for Disbursement of Construction Funds
- ❑ Terms for Trustee to safeguard and administer proceeds

**EXHIBIT B**

**FORM OF SERIES 2013 PROJECT FUND REQUISITION**

**Requisition No.** \_\_\_\_\_

**Series 2013 Project Fund**

The undersigned, hereby certifies as follows:

1. I am [Name], [Title], of the CITY OF SACRAMENTO, a municipal corporation and chartered city duly organized and existing under and by virtue of the Constitution and laws of the State of California (the "City").
2. Pursuant to the provisions of the Indenture, dated as of March 1, 2013 (as supplemented and amended from time to time pursuant to its terms, the "Indenture"), between the City and U.S. Bank National Association, as trustee (the "Trustee"), I am filing this written requisition in the official records of the City on behalf of the City. All capitalized terms used and not otherwise defined herein shall have the meanings assigned to such terms in the Indenture.
3. The undersigned hereby certifies that the City is paying from the Series 2013 Project Fund created pursuant to Section 14.06 of the Indenture the amounts specified in Schedule I hereto to the persons identified in Schedule I.
4. The undersigned, acting on behalf of the City, hereby certifies that (a) obligations in the amounts set forth in Schedule I attached hereto have been incurred by the City and are now due and payable; (b) each item is a proper charge against the Series 2013 Project Fund and has not been previously paid from the Series 2013 Project Fund; and (c) there has not been filed with or served upon the City notice of any lien, right to lien or attachment upon, or claim affecting the right to receive payment of, any of the amounts payable to any of the persons named in the attached Schedule, which has not been released or will not be released simultaneously with the payment of such obligation, other than materialmen's or mechanics' liens accruing by mere operation of law.

Dated: \_\_\_\_\_

CITY OF SACRAMENTO

By: \_\_\_\_\_

# Indenture

SCHEDULE I TO REQUISITION NO. \_\_\_\_\_

<u>Name and Address of Party to be Paid</u>	<u>Payment Amount</u>	<u>Nature of Expenditure</u>	<u>Payment Instructions<sup>1</sup></u>
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<sup>1</sup> Payment instructions to include PO #, voucher #, or journal # effecting requested transaction.

# Indenture

**FORM OF SERIES 2013 PROJECT FUND REQUISITION**

**Requisition No. 66**

**Water Revenue Bond Series 2013 Project Fund**

The undersigned, hereby certifies as follows:

1. I am Susan Goodison, Business and Integrated Planning Division Manager, an Authorized Representative of the CITY OF SACRAMENTO, a municipal corporation and chartered city duly organized and existing under and by virtue of the Constitution and laws of the State of California (the "City").

2. Pursuant to the provisions of the Indenture, dated as of February 1, 2013 (as supplemented and amended from time to time pursuant to its terms, the "Indenture"), between the City and U.S. Bank National Association, as trustee (the "Trustee"), I am delivering this Requisition on behalf of the City. All capitalized terms used and not otherwise defined herein shall have the meanings assigned to such terms in the Indenture.

3. The undersigned hereby certifies that the City is paying from the Series 2013 Project Fund created pursuant to Section 14.06 of the Indenture the amounts specified in Schedule I hereto to the persons identified in Schedule I.

4. The undersigned, acting on behalf of the City, hereby certifies that: (a) obligations in the amounts set forth in Schedule I attached hereto have been incurred by the City or a constituent thereof and are presently due and payable; (b) each item is a proper charge against the Series 2013 Project Fund and has not been previously paid from the Series 2013 Project Fund; and (c) there has not been filed with or served upon the City notice of any lien, right to lien or attachment upon, or claim affecting the right to receive payment of, any of the amounts payable to any of the persons named in the attached Schedule, which has not been released or will not be released simultaneously with the payment of such obligation, other than materialmen's or mechanics' liens accruing by mere operation of law.

Dated: **February 19, 2016**

CITY OF SACRAMENTO

By:   
Authorized Representative

# Indenture

## SCHEDULE I TO REQUISITION NO. 66

### Water Revenue Bonds Series 2013 Project Fund

Vendor Name	Transaction Type		Project No.	Project Name	Payment Amount	Nature of Expenditure
	Acctg Journal No.	Voucher No.				
Omni Means, 943 Reserve Drive, Suite 100, Roseville, CA 95678		V.ID#00794236	Z14010066	E Sac Water Main Rpl Ph2	\$ 13,320.00	On-call master construction management.
Stay Safe Construction & Transport, 3941 Park Drive, Suite 20-297, El Dorado Hills, CA 95762		V.ID#00795241	Z14130203	FWTP HVAC Rehab	\$ 29,550.00	Mobilization, submittals; materials; installation labor; programming; commissioning/startup; closeout.
Teichert Construction, 24207 County Road 100A, Davis, CA 95616		V.ID#00795243	Z14010069	Oak Park & Colonial Manor WMR	\$ 37,058.93	Water service pipe replacement; install new water service. CO#4 - See attached.
Lawson Mechanical Contractors, 6090 South Watt Avenue, Sacramento, CA 95829		V.ID#00795249	Z14130203	FWTP HVAC Rehab	\$ 206,617.98	Design engineering and pre-construction; submittals.
C Overaa & Co, 200 Parr Blvd, Richmond, CA 94801		V.ID#00797462	Z14006000	TP Rehab Design	\$ 1,023,966.80	Sitework; start up and demo; yard piping; site electrical-duct banks; flocc basin; filter complex; high service pump station; plant elec sub station; basin 3 valves & basin. CO#7, 12 & 13 - See attached.
C. Overaa & Co., C/O The Mechanics Bank, Attn: Apryl DeMarco, 1111 Civic Drive, Suite 385, Walnut Creek, CA 94596		V.ID#00797463	Z14006000	TP Rehab Design	\$ 53,892.99	Escrow pymt portion for Pay Est #31 (Voucher ID#00797462), for Deposit to Acct#41-801474. Escrow Agreement #2013-0421-A.
RMC Water and Environment, 2175 N. California Blvd, Suite 315, Walnut Creek, CA 94596		V.ID#00797464	Z14010001	RWM-Project Mgmt	\$ 44,596.48	Project management services.
Twining, Inc., PO Box 47, Long Beach, CA 90801		V.ID#00797805	Z14010065	Little Pocket/Tahoe Main Rpl	\$ 630.00	On-call material testing.
<b>Total Expenditures - Req No. 66</b>					<b>\$ 1,409,633.18</b>	

