Exhibit A

# Shelby County, Tennessee
# Debt Management Policy

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January 2019

# Shelby County Debt Management Policy
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# Shelby County Debt Management Policy

## Introduction

The purpose of the Shelby County Debt Management Policy (Debt Policy) is to provide written guidance related to the purpose and use of debt to fund the County's capital needs and the process of issuance of the County's debt obligations. The Debt Policy is intended to assist in maintaining the County's ability to incur debt and other long-term obligations at favorable interest rates for capital improvements, facilities, and equipment beneficial to the County and necessary for essential services, infrastructure and growth, and to repay debt responsibly without impairing other resources. Responsible issuance of debt for capital needs provides an investment in our community and makes capital expenditures affordable to current users and allows capital costs to be more equitably distributed to both current and future users.

This Debt Policy formally establishes the parameters for issuing debt in consideration of the County's ability to repay financial obligations within the context of legal, economic, financial and debt market conditions. The Debt Policy is intended to provide guidance in debt issuance decisions, to promote sound financial management, to protect and enhance the County's credit rating, to ensure the legal use of debt proceeds and to provide for the evaluation of debt issuance options.

Regularly updated debt policies are an important tool to insure the efficient and cost-effective use of the County's resources to provide needed services and infrastructure to the citizens of Shelby County and to maintain sound financial management practices. This Debt Policy will allow for an appropriate balance between establishing debt parameters and providing flexibility to respond to unforeseen circumstances and new opportunities.

**Legislative Oversight**

Shelby County will comply with legal requirements for notice of public meetings related to debt issuance. All resolutions authorizing the issuance of debt, guarantee of debt and entering derivative agreements will be presented to the County Commission's Budget Committee. The Director of Administration and Finance will describe the purpose and use of the debt to be issued, the estimated cost of the debt, estimated cost of issuance of the debt and the method to be used to market the debt. The County Commission's Budget Committee will then report the authorizing resolution to the Board of County Commissioners.

**Administration of Policy**

The County Mayor is the Chief Executive Officer for Shelby County. The Director of Administration and Finance is the Chief Financial Officer for the County. The County Mayor is ultimately responsible for administration of County financial policies. The Board of County Commissioners is responsible for the approval of any form of County borrowing and the details associated therewith. Unless otherwise designated, the Director of Administration and Finance coordinates the administration and issuance of debt.

The Director of Administration and Finance is also responsible for the attestation of disclosure and other bond related documents. References to the "County Mayor or his designee" in such documents are assumed to assign either the Chief Administrative Officer or the Director of Administration and Finance as the "designee" for administration of this policy.

**Use and Purpose of Debt (Debt Plan)**

The County will annually prepare a five year Capital Improvement Plan for consideration and adoption by the

Shelby County Board of Commissioners as part of the County's budget process. The plan will contain a description of the funding sources and timing of the capital projects identified in the operating and capital budgets. The County's share of allocations in the Capital Improvement Plan is limited to a maximum of $75 million each year. If the amount for any year exceeds $75 million, the reasons will be clearly documented in the Capital Improvement Plan.

Decisions regarding the use of debt will be based in part on the long-term needs of the County versus the amount of other funding resources dedicated in a given fiscal year to capital outlay on a "Pay-As-You-Go" basis. It is the County's preference to provide capital outlay on a pay-as-you-go basis except for Education capital funding and for projects in excess of $5 million. In addition, the County includes pay-as-you-go funding in the Operating Budget for smaller asset acquisitions and improvements each year rather than in the Capital Improvement Budget. The proposed Capital Improvement Program will identify the projects intended to be financed by the issuance of debt. To the extent practical, no more than $60 million will be funded by debt each year. If more is required, the projected impact on future debt service requirements will be addressed.

**Bond Ratings**

Credit ratings issued by the bond rating agencies are a major factor in determining the cost of borrowed funds in the municipal bond market. The concept of debt capacity, or affordability, recognizes that Shelby County has a finite capacity to issue debt at a given credit level. It should be recognized however, that there are no predetermined debt level/credit rating formulas available from the rating agencies. There are many factors involved. Determination of a credit rating by a rating agency is based on the rating agency's assessment of the credit worthiness of an issuer with respect to a specific obligation. To arrive at a judgment regarding an issuer's credit worthiness, the rating agencies analyze the issuer in four broad, yet interrelated areas: economic base, debt burden, administrative management, and fiscal management.

In an effort to maintain the ability to access the municipal markets at the lowest cost, Shelby County intends to maintain or increase the current ratings assigned by the national rating agencies. Current ratings as of the implementation of this policy are AA1 (Moodys)/AA+ (S&P and Fitch).

The Director of Administration and Finance is responsible for maintaining relationships with the rating agencies that assign ratings to the County's various debt obligations. This effort includes providing periodic updates on the County's general financial condition, along with coordinating meetings and presentations in conjunction with a new debt issuance. Full disclosure of operations and open lines of communications shall be made to the rating agencies. The County will prepare the necessary materials and presentations to the rating agencies to help each credit analyst make an informed evaluation. The Director of Administration and Finance is responsible for determining whether or not a rating shall be requested on a particular financing, and which of the major rating agencies will be asked to provide such a rating. The County will make every reasonable effort to maintain its high quality credit ratings.

