

DEBT ISSUANCE STRATEGY AND POLICIES FOR THE CITY OF DENTON

Presented to the Government Finance Officers Association of Texas
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City of Denton Overview

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- Founded in 1857 and incorporated in 1866.
- City continues to grow in terms of size.
 - Completed annexation proceedings for approximately 7,500 acres in 2010.
 - 3,400 acres annexed immediately, and 4,100 acres were given five-year non-annexation agreements.
- With annexation, City of Denton is approximately 94.9 square miles.
 - Strategically located 35 miles northeast of Fort Worth and 37 miles northwest of Dallas (Intersection of I-35E and I-35W).
 - 18 miles from DFW Airport.
- Home of two major universities and approximately 51,000 students.
 - Texas Woman's University (TWU).
 - University of North Texas (UNT).
- Regional center for medical services with two major hospitals.
 - Denton Regional Medical Center.
 - Presbyterian Hospital of Denton.
 - Wide range of specialty surgery and treatment centers.

City of Denton Overview (Cont'd)

- Estimated population of approximately 125,000 in 2014.
 - ▣ Population was 66,270 in 1990 and 82,976 in 2000.
- In 2011, Denton named as 7th fastest growing city in the country with a population over 100,000.
 - ▣ Growth continues to move north on both I-35E and I-35W.
 - ▣ City will likely continue to have a rapid growth rate in the future due to available land in these corridors.
 - ▣ Center for Economic Development and Research at UNT estimates that the City of Denton's population will approach 210,000 by 2030.
- Growth will necessitate the issuance of debt to build required infrastructure for city services.

Service Profile

- City of Denton is considered to be a “full service” municipal operation.
- The City provides general government services including:
 - ▣ Police and Fire
 - ▣ Parks and Recreation
 - ▣ Library
 - ▣ Planning
 - ▣ Code Enforcement, etc.
- Ongoing general government activities are typically driven by personnel costs associated with the services provided.
 - ▣ In the General Fund, for example, approximately 73% of the cost is related to salaries and associated benefits.

Service Profile (cont'd)

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- The City of Denton also operates several other self-supporting (or enterprise) operations.
 - ▣ Electric utility (Distribution and Transmission services).
 - ▣ Water utility (Water Treatment Plant).
 - ▣ Wastewater utility (Wastewater Treatment Plant).
 - ▣ Solid Waste services (Landfill).
- These services are capital intensive operations.
 - ▣ In the Electric Fund, for example, only 6% of the costs are related to personnel.
 - ▣ As such, cost drivers and decision points are dramatically different from other activities.
 - ▣ Majority of expenses tied to capital program.
- Approximately \$300 million in debt is expected to be issued over the next five years for the services described above.
 - Does not include any general government activities!!

Municipal Bond Insurance

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- City of Denton General Obligation bond ratings:
 - 'AA' from Standard and Poor's.
 - 'AA+' from Fitch Ratings.
- City of Denton Utility System bond rating is 'AA-' from Standard and Poor's.
- In prior years, the City purchased municipal bond insurance to achieve a 'AAA' rating.
 - Bond insurance cost was significantly lower than projected interest cost savings associated with AAA rating.
 - Due to 2008 financial crisis, AAA bond insurance is no longer available.
 - As such, a different approach to issuing debt was considered.

Debt Strategy

- Without bond insurance, the City would be required to utilize the 'AA-' rating for utility system revenue debt.
 - ▣ This rating results in a interest rate that is approximately 0.30% higher than AA rated bonds with a tax pledge.
 - ▣ On a \$50 million bond sale, this equates to approximately \$2 million in savings over a 20 year repayment term.
- As a result, the City of Denton began issuing Certificates of Obligation (COs) to fund utility system projects in 2010.
 - ▣ Counteracts absence of bond insurance and widening of credit spreads.
 - ▣ Lowers overall borrowing costs for the City.
 - ▣ Existing Revenue Bonds have also been refunded with General Obligation Refunding Bonds when economical.
 - ▣ Unlike Revenue Bonds, COs require that the City publish a Notice of Intent to issue debt.

Interest Cost Savings

- Although it is planned that the utility ratepayer will pay the debt service, the taxpayer is ultimately responsible for the debt.
 - ▣ Accordingly, the taxpayer is acting as a guarantor of the debt, much like bond insurance.
 - ▣ Converts from “implicit” to “explicit” guarantee.
- Due to this fact, the City of Denton has elected to dedicate any interest cost savings associated with COs to Street Improvements.
 - ▣ Costs are reduced by using ‘AA’ versus ‘AA-’ bond rating.
 - ▣ Savings transferred from utility operations.
- For FY 2014-15, savings are \$540,000 per year.
 - ▣ Expected to approach \$1.3 million annually by FY 2018-19.
 - \$26 million over a 20 year period!

