ADOPTED BY THE
MAYOR AND COUNCIL

November 18, 2014

RESOLUTION NO. 22319

RELATING TO FINANCE; APPROVING THE COMPREHENSIVE FINANCIAL POLICIES FOR THE CITY OF TUCSON AS IT RELATES TO THE ISSUANCE OF CERTIFICATES OF PARTICIPATION (COPs); AND DECLARING AN EMERGENCY.

BE IT RESOLVED BY THE MAYOR AND COUNCIL OF THE CITY OF TUCSON, ARIZONA, AS FOLLOWS:

SECTION 1. The Comprehensive Financial Policies for the City Of Tucson as it relates to the issuance of Certificates of Participation (COPs), HAVE BEEN REVISED AND UPDATED TO IMPROVE THE City's debt management policy, attached as Exhibit A, are approved.

SECTION 2. WHEREAS, it is necessary for the preservation of the peace, health, and safety of the City of Tucson that this Resolution become immediately effective, an emergency is declared to exist and this Resolution shall be effective immediately upon its passage and adoption.

PASSED, ADOPTED, AND APPROVED by the Mayor and Council of the City of Tucson, Arizona, November 18, 2014.

MAYOR

ATTEST:

CITY CLERK

APPROVED AS TO FORM:

CITY ATTORNEY

REVIEWED BY:

CITY MANAGER

SS/tl
10/31/14

COMPREHENSIVE FINANCIAL POLICIES

November 2014

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Introduction

The City has an important responsibility to its citizens to carefully account for public funds, to manage municipal finances wisely, and to plan for the adequate funding of services desired by the public, including the provision and maintenance of public facilities. The City needs to ensure that it is capable of adequately funding and providing those government services desired by the community taking into account tight budgets, major changes in federal and state policies toward local government funding, and changes in economic conditions. Ultimately, the City's success and reputation will depend on the public's awareness and acceptability of the management and delivery of these services.

This Financial Policy document is intended to establish guidelines for the City's overall fiscal planning and management. These principles are intended to foster and support the continued financial strength and stability of the City of Tucson as reflected in its financial goals. The Chief Financial Officer/Finance Director has the authority under the City Charter to take appropriate measures to ensure the administration of the financial affairs of the City. If such measures do not follow these policies, the Chief Financial Officer will notify Mayor and Council of such actions.

The financial goals are broad, fairly timeless statements of the financial position the City seeks to attain:

- To deliver quality services in an affordable, efficient and cost-effective basis providing full value for each tax dollar.

- To maintain an adequate financial base to sustain a sufficient level of municipal services, thereby preserving the quality of life in the City of Tucson.

- To provide essential public facilities and prevent deterioration of the City's public facilities and its capital assets.

- To have the ability to withstand local and regional economic fluctuations, to adjust to changes in the service requirements of our community, and to respond to changes in Federal and State priorities and funding as they affect the City's residents.

- To protect and enhance the City's credit rating in the financial community to assure the City's taxpayers that the city government is well managed and financially sound.

- To ensure the legal use of all City funds through adherence to the highest accounting and management practices as set by the Government Finance Officers Association (GFOA) standards for financial reporting and budgeting, by the Governmental Accounting Standards Board (GASB) and other professional standards, and by adherence to State Law.

Following these principles will enhance the City's financial health as well as its image and credibility with its citizens, the public in general, bond rating agencies and investors.

It will also protect the Council's policy-making ability by ensuring that important policy decisions are not controlled by financial problems or emergencies.

To achieve these purposes, it is important to regularly engage in the process of financial planning, including reaffirming and updating these financial policies as City of Tucson continues to grow and develop. Policy changes will be needed as the City continues to grow and becomes more diverse and complex in the services it provides. The City's organization will also require changes to provide these diverse services to its citizens.

I. Fiscal Planning and Budgetary Policy

A. Fiscal Planning

Fiscal planning refers to the process of identifying resources and allocating those resources among competing purposes. The primary vehicle for this planning is the preparation, monitoring and analysis of the City's budget. It is increasingly important to monitor the performance of the programs competing to receive funding.

1. The City uses a five-year long-range financial forecasting system that incorporates both revenue and expenditure estimates for all City funds. The five-year long-range forecast will be updated annually and presented to the City Council prior to the start of the City budget process.

2. Revenue projections will be prepared by the Finance Department and will be budgeted on a conservative basis.

3. The City Manager shall submit to the City Council a proposed annual budget, and with their recommendations, shall execute the budget as finally adopted, pursuant to ARS §42.17101 through §42.17105. The City will budget revenues and expenditures on the basis of a fiscal year which begins July 1 and ends on June 30. The City Council will adopt the budget no later than June 30.

B. Balanced Budget

A balanced budget is a requirement of almost any budget process and is a requirement of State law and City Charter. There are various definitions of a balanced budget. They are:

1. Legally Balanced – This is a budget where the sources of money used to fund the budget are at least equal to the uses of the money. It is a violation of State law and the City Charter to not have this type of balanced budget. Sources include revenues, fund balances, reserves, and borrowings. This minimum level of balancing typically uses one-time monies or fund balance (reserves) to fund expenditures. It is commonly used in difficult budget times.

2. Operationally Balanced – This is a budget that does not use fund balance, reserves, or debt to fund the operating budget. Normal operating revenues are used to fund normal operating expenditures. Reserves, fund balance or debt may be used to fund one-time costs or capital expenditures.

3. Structurally Balanced – This is the most desirable type of budget balancing. In this type of balanced budget, operating revenues equal or exceed operating expenditures in the current year as with an operationally balanced budget AND a realistic projection of the ongoing operating expenditures and revenues into the future shows that operating revenues will continue to equal or exceed

operating expenditures. Reserves, one-time revenues, fund balance or debt may be used to fund one-time cost or capital expenditures.

The City of Tucson must adopt a legally balanced budget and should strive to adopt a structurally balanced budget while considering the long-term impact on the City's financial health. In difficult budget times, the City should strive first to maintain balanced operating budgets and then to achieve a structurally balanced budget as quickly as possible.

C. Budgetary Policies

Annually, the Mayor and Council is to adopt a balanced budget on or before the third Monday in June preceding the beginning of the fiscal year, which sets out the year's revenues and appropriations for each program and item of expenditures.

1. The basis of budgeting is best described as a modified cash basis, because funds are budgeted in the year expended. The adopted annual budget is the basis for the implementation, control, and management of that year's programs and use of funds. The budget will reflect the needs being met, services provided, resources used, and sources of funds.

2. The operating budget will be based on the principle that current operating expenditures, including debt service, will be funded with current revenues creating a structurally balanced budget. The City will not balance the current budget at the expense of increasing future years' needs; for example accruing future years' one-time revenues or rolling over short-term debt to avoid planned debt retirement. NOTE: *Due to the severe economic downturn the City is not currently meeting this goal. The implementation of the Five-Year Financial Planning process will be used to achieve this goal over a reasonable period of time.*

3. The budget will fully appropriate the resources needed for authorized regular staffing. At no time shall the number of regular full-time employees on the payroll exceed the total number of positions authorized by the City Council. All personnel actions shall be in conformance with applicable Federal and State law and all City ordinances and policies.

4. The Budget Office, in consultation with the City Manager, shall provide annually a budget preparation schedule outlining the preparation timelines for the proposed budget. Budget packages for the preparation of the budget, including forms and instructions, shall be distributed to City departments in a timely manner for the Department's completion. Department officials shall prepare and return their budget proposals to the Budget Office, as required in the budget preparation schedule.