# Indenture

## SCHEDULE I TO REQUISITION NO. 66

### Water Revenue Bonds Series 2013 Project Fund

Vendor Name	Transaction Type		Project No.	Project Name	Payment Amount	Nature of Expenditure
	Acctg Journal No.	Voucher No.				
Omni Means, 943 Reserve Drive, Suite 100, Roseville, CA 95678		V.ID#00794236	Z14010066	E Sac Water Main Rpl Ph2	\$ 13,320.00	On-call master construction management.
Stay Safe Construction & Transport, 3941 Park Drive, Suite 20-297, El Dorado Hills, CA 95762		V.ID#00795241	Z14130203	FWTP HVAC Rehab	\$ 29,550.00	Mobilization, submittals; materials; installation labor; programming; commissioning/startup; closeout.
Teichert Construction, 24207 County Road 100A, Davis, CA 95616		V.ID#00795243	Z14010069	Oak Park & Colonial Manor WMR	\$ 37,058.93	Water service pipe replacement; install new water service. CO#4 - See attached.
Lawson Mechanical Contractors, 6090 South Watt Avenue, Sacramento, CA 95829		V.ID#00795249	Z14130203	FWTP HVAC Rehab	\$ 206,617.98	Design engineering and pre-construction; submittals.
C Overaa & Co, 200 Parr Blvd, Richmond, CA 94801		V.ID#00797462	Z14006000	TP Rehab Design	\$ 1,023,966.80	Sitework; start up and demo; yard piping; site electrical-duct banks; flocculation basin; filter complex; high service pump station; plant elec sub station; basin 3 valves & basin. CO#7, 12 & 13 - See attached.

# Trustee Agreement

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- ▣ Fiduciary acting on behalf of bondholders
- ▣ Holds bond funds and accounts
- ▣ Invests bond funds
- ▣ Ensures maintenance of reserve requirements
- ▣ Ensures compliance with covenants in the official statement
- ▣ Accepts and disburses bond proceeds
- ▣ Maintains current balances of bond funds

# Tax Certificate

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- ▣ Requirements for use of proceeds
- ▣ Spend down targets
- ▣ Requirements for disbursements of construction funds
- ▣ Record retention requirements
- ▣ Private use restrictions
- ▣ Due dates for arbitrage rebate and yield restriction filings

# Tax Certificate

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- City of Sacramento Utilities Activities to Support Tax Certificate Compliance
  - Monthly meetings between fiscal and engineers to monitor budget to actuals for capital projects
  - Regular reiteration of need to expend 85% of gross proceeds within 3 years of issuance
  - Monitoring of proposed projects and expenditures against tax certificate for compliance
  - Development and implementation of private use calculation

# Continuing Disclosure Agreement

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- ▣ Requires annual filing with Municipal Securities Rulemaking Board
- ▣ Describes information to be contained in the filing
- ▣ Describes material event disclosure requirements
- ▣ Provides due dates for filings
- ▣ Examples of required content, material event and voluntary disclosures

# Tying Documents to Procedures

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Control Activity	Governing Document
Establish Accounts	Indenture; Tax Certificate
Set Targets for IRS Reporting	Tax Certificate
Timely Submission of Material Events	Continuing Disclosure Agreement
Establish Authorized Expenditure Approvers	Indenture

# Tying Documents to Procedures

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Common Finance Questions	Document Governing Response
When do I need to file my disclosure report with EMMA?	Continuing Disclosure Agreement
What do I need to include in my disclosure filing?	Continuing Disclosure Agreement
Can I use grant funds on a bond funded project?	Tax Certificate
I have \$X in my reserve fund at year end. Is that enough? If not, how do I replenish?	Indenture
I've completed all construction and have remaining funds. What can I do with them?	Indenture, Tax Certificate

## Debt Issuance and Management Review Checklist

The Debt Issuance and Management Review Checklist is a tool that will allow public agencies to track their compliance with specific requirements associated with the issuance of bonds and the treatment of bond proceeds.

