
Techniques for Managing Debt

***Are You Ready to Answer the Question ...
“What is our exposure to ____?”***

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Are You Ready to Answer the Question ... *“What is our exposure to ____?”*

- How’s your roller-coaster ride?
- How many times have you been asked that question in the last several months?
- If you couldn’t readily answer the question, then you need some techniques for managing your debt portfolio

Techniques for Debt Management

- Basic
- Better
- Best Practices

**Often times a function of staffing levels,
but must be priority in your organization**

Basic Debt Management

- Managing the Documents
- Trustee Oversight
- Debt Service Payments
- (Re) Investment of Bond Proceeds
- Regulatory Compliance

Basic Debt Management -- Managing the Documents

- Pre-Debt Issuance
 - Use of web-based applications for document distribution
 - Making primary disclosure documents available to all
 - Understanding Business Terms
- Post Debt Issuance Record Retention
 - Tracking Compliance (Regulatory and Bond Covenants)
 - Budgeting and Accounting

Basic Debt Management Trustee/Investment Agreement Oversight

- Use technology to your advantage -- Get online access from day of closing
- Online reporting reduces paper
 - Ease of creating electronic records
 - Easier to get documents to rebate consultant
- Methodology for monitoring activity
 - Transfer of funds
 - Interest earnings appropriate credits

Basic Debt Management Trustee/Investment Agreement Oversight

- Provides real-time data on bond issue
- Online – Real time access
- Investment of Bond Proceeds
- Investment Agreements
 - Mark-to-market
 - Collateral requirements

Basic Debt Management

Timely & Accurate Debt Service Payments

- Identify responsible unit(s) for debt service activities
- Require Trustee/Fiscal Agent to send debt service invoice
 - Always verify amount
 - Verify any credits from reserve funds
- Ensure sufficient time for internal wire/check processing
- Work with investment/cash management staff, debt service critical component of any cash flow analysis

Basic Debt Management

Investment of Bond Proceeds

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

Basic Debt Management

Investment of Bond Proceeds

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

Basic Debt Management

Adhering to Disclosure & Compliance Duties

- Arbitrage Rebate Compliance
- Annual Disclosure
 - Use electronic filing
- Compliance Reporting
 - Allow for electronic receipt of documents

Basic Debt Management

Arbitrage Rebate Compliance Activities

- Internal monitoring of rebate compliance
- Recommend annual calculations during construction period
 - Set aside annual rebate liability in Rebate Fund
 - Get it out of the Construction Fund
- Paying rebate is not bad, just need to monitor and pay as required
- Pay attention to requirements in Tax/Arbitrage Certificate **BEFORE** you sign!

Basic Debt Management

Continuing Disclosure Annual Reporting

- Designate key contact for disclosure decisions
- Contents of Annual Report
 - Issuer should decide contents
 - Annual Audits
 - Updated financial information – make this reasonable and based on reports currently producing
 - Material Event Disclosure – who?
- Use the CPO (www.disclosureUSA.com)
- Create universal e-mail address for reporting and noticing
 - Example: debt.management@sanjoseca.gov

Better Debt Management

- Bond Covenant Compliance
- Credit and Liquidity Administration
- Bond Call Redemption
- Regulatory Compliance
 - Record Retention
 - Electronic Distribution – CPO
- Annual Audit Preparation

Better Debt Management – Compliance - Bond Covenants & Agreements

- Develop internal tickler system from beginning
- Keep up-to-date
- Don't reinvent the wheel with every deal; similar reporting requirements are okay and always preferred
- Keep as simple as possible
 - Consider providing multiple parties to deal the same compliance reports

Better Debt Management

Credit/Liquidity Provider Administration

- Ultimate Credit - Determines Ratings
- Bond Insurance Premium
 - Up-front vs. Periodic Payment
- Prompt Invoice Payment for Liquidity Facilities
- Track expiration dates
 - LOC expiration
 - Commitment expiration
 - Stated amount expiration dates
- Research extension terms and fees to current market conditions; take into account internal costs

- Remarketing Agent/CP Dealer Key Player

Better Debt Management

Bond Call/Redemption Management

- Follow Provisions in Indenture
 - Mandatory Redemption
 - Sinking Fund
 - Prepayments
 - Optional Redemption
 - Extraordinary Redemption
- Track Source of Funds
- Principal Reductions
 - Reserve Requirement
 - Basis for administrative invoices

Better Debt Management Record Retention

- Establish Record Retention Requirements and Procedures
- IRS record retention requirements
 - Term of bonds + 6 years
 - Types of records
- IRS Website –
 - www.irs.gov/taxexemptbond/index.html
 - FAQ's -- Record Retention Requirements
www.irs.gov/taxexemptbond/article/0,,id=134435,00.html

Better Debt Management Regulatory Compliance

- Eliminate paper in compliance reporting to extent possible
- Electronic distribution of documents
 - CAFR
 - Annual Continuing Disclosure Report
 - Material Event Notices
 - General administrative notices
- Pay special attention to electronic record retention requirements of IRS

