Office of the Chief Financial Officer
City of Detroit

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CFO DIRECTIVE
NO. 2018-101-007A

SUBJECT: Debt Issuance and Management Policy
ISSUANCE DATE: May 1, 2018
AMENDED DATE: September 8, 2020

1. AUTHORITY

1.1. State of Michigan Public Act 279 of 1909, as amended ("Act 279"), known as the Home Rule Cities Act, Section 4s(2) states the City's chief financial officer shall supervise all financial and budget activities of the City and coordinate the City's activities relating to budgets, financial plans, financial management, financial reporting, financial analysis, and compliance with the budget and financial plan of the City.

1.2. Act 279 provides for the borrowing of money and issuance of bonds or other evidences of indebtedness by cities and sets forth certain limitations and requirements related to such issuances.

1.3. State of Michigan Public Act 34 of 2001, as amended ("Act 34"), known as the Revised Municipal Finance Act, authorizes the issuance of certain debt and municipal securities by municipalities and sets forth certain limitations and requirements related to such issuances.

1.4. State of Michigan Public Act 227 of 1985, as amended ("Act 227"), sets forth certain authorities and requirements for municipalities to issue municipal securities to the Michigan finance authority, including the authority to pledge and authorize the intercept of certain revenues of the municipality.

1.5. State of Michigan Public Act 175 of 1952, as amended, authorizes the issuance of bonds in anticipation of future payments from the State motor vehicle highway fund.

1.6. State of Michigan Public Act 94 of 1933, as amended, authorizes the issuance of revenue bonds by public corporations, which include cities, counties, authorities, municipal health facilities, etc.

1.7. State of Michigan Public Act 436 of 2012 allows local governments under certain conditions to issue financial recovery bonds in amounts greater than limitations established by City Charter.

1.8. The 2012 Charter of the City of Detroit, Article 8, Chapter 5, provides the general power for the city to borrow money and issue bonds or other evidence of indebtedness and describes specific kinds of borrowing and related requirements.

1.9. The 2019 Detroit City Code, Chapter 17, Article II, Section 17-2-10 requires the City to issue a tax statement and a bond statement to represent amounts required to be raised to support the adopted budget.

1.10. The 2019 Detroit City Code, Chapter 17, Article VII, provides various requirements for registered bonds of the City.

2. OBJECTIVES

   2.1. To maintain a high quality of decision-making, provide guidelines for the structure of debt, and demonstrate a commitment to long-term capital and financial planning.

   2.2. To establish written guidelines to guide the debt issuance practice of the City, including the issuance process, adherence to federal, state and local laws and regulations, post issuance compliance for IRS purposes and post issuance compliance for continuing disclosure purposes.

   2.3. To provide guidelines for the City to manage its debt program within its financial resources while retaining the highest possible credit rating.

   2.4. To establish practices that minimize the City's debt service and costs while maintaining and preserving access to the capital markets in a cost-effective manner.

   2.5. To set forth guidelines that consider the impact on the City's operating budget and on City taxpayers and frame the decision-making for when new debt is being considered.

3. PURPOSE

   3.1. To establish the City's debt issuance and management policy.

4. RESPONSIBILITIES

   4.1. As delegated by the Chief Financial Officer (CFO), the Deputy CFO-Treasurer ("Treasurer"), in coordination with the Chief Deputy CFO/Finance Director, shall be responsible for the administration and oversight of this Directive and shall ensure coordination of activities with the CFO's Office and the Office of Budget.

   4.2. The Deputy CFO- Budget Director ("Budget Director") shall be responsible for certain activities as stated in this Directive.

   4.3. The CFO's Office, with assistance from other City departments and agencies as necessary, shall be responsible for certain analyses and communications with credit rating agencies as stated in this Directive.

5. DEFINITION OF DEBT

   5.1. This Directive covers all forms of borrowing money and issuance of debt obligations by the City, including but not limited to bonds, notes, capital leases, installment purchase agreements, and loans of any type.

   5.2. This Directive does not cover other obligations such as contracts payable, net pension liability obligation and/or pension Unfunded Actuarial Accrued Liability (UAAL) and Other Post-Employment Benefits (OPEB) UAAL.

   5.3. This Directive does not cover, except to the extent they are included in the measurements of City debt in Section 8 of this Directive, the obligations of certain authorities of the City, such as the Public Lighting Authority, the Local Development Finance Authority, and the Downtown Development Authority.