<b>Debt Issuance and Management Review Checklist<sup>52</sup></b>		
Checklist Item	Completed (✓ = Yes)	Comments/Remarks
<b><i>Agency's General Debt Profile</i></b>		
The agency maintains a complete inventory of its outstanding bonds. This list is updated after each bond issuance.		
Bond covenants for the agency's outstanding bonds - both financial and non-financial - have been identified and are regularly reviewed and complied with.		
The agency has identified and is currently meeting the terms of the underlying documents (i.e., indenture, loan agreement, and tax certification) to the bonds.		
Debt service payments for the outstanding bonds have been incorporated into the agency's annual budget.		

<b><i>Use of Bond Proceeds (for each bond issuance)</i></b>		
Identify and describe the proposed use of the bond proceeds		
Identify the source of repayment for the bonds.		
Identify additional sources of funds, e.g., grants, loans, or other funding sources.		
Confirm proposed uses of bond funds are included in agency budget. <sup>53</sup>		
Confirm proposed uses of bond funds were established in conformity with controlling bond document(s).		
Confirm the agency follows generally accepted accounting principles (GAAP) to account for allocation of permitted expenditures in		

<sup>52</sup> An agency should work with bond counsel, disclosure counsel, tax counsel, and other special consultants to meet the specific requirements of the Internal Revenue Code (IRC), federal securities laws, continuing disclosure agreements (CDAs), or other documents. This checklist should only indicate that those specific processes have been completed; this checklist by itself would not satisfy compliance with these technical processes.

<sup>53</sup> Line items can include land acquisition, engineering, design, planning, and construction.

accordance with Governmental Accounting Standards Board (GASB) principles.		
Maintain a detailed timeline and measure the progress against the timeline.		
Establish and maintain an expenditure schedule that includes cash flows in accordance with the timeline.		
Establish a system to track expenditures that includes a review and approval process that conforms to the controlling bond document(s).		
Establish and follow procedures for the disbursement of bond proceeds.		
Monitor expenditures in conformity with controlling bond document(s):		
<ul style="list-style-type: none"> <li>Identify project line items for which bond proceeds will not be used</li> </ul>		
<ul style="list-style-type: none"> <li>Indicate where bond funds will be used to reimburse the agency for prior expenditures (e.g., planning and design) and identify the type and timing of the reimbursement<sup>54</sup></li> </ul>		
Track progress of projects:		
<ul style="list-style-type: none"> <li>Identify project line items in agency's proposed expenditure report or budget.</li> </ul>		
<ul style="list-style-type: none"> <li>Identify completed projects.</li> </ul>		
<ul style="list-style-type: none"> <li>For incomplete projects, provide estimated start and completion dates.</li> </ul>		
<ul style="list-style-type: none"> <li>Note total amount of bond proceeds expended on each project to date as well as the cumulative amount of proceeds available for each project.</li> </ul>		
Regularly review and validate trustee reports:		
<ul style="list-style-type: none"> <li>Acceptances and disbursements of bond proceeds.</li> </ul>		
<ul style="list-style-type: none"> <li>Current balances of bond funds.</li> </ul>		
<ul style="list-style-type: none"> <li>Meeting/maintaining reserve fund requirements.</li> </ul>		
<ul style="list-style-type: none"> <li>Investment of bond proceeds.</li> </ul>		
If the project was approved by voters, certify that the project is in conformity with voter authorization.		

<sup>54</sup> Reimbursement of prior expenditures is limited in certain ways and may require the adoption of a reimbursement resolution by the public agency.

<b>Covenants</b> <sup>55</sup>		
Complete and file tax certificate. <sup>56</sup>		
Identify information to be reported in compliance with the bond's continuing disclosure agreement (CDA):		
<ul style="list-style-type: none"> <li>Identify the date the agency's annual financial information is due. Was the filing made on time?</li> </ul>		
<ul style="list-style-type: none"> <li>When appropriate, the agency filed material event notices in a timely manner.</li> </ul>		
<ul style="list-style-type: none"> <li>Ensure agency's complete, accurate, and timely filing of information through periodic reviews on what is posted to EMMA.<sup>57</sup></li> </ul>		
Review agency's website and update with currently available debt information.		
If there is a safekeeping requirement in the controlling bond documents, establish procedures to assure property custody and security.		
Establish and maintain a record retention system for documents associated with the bond financing. See tax certificate for agency record retention requirement.		
Regularly monitor the investment of bond proceeds in conformity with the bond documents and state law.		
Regularly schedule audits.		
Prepare reports (such as a Bond Accountability Report) for the governing board and/or oversight committee as required, that include: <ul style="list-style-type: none"> <li>Expenditures to date and remaining balance;</li> <li>Estimate of future expenditures tied to specific projects;</li> <li>Project(s) descriptions tied to voter authorization and controlling bond document(s);</li> </ul>		

<sup>55</sup> Compliance with a tax certificate and reporting requirements contained in a continuing disclosure agreement (CDA) may require the agency to work with special counsel (bond/disclosure/tax) or consultants (arbitrage/tax). This checklist should only indicate that those specific processes have been completed; this checklist would not satisfy compliance with those technical processes.

<sup>56</sup> For detailed information on tax compliance for tax-exempt bonds refer to the IRS's *Tax-Exempt Governmental Bonds: Compliance Guide* available at [www.irs.gov/pub/irs-pdf/p4079.pdf](http://www.irs.gov/pub/irs-pdf/p4079.pdf).

<sup>57</sup> The Electronic Municipal Market Access (EMMA) system is operated by the Municipal Securities Rulemaking Board (MSRB) and is the official source for municipalities to report securities disclosures and related information.