## Debt Capacity Assessment and Affordability

In determining the amount of planned debt to be included in the Capital Improvement Plan the County will analyze the existing debt position to assess the impact of the County's future financing obligations on the County's ability to service the additional debt. The analysis should link projected long-term financings with the economic, demographic and financial resources expected to be available to pay for that debt and the maintenance of credit quality and market access.

**Structural Approach to Debt Management**

The County's debt position is currently considered high by the rating agencies when compared to similar sized counties across the nation. However, the bond rating agencies consider the County’s debt "manageable" due to the County's continued strong financial management along with generally consistent growth and economic conditions.

Shelby County must continually evaluate how much tax-supported debt is prudent (i.e. what the tax base can support and what the taxpayers can afford). If the County's tax-supported debt were to increase significantly beyond the current levels, it is possible that credit analysts would begin to question their current view of the County's debt position. However, progress is being made as Shelby County's tax-supported debt level peaked in fiscal year 2007 at $1.85 billion and has been declining since then. It is the County’s intent to consistently reduce its outstanding debt; a slow decline in debt is projected to continue based upon the debt plan noted above in this Debt Policy until the outstanding debt is under $1 billion.

It is important to continue to match capital needs with economic resources on an annual basis to ensure that the proposed level of debt issuance does not place a constraint on maintenance of the County's excellent credit worthiness or future credit rating improvements. Periodic monitoring of issuances will be done to ensure that an erosion of the County's credit quality does not occur.

**Debt Affordability Targets**

The County's General Obligation Bonds and Notes shall be maintained at a level considered manageable by the rating agencies based upon current economic conditions including among others, population, per capita income and assessed valuation. The following debt ratio targets provide guidance for this purpose.

| Debt Ratios Description | Target |
|---|---|
| Debt to Appraised Property Value Percentage | Under 5% |
| Debt to Assessed Property Value Percentage | Under 12% |
| Debt to Per Capita Personal Income Percentage | Under 6% |
| Principal Debt Percent Retired in Ten Years | Over 50% |
| Debt per Capita | Under $2,000 |
| Governmental Funds - Debt Service as Percent of Non Capital Expenditures | Under 20% |

Fund balance target ranges for both the Debt Service Fund and the General Fund have been established in the Fund Balance Policy, as adopted by the Board of County Commissioners. Adherence to these targeted levels will ensure that sufficient resources are available for cash flow for operations and debt payments, to adapt to variable economic conditions and unforeseen emergencies and to secure and maintain favorable bond agency ratings.

## Debt Issuance

**Security Considerations**

***General Obligation Bonds***

Shelby County's ability to meet its future debt obligations will primarily depend on the financial and other economic resources available at that time. The County has unlimited tax authority to meet its obligations.

### *Revenue Bonds*

Revenue Bonds may be issued to fund capital needs where there is a designated funding source for the repayment of the debt on the bonds.

### *Self-Supporting Debt*

The County may sponsor conduit financing for those activities (i.e. economic development, housing, health facilities, etc.) that have a general public purpose and are consistent with the County's overall service and policy objectives as determined by the County Commission. All conduit financings generally should insulate the County completely from any credit risk or exposure and must first be approved by the Director of Administrator and Finance before being submitted to County Commission for authorization and implementation. From time to time, the County will issue debt for which there is an identified repayment source. For debt to be characterized as self-supporting, the repayment source must support the issue through its maturity.

### *Lease-Purchase Financing of Equipment and Furnishings*

The County may enter into lease-purchase obligations to finance the acquisition of capital equipment and furnishings with estimated useful lives of ten years or less. Outstanding lease-purchase obligations issued to finance capital equipment and furnishings shall be evaluated in terms of the requesting division's ability to cover lease payments within its annual operating budget. Repayment of these lease-purchase obligations shall occur over a period not to exceed the useful life of the underlying asset or in any case no longer than ten years from the date of such obligations.

The Finance Department shall be responsible for developing procedures for use by County departments interested in participating in the lease-purchase program, and for setting repayment terms and amortization schedules, in consultation with the participating departments. Each department should include all capital lease requirement(s) within the relevant fiscal year's operating budget as an annual appropriation.

A capital lease allows the County the choice to finance vehicles and/or equipment but the cost will generally be somewhat higher than for general obligation bonds. Either Notes or Leases can be used for the same purposes. In compliance with GFOA Recommended Practices, the Director of Administrator and Finance is to have full knowledge of any lease agreements under taken by any department.

### *Limitations on General Fund Loan Guarantees and Credit Support*

As part of the County financing activities, General Fund resources may be used to provide credit support of loan guarantees for public or private developments that meet high priority County needs. Key factors that will be considered in determining whether or not the General Fund should be used to secure a particular debt obligation will include the following:

1) Demonstration of underlying self-support, thus limiting potential General Fund financial exposure.
2) Use of General Fund support as a transition to a fully stand alone credit structure, where interim use of General Fund credit support reduces borrowing costs and provide a credit history for new or hard to establish credits.
3) General Fund support is determined by the Director of Administrator and Finance to be in the County's overall best interest.

