CITY OF ST. CHARLES ILLINOIS • 1834	**AGENDA ITEM EXECUTIVE SUMMARY**	**Agenda Item Number: 5b**
	Title:	Recommendation to Discuss and Approve a Resolution Adopting a Debt Issuance and Management Policy
	Presenter:	Bill Hannah, Finance Director

Meeting: Government Operations Committee **Date**: October 3, 2022

Proposed Cost: $ N/A	Budgeted Amount: $ N/A	Not Budgeted: ☐

Executive Summary (*if not budgeted please explain*)**:**

In December of 2021, the City completed a general obligation bond issuance consisting of both new money for various capital projects and a refunding of prior issued debt obligations to achieve interest savings due to lower rates. The City's outstanding debt rating from Moody's at that time was confirmed at Aa1, the 2nd highest rating attainable through Moody's. During the rating discussion process, it was recommended that the City develop and adopt a formal debt issuance and management policy in lieu of the informal debt guidelines and metrics currently in place. A formally adopted debt policy with provisions that guide the City when considering the issuance of debt or managing the City's outstanding debt would be viewed as a positive strengthening attribute to the City's overall debt rating profile.

Over the last few months, Finance has developed the attached debt issuance and management policy for discussion and consideration. The policy formalizes many current practices that the City considers when issuing debt. The policy also provides for new parameters and considerations, all summarized below, as part of the policy:

- Debt will not be issued to finance general operating expenses or funding of operating deficits
- Alternatives to debt financing will be considered first such as other available revenues, interfund loans, grants, etc.
- The potential impact of debt issuance on the City's outstanding credit rating and metrics will be evaluated prior to debt issuance.
- Capital or other projects with a cost of $500,000 or less will not be debt-financed, but rather, will be funded with pay-as-you-go financing through current or new revenue sources.
- Debt will be amortized over 20 years or less, and consideration of the overall revenue stream dedicated to the repayment of the debt service, will be given when structuring principal repayments.
- Level or declining total debt service will be used if possible, and the potential benefits of bank qualification for the bonds will be considered.
- Call provisions of 10 years or less will be included if market conditions indicate a potential benefit.
- Variable rate debt will generally not be issued instead of fixed rate debt, and derivative products will not be used.
- Total annual governmental fund debt outstanding (excluding TIF and specific revenue bonds) shall be targeted to be 10% or less of total General Fund revenues.
- Appropriate debt service coverage ratios shall be maintained for each individual Enterprise Fund of at least 1.0 times of available revenues.
- Consistent with the City's Economic Incentive Policy, requests for TIF funding will be considered within the "pay-as-you-go" structure, with specific TIF funded debt parameters laid out in the event an exception is made.

The draft policy also addresses the types of debt that may be issued, the use of underwriters, bond counsel and financial advisors, the methods of bond issuance sale and use of credit enhancements, revenue bonds versus general obligation bonds, the importance of maintaining ongoing disclosure with credit agencies and the SEC through the MSRB, parameters as to when a bond refunding is appropriate, and other related provisions.

The City currently has, as of April 30, 2022, $108,920,000 in outstanding general obligation bonds and $48,962,653 in outstanding IEPA loans. The breakdown of this is detailed on pages 44-50 in the City's recently completed Annual Comprehensive Finance Report (ACFR) as of April 30, 2022 that will also be presented for discussion at the October 3rd GOC meeting. While the City currently has no immediate plans to issue new general obligation debt, the City has a number of IEPA low-interest loan funded projects ongoing that will result in a significant increase in the total outstanding IEPA loans over the next few years.

A presentation will be made at the Monday, October 3rd meeting, which will discuss the policy and provide more information on the current outstanding debt by repayment source, as well as comparative information to other municipalities. Staff has reviewed this policy with legal counsel and the City's underwriter for feedback.

Attachments (*please list*)**:**
Resolution
Draft Debt Issuance and Management Policy

Recommendation/Suggested Action (*briefly explain*)**:**

Discussion of Draft Debt Issuance and Management Policy and recommendation for Adoption

City of St. Charles, Illinois
Resolution No.

A Resolution to Adopt a Debt Issuance and Management Policy in the City of St. Charles, Kane and DuPage Counties, Illinois.

Presented & Passed by the
City Council on_____

WHEREAS, the City of St. Charles, Illinois (the "City"), has determined that it is in the best interests of the City to adopt a formal Debt Issuance and Management Policy (the "Policy") described in Exhibit A hereto; and

NOW, THEREFORE, BE IT RESOLVED by the Mayor and City Council of the City of St. Charles, Kane and DuPage Counties, Illinois, in the exercise of its home rule powers, as follows:

Section 1. The foregoing recital clauses to this Resolution are adopted as the findings of the corporate authorities of the City and are incorporated herein by specific reference.