<ul style="list-style-type: none"> <li>• Status of projects with amounts spent on each project; and,</li> <li>• Identifications and explanations of incomplete projects.</li> </ul>		
<p>Report to trustee, rating agency(ies), bond insurer, and/or credit enhancer as required.</p>		

# QUESTIONS

# BREAK

We will reconvene at 3:00 PM

**CDIAC**

**CALIFORNIA  
DEBT AND  
INVESTMENT  
ADVISORY  
COMMISSION**

# **ADMINISTERING ONGOING MONITORING**

**CASE STUDIES ON BOND ACCOUNTABILITY  
LESSONS LEARNED AND BEST PRACTICES**

**MAY 5, 2017**

**SACRAMENTO, CA**

# Municipal Bond Fraud

99

- The Securities and Exchange Commission (SEC) has stepped up enforcement on the Municipal Bond Market.
- Recent Years SEC targets municipal bond fraud
- Increased Risk for Municipal Officials and Public Agencies

# Municipal Bond Fraud

100

- Increased Risk for Municipal Officials
  - ▣ Personal liability – financial penalties
  - ▣ Risk of Prison
- Increased Risk for Municipalities
  - ▣ SEC settled fraud cases with states/local governments
  - ▣ Restricted municipalities ability to issue bonds

# Municipal Bond Fraud

101

- Message is loud and clear to:
  - ▣ City *Mayors, councils, elected officials*
  - ▣ Public administrators
  - ▣ Finance Officers
  - ▣ Staff involved in bond issuance and disbursement of bond funds
- Take a more active role to ensure:
  - ▣ Acting in good faith
  - ▣ Providing accurate up-to-date information

# Case Study - Examples

102

- New Jersey – 2010
- San Diego – 2010
- *Harvey, IL - 2014*

# Case Study - Examples

103

- New Jersey – 2010
  - In August 2010, New Jersey became the first state charged with breaking federal securities laws for misleading investors about the financial condition of two major pension funds for teachers and public employees. New Jersey sold more than \$26 billion of municipal bonds in 79 offerings between 2001 and 2007.

# New Jersey - What went wrong?

104

- ❑ The state concealed the fact that they were unable to make contributions to the funds without raising taxes, cutting services, or otherwise affecting the state budget.
- ❑ Investors were not able to adequately judge the state's financial condition.
- ❑ SEC's finding:
  - New Jersey misrepresented and omitted financial information in bond documents, preliminary official statements, official statements, and continuing disclosures.

# San Diego - 2010

105

- October 2010 - SEC fined municipal officials in a municipal bond fraud case for the first time in a case involving former San Diego city officials.
- Related to five municipal offerings – including revenue bonds and tax anticipation notes (TANs) – totaling over \$260 million between 2002 and 2003.

# San Diego – What went wrong?

106

- The SEC alleged:
- The city intentionally failed to disclose to investors, or was reckless in not knowing:
  - The City's significant pension and retiree health care liabilities, and the difficulty the city would have in funding those liabilities.
  - This information was not reflected in the bond disclosure statements.

# San Diego – SEC Settlement

107

- Four officials assessed fines:
  - ▣ Former City Manager (\$25K)
  - ▣ Comptroller (\$25K)
  - ▣ Deputy City Manager (\$25K)
  - ▣ Treasurer (\$5K)

# Harvey, IL - 2014

108

- First time the SEC filed an emergency court order to keep a municipality's bonds off the market.
- Harvey issued three limited obligation bonds from 2008 to 2010 totaling \$14 million, which were supposed to be repaid from dedicated revenue streams and not the City's general funds.

# Harvey, IL – What went wrong?

109

- The city issued bonds to supposedly rebuild a large Holiday Inn to spur job growth.
- Rather than renovating the hotel, Harvey siphoned funds to meet payroll obligations and other general city operations.
- In addition, the City Comptroller received and failed to disclose \$269,000 in bond proceeds while working for both the city and the developer on the project.

# Harvey, IL – SEC Complaint

110

- Asks the court to stop the City and its officials from offering any municipal bonds for five years, unless;
- The City retains a court-appointed independent consultant.
- SEC also asked the court to make the Comptroller forfeit the bond proceeds and pay unspecified civil penalties.
- The case has yet to conclude

# Lessons Learned: Take Aways

111

- Provide accurate, up-to-date information in the bond documents.
- If budgetary projections have changed, then those changes must be communicated to the proper individuals and reflected in the bond documents.
- This is particularly the case with revenue streams, which can be subject to greater flux for municipalities.

# Lessons Learned : Take Aways

112

- If legislative or statutory changes are going to affect a government's financial condition, ability to pay debt service on the bonds, or another portion of the budget, that legislative or statutory change *and* the effect of that change must be reported and explained to the investing public.

# Lessons Learned : Take Aways

113

- If the scale of the project for which you are bonding materially changes, that must be communicated to the proper individuals and reflected in the bond documents.
- This may impact the viability of the project, which is why solid preparation beforehand is important.

# Lessons Learned : Take Aways

114

- Cover all your bases.
- If information can be reasonably expected to reach the investing public, it must be accurate.
- This includes providing accurate, up-to-date information in public statements, publicly available documents, and even speeches (e.g. State of the City).

