POLICY 6.085

I recommend that the Board approve development of the proposed revised Policy 6.085, entitled “Debt Management.”

[Contact: Leanne Evans, PX 48142]

Development **CONSENT ITEM**

- This change to the debt policy, in Paragraph 6**(**Measures of Debt Levels and Debt Issuance Limits), is in response to the legislative reduction of the capital millage levy.
  - The current policy limits the amount of Certificates of Participation (COPs) outstanding to the maximum amount of the capital outlay levy that can be used for the required lease payments. The limit is currently no more than 50% of the capital outlay millage.
  - The legislature recently changed the maximum capital outlay millage from 2 mills to 1.75 mills. As a result, the maximum allowed for lease payments was reduced from 1 mill to .875 mils.
  - The lease payment required for the currently outstanding COPs equates to .925 mills.
  - The proposed change to the debt policy is necessary to support the lease payments for the Certificates already outstanding.

- The policy is also amended to provide technical amendments which add headings of “Debt Management Guidelines” to Paragraph 2 and a heading of “Policy Review” to Paragraph 4.

POLICY 6.085

DEBT MANAGEMENT

1. **Purpose. --** The purpose of this Policy is to establish guidance for the issuance and management of the debt of the School District. Such debt includes short-term and long-term obligations issued by the School Board and any associated financing entities, such as traditional financing vehicles like tax-, revenue- and/or bond-anticipation notes; capital and operating leases, general obligation bonds; sales tax bonds; and certificates of participation. The Policy also contemplates new/unique financing concepts such as leveraged leases, qualified zone academy bonds (QZABs) and other financial management tools that may evolve in the future. This Policy is designed to:

    a. set forth a liability management structure to facilitate the sound and efficient management of District debt, addressing both practical aspects of liability management and philosophical aspects;

    b. provide guidelines to control the overall debt management process so that all liabilities are managed in accordance with stated objectives;

    c. encourage and require communication between staff, the Board, the Finance Committee, and the District's legal and financial advisors; and

    d. develop formalized criteria for evaluating and establishing the basis for comparing actual performance results achieved by debt management.

2. **<u>Debt Management Guidelines. --</u>** Additionally, in concert with the Finance Committee, the District will maintain separate Debt Management Guidelines ("Guidelines") that will provide specific direction to the Finance Committee in its recommendations regarding debt issuance and will be revised as needed to reflect current innovative and prudent practices in the financial markets.

3. **Implementation**. -- The Chief Operating Officer and the Treasurer on behalf of the Superintendent shall be responsible for the implementation of the policies set forth in this Debt Management Policy. District staff shall solicit advice and comments from the Finance Committee on debt-related matters, consistent with the Finance Committee charter in Policy 1.094

4. **<u>Policy Review. --</u>** The Chief Operating Officer, Treasurer, and Finance Committee shall review this Policy as needed due to changes in the financial markets, but not less than every two (2) years, and suggest that the Superintendent recommend any needed revisions to the Board.

5. **Permissible Debt**. -- The Board recognizes that debt is an integral part of the District's ongoing financial management program; and both short-term and long-

term debt help the District accomplish its core goals. The Board also recognizes that annual operating and capital revenues are cyclical, which often necessitate the use of short-term financings, while the useful life of new and renovated facilities is often thirty to forty years. As a result, prudent financial management will employ short-term and long-term financing tools to facilitate matching assets and liabilities.

a. **Short-Term Debt**

i. In accordance with applicable laws such as Fla. Stat. § 1011.12(2) and §§ 1011.13 and 1011.14, the District may issue obligations with a maturity of not more than one year ("Notes") to fund anticipated short-term cash flow needs due to the timing of the receipts of the annual current year ad valorem tax collections from the county tax collector and other revenues. The principal of the Notes and the interest thereon will be payable from, and secured by, a pledge of such ad valorem taxes and other revenues, as may be appropriate.