PRESENTED to the City Council of the City of St. Charles, Illinois, this _____ day of _____, 2022

PASSED by the City Council of the City of St. Charles, Illinois, this _____ day of _____, 2022

APPROVED by the Mayor of the City of St. Charles, Illinois, this _____ day of _____, 2022

_____
Lora Vitek, Mayor

ATTEST:

_____
City Clerk

COUNCIL VOTE:
Ayes:
Nays:
Absent:
Abstain:

EXHIBIT A

City of St. Charles, Illinois
Debt Issuance and Management Policy
Adopted: _____

DRAFT

I. PURPOSE

This Debt Issuance and Management Policy ("Policy") sets forth comprehensive guidelines and promotes sound decision-making regarding the issuance and management of debt by the City of St. Charles ("City") in order to provide funding for capital improvements and other purposes for the community while maintaining the City's fiscal strength, stability and future financial flexibility.

II. OBJECTIVE

It is the objective of this Policy for the City to obtain debt financing only when necessary; to set forth the process to identify the timing and amount of debt needed to be as efficient as possible.

III. GOALS AND PARAMETERS

In following this Policy, the City shall pursue and adhere to the following goals and parameters when considering the issuance of debt:

1. Debt will not be issued to finance general operating expenses or fund operating deficits.

2. Alternatives to debt financing will be considered such as other available revenue sources, interfund loans, application of grant proceeds, State/Federal aid or other funding options to meet the long-term capital needs of the City.

3. Current credit rating metrics used by the City's rating agency(s) will be evaluated to determine if the rating may be impacted by the issuance of debt, acceptance of long-term loans, or other financial decisions or actions by the City.

4. Capital projects with an estimated cost of $500,000 or less will ideally be funded with funds on hand or pay-as-you-go financing, and not funded with new debt or loans. Utility rates and other revenue sources will be adjusted if needed to ensure that adequate funding will be available for projects under $500,000. Depending on the circumstances, consideration will be given to combine multiple capital projects that are under $500,000 into one debt issuance.

5. Debt issuances shall be structured to amortize within a twenty (20) year period, or shorter, to match the expected useful life of the assets to be financed. Principal will be amortized to best fit within the overall debt structure of the City's general obligation debt, the repayment source and/or related tax levy at the time the new debt is issued. For issuance of revenue bonds, or general obligation bonds paid by revenues other than property tax, principal will be amortized to best fit with the overall debt structure of the specific enterprise fund or related revenue source.

6. Debt repayment shall be structured so that level or declining debt service shall be used unless operational or financial reasons dictate otherwise, or if to achieve overall level debt service with existing bonds.

7. The potential financial benefits of issuing bank qualified bonds will be considered and, if possible, strive to limit annual issuance of debt to $10 million or less when such estimated benefits are greater than the benefits of exceeding the bank qualification limit. Should subsequent changes in the law change this limit, the City policy will be adjusted accordingly.

8. Call provisions of approximately ten (10) years or less will be considered to provide the City flexibility to refinance debt in the future. Consideration of the call feature will be determined at the time of sale based on overall market conditions and investor acceptance.

9. Fixed rate debt as opposed to variable rate debt will be issued to minimize exposure to certain risks. If unusual circumstances warrant the issuance of variable rate debt, explanation must be provided and approved by the City Council. The par amount of outstanding variable rate debt shall not exceed 10% of the City's total outstanding debt. The City will not use derivative products in its debt structure.

10. The ratio of total annual governmental funds debt (excluding outstanding debt issued for TIF purposes and specific revenue bonds) shall be reduced and maintained to be 10% or less of total General Fund revenues.

11. Debt service coverage of at least 1.0 shall be maintained for each individual Enterprise Fund through adjustments to the utility rate structure. The 1.0 coverage ratio is applicable to general obligation debt and IEPA loans repayable by the applicable utility rate structure.

12. Consistent with the City's current *Economic Incentive Policy Section V.*, financial assistance requested for projects within a tax-increment financing (TIF) district will be considered through the pay-as-you-go increment method. General obligation bonds with a pledge of repayment by TIF revenues or straight TIF revenue bonds will not be considered unless the TIF increment revenues available to repay the bonds are already being received, or are projected to be received based on completed construction. Current or projected increment must be at least 120% of the highest annual debt service payment, unless separately approved and authorized by the City Council. The City may require credit enhancements from a private entity as part of the payment guarantee process.

IV. LEGAL CONSTRAINTS AND OTHER DEBT LIMITATIONS

The City Council may utilize the guidelines established by this Policy, or may choose, in its discretion, to consider other relevant factors in incurring debt. The validity of any debt incurred in accordance with applicable law shall not be invalidated, impaired, or otherwise affected by non-compliance with any part of the procedures set forth pursuant to this Policy.

Authority and Purposes of the Issuance of Debt

The laws of the State of Illinois authorize the issuance of debt by the City. The Illinois Municipal Code confers upon municipalities the power and authority to contract debt, borrow money, and issue bonds. The City may, by bond ordinance, incur indebtedness or borrow money, and authorize the issue of negotiable obligations, including refunding bonds, for any capital improvement of property, land acquisition, or any other lawful purpose.