**Types of Debt**

1) Short-term Debt for working capital cash flow needs - To fund internal working capital cash flow needs. The County must receive approval from the State of Tennessee to issue these notes. Such notes must be repaid by the end of the fiscal year in which issued. Alternatively, the County may enter into a private placement note or a line or letter of credit.
2) Short-term Debt (generally up to two years) for capital projects - To provide interim financing for capital project needs approved in the Capital Improvement Plan. The form of this debt may include capital outlay notes, commercial paper, extendible municipal commercial paper and bond anticipation notes. This debt is generally issued for up to two years and some forms, such as bond anticipation notes, may be rolled over for up to an additional two years. The approval of the State of Tennessee must be granted before the issuance of short-term debt. The Director of Administration and Finance shall evaluate the most cost effective method of issuing short-term debt.
3) Capital Leases - For the purchase of capital assets where it is deemed to be cost effective.
4) Long Term Debt – General Obligation Bonds or Revenue Bonds for capital projects or to refund short-term debt that was issued for capital projects.

**Structure of Interest**

***Fixed Rate Debt***

The County may issue debt which has an interest rate that remains constant throughout the life of the bond. This debt will usually be serial bonds but may also be term bonds or capital appreciation bonds.

***Variable Rate Debt***

The County may issue securities that pay a rate of interest that varies according to a pre-determined formula, or results from a periodic remarketing of the securities. The County will have no more than 30% of its outstanding debt in a variable rate form, excluding variable rate debt that is swapped to a fixed rate with identical terms.

***Interest Rate Swaps***

The County may consider the use of interest rate swaps on a case by case basis in compliance with existing state statutes and the Derivative Guidelines and Policy section of this policy.

**Debt Refunding**

The Director of Finance and Administration, with the assistance of the County's financial advisors, shall monitor the municipal bond market for opportunities to obtain interest savings by refunding outstanding debt.

Key definitions related to refunding are described as follows:

> **Advance Refunding** - A method of providing for payment of debt service on a bond until the first call date or designated call date from available funds. Advance refundings are done by issuing a new bond or using available funds and investing the proceeds in an escrow account in a portfolio of U.S. government securities structured to provide enough cash flow to pay debt service on the refunded bonds.
>
> **Current Refunding** - The duration of the escrow is 90 days or less.

**Gross Savings -** Difference between debt service on refunding bonds and refunded bonds less any contribution from a reserve or Debt Service Fund.

**Present Value Savings -** Present value of gross savings discounted at the refunding bond yield to the closing date plus accrued interest less any contribution from a reserve or Debt Service Fund.

Prior to beginning a refunding bond issue, the County will review an estimate of the savings expected to be achieved from the refunding. The County will generally consider refunding outstanding bonds if one or more of the following conditions exist:

1) Total present value savings are at least 3% of the par amount of the refunded bonds,
2) Current savings are acceptable when compared to savings that could be achieved by waiting for more favorable interest rates and/or call premiums
3) The bonds to be refunded have restrictive or outdated covenants or are required to be refunded for tax purposes, or
4) Restructuring debt is deemed to be in the best interest of Shelby County by the Director of Administration and the Financial Advisors.

**Debt Structuring**
***Maturity structures***

The term of County debt issues should not extend beyond the useful life of the project or equipment financed. The repayment of principal on tax supported debt will not extend beyond 25 years unless there are compelling factors which make it necessary to extend the term beyond this point. To the extent bonds are used to finance computer hardware and software, repayment of principal shall not exceed 10 years.

General Obligation debt issued by the County for "new money" projects should be structured to provide for either level principal or level debt service. Ascending debt service should generally be avoided.

***Balloon Debt***

According to Public Chapter 766, Acts of 2014 (balloon debt), a credit rating of Aa1/AA+, allows a local government to issue debt that is considered balloon debt per state law.

The County's current credit ratings of Aa1/AA+ allows for the issuance of balloon debt; however, as stated above, General Obligation debt will be structured to provide either level principal or level debt service.

- The County may issue debt that is considered balloon debt, as defined by T.C.A. § 9-21-134, as part of a refinancing of existing debt. In the case of a refinancing that is considered balloon debt, the refunding debt service must be structured to mirror or match the refunded debt service for each series being refunded or in aggregate.
- County refinancing opportunities will be considered in accordance with the Debt Refunding section contained herein.

***Available Revenue/Call Features***

The County's long-term debt is generally sold with a 10 year prepayment or call option. When available revenues are identified, the Director of Administration and Finance should consider prepaying or defeasing portions of its outstanding debt.

***Credit Enhancement/Bond Insurance***

Bond insurance is an insurance policy purchased by an issuer or an underwriter for either an entire issue or specific maturities, which guarantees the payment of principal and interest. This security provides a higher credit rating and thus a lower borrowing cost for an issuer. However, for entities like Shelby County with high bond ratings, the cost of insurance usually exceeds the lower borrowing cost.