ii. Except for any issuance of taxable obligations, the District will comply with the requirements of the Internal Revenue Code, prior to and subsequent to the issuance of the Notes, for spending the proceeds in a manner consistent with the exceptions for interest on the Notes not being included in gross income for federal income tax purposes.

b. **Long-Term Debt**

i. In accordance with applicable laws such as Florida Statutes Chapters 1010, 1011, and 1013 Part IV, the District will not issue long-term debt obligations or use long-term debt proceeds to finance current operations (except when using excess proceeds to make debt service/lease payments as provided for in the financing documents). For purposes of this Policy, long-term debt includes bonds, leases, certificates of participation, and other similar obligations.

ii. The District may utilize long-term debt for the acquisition, construction or renovation of facilities or, consistent with Florida law, for the acquisition of equipment that cannot be funded from current revenue sources or in such cases where it is more equitable to finance the facility or equipment over its useful life. The District may also issue long-term debt to refund all or a portion of its outstanding debt subject to limitations detailed in this Policy.

iii. When debt is used to finance capital improvements, the financing term will be for a period not to exceed the useful life of the facilities or equipment, but never greater than 30 years.

6. **Measures of Debt Levels and Debt Issuance Limits**

a. **Short Term Debt**.- - The District will not exceed the maximum allowable issuance size, if any, as determined by regulations governing the federal taxability of the interest earned by holders of such debt.

b. **Long Term Debt**

i. **General Obligation Bonds**.-- Pursuant to State Board of Education rule 6A-1.037(2), the measure shall be the outstanding debt-to-taxable property ratio, such that a bond issue, together with other school bonds outstanding against the District shall not exceed ten percent (10%) of the nonexempt assessed valuation of the District.

ii. **Certificates of Participation**

A. The measure shall be lease payments as a percentage of capital outlay millage dollars and shall not exceed 50% of the authorized capital outlay millage or 1 mill, whichever is greater, unless approved by a supermajority of the School Board.

B. Additionally, the District will comply with all applicable Florida statutory requirements and State Board of Education rules, and take into account other factors suggested or required by the credit rating agencies and/or bond insurers when preparing its capital budget and each specific plan of finance.

7. **Selecting Debt Sale Methods**

a. **Short-term Debt**.-- Short-term debt shall be issued through a competitive bid process, except in instances where a private placement or a negotiated sale is more cost effective because of unique market conditions or other extraordinary factors.

b. **Long-term Debt** .-- The District, with the advice and counsel of the Finance Committee and the Financial Advisor, will determine whether the sale of long-term debt shall be sold via competitive sale or negotiated sale after considering such factors as the size, complexity of the offering, market conditions, and timing of the transaction. Except where sold by negotiated sale through underwriters pursuant to Fla. Stat. § 218.385, bonds must be sold to the highest and best bidder at a public sale except as otherwise allowed by Fla. Stat. § 1010.47(2).

8. **Financing Structure**.--The financing structure-consisting of matters such as principal amortization, call provisions, coupons/yields, credit enhancement, and use of hedging products-will be developed for each financing after considering relevant market conditions and then-current practices. Each structure will be developed to provide the lowest long-term effective financing cost while providing the greatest flexibility to extract additional value as market conditions change over time (such as refund debt or terminate swaps).

9. **Amortization Structure**.-- Principal should be structured to provide level debt-service payments for the life of the transaction. "Wrapped debt service" and "bullet maturities" may be appropriate for certain financings, but should only be employed when necessary.

10. **Issuing Variable Rate Debt**.-- The District may issue variable rate obligations in amounts, and in proportion to its fixed-rate debt, that the District, with the advice and counsel of the Finance Committee and the Financial Advisor, determines to be appropriate to achieve the District's goals.