5. The budget will be prepared in accordance with the policies and priorities of the Mayor and Council, including the City's approved strategic plan, and in accordance with the guidelines established by the Government Finance Officers

Association in its Distinguished Budget Award Program. The City’s budget will be submitted to the GFOA Distinguished Budget Presentation Program.

6. Performance measurement indicators will be an integral part of the budget process. The departments will annually report progress against their respective performance measures.

7. Alternatives for improving the efficiency and effectiveness of the City's programs and the productivity of its employees will be considered during the budget process. Duplication of services and inefficiency in service delivery will be eliminated whenever they are identified.

8. Consistent with the annual budget process, a five-year capital improvement program will be approved.

D. Use of Non-Recurring Funding Sources

Non-recurring funding sources or “one-time” monies are available for use only once and are not expected to reoccur year after year. One-time monies include fund balance from previous years, unexpected revenues, one-time revenues, or savings from unexpectedly lower expenses in any year. Because these monies are not regular revenues that recur from year to year, good financial practices avoid uses that have ongoing costs because spending could increase to a level that would not be supported by future years’ revenues.

1. Non-recurring monies should not be relied on for ongoing operating purposes.

2. Generally, one-time monies should be used for additions to reserves, for capital purchases, or for one-time expenditures.

3. One-time monies could, under appropriate circumstances, include short-term funding for operating costs. Examples of short-term funding may include the start-up or bridging of an operating program over a short-time period until permanent funding is available, or to shut-down a program over time.

II. Capital Management Policy

The purpose of the Capital Improvement Program is to systematically plan, schedule, and finance capital projects to ensure cost-effectiveness as well as conformance to established policies.

A capital project is an equipment acquisition, a computer/software systems acquisition, or a public improvement that involves construction of new infrastructure, additions to existing structures, renovation of existing structures, and major repairs to infrastructure of a comprehensive and non-routine nature. A capital project is defined in financial terms as a project with a projected final cost of at least $100,000 and is a non-recurring expense. In addition, the capital asset(s) resulting from the project should have a useful life of at least 5 years.

1. The City will develop, maintain and revise when necessary a continuing Capital Improvement Program (CIP).

2. The CIP will cover a five-year planning horizon, identifying infrastructure and facility projects along with the funding sources available for projected expenditures. Capital improvement projects will not be authorized or awarded until the funding sources have been identified to finance the project.

3. The City Council shall approve the annual CIP that addresses all capital investments planned for the budget year and for the subsequent four budget years at the time of adoption.

4. The CIP must include a list of proposed capital improvements with cost estimates, funding sources, time schedules for each improvement and estimated operating and maintenance costs.

5. The CIP will monitor projects in progress to insure their timely completion or the substitution of alternative projects.

6. For major capital projects, the unencumbered and encumbered balances will be considered for reappropriation in the subsequent fiscal year.

7. Studies directly identified with a specific capital project will be included in the CIP. Feasibility studies will be budgeted as an operating expense.

III. Fund Balance Policy – General Fund

An important component of good fiscal practice for any organization is to have a policy on the amount of reserves to be maintained, the purposes for which their use is allowed, and the manner in which reserves are restored after use. Fund balance is an important indicator of the City's financial position.

Fund Balance is comprised of Nonspendable, Restricted, Committed, Assigned, or Unassigned components. This policy refers to unrestricted fund balance which would include the latter three fund balance components: Committed, Assigned, or Unassigned.

City of Tucson's General Fund unrestricted fund balances will be maintained to provide the City with sufficient working capital and a comfortable margin of safety to address emergencies and unexpected declines in revenue without borrowing. This is needed to maintain the City's creditworthiness and to adequately provide for economic and legislative uncertainties, cash flow needs and contingencies.

1. <u>Committed Fund Balance</u>

Mayor and Council action is required to "Commit" and "Uncommit" funds for a specific purpose.

The City will maintain a stabilization fund or "Rainy Day Fund" as a Committed fund balance in the General Fund of ten percent (10%) of General Fund revenues. *NOTE: The City is currently not in conformity with this goal but will strive to achieve within five years.*

The stabilization fund may only be used if specific action is taken by Mayor and Council after the Unassigned/Contingency fund balance is depleted. The stabilization fund will be funded from balances that have remained unspent in assigned fund balance after one fiscal year.

In the event the stabilization fund must be used to provide for temporary funding, the City must restore it to the ten percent level over a period not to exceed five fiscal years following the fiscal year in which the event occurred. If the depletion of the stabilization fund was a result of an ongoing economic downturn the City's goal is to restore the fund balance within five years of revenue stabilization.

2. <u>Assigned Fund Balance</u>

The Chief Financial Officer/Finance Director will approve any designation to "Assigned" Fund Balance as deemed appropriate for potential future needs. Typically, the year-end Assigned Fund Balance represents those fund balance monies budgeted for use in the following fiscal year or for known expenditures in near future.

If the City Manager is recommending assigning a portion of the fund balance, Mayor and Council will be informed within 30 days prior to the finalization of the comprehensive annual financial report.

3. Unassigned Fund Balance

A target of a minimum of seven percent (7%) of General Fund revenues will be "Unassigned/Contingency", with the intention to provide additional stability to the General Fund recognizing the cyclical nature of the economy and the volatility of the major revenue sources of the City. Funds in excess of the seven percent target will be retained in the Unassigned General Fund Balance, and may be considered to supplement "pay as you go" capital outlay expenditures, or may be used to prepay existing City debt. These funds may not be used to establish or support costs that are recurring in nature.

IV. Expenditure Control

Management must ensure compliance with the legally adopted budget. Additionally, purchases and expenditures must comply with legal requirements.

1. Expenditures will be controlled by an annual budget at the purpose level. The City Council shall establish appropriations through the budget process. The Council or City Manager may transfer these appropriations as necessary through the budget amendment process.

2. Department directors are required to control expenditures to prevent exceeding their total departmental expenditure budget. It is the responsibility of these department heads to immediately notify the Budget Director and the City Manager of any exceptional circumstances that could cause a departmental expenditure budget to be exceeded.

3. If a deficit is projected during any fiscal year, the City will take steps to reduce expenditures, increase revenues or use fund balance in accordance with the Fund Balance Policy.

4. The City will maintain a purchasing system that provides needed materials in a timely manner to prevent interruptions to the delivery of services. All purchases shall be made in accordance with the City's purchasing policies, guidelines and procedures as contained in the Tucson Procurement Code in the City Charter, and applicable Federal and State laws. The City will endeavor to obtain supplies, equipment and services as economically as possible.

5. Expenditures will be controlled through appropriate internal controls and procedures for processing invoices for payment. Expenditures will be accounted for in the appropriate accounts.

6. The City shall pay applicable contractor invoices in accordance with the requirements of Arizona Revised Statutes (ARS) §34-221.

7. The State of Arizona sets a limit on the expenditures of local jurisdictions. The City will comply with these expenditure limitations and will submit an audited expenditure limitation report, audited financial statements, and audited reconciliation report as defined by the Uniform Expenditure Reporting System (ARS §41-1279.07) to the State Auditor General each year.

8. The City will monitor the expenditure limitation every year and may choose to pursue a periodic adjustment to its expenditure limitation. This adjustment may be every four years through the City submitting an alternative expenditure limitation (Home Rule) option for approval by the voters at a regular City election (Article IX, Section 20, Subsection 9, Arizona State Constitution). The City may choose to pursue other legally permitted adjustments to its expenditure limitation such as through voter approval of a permanent base adjustment (Article IX, Section 20, Subsection 6, Arizona State Constitution).