6. GENERAL GUIDELINES

6.1. Debt shall only be issued in conformance with all applicable state and federal laws, City Charter and ordinances, and as well as this Directive.

6.2. The City shall pay all debt principal and interest in a timely manner and ensure that all debt service payments are budgeted.

6.3. The City shall track and adhere to all bond covenants. A bond covenant is a legally binding term of agreement between a bond issuer and a bondholder. Negative or restrictive covenants forbid the issuer from undertaking certain activities; positive or affirmative covenants require the issuer to meet specific requirements.

6.4. The City shall ensure that the requirements under the Internal Revenue Code for governmental bonds are met throughout the life of the bonds in order to protect their tax-exempt status. These requirements include information filing and other requirements related to issuance, the proper and timely use of bond-financed property, and limitations on how bond proceeds may be invested.

6.5. The City shall promote debt transparency through the regular reporting and posting of information about City debt.

6.6. Long-term debt shall only be used for capital purchases, construction, demolition, rehabilitation or other legally permissible uses and as identified in the City's capital plan (the "Capital Agenda") pursuant to the City's budget processes. Long-term debt shall not be used to finance current operations.

6.7. Pursuant to Act 279 and Act 34, short-term debt may be used for equipment financings, operational borrowing, and other uses permitted by state law. The City shall seek to avoid the use of short-term debt for operational purposes by maintaining adequate working capital and through detailed cash management.

6.8. As the City pays down its general fund debt overtime and general fund debt service decreases as a percentage of general fund, the City should use those general fund revenues to support legacy pension obligations, make contributions to the budget reserve fund and/or support capital investment on a pay-go basis.

7. TYPES OF DEBT AND STATUTORY DEBT LIMITS

7.1. The City shall assess all financial alternatives for funding capital, construction, rehab, equipment, and other permitted uses as identified by state law prior to issuing debt. Pay-go financing should be considered before issuing any debt. Once the City has assessed the amount of pay-go financing available, the City may issue the following types of debt.

7.1.1. General Obligation Debt

7.1.1.1. There are two types of general obligation debt: (1) Limited tax general obligation debt and (2) Unlimited tax general obligation debt. Limited tax general obligation debt pledges the full faith and credit of the taxing power of the City within the existing tax rate limits. For some long-term limited tax general obligation debt, state law requires that the city publish a notice to the electors in the local newspaper providing for a right of referendum period.

Unlimited tax general obligation debt pledges the full faith and credit of the taxing power of the City beyond the existing rate limits, provided the voters have given their approval.

7.1.1.2. For cities, Act 279 limits "net indebtedness" to ten percent of assessed value. The definition of assessed value for the debt limit computation under Act 279 includes certain assessed value equivalents not otherwise included in assessed valuation. (For this reason, the assessed value equivalent used in the City's calculation of its legal debt limit is almost always considerably higher than the City's assessed value.) Under Act 279, net indebtedness is comprised of all of the municipality's debt, with specific exclusions (e.g., Michigan Transportation Fund debt is excluded). Additionally, Act 279 specifies that the ten percent limit does not apply to financial recovery bonds.

7.1.1.3. For cities that have financial recovery bonds outstanding, Act 279 limits net indebtedness – including financial recovery bonds - to 20 percent of assessed value. Section 9(a) of Act 279 provides for additions to assessed value for purposes of this calculation.

7.1.2. Revenue Bonds

7.1.2.1. Revenue bonds are bonds that are issued and supported by the revenue generated from a specific project, such as debt for a utility. Revenue bonds are considered when there is a definable revenue source (e.g., user fees) which could be pledged and used to pay the debt.

7.1.2.2. State law does not set limits for revenue bonds. Revenue bonds normally must meet certain bond covenants stipulated by the lender. The lender may also require certain debt ratios, such as pledged revenues to debt service, be met initially and then reported periodically.

7.1.3. Short-term Borrowings

7.1.3.1. Examples of short-term borrowings include tax anticipation notes and bond anticipation notes. Notes generally mature in one year or less.

7.1.3.2. Act 34 limits the amount of tax anticipation notes based on budgeted property tax revenue.

7.1.4. Refinancing/Refunding of Existing Debt

7.1.4.1. In accordance with federal tax laws, municipalities may refinance outstanding bonds by issuing new bonds. This may serve either to reduce interest costs or to remove a restrictive bond covenant on the existing bonds.