General Obligation Debt Limitation

Under Illinois Compiled Statutes, municipalities of less than 500,000, unless they are a home rule unit, are limited to the amount of general obligation bonded debt they can incur at any one time to no more than 8.625% of the total equalized assessed value of real estate property. Since the City is a home rule community, the City is not subject to this limitation.

V. DEBT ISSUANCE CONSIDERATIONS

Use of Professional Service Providers

The City will consider seeking the assistance and expertise of a qualified Financial Advisor prior to undertaking a debt issuance process separate from the Underwriter of the Bonds. The City will also ensure that a qualified Bond Counsel is also retained by the City.

Types of Debt Issued

1. Short-Term. (three years or less) The City may issue short-term debt to finance the purchase of equipment or other items having a life exceeding one year or to provide increased flexibility in financing programs. The City will not issue debt for deficit financing.
2. Long-Term. (more than three years) The City may issue long-term debt which may include, but is not limited to, general obligation bonds, certificates of participation, installment notes, revenue bonds, and special assessment bonds.

General Obligation Bonds vs. Revenue Bonds

The City may consider the issuance of revenue bonds in lieu of general obligation bonds if:

1. There are sufficient annual revenues for the repayment of the proposed bonds - debt service coverage (annual revenue minus cash operating expenses divided by annual debt service payments). The debt service coverage ratio will be used to determine the limit of future revenue bonds payable from the identified revenue source;
2. The project being financed benefits the users of an enterprise system and debt service on the bonds would be paid from enterprise fund revenues;
3. There is not a significant cost differential between the two financing types; and/or
4. An amortization longer than twenty years is more advantageous for repayment from enterprise fund revenues.

Abatement of Property Tax Debt Service for General Obligation Bonds

If the City plans to repay debt service using a specific revenue source when issuing General Obligation bonds, the City will use conservative revenue projection assumptions to ensure the identified funding source is sufficient to pay off the bonds. When issuing general obligation bonds in lieu of revenue bonds with the intent to abate the debt service property tax levies, the City Council will adopt ordinances abating the debt service levies and pay debt service costs with the identified revenues.

Methods of Sale

When issuing debt, the City will consider multiple methods of sale, including competitive, negotiated or private placement. If the City retains the services of a Financial Advisor, the Advisor will not bid on or underwrite any City debt issuances on which it is advising.

Credit Enhancements

The City may enter into agreements with commercial banks or other financial entities for the purpose of acquiring letters of credit, municipal bond insurance, or other credit enhancements that will provide the City with access to credit under terms and conditions as specified in such agreements when their use is judged cost effective or otherwise advantageous.

Conduit Debt

Conduit debt is debt issued in the name of the City but payable by third parties only, and for which the City does not provide credit or security. The City will consider issuing conduit debt when such actions meet the financial objectives of plans and/or policies adopted by City Council.

VI. DEBT ADMINISTRATION

Financial Disclosures

The City shall prepare all appropriate annual and other financial disclosures as required by the City's continuing disclosure undertakings as well as any specific event notices required by the Securities and Exchange Commission (SEC) to the Municipal Securities Rulemaking Board (MSRB), and any other filings required by the federal government, the State of Illinois, rating agencies, underwriters, investors, taxpayers, and other appropriate entities and persons to the ensure compliance with applicable laws and regulations.

Review of Financing Proposals

All financing proposals that may involve a pledge of the City's credit through the sale of securities, execution of loans or lease agreements and/or otherwise directly involve the lending or pledging of the City's credit shall be referred to the Director of Finance who shall determine the financial feasibility, financial impact, and the impact on existing debt of such proposal, and shall make recommendations accordingly to the City Administrator and City Council for approval.

Rating Agency Relations

The City shall endeavor to maintain effective relations with rating agencies. The Director of Finance and other appropriate parties should meet with, make presentations to, or otherwise communicate with the rating agencies on a consistent and regular basis in order to keep the agencies informed concerning the City's capital plans, debt issuance program, and other appropriate financial information on the economic and fiscal status of the City.

Refunding Policy on Existing Issuances

The City shall consider refunding outstanding debt when legally permissible and financially advantageous. A net present value debt service savings of at least three percent (3%) of the refunded par amount or greater must be achieved, unless otherwise justified and authorized by City Council.

Investment of Borrowed Proceeds

The City shall invest proceeds of debt in accordance with the City' adopted investment policy.

The City acknowledges its ongoing fiduciary responsibilities to actively manage the proceeds of debt issued for public purposes in a manner that is consistent with Illinois statutes that govern the investment of public funds, and consistent with the permitted securities covenants of related bond documents executed by the City. The management of public funds should enable the City to respond to changes in markets or changes in payment or construction schedules so as to (i) minimize risk, (ii) ensure liquidity, and (iii) optimize returns.