RESOLUTION NO. 510

RESOLUTION OF THE COUNTY COUNCIL OF DORCHESTER COUNTY, MARYLAND ADOPTING A DEBT MANAGEMENT POLICY

WHEREAS, the adoption of financial policies is recognized as a best practice in public budgeting; and

WHEREAS, financial policies should be an integral part of the development of service, capital and financial plans and the budget; and

WHEREAS, the County Council desires to develop a policy to recognize a binding commitment to full and timely repayment of all debt as an intrinsic requirement for entry into the capital markets and that adherence to a debt management policy helps to ensure that a government maintains a sound debt position and that credit quality is protected.

NOW THEREFORE, BE IT RESOLVED, by the County Council of Dorchester County, Maryland that the Fiscal Policy on Debt Management (summarized below) be adopted:

DORCHESTER COUNTY, MARYLAND

Fiscal Policies and Procedures – Debt Management

SECTION I - INTRODUCTION

The County Council of Dorchester County, Maryland approved on September 6, 2011 by resolution, the following policy on debt management.

SECTION II - AUTHORITY AND DELEGATION

Article 25, Section 3 of the Annotated Code of Maryland authorizes the County Council to adopt by Resolution administrative acts. Pursuant to Resolution Number 510 of the County Council of Dorchester County, Maryland this policy shall supersede any previously adopted or practiced policy on debt management.

SECTION III – PURPOSE

The debt management policy recognizes a binding commitment to full and timely repayment of all debt as an intrinsic requirement for entry into the capital markets. Adherence to a debt management policy helps to ensure that a government maintains a sound debt position and that credit quality is protected. Advantages of a debt policy are as follows:

- Enhances the quality of decisions;
- Rationalizes the decision-making process;
- Identifies objectives for staff to implement;
- Demonstrates a commitment to long-term financial planning objectives; and

• Is regarded positively by the rating agencies.

This policy's primary objective is to establish conditions for the use of debt and create procedures and policies that minimize the County's debt service and issuance costs, retain the highest practical credit rating, and maintain full and complete financial disclosure and reporting. These policies are guidelines for general use, and allow for exceptions in extraordinary conditions.

Regular, updated debt policies can be an important tool to ensure the use of the County's resources to meet its commitments to provide needed services to the citizens of Dorchester County and to maintain sound financial management practices. The County's debt program should be continuously monitored to ensure that it is in compliance with the debt policy. The debt policy should also be periodically updated to ensure that it remains consistent with financial and management objectives and capital market trends.

SECTION IV - APPLICABILITY

This fiscal policy applies to all elected officials and all departments, offices, agencies, boards, and commissions of Dorchester County, Maryland government unless otherwise excluded.

SECTION V - EXCLUSIONS

None

SECTION VI - POLICY

USE OF DEBT FINANCING

Debt financing will not be used for any recurring purpose such as current operating and maintenance expenditures. The County will use debt financing only for one-time capital improvement projects and unusual equipment purchases, and only under the following circumstances;

- When the project is included in the County Capital Improvement Budget;
- When the project involves acquisition of equipment that can't be purchased outright without causing an unacceptable spike in the property tax rate;
- When the project is the result of growth-related activities within the community that require unanticipated and unplanned infrastructure or capital improvements by the County;
- When the project's useful life, or the projected service life of the equipment, will be equal to or exceed the term of the financing;
- When there are designated revenues sufficient to service a debt, whether from project revenues, other specified and reserved resources, or infrastructure cost sharing revenues.

The following criteria will be used to evaluate pay-as-you-go versus debt financing in funding capital improvements:

Factors which favor pay-as-you-go financing include circumstances where:

- The project can be adequately funded from available current revenues and fund balances;
- The project can be completed in an acceptable timeframe given the available revenues;
- Additional debt levels could adversely affect the County's credit rating or repayment sources;
- Market conditions are unstable or suggest difficulties in marketing debt.

Factors which favor long-term financing include circumstance where:

- Revenues available for debt issues are considered sufficient and reliable so that long-term financing can be marketed with an appropriate credit rating, which can be maintained;
- Market conditions present favorable interest rates and demand for County debt financing;
- A project is immediately required to meet or relieve capacity needs and existing un-programmed cash reserves are insufficient to pay project cost;
- The life of the project or asset financed is five years or longer.