7.1.4.2. Except for certain pre-approved exceptions, Act 34 requires that the refunding of bonds result in a positive net present value savings.

8. DEBT AFFORDABILITY AND DEBT METRICS

8.1. Debt Affordability Limits

8.1.1. When considering the issuance of new debt, in addition to considering the impact on statutory debt limits, the City shall also seek to adhere to the following financial caps.

8.1.1.1. _General Fund Debt Service as a Percent of General Fund Expenditures_ shall have a maximum cap of ten (10) percent. As the City pays off legacy debt, the City shall target this metric at or below eight (8) percent. To measure this ratio, the City shall include all of its limited tax general obligation debt and any other debt for which the revenue paying the debt service currently flows through the general fund or will flow through the general fund once the bonds are no longer outstanding. An example of the latter is the 2014 Public Lighting Authority Bonds.

8.1.1.2. _Overall Debt Service as a Percent of Governmental Expenditures_ shall have a maximum cap of 15 percent. As the City pays off legacy debt, the City shall target this metric at or below ten (10) percent. To measure this ratio, consistent with the debt that would be used by the national rating agencies included in similar measures (which does not necessarily reflect the legal structure of the debt), the City shall include the General Fund Debt Service identified in Section 8.1.1.1 of this Directive, its unlimited tax general obligation debt, and other debt of the City that is paid with revenue of other governmental funds. Examples of the latter include the City's 2017 Michigan Transportation Fund bonds and its HUD Section 108 Notes.

8.2. Debt Metric Tracking

8.2.1. In considering its outstanding debt, the City shall track the following measurements and, where present, use the indicated guideline to inform its decision-making.

8.2.1.1. _Overall Debt as a Percent of Full Market Value_ should be measured annually. As the City pays off legacy debt, the City shall target this metric at or below 10 percent. To measure this ratio, the City shall include it overall debt as identified in Section 8.1.1.2 of this Directive. The City shall calculate full market value as two times the assessed value as reported in the Finance Officers Report of the City Assessor.

8.2.1.2. _Overall Debt as a Percent of Governmental Funds Revenue_ measured annually. As the City pays off legacy debt, the City shall target this metric at or below 120 percent.

9. DEBT STRUCTURING PRACTICES FOR LONG-TERM DEBT

9.1. The size of the bond issue shall be based on the capital project needs and consistent with the City's Capital Agenda. During pre-issuance planning, the CFO's Office shall work with the Office of Budget to determine the projected draw schedule for the proceeds in an effort to meet any investment or arbitrage limitations under federal tax law.

9.2. The term of the bonds shall not be more than the useful life of the assets purchased or financed with the debt. The City maintains a preference for the shortest possible average maturity considering the project type and availability of annual payment resources.

9.3. The City shall seek to structure debt with level or declining debt service payments over the life of each individual bond issue or loan. However, the City may utilize non-level debt methods for refunding opportunities, creating overall level debt taking into account other long-term obligations such as pension payments, or in consideration of non-general fund revenues, natural disasters, and other external factors. In structuring debt, the City shall be subject to the requirements in Section 503(1) of Act 34 and other applicable statutory requirements.

9.4. The interest on the bonds may be fixed or variable. In general, for projects with a long useful life, the City prefers fixed interest rate structures. With fixed interest rates, the effectiveness of annual capital budgeting is enhanced because the annual debt service for the life of the bonds is known upon closing. Infrequently, the City may determine that the use of variable rate debt in financing capital improvements is beneficial. In such cases, the City will implement steps to mitigate the inherent risks associated with the use of variable rate debt.

9.5. The Financing Team will recommend to the CFO the use of a call option on a case-by-case basis. The City's preference is for optional call provisions when appropriate.

10. DEBT ISSUANCE PRACTICES

10.1. Composition and Selection of the Determination of Sale Method (Competitive or Negotiated) -

10.1.1. The City shall issue its debt obligations through a competitive sale unless the CFO determines that such a sale method will not produce the best results for the City. The conditions, which indicate the appropriate method for selling a particular bond issue, are generally described below:

10.1.2. Competitive Sale Criteria

- Bond prices are stable and/or demand is strong;
- Debt issuance markets are stable;
- The credit rating is well established and stable;
- There are no complex explanations required during marketing regarding a specific project, media coverage, political structure, political support, tax status, funding, or credit quality;
- The bond type and structural features are conventional; and
- The transaction size is manageable.