V. General Fund Revenues and Collections

All government employees are considered stewards of public funds. In order to provide funding for service delivery, the City must have reliable revenue sources. These diverse revenues must be collected equitably, efficiently, and in a timely manner.

The City's goal is a revenue base balanced between taxes, intergovernmental shared revenues, and other revenue sources such as licenses and permits, user fees, and other miscellaneous revenues.

1. The City will attempt to develop and maintain a diversified and stable revenue base to shelter it from economic changes or short-term fluctuations in any one revenue source by doing the following:

   A. Establishing new charges and fees as needed and as permitted by law
   B. Pursuing legislative change, when necessary, to permit changes or establishment of user charges and fees
   C. Aggressively collecting all revenues, late penalties and related interest as authorized by the Arizona Revised Statutes

2. The City cannot meet the growing demand for services without diversifying its revenue base. Although the State places certain restrictions on raising revenues, restrictions due to the City Charter can be lifted if approved by the voters. The City must continue its efforts to expand revenues such as fees for services, and to remove limitations set by the City Charter where feasible.

3. The City will monitor all taxes to insure they are equitably administered and collections are timely and accurate. Fees and charges should be based on benefits and/or privileges granted by the City, or based on costs of a particular service.

4. The City should pursue intergovernmental aid for those programs and activities that address a recognized need and are consistent with the City's long-range objectives. Any decision to pursue intergovernmental aid should include the consideration of the following:

   A. Present and future funding requirements
   B. Cost of administering the funds
   C. Costs associated with special conditions or regulations attached to the grant award

5. The City will attempt to recover all allowable costs--direct and indirect--associated with the administration and implementation of programs funded through intergovernmental aid. In the case of other governmental entities and school districts, Council may determine to recover less than full cost of services provided. In the case of State and Federally mandated programs, the City will attempt to obtain full funding for the service from the governmental entity requiring the service be provided. Indirect cost rates will be determined based upon a “Cost Allocation Study” prepared periodically.

VI. User Fee and Service Charge Cost Recovery Policy – General Fund

User fees and charges are payments for purchased, publicly provided services that benefit specific individuals. The City relies on user fees and charges to supplement other revenue sources in order to provide public services. This policy does not apply to enterprise funds.

A. General Statement of Policy Purpose

The purpose for this policy is to establish City guidelines regarding the recovery of costs related to services for which fees are charged, including methods for costing and pricing fees, updating fees, etc. One purpose of the fee policy is to offset the need for reductions in City services when there are decreases in revenues or specific mandated increases in expenditures.

B. General Policy Statement

The general policy of the City regarding user fees is based upon the following considerations:

1. The financial policy of the City is that tax dollars should be used towards City services that are available to and benefit everyone in the community.

2. For services that largely or solely benefit individuals, the City should recover full or partial costs of service delivery through user fees.

3. The City should strive to recover the full cost of providing services that principally benefit specific groups or individuals.

4. Administrative costs of imposing and collecting a fee should not exceed revenue expected from the fee.

5. The pricing of user fees will take into consideration:

    a. Whether the service benefits the community in general or only the individual or group receiving the service.
    b. Whether the service is provided only by the public sector, or also by the private sector.
    c. Whether imposing the full cost fee would pose a hardship on specific service users.
    d. Whether imposing the full cost fee would place the City at an economic disadvantage.
    e. Whether <u>not</u> imposing the full cost fee would place the City at an economic disadvantage (e.g., not being able to fund needed recreation programs for already existing recreation facilities).

6. Costs of providing services for which fees are charged should be reassessed annually.

7. Ordinances should not list specific amounts for each fee, but rather how fees should be priced, based upon the fee pricing policies outlined below.

8. For those fees deemed appropriate, a sliding scale discount may be implemented in order to provide low income citizens access to services they may otherwise not be able to utilize.

C. Fee Pricing Policies

Although the City's general policy is that the full cost of services should be recovered, the following criteria are to be used in developing specific fee pricing recommendations, keeping in mind that a service does not have to meet every criteria. An illustration of the pricing policy decision tree is included at the end of this section.

1. Services for which no fee should be charged

   a. The service is equally available to everyone in a community and should benefit everyone.
   b. Because the service is basic, it is difficult to determine benefits received by one user.
   c. The level of service use attributed to a user is not known.
   d. Administrative costs of imposing and collecting a fee exceed revenue expected from the fee.
   e. Imposing a fee would place the City at a serious competitive disadvantage.
   f. The service is primarily provided by the public sector.

2. Partial Fee

   a. Services benefit those who participate but the community at large also benefits.
   b. The level of service use attributed to a user is known.
   c. Administrative costs of imposing and collecting the fee are not excessive.
   d. Imposing a full cost fee would place the City at a competitive disadvantage.
   e. The service is usually provided by the public sector, but may also be provided by the private sector.

3. Full Cost Fee

   a. The individual or group using the service is the primary beneficiary, but the community also benefits.
   b. The level of service use attributed to a user is known.
   c. Administrative costs of imposing and collecting the fee are not excessive.
   d. Imposing a full cost fee would not place the City at a competitive disadvantage.

e. The service is usually provided by the private sector, but may also be provided by the public sector.

4. Market Rate Fees

   a. Individuals or groups benefit from the service and there is little community benefit.
   b. The level of service use is known and the service might not be provided unless a market rate can be charged.
   c. The private sector provides this service, but service demand exceeds supply; therefore, allocation of limited services is required.
   d. Administrative costs of imposing and collecting the fee are not excessive.
   e. The service is provided at market price by the private sector.

D. Cost to Be Considered in Cost Recovery

The following should be considered when determining the cost of providing a service:

1. Direct costs associated with providing the service, including:

   a. The cost of the time all employees spend on the service, including fringe benefits.
   b. Other direct costs, such as supplies and materials, contractual services, or internal service fund charges associated with the service.

2. Building and equipment depreciation.

3. Unit, section, or division supervision, clerical support, etc.

4. Departmental indirect costs.

5. Citywide indirect costs.

In those cases where market pricing is deemed to be appropriate, fees may be based on market rate rather than on cost.

E. Update of Fees

1. Ordinances should not list specific amounts for each fee, but should list the services for which charges are allowed and should reference the pricing methodology (e.g., partial fee or 50% of full cost). Fee policies/pricing methodologies will be reviewed and approved as required by the City's usual administrative regulations.

2. Costs associated with each fee-supported service should be reassessed annually.

3. Fee pricing analyses should also be reconsidered each year.

4. Fee revisions will be submitted to the City Manager for review and presented to Mayor and Council for approval.

PRICING POLICY DECISION TREE

WHO BENEFITS	Entire Community	Primarily the Community & also the Individual	Primarily the Individual & also the Community	The Individual Only
TYPE OF SERVICE	Public	Public/ Private	Public/ Private	Private
APPROPRIATE FUNDING PRICING METHOD	Tax Supported	Partially Tax & Fee Supported	Fee Supported	Market Based Fee Supported
COST RECOVERED	None	Direct Operating Costs Recovered	All Direct Costs & Some Overhead Costs Recovered	All Costs Recovered or Market Rate
EXAMPLES	Fire Suppression Police Library	Fire Medical Sun Tran	Adult Recreation Programs Development Services	Golf Utility Water Utility Commercial Sanitation

VII. Deferred Maintenance Policy

Deferring maintenance is a typical consideration during difficult budget times. Deferred maintenance can include items such as buildings, vehicles, computer hardware and computer software, roads, parks and trees. Deferred maintenance can be relatively benign or it can be problematic and result in higher operating costs and other long term issues.