Bond insurance can be purchased directly by the County prior to the bond sale (direct purchase) or at the underwriter's option and expense (bidder's option). Insurance should only be purchased by the County if it has been determined that it is cost beneficial to purchase the policy.

**Method of Sale**

Bonds may be sold through a competitive process or through a negotiation with a pre-selected underwriting syndicate. Either method should be structured to provide for flexibility in issue size, maturity amounts, term bond features, etc. A competitive sales process is generally required by State law for new money bond issues.

**Competitive Sale -** With a competitive sale, any interested underwriter(s) is invited to submit a proposal to purchase an issue of bonds. The bonds are awarded to the underwriter(s) presenting the best bid complying with the criteria set forth in the notice of sale and offering the lowest overall interest rate. Competitive sales should be used for all issues unless the Director of Administration and Finance recommends a negotiated sale based upon the criteria stated herein.

**Negotiated Sale -** A securities sale through an exclusive arrangement between the issuer and an underwriter or underwriting syndicate. Negotiated underwriting may be considered upon recommendation of the Director of Administration and Finance based on one or more of the following criteria:

- Extremely large issue size
- Complex financing structure (i.e., variable rate financings, new derivatives and certain revenues issues, etc.) which provides a desirable benefit to the County
- Market conditions
- Credit strength
- Other factors which lead the Director of Administration and Finance to conclude that a competitive sale would not be as effective.

**Role of the Underwriter**

The County generally employs a syndicate of underwriters for each bond sale. The process of selecting underwriters is provided below. All underwriters are clearly notified that the County engages financial advisors. For negotiated bond sales, the request for proposals will require each underwriter to acknowledge its primary role as a purchaser and that it has financial interests that differ from the County and they shall be required to provide pricing information both as to interest rates and to takedown per maturity to the Director of Administration and Finance in advance of pricing the debt.
The selection of underwriters for a negotiated sale shall generally be as follows:

- The underwriting group will include a minimum of 20% minority or women owned firms (MWBE)
- The underwriting group will include a minimum of 20% of firms which have a significant local presence
- Proposals shall be solicited from at least ten underwriters considered to be qualified to underwrite the proposed bond issue

Proposals submitted by firms to serve as the County's underwriter shall be evaluated based upon 1) cost, 2) MWBE Status, 3) local presence/ownership, 4) underwriting experience nationally, in Tennessee and with the type of bonds being issued, 5) structure ideas, 6) marketing and distribution capabilities, and 7) ability to underwrite/capital position. The selection of the senior book-running manager will be more heavily weighted on applicable underwriting experience, ability to underwrite and cost. The number of underwriters selected will depend on the size, nature and complexity of the bond issue. The evaluation of the proposals submitted by the underwriters shall be conducted by the Financial Advisors and the Director of Administration and Finance.

The Request for Proposals shall request that the underwriter submit a detailed estimate of all components of their compensation.

**Priority of Orders**

For negotiated sales, the Director of Administration and Finance shall establish the priority of orders working with our financial advisor and the underwriter on each financing to determine priority of orders to be filled from customers and rules, if any, for the allocation of bonds among members of the underwriters group. Such priority of orders and allocation guidelines will be established to accomplish the County's goals on the financing and to adapt to the current market conditions.

**Allocation of Bonds**

1) The book-running senior manager will be responsible for ensuring that the overall allocation of bonds meets the County's goals of obtaining the best price for the issue and a balanced distribution of the bonds.
2) The Director of Administration and Finance must approve the final bond allocation process with input from the book-running senior manager.

## Other Professionals Engaged in the Process of Issuing Debt

All professionals engaged in the issuance of debt shall be required to clearly disclose all compensation and consideration related to the services provided in the debt issuance process both from Shelby County and from any other parties involved in the debt issuance. This shall include "soft" costs or compensation in lieu of direct payments.

Professionals involved in a debt transaction hired or compensated by the County shall be required to disclose to the County existing client relationships between and among the professionals to a transaction (including but not limited to financial advisor, swap advisor, bond counsel, trustee, paying agent, underwriter, counterparty, and remarketing agent), as well as conduit issuers, sponsoring organizations and program administrators. This disclosure shall include that information reasonably sufficient to appreciate the significance of the relationships. Professionals who become involved in the debt transaction as a result of a bid submitted in a widely and publicly advertised competitive sale conducted using an industry standard, electronic bidding platform are not subject to this disclosure. No disclosure is required that would violate any rule or regulation of professional conduct.

**Financial Advisor**

The County will retain external financial advisor(s) who shall assist the County in the ongoing evaluation and modification of it's long-term and short-term debt strategies for both capital and operating cash flow needs. The County will enter a written agreement with each financial advisor. Such agreement will specify that the financial advisor shall not be permitted to bid on, privately place or underwrite a bond issue for which they have been providing advisory services for the issuance. They will recommend or review and comment on recommendations from others on potential financing transactions and methodologies. The firm may provide such additional services as the County might request in connection with securities, including but not limited to budgeting, debt planning, financial management, investments, or other related matters. The financial advisor will assist County officials in evaluating and selecting prospective underwriters, dealers, or swap counterparties with respect to the negotiated sale or remarketing of securities and in evaluating and selecting providers of credit or liquidity support for securities and to negotiate with such providers on behalf of the County.