COMPREHENSIVE CAPITAL PLANNING

<u>Capital Improvement Plan</u>
The County will prepare a capital budget for consideration and adoption by the County Council as part of the County's budget process. The plan is updated annually. The Plan shall contain a comprehensive description of revenue sources and expenditures, the timing of capital projects for future operating and capital budgets, effect of the projects on future debt sales, debt outstanding and debt service requirements, and the impact on future debt burdens and current revenue requirements.

<u>Debt Authorization</u>
No County debt issued for the purpose of funding capital projects may be authorized by the County Council unless an appropriation has been included in the Capital Improvement Plan or until the County Council has modified the Plan. Limitations on debt are set by State authorization, 25% limitation on utility debt, and a self-imposed debt affordability analysis.

MAXIMUM AMOUNTS OF DEBT FINANCING

General Obligation Bonds - Debt capacity shall be evaluated on an annual basis, at the time of the adoption of the Capital Improvement Plan. The County should examine statistical measures to determine debt capacity and compares these ratios to other counties, rating agency standards, and Dorchester County's historical ratios to determine debt affordability. Only one measure is legally binding -- the County's utility debt cannot exceed 25% of the total assessed valuation of all of the property in the County that is subject to County taxation during the County's most recent fiscal year. In order to determine the County's relative debt position, four additional measures should be used.

Debt measured against the population on a per-capita basis - This tax-base concept reflects the philosophy that all taxes, and therefore the total principal on outstanding debt, are paid by the citizenry. The County's goal should be the peer group ratio for Maryland counties in net direct debt per capita, not to exceed $1,500.

Debt as a percentage of Fair Market Value (FMV) of taxable property - The fair market value of all taxable property within the County is an important measure of the County's wealth to support present and future revenue/taxing capacity to meet obligations. This tax-base concept reflects the predominant use by municipalities of property taxes as the earmarked source of debt service for general obligation bonded debt. The County's goal should be the peer group ratio for Maryland counties of approximately in net direct debt, not to exceed 1.5%.

Debt service as a percentage of General Fund revenues - This concept reflects the measure of resources that are available for day-to-day operations of the municipality; this measure is appropriate when debt service is essentially paid for with General Fund revenues, as is largely the case in Dorchester County. The County's goal should be the peer group ratio for Maryland counties, not to exceed 8%.

Debt service per capita as a percentage of personal income per capita – This concept incorporates an *ability to pay* component into the evaluation of debt service burden. The County's goal should be the peer group ratio for Maryland counties, not to exceed .5%.

Revenue Bonds - For the County to issue revenue bonds, projected revenues in excess of operating expenses less capital expenditures shall be a minimum of 125% of the average annual debt service and 110% of the debt service for the year in which requirements are scheduled to be the greatest.

TYPES OF DEBT

The County is encouraged to issue long-term, tax-exempt revenue or General Obligation debt. It is acknowledged that circumstances may warrant the use of other debt instruments, and decisions should be made on a case-by-case basis.

General Obligation Bonds – The County shall use an objective analytical approach to determine whether it can afford to issue new bonds for County facilities beyond what it retire each year. Generally, this process will compare a variety of measure of debt benchmarks relative to key demographic data of the County. The decision on whether or not to assume new general obligation bonds, in part, is based on (a) costs and benefits, (b) the current conditions of the municipal bond market, and (c) the County's ability to assume new general obligation bonds as determined by the aforementioned benchmarks.

Short-Term Debt and Interim Financing - Use of short-term borrowing, such as bond anticipation notes (BANs) and tax-exempt commercial paper, should be undertaken only if the transaction costs plus interest of the debt are less than the cost of internal financing, or available cash is insufficient to meet working capital requirements. The term of short-term financing will be limited to the usual useful life of the asset, but in no case will exceed ten years.

Variable-Rate Debt - When appropriate, the County may choose to issue securities that pay a rate of interest that varies according to a predetermined formula or results from a periodic remarketing of the securities. The County should have no more than 15% of its outstanding general obligation bonds in variable rate form.

Lease/Purchase Agreements - The use of lease/purchase agreements in the acquisition of vehicles, equipment and other capital assets shall be considered carefully relative to any Dorchester County, other financing options or a "pay-as-you-go" basis. The lifetime cost of the lease typically will be higher than other financing options or cash purchases. Nevertheless, lease/purchase agreements may be used by the County as funding options for capital acquisitions if operational or cash-flow considerations preclude the use of other financing techniques. See Annual Appropriation Financing Policy for additional detail on lease/purchase financings.