# Lessons Learned : Take Aways

115

- Municipal officials should;
  - take an active role to ensure staff are doing their jobs properly
  - responsibly seek the appropriate counsel
  - ensure that staff are properly trained in communicating information to bond counsel and other individuals who may be involved in the issuance of bonds

# Group Discussion – Let's Talk

116

- What have we learned from Session 1?
  - ▣ The Control environment
  - ▣ Risk Assessment
  - ▣ Pre-Issuance
  - ▣ Policies, Practices and Procedures
  - ▣ Disbursement of Bond Proceeds
  - ▣ Auditing and Testing Compliance

# Group Discussion – Let's Talk

117

- What have we learned from Session 2?
  - ▣ Control Activities
  - ▣ Information and Communication
  - ▣ Monitoring

# Group Discussion – Let's Talk

118

- What have we learned from Session 3?
  - ▣ Debt Management Policies
  - ▣ Internal Controls
  - ▣ Policies, Procedures and Controls
  - ▣ Training
  - ▣ Continual Review and Improvement

## Internal Control System Checklist

The Internal Control System Checklist is a tool to allow public agencies to assess their internal control system for the management of bond funds. For additional information on how to evaluate internal controls, refer to the U.S. Government Accountability Office (GAO) Internal Control Management and Evaluation Tool.<sup>58</sup>

<b>Internal Control Checklist for Bond Requirements</b>		
Task/Deliverable	Completed? ( <input type="checkbox"/> )	Comments/Remarks
<b>Part 1. Control Environment:</b>		
1. Do you have a designated compliance officer? <sup>59</sup> (Identify a compliance officer or establish a compliance team to verify internal controls and bond requirements.)		The designated compliance officer should be a staff person that, with respect to their regular duties, are not responsible for processing invoice payments, but may be a member of the governing body of the public agency.
2. Compliance officer and compliance team members have participated in training on internal control and bond administration requirements.		
3. Establish an inventory of outstanding bonds and obtain or prepare a list of bond requirements, including covenants in the following controlling bond documents: <sup>60</sup> <ul style="list-style-type: none"> <li>a. Indenture</li> <li>b. Loan or Lease Agreement</li> <li>c. Tax Certificate and Continuing Disclosure Agreement</li> </ul>		<i>(Refer to Part 3. Control Activities of this checklist for examples of bond requirements)</i>
4. Establish written procedures for bond administration processes and bond requirements that support the agency's internal control system.		
5. Adopt a debt policy with objectives and		Debt policy and procedures are

<sup>58</sup> This tool can be accessed at <http://www.gao.gov/products/GAO-01-1008G>.

<sup>59</sup> If practicable, an agency may utilize a compliance team that represents a cross-section of bond administration roles and responsibilities throughout its program operations and organizational structure. If a compliance team is utilized, a single point of contact should be identified by the agency to coordinate compliance activities.

<sup>60</sup> A thorough review and understanding of covenants or provisions in controlling bond documents is necessary to prepare a list of bond requirements for compliance purposes. If necessary, an agency should seek advice or assistance from bond counsel and/or a financial advisor regarding the development of its list of bond requirements. Lists of post-issuance requirements for the specific purpose of compliance with federal tax law regarding arbitrage rebate, yield restriction, and private use and legal or regulatory requirements for continuing disclosure are available from the IRS or organizations such as the National Association of Bond Lawyers (NABL) and the Government Finance Officers Association (GFOA).

specifications for bond administration and integrate into the agency's organizational policies, procedures, and long-term plans. <i>(Refer to Part 2. Risk Assessment of this checklist for additional information)</i>		maintained in the agency's policy and procedures manual.
6. Establish an audit committee to review compliance with testing of bond requirements. <sup>61</sup>		<i>(Refer to Part 4. Monitoring of this checklist for additional information on compliance tests for bond requirements)</i>
<b>Part 2. Risk Assessment:</b>		
1. Clearly define the objectives <sup>62</sup> of the bond administration program related to: <ul style="list-style-type: none"> <li>a. Operations (related performance measures are effectiveness and efficiency)</li> <li>b. Reporting (related performance measures are accuracy and precision)</li> <li>c. Compliance</li> </ul>		Objectives are clearly measurable and easily understood at all levels of the agency. Objectives relate to activities within all stages of the debt lifecycle.
2. Include objectives of the bond administration program in a debt policy and integrate risk assessment for all stages of the debt lifecycle into the agency's decision-making and planning process.		The agency's objectives in its strategic plan include elements of bond administration and define strategies the agency uses to manage risk.
3. Establish performance measurements <sup>63</sup> to monitor how successfully the agency achieves its objectives for the bond administration program.		Performance measurements for the bond administration program are defined and included in a strategic plan.
4. Establish risk tolerance relative to each of the objectives of the bond administration program. Risk tolerance is equal to the variation of performance or condition that the agency has determined to be within its risk appetite.		A debt policy defines the level of risk that is deemed reasonable for an agency to accept in the achievement of its objectives (risk appetite) and identifies the conditional elements of the bond administration program that are monitored within the agency's internal control system.
5. Identify and analyze risks (including potential fraud and misuse) related to the objectives		Risk analysis estimates the significance of each risk, assesses

<sup>61</sup> Such tests commonly include procedures that validate statutory authority to borrow, legal requirements of debt sales, tracing authorized debt to accounting records, and confirming compliance with bond documents, covenants, and other legal requirements.

<sup>62</sup> Objectives of the bond administration program may reflect issuer responsibilities specified in controlling bond documents as well as specifications required by laws, regulations, or an agency's policies and procedures.