City of Denton Debt Profile

As of September 30, 2014

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Type of Debt	Remaining Principal	Remaining Interest	Total
Revenue Supported GOs	\$79,222,885	\$18,132,679	\$97,355,564
Tax Supported GOs	78,282,115	20,537,600	98,819,715
Total General Obligation Bonds (GOs)	\$157,505,000	\$38,670,279	\$196,175,279
Revenue Supported COs	\$286,665,000	\$122,837,985	\$409,502,985
Tax Supported COs	45,545,000	13,231,097	58,776,097
Total Certificates of Obligation (COs)	\$332,210,000	\$136,069,082	\$468,279,082
Utility System Revenue Bonds	\$112,170,000	\$30,031,257	\$142,201,257
Total Revenue Supported Debt	\$478,057,885	\$171,001,921	\$649,059,806
Total Tax Supported Debt	123,827,115	33,768,696	157,595,811
Total Debt Outstanding	\$601,885,000	\$204,770,618	\$806,655,618

Debt Policy Fundamentals

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- City of Denton Debt Policy provides framework to guide decision making process for City Council.
 - ▣ Not expected to cover all potential issues that may arise in the future.
 - Despite this – policy is still 24 pages long!
 - ▣ While detailed, policy still provides management with flexibility to meet changing circumstances.
- Policy is reviewed annually and approved by Audit/Finance Committee and City Council.
- Formal policy provides structure to achieve continuity in debt issuance program.
 - ▣ GFOA recommended practice.
 - ▣ Allows annual discussion of key issues.
 - ▣ Provides opportunity for City Council to discuss debt in the context of long term strategic/policy approach.
- Key policy components for Denton include: Debt Management Committee, Limitations of Indebtedness, Acceptable Types of Debt, Compliance Elements, and Disclosure.

Debt Management Committee

- Committee consists of:
 - ▣ City Manager
 - ▣ Assistant City Managers
 - ▣ Director of Finance
 - ▣ Bond Counsel and Financial Advisory serve as consultants to the Committee as needed.
- Committee meets annually to review:
 - ▣ Debt Policy.
 - ▣ Status of Capital Improvement Program.
 - ▣ Status of outstanding debt and unspent bond proceeds.
 - ▣ Timing of additional financing needs.
 - ▣ Financing options, interest rates, etc.

Limitations of Indebtedness and Affordability Statement

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- Annual debt service on GO debt (excludes self-supporting) limited to 30% of General Fund Expenditures.
 - ▣ Contributed to rating agency increasing our management rating from “Good” to “Strong”.
- Coverage ratios dictated in bond covenants.
 - ▣ Policy also states that City will maintain at least a 1.25 coverage ratio on all COs issued for Utility System.
 - ▣ Further, City will strive to maintain 1.25 coverage ratio for each separate utility.
- While not in policy, City also benchmarks debt to other communities based upon various factors (per capita, percentage of revenue, percentage of taxable value, etc).

Acceptable Types of Debt

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- Describes uses and limitations for:
 - ▣ Long-term debt such as General Obligation Bonds (GOs) and Certificates of Obligation (COs).
 - ▣ Short-term debt such as Commercial Paper, Anticipation Notes, Capital Leasing, and Lines of Credit.
- Methods for the sale of debt (Competitive, Negotiated, and Private Placement).
- Discusses acceptable structure for debt.
 - ▣ Voter approved debt will strive to have final maturities of 20 years or less.
 - ▣ Revenue bonds/COs will strive to have final maturities of 30 years or less.
 - ▣ Encourages, but does not require, level debt structure.
 - ▣ Stipulates that debt will not exceed useful life of asset acquired.
- Variable Rate Debt is explicitly prohibited.
 - ▣ Contributed to rating agency increasing our management rating from “Good” to “Strong.”

Compliance Elements in Policy

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- Federal arbitrage requirements with respect to bond proceed investments.
 - ▣ Details arbitrage requirements.
 - ▣ Requires arbitrage rebate calculations to be performed on an annual basis.
- Restrictions on Private Business Use.
 - ▣ Requires the tracking of all property financed with tax-exempt obligations.
 - ▣ Discusses disposal and use of property financed with tax-exempt obligations.
 - ▣ When in doubt, check with bond counsel.
- Relevant compliance items will be discussed in more detail later in this session.

Disclosure

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- Intent is to provide full and complete disclosure of operating, financial, and legal conditions of the City.
 - ▣ When in doubt, double check with bond counsel.
- Policy defines which events, if material, must be disclosed to MSRB.
 - ▣ Examples include: bond calls, asset sales, litigation, etc.
 - ▣ Bond Counsel assists with determining “materiality.”
- Also defines events, regardless of materiality, that must be reported.
 - ▣ Examples include: Payment delinquencies, rating changes, adverse tax opinions, etc.
- Relevant disclosure items will be discussed in more detail later in this session.