Conduit Financings - Conduit financings are securities issued by a government agency to finance a project of a third party, such as a non-profit organization or other private entity. The County may sponsor conduit financings for those activities (e.g., economic development, housing, etc.) that have a general public purpose and are consistent with the County's overall service and policy objectives. Unless a compelling public policy rationale exists, such conduit financings will not in any way pledge the County's faith and credit. See Annual Appropriation Financing Policy for additional detail on conduit debt.

Taxable Debt - State and local governments can gain several advantages by issuing taxable debt, namely the removal of arbitrage regulations and volume cap restraints. However, taxable debt also carries a higher interest rate than tax-exempt debt and eliminates one of the main advantages of purchasing municipal debt for bondholders. Accordingly, if the use of taxable debt is considered, the County will complete a thorough analysis of all attributes of such use, giving consideration to factors outlined in GFOA's *Recommended Practice on Issuing Taxable Debt by U.S. State and Local Governments*, including careful consideration of its legality and market conditions. Development Financing - Development Financing may be established when revenues will recover the public cost of debt with adequate safety margin. All proposed Development debt issuances are to follow the Development Financing Policy which is separate from the Debt Management Policy.

STRUCTURAL FEATURES

Structure - Debt will be structured to achieve the lowest possible net cost to the County given market conditions, the urgency of the capital project, and the nature and type of security provided. The County may choose to structure debt repayment so as to wraparound existing obligations or to achieve other financial planning goals, but in most cases, it should strive for level debt service.

Repayment Schedule - To the extent possible, the County will design the repayment of its overall debt so as to recapture rapidly its credit capacity for future use. The County will strive to repay at least 25 percent of the principal amount of its general obligation debt within five years and at least 50 percent within ten years.

Asset life - Debt will not be issued for periods exceeding the useful or average useful lives of the project or projects to be financed, not be greater than 30 years.

Call provisions – Call provisions for bond issues shall be made as short as possible consistent with the lowest interest cost to the County. Unless specific compelling reasons exist all bonds shall be callable only at par.

Credit Enhancement - The County may use credit enhancement (letters of credit, bond insurance, etc.) when net debt service on the bonds is reduced by more than the costs of the enhancement or to achieve the County's minimum bond rating requirement.

Use of Subordinate Lien Obligations - The County shall issue subordinate lien debt only if it is financially beneficial to the County or consistent with creditworthiness objectives.

Derivative Products - The use of derivatives in administering debt can be useful to minimize risk, reduce costs, and provide flexibility. However, they can also add risk, restrict flexibility, or add cost. Accordingly, if the use of derivatives is considered, the County will complete a thorough analysis of all attributes of such use, giving consideration to factors outlined in GFOA's *Recommended Practice on Use of Derivatives by State and Local Governments* and consulting with the Financial Advisor.

Capitalized Interest – The capitalized costs of interest during construction for debt financed projects are the costs of interest related to the acquisition or construction of an asset. The interest costs should be capitalized during the period of time that is required to complete and prepare the asset for its intended use. Interest shall not be capitalized beyond a three year period or if the calculated capitalization cost are equal to or below the asset threshold of $10,000.

METHOD OF SALE

Competitive Sale - The County should seek to issue its debt through a competitive bidding process unless other methods are deemed more appropriate due to market conditions and or complicated borrowings. Bids will be awarded on a true interest cost basis (TIC), providing other bidding requirements are satisfied. In such instances where the County in a competitive bidding deems the bids received unsatisfactory, it may enter into negotiation for sale of the securities. The County shall adopt a form of notice of sale and advertisement in accordance with State law.

Negotiated Sale - Negotiated sales of debt will be considered only in extraordinary circumstances when the complexity of the issue requires specialized expertise, when a change of underwriter may result in losses (for example, changing the remarketing agent in mid program for variable rate debt), when the negotiated sale would result in substantial savings in time or money, or when market conditions or County credit are unusually volatile or uncertain. Selection of the underwriting team shall be made pursuant to selection procedures set forth in this Debt Policy.

Electronic Sale - When deemed appropriate for cost savings, time savings, or marketing purposes, the County may conduct electronic bond sales. Like traditional sales, electronic sales should be conducted on a competitive basis except in extraordinary circumstances. Selection of the electronic bidding platform shall be made pursuant to selection Dorchester County, Maryland Debt Management Policy procedures set forth in this Debt Policy, including cost and market presence, and the advice of the County's financial advisor.

Private Placement - In some unusual circumstance, the County may elect to sell its debt through a private placement or limited public offering.