<sup>63</sup> Performance measurements relate to elements of bond administration objectives and are used to evaluate variances of performance (levels of risk) for each element on a conditional basis, i.e., Is the objective achieved in a manner that is effective, efficient, accurate, precise, or in compliance?

and conditional elements of the bond administration program. (Refer to the Task Force Guidelines in Part 3 – Control Activities for additional information on appropriate responses an agency may deploy to manage risks)		the likelihood of occurrence, and forms the basis for the types of control activities that are used to prevent and detect risks, including remedies that management may use to immediately respond to risk events.
<b>Part 3. Control Activities:</b>		
1. At a minimum, the agency applies the same system of internal control activities to bond funds as it does to all other governmental funds.		Based on bond requirements and risk assessment findings, control activities provide a reasonable assurance of internal control for bond funds applicable to all stages of the debt lifecycle.
2. Review and update inventory of outstanding bonds and related bond requirements.		Review official bond transcripts.
3. Review and update bond administration procedures.		
4. Review and update debt policy for changes to legal requirements, new debt and revised objectives, strategies, and procedures.		The debt policy is reviewed on a periodic basis for approval by the governing body.
5. Confirm compliance with policies, covenants, and bond administration procedures that support the agency's internal control system (all control activities).		All control activities sufficiently evaluate risk factors of fraud and misuse of bond proceeds.
<b>Control Activities for Legal and Financial Requirements:</b>		
6. Confirm legal requirements of debt sales (new issues and refunding transactions) are met.		
<ul style="list-style-type: none"> <li>Receive copies of approvals, authorizations, and controlling bond documents (official bond transcripts) and maintain in a safe and secure but accessible location.</li> </ul>		
<ul style="list-style-type: none"> <li>Monitor/track bond authorizations to debt issuances and refunding transactions.</li> </ul>		Update inventory of outstanding bonds.
<ul style="list-style-type: none"> <li>Bond documents and amendments are appropriately approved pursuant to the agency's administrative or legal policies and procedures.</li> </ul>		
<ul style="list-style-type: none"> <li>Confirm bond projects and related expenditures are consistent with approvals, authorizations, and controlling bond documents.</li> </ul>		Conduct site visits to confirm work is performed as reflected in progress estimates submitted by contractors.

7. Confirm compliance with financial covenants and other restrictions.		
<ul style="list-style-type: none"> <li>Confirm funds and accounts are established in the agency's accounting system to record the receipt of proceeds and account for bonds payable.</li> </ul>		<p>Applies to new issues and refunding transactions at the time of closing. For tax-exempt borrowing, proceeds include investment earnings.</p>
<ul style="list-style-type: none"> <li>Confirm funds and accounts established by the trustee and deposits of bond proceeds reconcile with controlling bond documents.</li> </ul>		
<ul style="list-style-type: none"> <li>Monitor trustee funds and accounts and perform periodic reconciliations of trustee statements with agency records for bond expenditures, including costs of issuance for new issues or refunding transactions.</li> </ul>		<p>Officer certificates or requisitions match trustee records and statement activity.</p>
<ul style="list-style-type: none"> <li>Confirm expenditures for bond proceeds are processed pursuant to appropriate segregation of duties and practicable checks and balances (three-way matching) or, alternatively, by appropriate compensating controls.</li> </ul>		<p>Officer certificates or requisitions have required agency authorizations supported by audit trail documents that support the reconciliation of expenditures with capital budget and agency records.</p>
<ul style="list-style-type: none"> <li>Confirm deposit of funds with trustee for debt service and maintenance of reserve funds or other accounts, including the rebate account and monitor cash flow activity on a periodic basis.</li> </ul>		<p>Confirm any excess funds at the trustee are applied pursuant to the terms of the indenture or other controlling bond document.</p>
<ul style="list-style-type: none"> <li>Confirm trustee is performing compliance activities for financial covenants required by indenture, loan or lease agreements, or other bond documents.</li> </ul>		<p>Trustee is correctly following procedures contained in bond documents including the maintenance of funds and accounts, insurance and credit rating filings, monitoring and adherence to debt coverage ratios and additional bonds tests, distribution of notices and corporate actions, and mandatory or optional redemption instructions.</p>
<ul style="list-style-type: none"> <li>Confirm compliance with debt policy provisions regarding financial performance measurements for conditional elements of the bond administration program. <i>(For</i></li> </ul>		<p>Conditional elements of a debt policy are consistent with the agency's objectives and strategies in the strategic plan or other long-term planning report.</p>