In addition to the foregoing, the financial advisor's responsibilities for each specific debt issue will include, but not be limited to, the following:

- Develop a financing plan in consultation with County officials which provides the required capital on a timely basis to achieve the lowest available interest costs to Shelby County while providing the greatest degree of operating flexibility and in consideration of the risk profile

- Provide recommendations regarding the features of the debt issuance structure, including coupon structure and call provisions.
- Assist the County and their Counsel in the preparation of the official statement, official notice of sale, bid form and other market documents concerning the offering of securities and in such manner as is necessary and appropriate.
- For negotiated sales, assist the County in the selection of underwriters.
- Assist the County in the selection of paying agents, escrow verification agents, and escrow trustee.
- For competitive sales, market the debt issue among prospective underwriters and coordinate the competitive sale.
- Provide recommendations to the County and coordinate presentations to bond rating agencies.
- Assist Bond Counsel in preparing all documents related to each debt issue.
- Provide a post issuance evaluation of the bond issue.

The Financial Advisor shall possess the necessary expertise and have the required resources of the economic and financial markets and the ability to evaluate the existing debt profile and potential future debt issuances and interest rate swaps.

**Bond Counsel**

The County will retain external bond counsel for all debt issues. An engagement letter agreement shall be entered with Bond Counsel. Bond Counsel will work closely with County officials, its in-house counsel, staff and financial advisors with all financing transactions undertaken by the County. All debt issued by the County will include a written opinion by bond counsel affirming that the County is authorized to issue the debt, stating that the County has met all state constitutional and statutory requirements necessary for issuance. Bond Counsel shall assure the validity of any chosen method of financing and the legal authority for any proposed alternative method. They shall review the bond closing documents related to the issuance of all debt, prepare resolutions, trust indentures and security agreements where necessary and determine the debt's federal income tax status. Bond Counsel will provide advice on application of bond proceeds and federal income tax and securities law compliance issues.

**Other Service Providers**

The Director of Administration and Finance shall have the authority to select other service providers such as escrow agents, verification agents, and trustees as necessary to meet legal requirements and minimize net County debt costs.

# Transparency: Reporting and Disclosure

**Issuance Compliance**

The County shall comply with legal requirements for notice and for public meetings related to debt issuance. The County will provide timely information to the public and to the investors in its debt instruments. In the interest of transparency, all expected costs (including interest, issuance, continuing and one-time) will be disclosed in documents attached to the resolution authorizing the bond issuance to the extent practical and in a timely manner. As required by State Law, the County will file the "Report on Debt Obligation" to the State of Tennessee (State form No. CT-0253) detailing all actual costs of each bond issue and will be available as a public record. The County's Comprehensive Annual Financial Report and its Annual Adopted Budget, as well as other appropriate information are on Shelby County's website. In addition, all appropriate disclosures will be made on the Electronic Municipal Market Access (EMMA) system operated by the Municipal Securities Rulemaking Board.

***Preliminary and Final Official Statement***

The official statement is the disclosure document prepared by or on behalf of the County for an offering of securities. The preparation of the official statement is the responsibility of the Director of Administration and Finance.

***Continuing Disclosure***

In complying with U.S. Securities and Exchange Commission Rule 15c2-12 related to notice of competitive sales, the County will provide certain financial information and operating data by specified dates, and will provide notice of certain enumerated events with respect to the bonds, if material. This information must be provided to the Electronic Municipal Access (EMMA) system.

Material events include the following:

- Principal and interest payment delinquencies
- Nonpayment-related defaults
- Unscheduled draws on reserves
- Unscheduled draws on credit enhancements
- Substitution of credit or liquidity providers or the failure of performance on the part of a liquidity provider
- Adverse tax opinions or events affecting the tax-exempt status of the bonds
- Modifications to rights of bond holders
- Bonds calls
- Defeasances
- Matters affecting collateral
- Rating changes

**Post Issuance Compliance**

***Arbitrage Compliance***

Section 148(f) of the Internal Revenue Service Code requires that certain earnings on non-purpose investments allocable to the Gross Proceeds of an issue be paid to the United States to prevent the bonds of the issue from being arbitrage bonds. The arbitrage that must be rebated is based on the difference between the amount actually earned on non-purpose investments and the amount that would have been earned if those investments had a yield equal to the yield on the issue. The arbitrage rebate is generally calculated and rebated, if applicable, every five years after the issue date of the bonds. The Department of Finance shall maintain a system of record keeping and reporting to meet the arbitrage rebate compliance requirements of federal tax code.

***Record Keeping***

Detailed records of each bond issue are required to be maintained for seven years following the bonds and any refunding of the bonds are paid in full. These records including the detailed records of the disbursements of the proceeds of the bond issue and any interest earned on the proceeds prior to being expended. Records will also be maintained of all disbursements for repayment of the bonds and any costs related to the bond issue and, if applicable, related swaps and the associated costs.