SELECTION OF FINANCING TEAM CONSULTANTS AND SERVICE PROVIDER

The County's Director of Finance shall be responsible for establishing a solicitation and selection process for securing professional services that are required to develop and implement the County's debt program. Goals of the solicitation and selection process shall include encouraging participation from qualified service providers, both local and national, and securing services at competitive prices.

The County's Director of Finance shall be responsible for establishing a solicitation and selection process for securing professional services that are required to develop and implement the County's debt program. Goals of the solicitation and selection process shall include encouraging participation from qualified service providers, both local and national, and securing services at competitive prices.

Bond Counsel - The County will retain external bond counsel for all debt issues. All debt issued by the County will include a written opinion by bond counsel affirming that the County is authorized to issue the debt, stating that the County has met all requirements necessary for issuance, and determining the debt's federal income tax status. Bond counsel will be selected for a term of up to five years through a competitive process. Upon expiration of a multi-year contract, the County has the option, after a full competitive process, of signing a new contract with its existing bond counsel.

Financial Advisor - The County will retain an external financial advisor, to be selected for a term of up to five years, through a competitive process. Upon expiration of a multiyear contract, the County has the option, after a full competitive process, of signing a new contract with the existing financial advisor. For each County bond sale the financial advisor should provide the Director of Finance with information on pricing and underwriting fees for comparable sales by other issuers.

Underwriters - The County shall solicit proposals for underwriting services for all debt issued in a negotiated sale mode. The selection of underwriters may be for an individual or series of financings or a specified time period.

REFUNDING OF DEBT

Periodic reviews of all outstanding debt will be undertaken to determine refunding opportunities. Refunding will be considered (within federal tax law constraints) if and when there is a net economic benefit of the refunding or the refunding is essential in order to modernize covenants essential to operations and management.

Debt Service Savings - In general, advance refunding for economic savings will be undertaken when a net present value savings of at least 3-5 percent of the refunded debt can be achieved. Current refunding which produce a net present value savings of less than three percent will be considered on a case-by-case basis. Refunding with negative savings will not be considered unless there is a compelling public policy objective.

Restructuring of Debt - The County may choose to refund outstanding indebtedness when existing bond covenants or other financial structures impinge on prudent and sound financial management. Savings requirements for current or advance refunding undertaken to restructure debt may be waived upon a finding that such a restructuring is in the County's overall best financial interests.

INVESTMENT OF BOND PROCEEDS

All investments of bond proceeds will be consistent with those authorized by existing state law and the County's investment policies.

ARBITRAGE REPORTING AND COVENANT COMPLIANCE

The County will comply with all arbitrage rebate requirements as established by the Internal Revenue Service and all disclosure requirements established by the Securities and Exchange Commission. This effort includes tracking investment earnings on bond proceeds, calculating rebate payment in compliance with the tax law and remitting rebatable earnings to the federal government in a timely manner in order to preserve the tax exempt status of the County's outstanding debt issues. Additionally, general financial reporting and certification requirements embodied in bond covenants shall be monitored to ensure that all covenants are comply with.

MARKET AND INVESTORS RELATIONS

Rating Agency Relationships - The Director of Finance, in coordination with the County's financial advisor, shall be responsible for maintaining relationships with the rating agencies that currently assign ratings to the County's various debt obligations. This effort shall include providing regular updates on the County's general financial condition along with coordinating meetings and presentations in conjunction with a new debt issuance.

Use of Rating Agencies - County debt obligations should always carry a credit rating. The rating agencies that currently assign ratings to the County's various debt obligations should be periodically reviewed to determine if their service and prices are reasonable, and if not, agency selection should be reconsidered for future bond sales.

Minimum Long-Term Rating Requirements - The County's minimum rating requirement for its direct, long-term, debt obligations is a rating of A from Standard & Poor's or A2 from Moody's. 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.

ONGOING DISCLOSURE

The County is committed to full and complete financial disclosure, and to cooperating fully with rating agencies, institutional and individual investors, other levels of government, and the general public to share clear, comprehensible, and accurate financial information. The County is committed to meeting secondary disclosure requirements on a timely and comprehensive basis. The Department of Finance shall be responsible for providing ongoing disclosure information to established national information repositories and for maintaining compliance with disclosure standards promulgated by state and national regulatory bodies.

PASSED AND **ADOPTED** THIS 6th DAY OF September, 2011.

COUNTY COUNCIL OF
DORCHESTER COUNTY

ATTEST:

Jane Baynard
Jane Baynard, County Manager

Jay Newcomb
Jay L. Newcomb, President

William V. Nichols
William V. Nichols, Vice President

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