10.1.3. Negotiated Sale Criteria

- Bond prices are volatile and/or demand is weak and/or the supply of competing bonds is high;
- Debt issuance markets are less stable and market timing is important for circumstances such as refinancing transactions that are interest rate sensitive;
- Coordination of multiple components of the financing is required;

- The credit rating is not well established and stable;
- Sale and marketing of the bonds will require complex explanations about the City's projects, media coverage, political structure, political support, tax status, funding, or credit quality;
- The bond type and/or structural features are non-standard;
- Early structuring and market participation by underwriters is desired;
- Large transaction size; and
- Strong retail participation is desired and expected to enhance pricing efforts.

10.2. Use of Credit Ratings

10.2.1. In general, the City shall seek a rating from at least one nationally recognized rating agency. For a direct bank loan or limited public offering, the City may request an exemption from seeking a rating pursuant to Act 34.

11. DEBT MANAGEMENT PRACTICES

11.1. Investment of Bond Proceeds. If bond proceeds are held in trust, the Treasurer shall direct the Trustee to invest the proceeds of a bond sale until those proceeds are used for the intended purpose. If bond proceeds are held by the City, the Treasurer shall invest the proceeds pursuant to any investment policies of the City. The investments shall be made to minimize negative arbitrage to the greatest extent possible and to ensure the highest level of security.

11.2. Monitoring the Use of Bond Proceeds. The Office of the Treasury, with assistance from other City departments and agencies as necessary, shall monitor and track, for the life of the bonds or as otherwise required under the Internal Revenue Code, the proper and timely use of bond proceeds and bond-financed properties of the City.

11.3. Annual Disclosure. The City shall meet its continuing disclosure requirements in a timely and comprehensive manner, as stipulated by the SEC Rule 15(c)2-12 and other applicable laws, rules and regulations, as well as set forth in the continuing disclosure agreements implemented with each financing. The Office of the Treasury shall be responsible for providing ongoing disclosure information to the MSRB Electronic Municipal Market Access (EMMA) system, the central repository designated by the SEC for ongoing disclosures by municipal issuers. The Treasurer may lead a process to select a qualified third party (such third party may include Bond Counsel or Disclosure Counsel) to assist the City in the maintenance of its continuing disclosure undertakings. The City may enter into an agreement with a Disclosure Dissemination Agent for purposes of annual disclosure filings. The CFO's Office shall not be responsible for annual disclosure of the authorities not covered under this Directive as identified in Section 5.3.

11.4. Arbitrage Rebate Reporting. The Office of the Treasury shall maintain a system of record keeping and reporting to meet the arbitrage rebate compliance requirements as required by the federal tax code. This shall include tracking investment earnings on bond proceeds, calculating rebate-able earnings, and remitting any rebate payments to the federal government. No less than every five (5) years, the Treasurer may lead a process to select a qualified third party (such third party may include Bond Counsel) to assist the City in fulfilling its obligations with regard to arbitrage compliance.

11.5. Derivative Products. The City chooses not to use derivatives or other exotic structured finance products in the management of its debt portfolio. A derivative is a financial instrument created from or whose value depends upon the value of one or more separate assets or indices of asset values.

12. TRANSPARENCY AND REPORTING

12.1. The City shall provide full and complete financial disclosure to credit rating agencies, the MSRB via Electronic Municipal Market Access (EMMA), other levels of government, and the public in order to share clear, comprehensible, and accurate financial information. The City shall employ a dissemination agent to ensure timely filing of such disclosures.

12.2. The CFO's Office shall ensure relevant information is posted to the City's public website and the City's investor relations public website. The CFO's Office and the Office of Treasury shall review the information on these websites no less than quarterly to ensure the most recent information is available. The CFO's Office shall continuously review new methods and tools to improve and enhance transparency.

12.3. The City shall report, at least quarterly, a statement of its outstanding debt by type, including debt service payments made during the fiscal year and the status of any requirements to set-aside revenues for the purpose of paying debt service.

12.4. The Office of the Treasury shall monitor and report on the debt metrics identified in Section 8 of this Directive and shall report this information to the CFO's Office, at a minimum, on an annual basis. The metrics shall also be reported to the CFO as part of the CFO's review of a proposed debt issuance.

APPROVED

David P. Massaron
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