Better Debt Management Annual Audit Activities

- Get CAFR in electronic form for Annual Disclosure Requirements
 - Make it a requirement of printer or auditor
- Work closely with Accounting Staff
 - Prepare appropriate Notes to Financial Statements
 - Keep data centralized
 - Report consistently same information in all financial/budget reports
 - Keep good records on source of data and calculation methods

Best Debt Management

- Aggressive and Active Bond Disbursement Review
- Project Monitoring – Construction & Facility Use
- Active Budget Preparation Involvement
- Database Development and Maintenance
- Refunding analysis

Best Debt Management

Active Bond Proceeds Disbursement Review

- Cash Management
 - Incoming wire for reimbursements
 - Trustee wire payment to Contractor
- Accounting Activities
 - Appropriate recording of all activities in issuer's financial/accounting systems
 - Disbursement of bond proceeds
 - Record retention requirements different from "normal" accounts payable
 - Special District Administration

Best Debt Management

Active Bond Proceed Disbursement Review

- Reimbursement or Trustee Disbursement
 - Contractor payments
 - City costs/reimbursements

- Liquidity of Investments in Construction Fund
 - Monitor security maturities
 - LAIF – rolling 30 day draw window

- Requisition
 - Sufficient detail to show qualified expenditures
 - Accuracy of expenditures and requisitions
 - Record Retention

Best Debt Management Bond Project Monitoring - Construction

- Critical to complete reinvestment activities
- Active involvement with project staff
 - Regular conversations
 - Understanding of current and future capital needs
- Review project encumbrance and expenditure needs
- Understand project delays
 - Implications for timely commencement of debt service
 - Develop contingency plan if significant project delays

Best Debt Management

Bond Project Monitoring – Facility Use

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

Best Debt Management Budget Preparation & Monitoring

- Annual Budgeting for Debt Service
 - Setting of rates and charges
 - GO Debt Service Annual Tax Rate Calculation – timing with County is key
- Budgeting for Variable Rate Debt
- Gross v. Net Debt Service
- Process for “cleaning out” debt service accounts at issuer level
 - Don’t let funds accumulate
 - May become have tax/rebate ramifications

Best Debt Management Budgeting Variable Rate Debt

- Create a methodology
- Involves a programmatic budgetary trade-offs
- Assume average rate in effect through next budget period
 - **Assume too high**: decrease budgetary resources available for other purposes at start of year and delays program/project implementation
 - **Assume too low**: diverts resources from other purposes late in the year and delays program/project completion\
- Objective: minimize programmatic impact by making a reasonable interest rate assumption
- Annual debt service = principal x interest rate
 - Future interest rates are unknown for variable rate debt

Best Debt Management Budgetary Impacts - Invoice Payment

- During bond document development identify source for various payments:
 - Debt Service Invoices
 - Administrative Invoices
 - Contract Invoices
- Establish and Maintain Tracking System
 - Trustee requisitions
 - Internal accounts payable
- Budget for all costs
- Reconciliation with Trustee Statements
 - Annual invoices are problematic for tracking trustee transaction charges

Best Debt Management Contract Management - Consultants & Service Providers

- Establish Contract Procedures
 - Contract Tracking
 - Database of Contracts and Consultants
- Track Payments and Encumbrances
 - Monitor accuracy of payments
 - Professional Services vs. Reimbursable Expenses
 - Encumbrances for Contracts
- Contract Payment Process
 - Internal Accounts Payable
 - Trustee Wire to Contractor

Best Debt Management Refunding Analysis

- Part of overall good debt management
- Review in context of multiple factors:
 - New money needs
 - Consolidation of refunding candidates to increase savings, minimize workload
 - Saving thresholds
 - Preservation of one-time advance refunding opportunity
 - Generally minimum 3% NPV for advance refundings
 - Debt restructuring opportunities

Best Debt Management Database Development & Maintenance

- Key Elements of outstanding debt issues
- Credit Exposure
- Weekly rates tracking for variable rate programs
- Development of comparables of weekly rates to your portfolio, SIFMA (tax-exempt) and LIBOR (taxable)

Some Electronic Tips for Issuers

- Create an e-mail address for notification purposes – not an individual
 - debt.management@sanjoseca.gov
- Create electronic ticker system for entire debt management team
 - Outlook calendar – “Debt”
 - Track everything!
- Monitor for compliance on regular basis (daily, weekly, monthly)
- Invest in Adobe Professional and Scanning capabilities
 - Save everything you can electronically

Summary

- It is just you and the trustee in the end
- Must be active, diligent and engaged
- City of San Jose spends 75% of our debt management resources on monitoring debt portfolio
- Prepare periodic reports on debt management activities to elected officials, public and senior management
 - Comprehensive Annual Debt Report
 - Quarterly Debt Reports
 - Available online at: www2.csjfinance.org/
- Debt Management is NOT a passive sport

