COUNTY OF SANTA CRUZ DEBT MANAGEMENT POLICY

Title I – Finance and Accounting

800 – DEBT MANAGEMENT POLICY A.

Introduction/Purpose

The purpose of the County of Santa Cruz Debt Management Policy (Policy) is to ensure sound and uniform practices for issuing and managing debt. The County of Santa Cruz (County) recognizes that it may need to enter into debt obligations to finance projects and to meet fiscal responsibilities. Accordingly, this Policy confirms the commitment of the Board of Supervisors (Board), County staff, advisors and other decision makers to adhere to sound financial management practices.

The Policy is also intended to comply with Government Code Section 8855(i), effective on January 1, 2017.

B. Policy Objectives

The objectives of this Policy are as follows:

1. Establish a systematic and prudent approach to debt issuance and debt management;
2. Ensure access to debt capital markets and direct purchase investors (private placement providers) through prudent and flexible policies;
3. Define specific limits or acceptable ranges for general fund-support debt obligations;
4. Minimize debt service and issuance costs;
5. Maintain access to cost-effective borrowing;
6. Achieve the highest practical credit rating;
7. Ensure full and timely repayment of debt;
8. Maintain full and complete financial disclosure and reporting; and
9. Ensure compliance with applicable State and federals laws.

C. Scope

The County's Comprehensive Annual Financial Report includes legally separate entities for which the Board is financially accountable. This Policy informs the actions of these entities to ensure a uniform approach to the issuance of debt. This Policy establishes the parameters within which debt may be issued by the County of Santa Cruz, Santa Cruz County Public Financing Authority, Santa Cruz County Capital Financing Authority, Santa Cruz County Redevelopment Successor Agency and the Santa Cruz County Sanitation District, or any related entity of the County for which the governing body consists of the same individuals as the Board of Supervisors of the County. Additionally, the Policy applies to debt issued by the County on behalf of assessment, community facilities, or other special districts, and conduit-type financing by the County for multifamily housing or industrial development projects.

Supplemental policies, tailored to specifics of certain types of financings, may be adopted by the Board in the future. These supplemental policies may address, but are not limited to, the general obligation, lease revenue, enterprise, multifamily housing, and land-secured financings.

The debt policies and practices of the County are subject to and limited by applicable provisions of State and federal law and to prudent debt management principles.

D. Debt Advisory Committee

The Debt Advisory Committee (DAC) is advisory to the County Administrator's Office. The DAC consists of personnel from the following departments: (1) County Administrative Office ("CAO"), (2) Auditor-Controller-Treasurer-Tax Collector, and (3) County Counsel. The DAC may utilize the services of an independent financial advisor when analyzing proposed financing. The Committee Chair will be rotated periodically. The Chair will schedule committee meetings no less than quarterly or more frequently if requested. Members may attend via conference call if needed. Agenda items must be submitted to the Auditor-Controller two weeks before the scheduled meeting to avoid meeting cancellation.

"Financing" shall mean any bonds, certificates of participation, lease-purchase agreements, notes, letters of credit or other financing arrangements that will create a long-term liability for the County or a component unit or a Board Governed special district.

The role of the DAC is as follows:

1. Review and make recommendations regarding department debt financing requests;
2. Select, subject to ratification by the Board of Supervisors, component unit Board or special district governing board, all financing professionals required to assist in the structuring of financings (bond counsel, disclosure counsel, underwriters, trustees, financial advisors, etc.);

3. Review and provide content for all debt financing documents;
4. Ensure that proper due diligence is completed for each financing in the preparation of the Official Statement or related loan documents; and
5. Advise on ongoing administration and compliance of debt issuances.

E. Delegation of Authority

Government Code §53635.7 requires that all borrowing be placed on the Board Agenda and the agenda of any separate financing participant as a separate item of business. This Policy requires that the Board specifically authorize each financing proposal based on the recommendation of the CAO. Policy implementation and the day-to-day responsibility for the authority over the County's debt program will lie with the Auditor-Controller-Treasurer-Tax Collector's Office and the CAO with participation by County Counsel, and other departments as necessary. The Auditor-Controller-Treasurer-Tax Collector and CAO will be supported on an as-needed basis by the DAC and a financial advisor. The services of other outside consultants may be retained as necessary.

This Policy will be reviewed annually and updated as necessary. Any changes to this Policy are subject to recommendation by the DAC and the approval of the Board. The revised Policy will be provided to all County entities. While adherence to the Policy is required, the County recognizes that changes in capital markets, County programs, and other unforeseen circumstances may produce situations not covered by this Policy. This may require modification or exception to achieve Policy objectives. In these cases, flexibility is appropriate until specific authorization from the Board or related entities Board of Directors is obtained.