- Deferring maintenance is an acceptable budget reduction tool. However, it should be done with a clear understanding of the impacts, and management should identify the implications.

- Whether there is deferred maintenance or not, periodic reports should be provided by staff of the maintenance status of all major assets such as building, fleet, roads, and utilities.

- The extent of deferred maintenance, whether temporary or permanent, should be an explicit decision made by Council.

VIII. Cash Management and Investment Policy

PURPOSE

Cash management includes the activities undertaken to ensure maximum cash availability and maximum investment yield at acceptable levels of risk on a government's idle cash. The purpose of this policy is to establish guidelines covering the investment of City monies and to establish reporting guidelines. Cash handling policies and procedures are addressed in Administrative Directive 3.02-1

SCOPE

This investment policy applies to all funds managed directly by the City of Tucson, excluding Certificates of Participation proceeds, Tucson Supplemental Retirement System Custodial/Trust Account or Deferred Compensation Plan funds. The aforementioned excluded funds are governed by the terms of their covenants and/or Boards. The City maintains various portfolios including the City portfolio and special district portfolios. Each portfolio is managed separately but will be referred to collectively as the "portfolio" for purposes of this policy. All funds are accounted for in the City's Comprehensive Annual Financial Report.

The City will maintain a cash flow tracking system for use in projecting the cash needs of the City to optimize the efficiency of the City's investment and cash management program.

POLICY

A. In accordance with Chapter XXIX Section 3 of the City Charter, the Chief Financial Officer/Finance Director is responsible for the investment of City monies. The Chief Financial Officer/Finance Director, or their designee, shall invest all funds of the City according to four criteria, in order of importance: (1) legality, (2) safety, (3) liquidity, and (4) yield.

B. City monies will be invested in accordance with provisions of Chapter XIII Section 12 of the City Charter, various City Ordinances and this Policy. The City shall also comply with the State statutes and Federal laws.

C. Investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived; safety of principal shall not be compromised to earn higher yields. Monies shall be invested at the highest interest rates obtainable after giving consideration to the provisions of this Directive. Payment of investment securities purchased shall be made only upon delivery of the securities to the City of Tucson's custodial bank.

D. Investment maturities shall be scheduled to enable the City to meet all operating requirements which might be reasonably anticipated. Surplus and idle money related to the day-to-day operation of the City may be invested in authorized investments with a final maturity not exceeding five years from the date of investment.

E. Investments shall be limited to the following instruments:

1. Obligations of the U.S. Government and Government Sponsored Enterprises (GSEs);

2. Repurchase agreements whose underlying collateral consists of the foregoing;

3. Commercial paper of ‘prime” quality of the highest ranking or of the highest letter and number rating as provided by a nationally recognized statistical-rating organization (NRSRO) with a maximum maturity of 180 days. Commercial paper of “prime” quality of the second highest ranking or of the second highest letter and number rating as provided for by a NRSRO with a maximum maturity of 90 days.

4. Bonds, notes, and debentures issued by U.S. corporations rated “A” or equivalent by a NRSRO;

5. Money Market funds whose portfolios are limited to the foregoing;

6. Certificates of deposit and other evidences of deposits at banks, savings and loan associations, and credit unions, located in the Tucson city limits, up to the amount insured by an agency of the federal government; deposits in excess of the amount insured are authorized if collateralized by obligations of the U.S. Government, its agencies, and instrumentalities, or General Obligation municipal bonds rated A or better, at the minimum state mandated required amount on deposit, calculated on market values. The collateral must be held by the Trust department of the financial institution or delivered to the City's agent.

7. The State of Arizona Local Government Investment Pool, within the provisions outlined in this directive.

8. Negotiable or brokered certificates of deposit issued by a nationally or state chartered bank or savings and loan association. Eligible negotiable certificates of deposit shall be rated “A” or its equivalent by a NRSRO.

9. Bonds, notes or other evidences of indebtedness of this state or any of its counties, incorporated cities or towns or school districts rated “AA” or equivalent by a NRSRO.

10. Except for direct obligations of the U.S. Treasury, and of GSEs not more than 5% of the portfolio shall be invested in securities of any one issuer.

11. A minimum of 15% of the portfolio shall be in invested in highly liquid securities with a maturity of 6 months or less.

12. Not more than 25% of the portfolio shall be invested in medium-term corporate notes, commercial paper, and negotiable certificates of deposit.

13. Not more than 20% of the portfolio shall be invested in the Arizona municipal securities.

14. Not more than 25% of the portfolio shall be invested in 144A securities. 144 Securities is a safe harbor provision of the Securities Act of 1933 that allows the issuance of securities to large investors without meeting the normal registration requirements established by the Securities and Exchange Commission. To be eligible for purchase, such securities must also meet the investment guidelines listed in this section.

F. Competitive Bidding

1. The City shall maintain a listing of financial institutions which are approved for investment purposes. Banks shall comply with the provisions of the City of Tucson Banking Policy (Administrative Directive 3.01-3). Financial institutions which have received a Community Reinvestment Rating of "Outstanding" or "Satisfactory" and which are determined to be in sound financial condition shall be given the opportunity to bid on City monies available for investment. At minimum, the City shall conduct an annual evaluation of each bank's creditworthiness to determine whether it should be on the "Qualified Institution" listing. Securities dealers not affiliated with a bank shall be required to be classified as reporting dealers affiliated with the New York Federal Reserve Bank, as primary dealers in government Securities.

2. If the City uses an investment advisor, the advisor may be granted discretion to execute transactions utilizing their own list of approved broker/dealers.

3. City monies will be invested with the financial institution offering the highest yield plus the maturity, quality (safety) and diversification required. At least three bids will be solicited for investment securities that are not new issues.

4. A record of bids requested, received, and awarded shall be maintained Finance Department.

5. Bids need not be taken on a rollover of proceeds of a maturing investment for 7 days or less, investments in Government and Agency securities on an initial offering, or on overnight investment of monies in clearing accounts if market rates are offered by the servicing financial institution. The purchase of securities on an initial offering shall be rotated among securities dealers.

6. Bids shall be taken as needed for cash not projected to be spent for immediate operating needs. Securities to be considered in the bid for liquidity funds will include money market funds, repurchase agreements, treasury bills, agency discount notes, and commercial paper.

G. Performance

The City’s portfolio is managed with the objective of obtaining a market rate of return, commensurate with identified risk constraints and cash flow characteristics. Because the composition fluctuates, depending on the market and credit conditions, an appropriate index will be selected by the Chief Financial Officer or Finance Director and used to monitor performance.

H. Reporting

Within 30 days of the last day of each calendar quarter the Finance Department shall prepare and file with the Chief Financial Officer/Finance Director or designee a report on the investment activity for that quarter. Such reports shall at a minimum indicate par value, coupon rate, maturity date, call date (if applicable), cost, market value, yield at cost, yield at market, and unrealized gain or loss. The reports shall also include a listing of purchases and sales/maturities and, if applicable, any realized gain or loss. The Finance Department shall prepare such other reports and analysis as required or requested. All such reports will be made available to the City's independent auditor on an annual basis.

IX. Risk Management

Risk management has become increasingly important in guarding against economic loss and in ensuring public safety during a time of increasing public liability and litigation. Risk management is involved in the identification, analysis, and implementation of the proper risk controls to minimize or eliminate the City's risk exposure.

- The City shall make diligent efforts to prevent or mitigate the loss of City assets and to reduce the City's exposure to liability through training, safety, risk financing and the transfer of risk when cost effective.