11. **Credit Ratings**.-- Because the credit review process incorporates both quantitative analysis (fund balance, debt levels, and wealth levels) and qualitative factors (management experience, political climate, and policies/procedures), the District recognizes that credit ratings provide an indication of both the short-term and long-term financial health of the District and that higher credit ratings also result in reduced borrowing costs and decreased cost of bond insurance. Accordingly, the District will exercise prudence and diligence in preparing its budget and managing its finances to maintain its current ratings and obtain rating upgrades that reflect the District's commitment to excellence. At the time of this Policy's development, the District's current ratings were:

	Moody's (09/03)	S&P (09/03)	Fitch (05/03)
General Obligation Bonds	Aa3	AA	AA-
Certificates of Participation	A1	AA-	A+
Short-term Notes	MIG-1	SP-1+	--

12. **Credit Enhancements**.-- Credit enhancements (such as insurance and letters of credit) will be used only in those instances where the anticipated present value savings in terms of reduced interest expense exceeds the cost of the credit enhancement.

13. **Investing Debt Proceeds**.-- Because safety of capital is regarded as the highest priority in handling of investment of debt proceeds, and all other investment objectives are secondary to the safety of capital, the District staff, in consultation with the Finance Committee and Investment Advisor, will follow investment strategies that are consistent with the written Investment Policy (Policy 6.08) and Fla. Stat. § 218.415 and provide the maximum return while complying with the requirements of the IRS Code.

    a. The District, with the guidance of the Finance Committee, Financial Advisor, and Investment Advisor, will attempt to structure investments that allow the District to meet exceptions to the rebate requirements in section 148(f) of the Code.

    b. Debt proceeds are only to be invested in permitted investments, as defined in financing agreements, escrow agreements, resolutions, law, and the School Board's Investment Policy (P-6.08). Neither the District nor any person under its control or direction will make any investment of bond proceeds in any manner that would cause the bonds to be deemed private activity bonds or arbitrage bonds by the IRS under sections 141 or 148 of the Code. The District will comply with all federal tax arbitrage regulations.

14. **Debt Refundings**. -- The District will monitor outstanding debt in relation to existing conditions in the debt market and may refund any outstanding debt when sufficient cost savings can be realized. Outstanding debt may be refunded as long as the net present value savings is equal to or greater than 3% of the refunded obligation's par amount, but this general criterion will be adjusted as outlined in the Guidelines.

15. **Interest Rate Hedge Contracts**.-- The Board recognizes that interest rate swaps, caps, collars and other hedging products (collectively referred to herein as "hedges") can be an effective tool to reduce financing costs, diversify certain risks and take advantage of unique market conditions.

    a. **Appropriate Use**.-- Hedges shall not be used for speculative purposes; and they may be used only when the District has received an opinion acceptable to the market from a nationally recognized bond counsel firm that the agreement relating to the hedge is a legal, valid and binding obligation of the District and entering into the transaction complies with applicable State and Federal laws. The following list includes many of the conditions under which entering into a hedge may be appropriate:

i. to achieve savings as compared to a traditional debt structure available in the bond market (both fixed and variable rate obligations);

ii. to achieve diversification of a particular debt offering;

iii. to reduce net interest expense within prudent risk guidelines;

iv. to prudently hedge risk in the context of a particular financing or the overall asset/liability management of the District (i.e. buying interest rate caps and entering into delayed start swaps);

v. to incur variable rate exposure within prudent guidelines; or

vi. to achieve more flexibility in meeting overall financial objectives than can be achieved in conventional markets (i.e., a swaption with an upfront payment).

vii. In evaluating a particular transaction involving the use of hedges, the District shall review long-term implications including costs of borrowing, historical interest rate trends, variable rate capacity, credit enhancement capacity, opportunities to refund related debt obligations and other similar considerations.

b. **Form and Content of Hedges**.-- Hedges should be in the form set forth by the International Swaps and Derivatives Association (ISDA) Master Agreement and the typical schedules. In preparing the agreement, the District should clearly delineate termination provisions, events of default and posting of collateral.