## Derivative Guidelines and Policy

This policy will provide direction regarding the County's use of derivative products, such as swaps, swaptions, cancellation options, caps, floors, and collars ("derivatives"). This policy, containing procedures and guidelines, establishes the process to be used by the County when entering into a derivative transaction. The County must determine that it is appropriate and advisable to enter into a derivative transaction based on the guidelines set forth herein. However, failure to comply in any manner with these swap guidelines shall not result in any liability on the part of Shelby County to any party.

The use of derivatives in administering debt can be useful to manage risk, reduce costs and provide flexibility. Use of derivative products will consider any addition of risk, restriction of flexibility and impact to expected cost. The County will adhere to the "Guidelines for Interest Rate and Forward Agreements" issued by the state if employing a derivative and receive a positive report of compliance with these guidelines by the State Comptroller. The State guidelines require that the Mayor and at least one member of the County Commission have a basic understanding of interest rate agreements and the related indebtedness and the County is responsible for maintaining staff able to understand, monitor and prepare required disclosures of interest rate agreements.

**Authorization – State**

Authorizing statutes for forward purchase agreements:
Local Government Public Obligations Act (Title 9, Chapter 21)
    TCA Sections 9-21-9302(b), 9-21-910(d), 9-21-1008(c)
        Public Chapter 432, Acts of 1991
        Public Chapter 253, Acts of 2001
School Bonds Act (Counties)(Title 49, Chapter 3, Part 10)
    TCA Section 49-3-1002(i)
        Public Chapter 253, Acts of 2001

Authorizing statues for interest rate agreements:
Local Government Public Obligations Act (Title 9, Chapter 21)
    TCA Sections 9-21-213(d), 9-21-305(c), 9-21-602(c), 9-21-907(c), 9-21-1006(c)
        Public Chapter 432, Acts of 1991
        Public Chapter 253, Acts of 2001
School Bonds Act (Counties)(Title 49, Chapter 3, Part 10)
    TCA Section 49-3-1002(h)
        Public Chapter 253, Acts of 2001

In addition, the State Funding Board has adopted "Guidelines for Interest Rate and Forward Purchase Agreements". These guidelines must be followed and prior to entering any interest rate or forward purchase agreement the State Comptroller must issue a report of positive compliance.

**Authorization - County**

The Director of Administration and Finance (the "Director") is responsible for evaluating and recommending derivative agreements. With the approval of the County Mayor, the Director may recommend derivative agreements to the Board of County Commissioners (the "Commission") in the form of an authorizing resolution. Derivative agreements must be approved by the Commission by resolution.

The authorizing derivative resolution will approve the derivative agreement and its details, including notional amount, security, payment, and other conditions relating to the transaction. In the authorizing resolution, the County must state the goals of the derivative transaction, and each resolution will identify the appropriate County officials authorized to make changes, within limits, to the derivatives agreement considered. In the event of a conflict between a swap resolution and this policy, the swap resolution will control.

The County must receive a written opinion from a reputable law firm that the proposed Derivative agreement is a legal and valid obligation of the County. Actions by the County must comply with applicable law, and the Director of Administration and Finance must determine that the proposed derivative is in accordance with the County resolutions and does not violate existing Indentures and other contracts.

**Goals and Purposes**

Derivative transactions can be an important aspect of the County's asset/liability and debt management strategy. The County, by utilizing derivatives, should reasonably expect to achieve one or more of the objectives listed below.

- When compared to conventional markets, the County will achieve more savings or more flexibility in meeting its overall financial objectives.

- Achieve diversification of a particular bond offering or achieve debt management goals and objectives through certain derivative structures.

- Enhance investment returns or incur variable rate exposure within prudent risk guidelines.

- Reduce or hedge an exposure to changes in interest rates in relation to a particular financing or the overall asset/liability management of the County.

- Take advantage of market opportunities to result in a lower net cost of borrowing with respect to debt obligations.

- Provide benefits and/or flexibility to the County with respect to its financial position.

- Accomplish a financial objective not otherwise obtainable using traditional Financing method.

*The County shall not enter into any derivative transaction for the purpose of speculation.*

*When using derivative instruments, the County should follow all guidelines established by the state of Tennessee.*

## General Guidelines

The County should follow the guidelines listed below in evaluating and recommending all derivative transactions:

- Ratings and Outstanding Obligations: Consideration should be given to the impact that any derivative agreement will have on the credit ratings of the County. The agreement should follow outstanding commitments with bond insurers, credit enhancers, and surety providers, if any.

- Bond Capacity: The execution of a derivative agreement should not impede the County's ability to issue traditional fixed rate or variable rate debt in the future. Additionally, the derivative transaction should not conflict with existing covenants and debt policies.

- Long-Term Implications: In evaluating derivative transactions, the County should review the long-term implications associated with the proposed derivative including historical interest rate trends, bond capacity (as noted above), and the potential impact on the ability to refund debt in the future.

- Accounting: The County should reflect the use of derivatives on its financial statements in accordance with generally accepted accounting principles and must comply with current GASB Technical Bulletins or other GASB issued directives. The Administration should determine the impact on the County's accounting before executing a derivative.