<p><i>examples of conditional elements refer to the GFOA model debt policy at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a></i></p>		
<p><b>Control Activities for Non-Financial Requirements:</b></p>		
<p>8. Confirm compliance with agency oversight requirements for bond administration activities.</p>		
<p>9. Confirm compliance with staffing plans for the bond administration program.</p>		
<p>10. Confirm compliance with agency records retention policy and procedures.</p>		<p>Records retention for bond related material is maintained pursuant to federal treasury regulations and tax law requirements. <i>(Refer to Other Control Activities in this checklist below)</i></p>
<p><b>Other Control Activities:</b></p>		
<p>11. Confirm compliance with tax certificate covenants, i.e., post-issuance tax compliance requirements for bonds. <i>(For detailed information on tax compliance for bonds refer to the IRS Compliance Guide at <a href="http://www.irs.gov/pub/irs-pdf/p4079.pdf">www.irs.gov/pub/irs-pdf/p4079.pdf</a>)</i></p>		<p>Pursuant to IRS guidelines, in order to comply with post-issuance federal tax rules, issuers ensure that the rules are met both at the time the bonds are issued and throughout the term of the bonds.</p>
<ul style="list-style-type: none"> <li>• Do you have a post-issuance tax compliance procedure similar to that referenced in IRS form 8038?</li> </ul>		
<ul style="list-style-type: none"> <li>• Do you have an arbitrage rebate consultant? (Consult with arbitrage rebate consultant and/or bond/tax counsel as necessary to ensure compliance with post-issuance tax requirements for tax-exempt bonds.)</li> </ul>		<p>Implement procedures that will enable adequate safeguards against post-issuance violations that result in loss of the tax-exempt status of bonds.</p>
<ul style="list-style-type: none"> <li>• Maintain copies of filings with the Internal Revenue Service (IRS) for each bond issuance, i.e., Information Return Form 8038-G and arbitrage rebate reports.</li> </ul>		<p>8038-G is included in official bond transcripts.</p>
<ul style="list-style-type: none"> <li>• Confirm due dates for arbitrage rebate and yield restriction filing requirements with the IRS.</li> </ul>		<p>First installment due on fifth bond year of bond issuance plus 60 days. Tax certificate provides the bond year to determining due date for tax filings.</p>
<ul style="list-style-type: none"> <li>• Monitor compliance with expenditure spend-down targets, use of proceeds, private use, and disposition of bond-financed</li> </ul>		<p>Maintain a separate list of compliance requirements for tax compliance and continuing disclosure, i.e., post-issuance</p>

facilities.		requirements for tax-exempt bonds. Request a compliance checklist from consultant or tax counsel or refer to the checklist developed by the National Association of Bond Lawyers (NABL) and the GFOA at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a> .
<ul style="list-style-type: none"> <li>Monitor compliance with records retention requirements for bond related records, pursuant to federal treasury regulations and tax laws.</li> </ul>		
12. Confirm compliance with continuing disclosure agreement covenants, i.e., post-issuance disclosure requirements.		
<ul style="list-style-type: none"> <li>Confirm annual filing on the Municipal Securities Rulemaking Board's (MSRB) Electronic Municipal Marketplace Access (EMMA) website due dates for annual reports and other financial reports applicable to each outstanding bond issuance.</li> </ul>		Continuing disclosure agreement for bond issue specifies filing due date.
<ul style="list-style-type: none"> <li>Update information in the agency's annual report required by the continuing disclosure agreement for the bond issue and file with EMMA no later than the required due date. If the agency utilizes a dissemination agent to file the annual report with EMMA, the compliance officer should locate the filing on EMMA and confirm the annual report has been filed prior to the due date and verify correct CUSIPs were used in the filing.</li> </ul>		Maintain a separate list of compliance requirements for tax compliance and continuing disclosure, i.e., post-issuance requirements for tax-exempt bonds. Request a compliance checklist from consultant or bond/disclosure counsel or refer to the checklist developed by NABL and the GFOA at <a href="http://www.gfoa.org/debt-management-policy">www.gfoa.org/debt-management-policy</a> .
<ul style="list-style-type: none"> <li>Monitor outstanding debt for events that are listed in the continuing disclosure as a material or listed event and file or arrange to file a notice of material event on EMMA for an occurrence within 10 business days of the event.</li> </ul>		Consult with bond/disclosure counsel as necessary to ensure compliance with post-issuance disclosure requirements
<b>Part 4. Information and Communications:</b>		
1. Establish process to alert personnel to changes in policies and procedures for internal controls and bond requirements.		
2. Establish an official structure of communication within the agency based on roles and responsibilities in the bond		Job descriptions define roles and responsibilities for essential bond administration functions. (Refer to

administration program.		<i>Control Activities for Non-Financial Requirements, Item 9.)</i>
3. Confirm that staff with internal control and/or bond administration responsibilities, including compliance, received or are scheduled to receive periodic training.		
<b>Part 5. Monitoring:</b>		
1. Perform period review of bond activities and report results to the governing body.		
2. Complete Internal Control Checklist and immediately report findings to management.		

# Group Discussion – Let's Talk

126

- What have we learned from Session 4?
  - ▣ Bond Documents to Accountability
  - ▣ Bond Oversight and Reporting
  - ▣ Task Force Review Checklist

## Debt Issuance and Management Review Checklist

The Debt Issuance and Management Review Checklist is a tool that will allow public agencies to track their compliance with specific requirements associated with the issuance of bonds and the treatment of bond proceeds.

<b>Debt Issuance and Management Review Checklist<sup>52</sup></b>		
Checklist Item	Completed (✓ = Yes)	Comments/Remarks
<b><i>Agency's General Debt Profile</i></b>		
The agency maintains a complete inventory of its outstanding bonds. This list is updated after each bond issuance.		
Bond covenants for the agency's outstanding bonds - both financial and non-financial - have been identified and are regularly reviewed and complied with.		
The agency has identified and is currently meeting the terms of the underlying documents (i.e., indenture, loan agreement, and tax certification) to the bonds.		
Debt service payments for the outstanding bonds have been incorporated into the agency's annual budget.		