c. **Method of Soliciting and Procuring Hedges**.--The District, with the guidance of the Finance Committee and Financial Advisor, will determine whether the hedge shall be sold/purchased competitively or via negotiation after considering such factors as the size and complexity of the offering and market conditions.

i. Unless the District procures a specific team of swap counterparties in the future, the District will use counterparties from its existing underwriting team (or their structured products affiliates) that meet the credit criteria included herein.

ii. Regardless of the method of procurement, the District shall obtain an independent finding that the terms and conditions of any hedge entered into reflect a fair market value of such hedge as of the date of its execution.

d. **Aspects of Risk Exposure Associated with Hedge Contracts**.-- The District shall evaluate all of the risks inherent in a hedge transaction before proceeding. The risks to be evaluated should include counterparty risk, termination risk, rollover risk, basis risk, tax event risk and amortization risk. The District shall endeavor to diversify its exposure to counterparties within prudent limits.

e. **Qualifications of Counterparties**.-- A counterparty must have demonstrated experience in successfully executing hedge transactions. A counterparty shall have a credit rating equal to or higher than the District's and credit ratings from at least one nationally recognized statistical rating agency that is within the two highest rating categories ("AAA" or "AA"), and ratings which are obtained from any other nationally recognized statistical rating agencies shall also be within the three highest investment grade categories ("A" or better), or the payment obligations of the counterparty shall be collateralized or unconditionally guaranteed by an entity with such credit ratings.

16. **Compliance and Reporting**

a. **Disclosure Policy**.-- The District will provide full and fair disclosure in connection with the initial sale and distribution of its publicly-marketed debt instruments and provide ongoing secondary market information, in compliance with the requirements of applicable federal and state securities laws and regulations, including Securities and Exchange Commission Rule 15c 2-12.

b. **Budget Debt Service Payments**.--Annually the Superintendent will include in the proposed budget presented to the School Board for its consideration and approval the appropriations necessary to make the required debt service and lease payments during the fiscal year.

c. **Compliance with Financing Covenants and the Law**.-- The District shall comply with all covenants and requirements of financing resolutions, and applicable state and federal laws authorizing and governing the issuance and administration of debt obligations.

d. **Bond Yield Arbitrage Monitoring**.--The District shall contract for arbitrage calculation services to monitor the earnings on its debt proceeds for each debt series and determine whether a rebate is necessary.

e. **Annual Report on Outstanding Debt**.-- No later than December 31st of each year, an annual report shall be submitted to the School Board, covering the previous fiscal year, that will include a summary of outstanding obligations and any associated hedges. At a minimum, the report will include the information included in Exhibit A of the Guidelines, as may be amended from time to time by the District with the guidance of the Finance Committee.

f. **Database**.-- In addition to the annual report, the Treasurer will maintain a database of existing debt/hedge obligations. The database will include at least the following information related the District's debt:

i. For all debt obligations:

- Debt service schedule including principal, interest, and coupon
- Issue date
- Interest rate mode (variable/fixed)
- Call provisions
- Credit enhancement
- Purpose (new money/refunding)
- Senior managing underwriter

ii. For all hedge obligations:

- Counterparty
- Type of swap (fixed receiver, fixed payer, basis, etc.)
- Key terms of the agreements, including notional amounts, interest rates and maturity
- The marked to market value as of the most recent fiscal year end
- Credit ratings of counterparty and any applicable guarantor
- Imbedded options
- Discussion of market/structural risks

STATUTORY AUTHORITY: Fla. Stat. §§1001.41(2); 1001.43(2)
LAWS IMPLEMENTED: Fla. Stat. §§218.385; 218.415; 1001.41(1); 1001.42(10)(e),(f); 1010.47(2); 1011.12 - 1011.16
HISTORY: 4/19/04; <u>___/___/08</u>

Legal Signoff:

The Legal Department has reviewed proposed, revised Policy 6.085 and finds it legally sufficient for development by the Board.

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Attorney Date