- Prior to execution, the County should obtain written estimates under various scenarios of the potential termination costs that might occur, and plan for how such costs would be funded. This information should be included in the resolution packet approving the derivative agreement.

## Counterparty Standards

Many derivatives create an exposure to the creditworthiness of the firms that serve as the County's Counterparties. To protect its interests, the County should use the following standards in choosing its Counterparties.

- The County shall attempt to enter into derivative transactions with Counterparties, at the time of the transaction, rated at least equal to the County, but in no event, lower than A-/A1/A by at least two of the three nationally recognized credit rating agencies (Standard & Poor's, Moody's, and Fitch Ratings, respectively) or the payment obligations of the Counterparty should be guaranteed by an entity with such ratings.

- The Counterparty must create and implement innovative ideas in the derivative market and maintain a market for such products.

- The Counterparty should have presence in the municipal derivatives market and should have demonstrated experience in the successful execution of derivative transactions.

## Derivative Solicitation and Procurement Methods

The County will have the option to negotiate agreements or use a competitive bidding process involving several Counterparties. The procurement method chosen by the Director will depend upon what they deem is in the best interests of the County. Regardless of the procurement method, the participating Counterparties should be in accordance with the Counterparty Standards (outlined in the previous section).

In general, the County should procure derivatives by negotiated methods in the following situations:

- The County determines that because of the size or complexity of the transaction, a negotiated process would be advantageous to the County.

- A negotiated method will promote the County's interests by rewarding innovative ideas or substantial time commitment and resources by a certain Counterparty.

If a competitive process is selected, the County will determine which Counterparties and the number of Counterparties it will permit to participate in the transaction. A solicitation for bid will be sent to the participating parties, and the award will be based on the best bid and other factors the County considers relevant. The County may also use a bidding process involving a combination of the competitive and negotiated methods. This "quasi-competitive" process may be used in situations in which the County wishes to award more than one firm or wants to diversify its Counterparty risk. Regardless of the method chosen, the County should get an independent written opinion from its swap or financial advisor that the terms and conditions of the executed derivative reflect a fair market price as of the execution date and such opinion should be provided to the County Commission.

**Form of Agreements and Other Documentation**

The derivatives entered into by the County shall contain the terms and conditions set forth in the International Swap and Derivatives Association, Inc. ("ISDA") Master Agreement, including any schedules, credit support annexes and confirmations. The schedules and credit support annex should reflect specific requirements and business terms desired by the County for a particular transaction.

Within the agreement documents, Events of Default should include the following:

1) Failure to make payments when due
2) Material breach of representations and warranties
3) Failure to comply with downgrade provisions or with any other provisions of the agreement after a specified notice period.

Upon certain credit rating events, the agreement should provide for the right of assignment by the affected party. If the County is the affected party, it should request that the Counterparty post collateral or provide some other credit support. If the Counterparty does not provide the required credit support, the County should have the right to assign the agreement to another Counterparty and based on terms acceptable to both parties. The credit rating thresholds should be included in the documents. The mechanics for determining termination values at various times and upon various occurrences must be explicit in the derivative agreement.

Prior to execution, the County will prepare a resolution pertaining to the transaction, and the resolution and approval of Commission is required prior to enter into the derivative transaction.

**Termination Provision**

All swap transactions shall contain provisions granting Shelby County the right to optionally terminate a swap agreement at any time over the term of the agreement at market value. In general, exercising the right to terminate an agreement should produce a benefit to Shelby County, either through the receipt of a payment from a termination or, if the termination payment is made by Shelby County, in conjunction with a conversion to a more beneficial debt obligation of Shelby County or by the purchase of a similar product from others or reduction of risk, all as determined by Shelby County.

**Evaluation and Management of Derivative Risks**

Before entering into a derivative, the County should assess all the risks inherent in the transaction. Certain risks will inevitably be created as the County enters into derivative transactions and the County should periodically evaluate these risks and exposures. In addition to the risks detailed below, market-access, interest rate, tax, and bankruptcy risks should be evaluated. Below are guidelines for the management and mitigation of certain risks.

1. ***Counterparty Risk:*** The risk of a defaulting Counterparty (or Counterparty's insurer) that will not fulfill its obligations according to the agreement should be evaluated and managed.

    - The County should require that the Counterparty meet the Counterparty Standards (described above).

    - If the Counterparty's credit rating is downgraded below a specified threshold, the County should require that its exposure to the Counterparty be collateralized according to the terms of the Credit Support Annex.

    - The County should also diversify its exposure to Counterparties. Before entering into a transaction, the County should determine its outstanding exposure to the relevant Counterparty and determine how the proposed transaction will affect that exposure. The exposure should not only be measured in notional amount but also in how the change in rates would affect the fair values.

    - The County should give written permission prior to the transfer of the derivative agreement from the Counterparty to another Counterparty. The County should not authorize the transfer of the agreement to another Counterparty unless the replacement Counterparty fits the Counterparty Standards detailed above.