F. Purposes for Which Debt may be Issued

The County will issue debt for the following purposes:

1. Long-term Borrowing

   Long-term borrowing may be used to finance the acquisition or improvement of land, facilities, or equipment for which it is appropriate to spread these costs over more than one budget year. Long-term borrowing may also be used to fund capitalized interest, costs of issuance, required reserves, and any other financing-related costs which may be legally capitalized. Long-term borrowing shall not be used to fund County operating costs, but may fund one-time extraordinary expenses, as appropriate. Whenever possible, the County will first attempt to fund capital projects with grants or state/federal funding, as part of its broader capital improvement plan. When such funds are insufficient, the County will use dedicated revenues to fund projects.

2. Short-term Borrowing

   Short-term borrowing may be issued to generate funding for cash flow needs in the form of Tax Revenue Anticipation Notes (TRAN). Short-term borrowing, such as commercial paper, and lines of credit, will be considered as an interim source of funding in anticipation of long-term borrowing. Short-term debt may be issued for any purpose for which long-term debt may be issued, including capitalized interest and other financing-related costs. Prior to issuance of the short-term debt, a reliable revenue source shall be identified to secure repayment of the debt. The final maturity of the debt issued to finance the project shall be consistent with the economic or useful life of the project and, unless the Board determines that extraordinary circumstances exist, must not exceed seven (7) years.

3. Refunding

Periodic reviews of outstanding debt will be undertaken to identify refunding opportunities. Refunding will be considered (within federal tax law constraints, if applicable) if and when there is a net economic benefit of the refunding. Refundings which are non-economic may be undertaken to achieve County objectives relating to changes in covenants, call provisions, operational flexibility, tax status of the issuer, or the debt service profile.

In general, refundings which produce a net present value savings of at least four (4) percent of the refunded debt will be considered economically viable. Refundings which produce a net present value savings of less than four (4) percent will be considered on a case-by- case basis, and will be subject to specific approval by the Board of Supervisors. All refundings will require approval of the Board of Supervisors.

G. Debt Issuance

1. Debt Capacity

The County will keep outstanding debt within the limits of applicable law and at levels consistent with its creditworthiness objectives. The County shall assess the impact of new debt issuance on the long-term affordability of all outstanding and planned debt issuance. Such analysis recognizes that the County has limited capacity for debt service in its budget, and that each newly issued financing will obligate the County to a series of payments until the bonds are repaid.

2. Credit Quality

The County seeks to obtain and maintain the highest possible credit ratings for all categories of short- and long-term debt. The County will not issue bonds directly or on behalf of others that do not carry investment grade ratings. However, the County will consider the issuance of non-rated special assessment, community facilities,
multifamily housing and special facility bonds.

3. Types of Debt That May Be Issued

   a. Debt Repayment

Debt will be structured for a period consistent with a fair allocation of costs to current and future beneficiaries of the financed capital project. The County shall structure its debt issues so that the maturity of the debt issue is consistent with or less than the economic or useful life of the capital project to be financed.

b. Variable-rate Debt
To maintain a predictable debt service burden, the County will give preference to debt that carries a fixed interest rate. An alternative to the use of fixed rate debt is floating or variable rate debt which shall require approval the Board of Supervisors after a recommendation of the County's Financial Advisor. The Board may choose to issue securities that pay a rate of interest that varies according to a pre-determined formula or results from a periodic remarketing of securities. When making the determination to issue bonds in a variable rate mode, consideration will be given to the useful life of the project or facility being financed or the term of the project requiring the funding, market conditions, credit risk and third party risk analysis, and the overall debt portfolio structure when issuing variable rate debt for any purpose. The maximum amount of variable-rate debt should be limited to no more than 20 percent of the total debt portfolio, unless otherwise directed by the Board of Supervisors.

c. Derivatives
The County will not employ derivatives, such as interest rate swaps, in its debt program. A derivative product is a financial instrument which derives its own value from the value of another instrument, usually an underlying asset such as a stock, bond, or an underlying reference such as an interest rate. Derivatives are commonly used as hedging devices in managing interest rate risk and thereby reducing borrowing costs. However, these products bear certain risks not associated with standard debt instruments.

d. Credit Enhancement
The County will consider the use of credit enhancements on a case-by-case basis, evaluating the economic benefit versus the cost for each case. Bond insurance, stand-by letters of credit other credit enhancements should be used only when they clearly demonstrate a net present value savings to the County or required as a basis to obtain a surety bond in lieu of cash funding of a reserve fund.

e. Senior/Subordinate Debt
Senior and Subordinate debt will be utilized in a manner that will minimize the costs of financing or maximize debt capacity.

f. Debt Service Reserve Fund
For long term debt and where appropriate for short-term debt, a Debt Service Reserve Fund will be utilized to achieve optimal pricing. Alternately, a Surety Bond may be evaluated and used if found to be economically advantageous.

H. Relationship of Debt to Capital Improvement Program and Budget

The County intends to issue debt for the purposes stated in this Policy and to implement policy decisions incorporated in the County's capital budget and the capital improvement plan.