- When cost effective, the City shall manage its exposure to risk through self-insurance or through transfer by the purchase of traditional third-party insurance in the following areas: general liability, automobile liability, public officials' errors and omissions, police professional liability, property loss, workers' compensation, and other specialized areas of insurance that may be required from time to time as determined by the City's Risk Manager.

- When cost effective, the City will further control its exposure to risk through the use of "hold harmless" agreements in City contracts and by requiring contractors to carry liability insurance and indemnify the City as determined by the City's Risk Manager.

- Insurance reserves shall be maintained at a level which, together with any purchased insurance, will adequately protect the City's assets and indemnify its elected officials, officers and directors against loss. An actuarial study will be conducted for value of potential unpaid losses and shall be used as a basis for determining self-insurance reserves based on historical loss data. The study will also be used in the rate setting process.

- The City will identify and disclose any material contingent liabilities in the City's Comprehensive Annual Financial Report (CAFR).

- The Risk Management fund has a negative fund balance at the current time. This negative balance has accumulated over many years. It is not possible to restore the fund balance in a short period of time. Rates will be set in the future to cover annual expected costs and reasonably build the fund balance over time.

- The Mayor and Council have established a Self-Insurance Trust. The Board of Trustees will set policies for the administration of the trust and will make recommendations to the Mayor and Council on responsibilities which will include setting policies related to the operation of the City of Tucson's Self-Insurance Trust Fund.

X. Accounting, Auditing and Financial Reporting

Accounting, auditing and financial reporting form the informational infrastructure for public finance. Internal and external financial reports provide important information to the City's legislative body, management, citizens, investors and creditors.

- The City will comply with generally accepted accounting principles (GAAP) in its accounting and financial reporting, as contained in the following publications:

  A. Codification of Governmental Accounting and Financial Reporting Standards, issued by the Governmental Accounting Standards Board (GASB)

  B. Pronouncements of the Financial Accounting Standards Board, (FASB)

  C. Governmental Accounting, Auditing, and Financial Reporting (GAAFR), issued by the Government Finance Officers Association (GFOA) of the United States and Canada

  D. Municipal Budget and Finance Manual, prepared by the League of Arizona Cities and Towns

  E. Audits of State and Local Governmental Units, an industry audit guide published by the American Institute of Certified Public Accounts (AICPA)

  F. Government Accounting Standards, issued by the Controller General of the United States

  G. U.S. Office of Management and Budget (OMB) Circular A-133, issued by the U.S. Office of Management and Budget

- Monthly financial reports will be issued to the City Manager on all departments summarizing financial activity comparing actual revenues and expenditures with budgeted amounts.

- A system of internal accounting controls and procedures will be maintained to provide reasonable assurance of the safeguarding of assets and proper recording of financial transactions of the City and compliance with applicable laws and regulations.

- In accordance with State law, a comprehensive financial audit, including an audit of federal grants according to the Single Audit Act of 1984 and the OMB Circular A-133, will be performed annually by an independent public accounting firm, with the objective of expressing an opinion on the City's financial statements. The City will prepare its financial statements in accordance with applicable standards and will account for its operations in a manner consistent with the goal of obtaining an unqualified opinion from its auditors.

- The City will prepare a Comprehensive Annual Financial Report (CAFR) in accordance with the principles and guidelines established by the Government Finance Officers Association “Certificate of Achievement for Excellence in Financial Reporting” program. The CAFR will be issued by December 31 of each year for the preceding fiscal year or as required by the Arizona Revised Statutes.

- All departments will provide notice of all significant events and financial and related matters to the Chief Financial Officer/Finance Director for the City’s annual disclosures, as required by the Securities Exchange Commission Regulation 15-C-2-12, to the municipal markets, financial statements and bond representations. The Chief Financial Officer/Finance Director will notify the Municipal Securities Rulemaking Board via the Electronic Municipal Market Access (“EMMA”) of material events.

- The City’s CAFR will include the bond related ongoing disclosure requirements and will fully disclose all significant events and financial and related issues as provided by the departments to the Chief Financial Officer/Finance Director. The City will provide the CAFR to the rating agencies, municipal bond insurers and national bond disclosure repositories.

XI. Debt Management Policy

- **Introduction**

This Debt Management Policy (the "Debt Policy") has been developed to provide guidelines for the issuance of bonds and other forms of indebtedness to finance necessary land acquisitions, capital construction, equipment, and other items for the City, and post-closing follow-up with respect to such financings.

While the issuance of debt is frequently an appropriate method of financing capital projects and major equipment acquisitions, such issuance must be carefully monitored to preserve the City's credit strength and to provide the necessary flexibility to fund future capital needs.

The debt policy shall conform to Federal and State regulations.

The debt policy is to be used in conjunction with the Adopted Budget, the Capital Improvement Program (CIP) and other policies as directed by Mayor and Council.

- **Scope**

This Debt Policy shall govern, except as otherwise covered by the City Charter and City Code, the issuance and management of all debt and lease financings funded in the capital markets. While adherence to the Debt Policy is desired, the City recognizes that changes in the capital markets as well as unforeseen circumstances may from time to time produce situations that are not covered by the Debt Policy and may require modifications or exceptions to achieve City goals.

- **Objectives**

This Debt Policy will assist the City in determining appropriate uses of debt financing, establish certain debt management goals, provide guidelines that will result in the lowest cost of borrowing for each transaction and assist the City in maintaining its current credit ratings, while assuming a prudent level of financial risk and preserving the City's flexibility to finance future capital programs and requirements.

- **Assessing Financing Needs for Capital Programs**

The Budget Office is generally responsible for the five-year capital improvement programs of the various City departments that are approved annually by the City Council. These capital programs shall provide the basis for determining long-term capital needs of the City and may be supplemented with longer term capital plans or master plans when appropriate. The Finance Department shall work with the Budget Office and the various City departments to develop a financial forecast related to the capital programs to identify the optimal method to finance the program, including the issuance of bonds. The Finance Department is responsible for reviewing the funding sources and financial forecast to ensure their adequacy in complying with existing bond covenants, debt limits and the potential impact on existing bond ratings prior to the issuance of any new debt.

- **Purpose of Financing**

Generally, financings may be undertaken to fund new projects (new money financing) or to refund existing bonds. Debt can be used to finance essential capital facilities, projects and certain equipment where it is appropriate to spread the cost of the project over more than one budget year and generally for a period not exceeding the useful life of the project being financed. In so doing, the City recognizes that future taxpayers who will benefit from the project will pay a share of its cost.

A. New Money Financing

New money financings are those that generate funding for capital projects. These funds will be used for necessary land acquisitions, capital construction, equipment, and other items for the City. New money bond proceeds are not used to fund operational activities. The City also may use a commercial paper program to provide interim new money financing. The commercial paper is typically retired upon receipt of bond proceeds from a long-term fixed rate financing.

B. Refunding Bonds

Refunding bonds are issued to retire all or a portion of an outstanding bond issue. Most typically this is done to refinance at a lower interest rate to reduce debt service. Alternatively, some refundings are executed for reasons other than to achieve cost savings, such as to restructure the repayment schedule of the debt, to change the type of debt instruments being used, or to retire an indenture in order to remove undesirable covenants. In any event, a present value analysis must be prepared that identifies the economic effects of any refunding being proposed to the City. The target savings amount shall be measured using the present value savings as percentage of par method. The target present value savings from any particular refunding candidate shall generally be at least 3% of the refunded par amount net of all transaction expenses. However, the target savings amounts listed above are not applicable for refunding transactions that are not solely undertaken to achieve cost savings. The Chief Financial Officer/Finance Director shall have discretion in making the final determination to include individual refunding candidates that are slightly below the target in order to optimize the City's financial objectives.