    - The County should require collateralization if the credit of the Counterparty negatively changes as a result of a merger or acquisition.

2. ***Termination Risk:*** The risk that a derivative's unscheduled end will affect the County's asset/liability strategy or will present the County with a significant unanticipated termination payment to the Counterparty can be mitigated in the following ways:

    - The County should have the right to optionally terminate an agreement at any time at the market value of the derivative at the time of termination (as long as a Counterparty receiving payment upon termination is not in default). Exercising this right should generally be in the County's favor, either with the receipt of a termination payment or if a termination payment is made by the County, with a change to a more beneficial position in relation to the County's debt. The termination value should be determined by the Second Method Market Quotation.

    - Upon downgrade or default by either party, a termination payment by the County may be required. In some instances, the defaulting party will be required to make a termination payment to the non-defaulting party. However, sometimes the non-defaulting party may be required to make a payment to the defaulting party. Prior to making a termination payment to a defaulting Counterparty, the County should evaluate whether it is financially advantageous for the County to obtain a replacement Counterparty or make the termination payment.
    - The County, upon a Counterparty default, should require that the termination occur on the side of the bid-offer spread that is most beneficial to the County. This would allow the

County, if it desires, to replace the defaulting Counterparty with another Counterparty at no cost to the County.

3. ***Term Risk:*** The County should determine the appropriate term for a derivative agreement on a case-by-case basis.

    - In choosing the appropriate term, the slope and steepness of the curve, the change in rates and/or cost from year to year along the curve, potential termination values, and the impact that the term of the derivative has on the overall exposure to the County should all be considered.

    - The term of any agreement should not exceed the final maturity of the County's bonds or other obligations issued or outstanding in connection with the agreement.

4. ***Liquidity Risk:*** Before entering into a derivative agreement, the County should consider the liquidity of the proposed transaction (if enough firms actively participate in the market for the proposed transaction to allow the County, if it wishes, to assign the trade and/or to have more transparent, fair pricing).

5. ***Basis Risk:*** Basis risk arises when the variable rates on the hedged item and the rates on the derivative are based on different indices. This variance can adversely affect the County's payments and/or synthetic interest rates and the savings may not be realized.

    - If there is not a direct relationship between the indices of the derivative and the underlying hedged item, the risk should be analyzed prior to execution of the derivative.

    - The index chosen as the basis of the derivative should be a recognized market index such as the Securities Industry and Financial Markets Index (SIFMA) or London Interbank Offering Rate (LIBOR).

6. **Tax Risk**: The risk that changes or proposed changes in the tax laws or events relating to the tax-exempt status of the Governmental Entity's obligations or of tax-exempt obligations generally will cause interest rates on the debt of the Governmental Entity to increase.

7. **Interest Rate Risk:** The risk that an adverse move in variable rates increases the overall cost of borrowing.

As a general guideline, neither tax risk nor interest rate risk should exceed 30% of the County's outstanding debt.

**Collateralization**

As appropriate, Shelby County, in consultation with its Bond Counsel and Swap Advisor, may require collateral or other credit enhancement to be posted by each swap Counterparty. At a minimum, collateral requirements shall be subject to the following guidelines for the County and the Counterparty:

- The Counterparty is required to post collateral should the credit rating of the either party fall below the "A-/A1/A" category by at least two of the nationally recognized rating agencies.

- Acceptable collateral is cash, treasuries, and AAA rated agency securities. The valuation of the collateral will be mutually agreed upon during negotiation of the agreement.

- The collateral should be marked-to-market periodically, either daily, weekly, or monthly, by an independent third party.

- The collateral should be requirement should be at least 110% of the market value and preferably 125% as the market value of a swap can change significantly on a daily basis.

- Failure by either party to collateralize when required under the agreement will be considered a default.

- The derivative agreement should provide the Minimum Transfer Amount and reasonable Threshold Amounts for the posting of collateral.

**Monitoring and Reporting Requirements**

The County will maintain an appropriate monitoring program for all its derivatives transactions. The County will issue a written status report on all its derivative transactions at least once per year, to include the following items:

- All changes to outstanding agreements or new derivative agreements entered into by the County since the last report presented to the Commission.

- The most recent Mark-to-market valuations as of a specified date for each of the County's outstanding derivatives.

- Termination analysis that shows the net impact to the County of 50, 100, and 150 basis point movements (up and down).

- The amount of collateral, if any, that has been required to be posted by either party and the amount that has actually been posted.

- The amounts that were required to be paid and received under the agreement and the amounts that were actually paid and received.

- A status of each outstanding transaction that consists of a summary of the terms and conditions such as outstanding notional amounts, interest rates, maturities, and indices.

- The full name, description and credit ratings of each Counterparty.

- A description of any default or rating change of a Counterparty and the impact of that on the County.

- The total notional amount and remaining term of all derivative contracts the County has outstanding with each Counterparty.

- Any future derivative transactions the County is considering and the risks, purposes, and impact that the transaction would have on the County's asset/liability program.

# Adoption of Policy

This Debt Management Policy was adopted by the Shelby County Board of County Commissioners on January 14, 2019.