<b><i>Use of Bond Proceeds (for each bond issuance)</i></b>		
Identify and describe the proposed use of the bond proceeds		
Identify the source of repayment for the bonds.		
Identify additional sources of funds, e.g., grants, loans, or other funding sources.		
Confirm proposed uses of bond funds are included in agency budget. <sup>53</sup>		
Confirm proposed uses of bond funds were established in conformity with controlling bond document(s).		
Confirm the agency follows generally accepted accounting principles (GAAP) to account for allocation of permitted expenditures in		

<sup>52</sup> An agency should work with bond counsel, disclosure counsel, tax counsel, and other special consultants to meet the specific requirements of the Internal Revenue Code (IRC), federal securities laws, continuing disclosure agreements (CDAs), or other documents. This checklist should only indicate that those specific processes have been completed; this checklist by itself would not satisfy compliance with these technical processes.

<sup>53</sup> Line items can include land acquisition, engineering, design, planning, and construction.

accordance with Governmental Accounting Standards Board (GASB) principles.		
Maintain a detailed timeline and measure the progress against the timeline.		
Establish and maintain an expenditure schedule that includes cash flows in accordance with the timeline.		
Establish a system to track expenditures that includes a review and approval process that conforms to the controlling bond document(s).		
Establish and follow procedures for the disbursement of bond proceeds.		
Monitor expenditures in conformity with controlling bond document(s):		
<ul style="list-style-type: none"> <li>Identify project line items for which bond proceeds will not be used</li> </ul>		
<ul style="list-style-type: none"> <li>Indicate where bond funds will be used to reimburse the agency for prior expenditures (e.g., planning and design) and identify the type and timing of the reimbursement<sup>54</sup></li> </ul>		
Track progress of projects:		
<ul style="list-style-type: none"> <li>Identify project line items in agency's proposed expenditure report or budget.</li> </ul>		
<ul style="list-style-type: none"> <li>Identify completed projects.</li> </ul>		
<ul style="list-style-type: none"> <li>For incomplete projects, provide estimated start and completion dates.</li> </ul>		
<ul style="list-style-type: none"> <li>Note total amount of bond proceeds expended on each project to date as well as the cumulative amount of proceeds available for each project.</li> </ul>		
Regularly review and validate trustee reports:		
<ul style="list-style-type: none"> <li>Acceptances and disbursements of bond proceeds.</li> </ul>		
<ul style="list-style-type: none"> <li>Current balances of bond funds.</li> </ul>		
<ul style="list-style-type: none"> <li>Meeting/maintaining reserve fund requirements.</li> </ul>		
<ul style="list-style-type: none"> <li>Investment of bond proceeds.</li> </ul>		
If the project was approved by voters, certify that the project is in conformity with voter authorization.		

<sup>54</sup> Reimbursement of prior expenditures is limited in certain ways and may require the adoption of a reimbursement resolution by the public agency.

<b>Covenants<sup>55</sup></b>		
Complete and file tax certificate. <sup>56</sup>		
Identify information to be reported in compliance with the bond's continuing disclosure agreement (CDA):		
<ul style="list-style-type: none"> <li>Identify the date the agency's annual financial information is due. Was the filing made on time?</li> </ul>		
<ul style="list-style-type: none"> <li>When appropriate, the agency filed material event notices in a timely manner.</li> </ul>		
<ul style="list-style-type: none"> <li>Ensure agency's complete, accurate, and timely filing of information through periodic reviews on what is posted to EMMA.<sup>57</sup></li> </ul>		
Review agency's website and update with currently available debt information.		
If there is a safekeeping requirement in the controlling bond documents, establish procedures to assure property custody and security.		
Establish and maintain a record retention system for documents associated with the bond financing. See tax certificate for agency record retention requirement.		
Regularly monitor the investment of bond proceeds in conformity with the bond documents and state law.		
Regularly schedule audits.		
Prepare reports (such as a Bond Accountability Report) for the governing board and/or oversight committee as required, that include: <ul style="list-style-type: none"> <li>Expenditures to date and remaining balance;</li> <li>Estimate of future expenditures tied to specific projects;</li> <li>Project(s) descriptions tied to voter authorization and controlling bond document(s);</li> </ul>		

<sup>55</sup> Compliance with a tax certificate and reporting requirements contained in a continuing disclosure agreement (CDA) may require the agency to work with special counsel (bond/disclosure/tax) or consultants (arbitrage/tax). This checklist should only indicate that those specific processes have been completed; this checklist would not satisfy compliance with those technical processes.

<sup>56</sup> For detailed information on tax compliance for tax-exempt bonds refer to the IRS's *Tax-Exempt Governmental Bonds: Compliance Guide* available at [www.irs.gov/pub/irs-pdf/p4079.pdf](http://www.irs.gov/pub/irs-pdf/p4079.pdf).

<sup>57</sup> The Electronic Municipal Market Access (EMMA) system is operated by the Municipal Securities Rulemaking Board (MSRB) and is the official source for municipalities to report securities disclosures and related information.

<ul style="list-style-type: none"> <li>• Status of projects with amounts spent on each project; and,</li> <li>• Identifications and explanations of incomplete projects.</li> </ul>		
<p>Report to trustee, rating agency(ies), bond insurer, and/or credit enhancer as required.</p>		

# QUESTIONS

- Case studies acknowledgement: Paul F. Bohn, Esq. – Fausone Bohn, LLP

# Thank you for participating!

CDIAC staff will collect your  
evaluation as you exit.