- **Debt Issuance**

A. Method of Sale

There are three methods of issuing debt obligations: competitive sale, negotiated sale and private placement.

1. Competitive Sale

The City, as a matter of policy, shall seek to issue its debt obligations in a competitive sale unless it is determined that such a sale method will not produce the best results for the City.

2. Negotiated Sale

The City may elect to sell its debt obligations through a negotiated sale. Such determination may be made on an issue by issue basis, for a series of issues, or for part or all of a specific financing program. Selection of the underwriting team shall be made pursuant to selection procedures set forth in these Debt Policies.

3. Private Placement

The City may elect to sell its debt obligations through a private placement or limited public offering. Selection of a placement agent shall be made pursuant to selection procedures developed by the Chief Financial Officer/Finance Director.

Each type of bond sale has the potential to provide the lowest cost given the right conditions. A decision as to the type of bond sale will consider market conditions at that time. Characteristics for which each type of bond sale is best used are provided below.

B. Method of Sale Considerations: Issuer Characteristics

1. Market Familiarity

A frequent issuer of a well-recognized credit such as general obligation bonds can generally sell these bonds through a competitive sale since investors and underwriters are familiar with the quality of the credit. A negotiated sale may be appropriate if extensive pre-marketing to investors is desired or required.

2. Credit Strength

The higher the credit quality of the bonds being issued, the more likely the bonds can be sold using a competitive sale due to the high demand for high quality municipal bonds. High quality credits fare well in competitive sales.

3. Policy Goals

A competitive sale does not provide the City with the flexibility of choosing the underwriter or underwriter syndicate. If the Chief Financial Officer/Finance Director concludes that determining the composition of the underwriter syndicate to achieve certain policy objectives is important, then a negotiated sale would be required.

C. Method of Sales Considerations: Financing Characteristics

1. Type of Debt Instrument

The market favors familiar debt instruments such as general obligation bonds backed by the full faith and credit of the City. New credit types may require an education process that is more conducive to a negotiated sale until the market becomes comfortable with the credit.

2. Issue Size

The size of the bond sale will influence both investor interest in the bonds and the market's ability to absorb the bonds. In general, if the bond sale is too small or too large, a negotiated sale may be necessary. A small sale may require greater marketing to obtain investor interest while a large sale may be difficult for the market to absorb without the presale activity available in the negotiated sale process.

3. Market Conditions and Timing

During periods of stable interest rates, market timing is not as critical. However, during periods of volatile interest rates, the timing of the sale becomes more critical. Bond refundings are also often very interest rate sensitive in terms of the potential level of savings or the general feasibility of the refunding. A negotiated sale provides more flexibility in terms of the structure of the bond sale as well as the timing of the bond sale and may be more appropriate when issuing refunding bonds and when interest rates are volatile.

4. “Story” Bonds

Bonds that require a detailed explanation due to the complexity of the credit or the security for the bonds are often referred to as "Story Bonds". Due to their complexity and the additional explanation these bonds require, an extensive pre-marketing campaign is necessary. Story Bonds often require a negotiated sale composed of an underwriting syndicate that is qualified to market the bonds in order to obtain the lowest financing cost for the City.

- **Financial Service Providers**

  The City's Chief Financial Officer/Finance Director shall be responsible for establishing a solicitation and selection process for securing professional services that are required to develop and implement the City's debt program. The solicitation and selection process for such services will comply with City Code requirements. In connection with debt financings, financial advisors, underwriters, bond counsel and other service providers will be selected from a Qualified Vendors List (QVL) developed through a periodic Request for Qualifications (RFQ) process or, for individual financings, through a Request for Proposals (RFP) process, whichever method is deemed most appropriate given the specifics of the financing. Contracts may be awarded on a sole source basis if it is clear that an RFQ/RFP process is not feasible or not in the best interest of the City. The City may also rely on statewide pools that have been formed through an RFP process. Underwriters or underwriter syndicates will be selected by the Chief Financial Officer/Finance Director. The firm selected as financial advisor may not serve as underwriter in any competitive public sale or negotiated sales issued by the City. Goals of the solicitation and selection process shall include encouraging participation from qualified service providers and securing services at competitive prices.

- **Tax Status**

  Prior to the issuance of any bonds, the Finance Department, in conjunction with bond counsel and the City Attorney will evaluate the tax status of any bond sales.

  A. Tax-Exempt

     Interest on tax-exempt bonds is excluded from the gross income of its owners for federal and Arizona income tax purposes and as a result tax-exempt bonds can be sold at a lower true interest cost than taxable bonds. The City, along with bond counsel, will evaluate all projects to be funded to assess their eligibility to be funded by tax-exempt bonds. The City will make every effort to ensure that all tax regulations are complied with to ensure the bonds maintain their tax-exempt status.

  B. Taxable

     Certain municipal bonds are sold as taxable bonds because they are issued for purposes that the federal government has determined do not provide a significant benefit to the public at large or involve "private activity". In addition, certain tax laws such as the alternative minimum tax (AMT) reduce the benefits of the tax exemption for certain types of bonds and for certain taxpayers. Taxable bonds will be used whenever a particular project has the potential for private activity or other uses that may call into question the eligibility to use tax-exempt financing.

The City may also issue taxable bonds to take advantage of special federal programs such as the American Recovery and Reinvestment Act (ARRA) Build America Bonds if a savings can be achieved.

- **Rate Structure for Debt**

A. Fixed Rate Debt

Long term fixed rate debt is debt where the interest rate for each maturity is “fixed” or set at the time the debt is issued and does not change over the life of the debt. Fixed rate debt provides the benefit of fixed payments during the life of the bonds and budget certainties for long-term capital planning. However, fixed rate debt is typically longer term and carries higher interest payments (assuming a normal upward sloping yield curve) than variable rate debt but is not subject to changes in interest rates and other risks. Fixed rate debt is the most common type of debt issued by the City.

B. Variable Rate Debt

The municipal bond market has developed several vehicles by which municipalities can borrow at short-term rates. Variable rate bonds or notes may be issued with interest rates that "reset" daily, weekly, monthly or semi-annually at the option of the City. Commercial paper is issued with a maturity of up to 270 days at the City's option. As the commercial paper matures, it may be resold by a remarketing agent for another period up to 270 days.

These products are structured as a rolling series of short-term investments and therefore are priced at the short-end of the yield curve at lower interest rates than long-term fixed rate bonds (assuming a normal upward sloping yield curve). By accepting the risks inherent in variable interest rates, the City can take advantage of the lower rates available in the current market.

Factors that will be considered in the use of variable rate debt are the availability and size of fund balances to cover variable rate risk, the budget flexibility of the program being financed and other remarketing risks. Programs with large complex capital programs may use short-term financing to fund uncertain construction cash flow requirements. The short-term debt can then be refinanced as fixed-rate, long-term debt once the projects are complete. A project that must be carried in anticipation of grant funding may also be a candidate for the use of variable rate financing.

C. Derivatives Policy

The City may in the future choose to enter into contracts and financing agreements involving interest rate swaps, floating/fixed rate securities, or other forms of debt bearing synthetically-determined interest rates as authorized under Arizona statutes. Before entering into such contracts or agreements, a review team consisting of the Chief Financial Officer/Finance Director, appropriate City staff and outside consultants shall be formed to review the risks and benefits of such financing techniques including the expected impacts on the City's long term financial operations and credit ratings. The City Manager or their designee will review and approve all plans before any recommendations are submitted to Mayor and Council for authorization and implementation.