The County shall integrate its debt issuances with the goals of its capital improvement program by timing the issuance of debt to ensure that projects are available when needed in furtherance of the County's public purposes and to avoid having to make unplanned expenditures for capital improvements or equipment from its general fund.

I. Policy Goals Related to Planning Goals and Objectives

The County is committed to financial planning, maintaining appropriate reserves levels and employing prudent practices in governance, management and budget administration. The County intends to issue debt for the purposes stated in this Policy and to implement policy decisions incorporated in the County's annual operating budget.

It is a policy goal of the County to protect taxpayers, ratepayers and constituents by utilizing conservative financing methods and techniques so as to obtain the highest practical credit ratings (if applicable) and the lowest practical borrowing costs.

The County will comply with applicable state and federal law as it pertains to the maximum term of debt and the procedures for levying and imposing any related taxes, assessments, rates and charges.

Except as described in Section F.3., when refinancing debt, it shall be the policy goal of the County to realize, whenever possible, and subject to any overriding non-financial policy considerations minimum net present value debt service savings equal to or greater than 4% of the refunded principal amount.

J. Professional Assistance

The County shall utilize the services of independent financial advisors and bond counsel on all debt financings. The Assistant County Administrative Officer and Auditor-Controller-Treasurer-Tax Collector shall have the authority to periodically select service providers as necessary to meet legal requirements and minimize net County debt costs. Such services, depending on the type of financing, may include financial advisory, bond counsel, disclosure counsel, underwriting, trustee, verification agent, escrow agent, arbitrage consulting, and special tax consulting. The goal in selecting service providers, whether through a competitive process or sole-source selection, is to achieve an appropriate balance between service and cost.

K. Method of Sale

The County's goal is to protect the public's interest by obtaining the lowest possible interest cost. To obtain this goal, the County may use a competitive negotiated, limited-competitive (hybrid), or private placement method of sale with input from the County's financial advisor. The appropriate method should be determined on a case-by-case basis.

L. Debt Administration

1. Investment of Bond Proceeds

   Investment of bond proceeds shall be consistent with federal tax requirements, the County's Investment Policy as modified from time to time, and with requirements contained in the governing bond documents.

2. Use of Bond Proceeds

   The Auditor-Controller-Treasurer-Tax Collector and other appropriate County personnel shall implement Internal Control procedures outlined below to ensure that the proceeds of the proposed debt issuance will be directed to the intended use:

   a. Monitor the use of Bond proceeds, the use of Bond-financed assets (e.g., facilities, furnishings or equipment) and the use of output or throughput of Bond-financed assets throughout the term of the Bonds to ensure compliance with covenants and restrictions set forth in applicable County resolutions and Tax Certificates. Monitoring will include providing an annual report to the DAC;

   b. Maintain records or contracts identifying the assets or portions of assets that are financed or refinanced with proceeds of each issue of Bonds and to document compliance with all covenants and restrictions set forth in applicable County resolutions and Tax Certificates. An applicable Record Retention Policy will be maintained by the Auditor-Controller-Tax Collector's;

   c. Consult with Bond Counsel or other professional expert advisors in the review of any contracts or arrangements involving use of Bond-financed facilities to ensure compliance with all covenants and restrictions set forth in applicable County resolutions and Tax Certificates;

3. Financial Disclosure

   The County is committed to full and complete primary and secondary market financial disclosure in accordance with disclosure requirements established by the Securities and Exchange Commission and Municipal Securities Rulemaking Board, as may be amended from time to time. The County is also committed to cooperating fully with rating agencies, institutional and individual investors, other levels of government, and the general public to share clear, timely, and accurate financial information as identified in its Continuing Disclosure and Compliance Procedures.

4. Arbitrage Compliance

   The Auditor-Controller-Treasurer-Tax Collector's Office shall maintain a system of record keeping and reporting to meet the arbitrage compliance requirements of federal tax law.

M. Independent Registered Municipal Advisors (IRMA) Letter

By publically posting a written notice on the County's website, the County and related entities intend that market participants receive and use it for purposes of the independent registered municipal advisor exemption to Rule 15B of the Securities and Exchange Commission (SEC) regarding Registration of Municipal Advisors (Municipal Advisors Rule). All solicitations or written proposals received shall be reviewed by the County's Financial Advisor
before being seriously considered. The notice may be relied upon until it is removed from the website or replaced with a subsequent notice.

N. Relationship to Other Policies

The County has adopted a Statement of Goals and Policies for the Use of the Mello-Roos Community Facilities Act of 1982, included as Exhibit A hereto. Special Tax Bonds issued on behalf of a community facilities district will also comply with these policy requirements.

EXHIBIT A

STATEMENT OF GOALS AND POLICIES FOR THE USE OF THE MELLO-ROOS COMMUNITY FACILITIES ACT OF 1982