- **Type of Debt**

A. General Obligation (GO) Bonds

GO bonds are backed by the full-faith and credit of the City and are secured by secondary property taxes. GO bonds are recommended by a Citizens' Bond Committee and referred to the voters for approval. The Bond Project Oversight Committee reviews and monitors the programs approved by the voters. Chapter IV, Section 2 of the Tucson City Charter currently sets an upper primary and secondary property tax limit of $1.75 per $100 assessed value as a condition upon the City's continuing ability to impose and collect transaction privilege taxes. Therefore, state laws notwithstanding, the City will not levy a combined primary and secondary property tax that exceeds $1.75.

B. Lease-Purchase Financing and Certificates of Participation (COPs)

Lease-purchase agreements are used to acquire tangible assets or improvements to tangible assets on behalf of the City, often, but not always, for smaller and short-lived assets or shorter terms than conventional bond issues or for pools of such assets. For larger financings, undivided proportionate interests in the lease-purchase agreement, known as certificates of participation, or COPs, may be sold. This structure mitigates risk to the investor and lowers borrowing costs for the City. From a legal perspective, because lease payments for COPs and lease-purchase financings are subject to annual appropriation, they do not constitute indebtedness of the City for Constitutional or statutory purposes. Consequently, they are also not subject to the statutory requirements for voter approval. However, from an accounting perspective, COPs are considered a long-term liability, since obligations extend beyond one year.

Typically the asset to be acquired or improved is acquired by or leased to a trustee (through a nonprofit corporation or directly with a corporate trust department) and, in turn, leased back to the City, which makes lease payments for the benefit of the investors in the lease or COP holders. The City shall not enter into a lease-leaseback transaction on one asset and use the proceeds to improve a different asset, unless appropriate consents and approvals have been granted by the bond insurer and trustee. Upon payment of the final lease payment, the City acquires all right, title and interest in the asset.

C. Highway User Revenue Fund (HURF) Bonds

HURF Bonds are payable from and secured by State-shared gas taxes and other highway user fees and are issued with voter approval to provide capital funding for City owned and maintained streets and highways.

D. Special Assessment Bonds

Special assessment bonds are a special type of municipal bond used to fund development projects that benefit a discrete group of taxpayers or a specified geographical area, known as a special assessment district. Principal and interest on the bonds is paid from assessments imposed on the individuals benefiting most directly from the particular bond-funded project. The creation of an improvement district must be approved by the Mayor and Council. The City traditionally has made limited use of special assessment debt.

E. Community Facilities District (CFD) Bonds

Community facilities districts (CFDs) are established pursuant to State law for the purpose of financing specified public improvements within the district. The City determines whether and for what specific purposes a CFD will be formed and the Mayor and Council typically serve as the board of directors of the CFD. CFDs may issue general obligation, revenue or special assessment bonds depending on the nature of the public improvement to be acquired or constructed and the most feasible financing source. The formation and operation of a CFD, including the issuance of any bonds, is reviewed and managed by the Finance Department. Depending on the type of bonds issued, debt service on CFD bonds is paid from an *ad valorem* tax or assessment on the real property in the district or from revenues of a revenue-generating improvement. The operation and maintenance of the CFD is paid from an *ad valorem* tax on the real property in the district. Mayor and Council approved guidelines and application procedures for the establishment of CFD per Resolution 21125 dated October 21, 2008.

- **Limitations on City Indebtedness**

The determination of how much indebtedness the City can afford begins by assessing the sufficiency of future tax and other revenues. The amount of debt issued is based on the requirements of the approved 5-year CIP, subject to the condition that sufficient revenues are projected to be available. Factors such as debt service coverage requirements outlined in the bond indentures, the impact on the businesses and citizens in the City (tax rates), and any impact on the bond ratings will be carefully considered. Different factors are considered for each type of credit.

A. Target Limitation on General Obligation Debt

State statutes limit the amount of debt that a municipality can have outstanding. In general the City's outstanding general obligation debt for the water, parks, public safety, transportation and street lighting programs is limited to 20 percent of the City's secondary assessed valuation (AV) and for all other programs the amount of outstanding debt is limited to 6 percent of the City's secondary AV. Other factors such as providing capacity for future programs will also be taken into consideration.

The Tucson City Charter limits the combined primary and secondary property tax rate to $1.75 per $100 of assessed valuation as a condition upon the City's continuing ability to impose and collect transaction privilege taxes.

B. Target Limitations on the Issuance of Revenue-Secured Debt Obligations.

The City will seek to finance the capital needs of its revenue producing enterprises through the issuance of revenue-secured debt obligations. Prior to issuing revenue-secured debt obligations, City Departments, in consultation with the Chief Financial Officer/Finance Director, will develop financial plans and projections showing the feasibility of the planned financing, required rates and charges needed to support the planned financing, and the impact of the planned financing on ratepayers, property owners, City Departments, and other affected parties. The amount of revenue-secured debt obligations issued by the City will be limited by the feasibility of the overall financing. Revenue secured debt levels shall be limited by coverage and parity bond covenants and potential credit rating impacts.

C. Target Limitation on Lease-Purchase Financing

In order to control fixed costs and maintain budget flexibility, the City shall carefully monitor debt levels for COPs. During each budget cycle, the Finance and Budget Departments shall work with requesting departments and Mayor and Council to review and prioritize long-term projects and equipment needs that may be eligible for financing. The long-term impact of project specific debt service on the General Fund, will be the first consideration, before any project or equipment need is approved for COPs. This analysis shall consider sustainability, affordability and direct impacts to General Fund fixed costs and subsidies.

The following limitations shall apply for the issuance of COPs.

The Average Annual Debt Service shall generally not exceed ten percent (10%) of the General Fund's Average Operating Revenues.

Average Annual Debt Service shall be defined as follows: Total Debt Service divided by five (5), where Debt Service:

1. Includes annual principal and interest payments due each year, for the subsequent five (5) years, on all outstanding COPs, including payments funded by a revenue source outside the General Fund.
2. Includes the projected annual principal and interest payments due each year, for the subsequent five (5) years, on COPs proposed to be issued to fund equipment or a long-term project that is eligible for financing.

Average Operating Revenues in the General Fund shall be defined as follows:

1. Total General Fund revenues excluding other financing sources and use of fund balance.
2. Incorporates a five (5) year average that includes four years of audited actual operating revenues and one year of the most recently adopted budgeted revenues.

Outside of COPs, the City may enter into short-term lease-purchase obligations to finance the acquisition of capital equipment with estimated useful lives of less than ten years. Repayment of these lease-purchase obligations must be within departmental budget and shall occur over a period not to exceed the useful life of the underlying asset.

The Finance Department shall be responsible for developing procedures for use by City Departments interested in participating in the lease-purchase program, and for setting repayment terms and amortization schedules, in consultation with participating departments.

D. Target Limitations on General Fund Loan Guarantees and Credit Support

As part of the City's financing activities, General Fund resources may be used to provide credit support or loan guarantees for public or private developments that meet high priority City needs. Before such General Fund commitments are made, specific policy goals and objectives that determine the nature and type of projects qualifying for such support, and specific limitations to be placed on the maximum amount of General Fund resources committed to such projects, shall be developed. The Finance Department shall be responsible for coordinating the development of such policies and goals, which shall not take effect until approved by the City Manager.

Recognizing the limited capacity of the City's General Fund to support both ongoing operating programs and secure long-term debt obligations, use of the General Fund to secure such obligations must first be approved by the City Manager. Key factors that will be considered in determining whether or not the General Fund should be used to secure a particular debt obligation will include the following:

1. Demonstration of underlying self-support, thus limiting potential General Fund financial exposure.

2. Use of General Fund support as a transition to a fully stand alone-credit structure, where interim use of General Fund credit support reduces borrowing costs and provides a credit history for new or hard to establish credits.

3. General Fund support is determined by the Mayor and Council to be in the City's overall best interest.

- **Transparency for COPs Debt and Use of Emergency Clause**

In order to enhance transparency to the community regarding the issuance of COPs, the request for Mayor and Council approval to issue COPs shall be placed on a Regular Agenda, as a separate item, and include a public hearing, prior to sale in the capital market.

The request for Mayor and Council approval to issue new money COPs must include documentation showing that the issuance is in compliance with target limitations set forth in this policy.

In order to facilitate timely entry into the capital markets, an emergency clause may be used in the COPs issuance resolution. The ultimate goal is to enter the market at such a time to capture favorable interest rates, enabling the City to take advantage of the lowest possible borrowing costs.

- **Structural Features**

A. Maturity

The final maturity of a bond sale shall be equal to or less than the remaining useful life of the assets being financed, and the average life of the financing shall not exceed 120% of the weighted average useful life of the assets being financed.

B. Debt Service Structure

The Chief Financial Officer/Finance Director will carefully consider the debt service structure for each bond issue. Factors such as the flow of revenues available for a particular credit, the need to fill in gaps created by refunding specific principal maturities or to structure savings from a refunding in a particular year will be considered. Accelerated repayment may be considered within the bonding capacity constraints to provide capacity for future capital programs.

C. Lien Levels

Senior, Junior and Subordinated Junior Liens for each revenue source will be utilized in a manner that will maximize the most critical constraint -- typically either cost or capacity -- thus allowing for the most beneficial use of the revenue source securing the bond.

- **Credit Ratings**

A. Rating Agency Relationships

The Chief Financial Officer/Finance Director shall be responsible for maintaining relationships with the rating agencies that assign ratings to the City's various debt obligations. This effort shall include providing periodic updates on the City's general financial condition along with coordinating meetings and presentations in conjunction with a new debt issuance.

B. Use of Rating Agencies

The Chief Financial Officer/Finance Director shall be responsible for determining whether or not a rating shall be requested on a particular financing, and which of the rating agencies shall be asked to provide such a rating.

C. Minimum Long-Term Rating Requirements

The City's minimum rating requirement for its direct, long-term, debt obligations is a rating of "A" or higher. If such a debt obligation cannot meet this requirement based on its underlying credit strength, then credit enhancement shall be sought to ensure that the minimum rating is achieved. If credit enhancement is unavailable or is determined by the Chief Financial Officer/Finance Director to be uneconomic, then the obligations may be issued without a rating.

A lower rating standard may be accepted for indirect or conduit obligations, subject to the approval of the Chief Financial Officer/Finance Director.

- **Credit Enhancement**

Although the City has high credit ratings, credit enhancement through the use of bond insurance or a bank facility such as a letter of credit to strengthen the underlying credit rating of certain bonds may be financially beneficial. Bond insurers will usually be rated AA or higher and, through the purchase of bond insurance, the insured bonds will also receive the rating and thus be able to be sold at a lower interest rate. Bank facilities, such as letters of credit from highly rated banks, can also be used to provide credit enhancement.

A. Bond Insurance

Bond insurance will be considered when it provides an economic benefit to a particular bond maturity or entire issue. Bond insurance provides improved credit quality for the bonds as a result of the insurance provider's guarantee of the payment of principal and interest on the bonds. Because of the decreased risk of non-payment, investors are willing to purchase insured bonds at lower yields than uninsured bonds, thus providing the issuer with interest cost savings.

1. Benefit Analysis

The decision to use bond insurance is an economic decision. The analysis compares the present value of the interest savings to the cost of the insurance premium. Insurance will be purchased when the premium cost is less than the present value of the projected interest savings.

2. Provider selection

The City or its financial advisor will undertake a competitive selection process when soliciting pricing for bond insurance, or in the case of a competitive sale, facilitating the prequalification of bonds by insurance providers. The City recognizes that all providers may not be interested in providing bids to the City or pre-qualifying the issue. For competitive sales with bidder’s option, the winning bidder will determine whether it will purchase insurance for the issue. For a negotiated sale, the Chief Financial Officer/Finance Director shall have the authority to purchase bond insurance when deemed advantageous and the terms and conditions governing the guarantee are satisfactory.

B. Bank Facilities (Letters of Credit)

When used for credit enhancement, letters of credit ("LOC") represent a bank's promise to pay principal and interest when due for a defined period of time, subject to certain conditions. In the case of a direct-pay LOC, the trustee will draw upon the LOC to make debt service payments and the City will reimburse the LOC provider the amount drawn on the LOC by the trustee. A standby LOC is used to ensure the availability of funds to pay principal and interest of an obligation only if the funds in the debt service account held by the trustee are insufficient to make the debt service payment on the bonds.

C. Capitalized Interest

Subject to Federal and State law, interest may be capitalized from the date of issuance of debt through the completion of the construction to a maximum of 3 years. Interest may also be capitalized for projects in which the revenue designated to pay debt service on the bonds will be collected at a future date, not to exceed six months from estimated completion of construction. Any use of capitalized interest will require a review by bond counsel and approval by the Chief Financial Officer/Finance Director.

- **Investment of Bond Proceeds**

  The City shall comply with all applicable Federal, State, and indenture restrictions, if any, regarding the use and investment of bond proceeds. This includes compliance with any restrictions on the types of investment securities allowed, restrictions on the permissible yield of invested funds as well as restrictions· on the time period over which some bond proceeds may be invested. The Chief Financial Officer/Finance Director, or his/her designee, will direct the investment of bond proceeds in accordance with the permitted investments for each particular bond issue. Investments such as guaranteed investment contracts may be considered when their use is in the best interest of the City and will be selected on a competitive basis.

- **Continuing Disclosure**

  The City will comply with its Continuing Disclosure Agreements with respect to Rule I5(c) 2-12 of the Securities and Exchange Commission, by filing an annual report and annual financial information, as well as material event notices, with the Electronic Municipal Market Access ("EMMA") system maintained by the Municipal Securities Rulemaking Board to provide certain financial information and operating data relevant to investors.

- **Post-Closing Compliance**

  The City shall comply with all arbitrage rebate requirements as established by the Internal Revenue Service and the Finance Department shall establish a system of record keeping and reporting to meet the arbitrage rebate and other compliance requirements of the federal tax code. This effort shall include tracking project expenditures financed with bond proceeds, tracking investment earnings on bond proceeds, calculating rebate payments in compliance with tax law, and remitting any rebatable earnings to the federal government in a timely manner in order to preserve the tax exempt status of the City's outstanding tax-exempt debt issues. The Chief Financial Officer/Finance Director, or his/her designee, may enter into agreements with arbitrage service providers to assist the City with complying with arbitrage regulations. In addition, the Finance Department will monitor the uses of tax exempt financed facilities to determine whether impermissible private use of those facilities is occurring.

XII. Policy Review

By their nature policies must change and evolve over time. As with any other policies, these financial policies should be subject to periodic review and revision.

The Finance Director/Chief Financial Officer will review the financial policies contained in this document every three years or revise as necessary when significant changes occur and Mayor and Council will affirm the revisions.

The Independent Audit and Performance Commission will review the policies as requested by the Council, City Manager, or the Finance Director and provide any recommended changes to the City Manager and Mayor and Council.