

# ATHENS UTILITIES BOARD ATHENS, TENNESSEE

## Debt Management Policy

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<b>Division of Accounting – Policies and Procedures Manual Standard Policies and Procedures</b>	
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## **INTRODUCTION**

This Debt Management Policy (the “Debt Policy”) is a written guideline with parameters that affect the amount and type of debt that can be issued by the Athens Utilities Board (the “Utility”), the issuance process, and the management of the Utility’s debt. The purpose of this Debt Policy is to improve the quality of management and legislative decisions and to provide justification for the structure of debt issuances consistent with the Debt Policy’s goals while demonstrating a commitment to long-term capital planning. It is also the intent of the Utility that this Debt Policy will signal to credit rating agencies, investors, and the capital markets that Athens Utilities Board is well managed and will always be prepared to meet its obligations in a timely manner. This Debt Policy fulfills the requirements of the State of Tennessee regarding the adoption of a formal debt management policy on or before January 1, 2012.

This Debt Policy provides guidelines for the Utility to manage its debt and related annual costs within both current and projected available resources while promoting understanding and transparency for our citizens, rate payers, businesses, investors and other interested parties.

Athens Utilities Board may, from time to time, review this Debt Policy and make revisions and updates, if warranted.

**Athens Utilities Board**  
**DEBT MANAGEMENT POLICY**

**I. INTRODUCTORY STATEMENT**

In managing its Debt (defined herein as tax-exempt or taxable bonds, capital outlay notes, other notes, capital leases, interfund loans or notes, and loan agreements); it is the Utility's policy to:

- Achieve the lowest cost of capital within acceptable risk parameters
- Maintain or improve credit ratings
- Assure reasonable cost access to the capital markets
- Preserve financial and management flexibility
- Manage interest rate risk exposure within acceptable risk parameters

**II. GOALS AND OBJECTIVES**

Debt policies and procedures are tools that ensure that financial resources are adequate to meet the Utility's long-term capital planning objectives. In addition, the Debt Policy helps to ensure that financings undertaken by Athens Utilities Board have certain clear, objective standards which allow the Utility to protect its financial resources in order to meet its long-term capital needs.

The Debt Policy formally establishes parameters for issuing debt and managing a debt portfolio which considers Athens Utilities Board's specific capital improvement needs, ability to repay financial obligations, and existing legal, economic, and financial market conditions. Specifically, the policies outlined in this document are intended to assist in the following:

- To guide the Utility in policy and debt issuance decisions
- To maintain appropriate capital assets for present and future needs
- To promote sound financial management
- To protect the Utility's credit rating
- To ensure the Utility's debt is issued legally under applicable state and federal laws
- To promote cooperation and coordination with other parties in the financing
- To evaluate debt issuance options

### **III. PROCEDURES FOR ISSUANCE OF DEBT**

#### **1) Authority**

a) The Utility will only issue debt by utilizing the statutory authorities provided by *Tennessee Code Annotated* (“TCA”) as supplemented and revised and the Internal Revenue Code (the “Code”).

b) The Utility will adhere to any lawfully promulgated rules and regulations of the State and those promulgated under the Code.

c) The Utility is a component unit of the City of Athens, Tennessee. It is an enterprise fund of the City consisting of four distinct divisions (Power, Water, Gas and Wastewater Treatment). Each division is a separate economic entity with its own separate funds and accounting records. Each division is managed by a Superintendent, and each of the Superintendents reports directly to the General Manager who manages all divisions of the Utility. The General Manager reports to a five-member Board of Directors that is responsible for the Utility as a whole. The Board of Directors is composed of four stake holders of the Utility and one City Council representative of the City of Athens, Tennessee. All of the Utility’s debt will be presented to, and approved by, the Utility’s Board of Directors. As a component unit of the City, all debt of the Utility must be presented to, and approved by, the City Council after approval of the Utility’s Board of Directors.

#### **2) Transparency**

a) It is recognized that the issuance of debt must have various approvals and on occasion, written reports provided to the State of Tennessee Comptroller’s office either prior to adoption of resolutions authorizing such debt, prior to issuance and/or following issuance. The Utility, in conjunction with any professionals (including, but not limited to, financial advisors, underwriters, bond counsel, etc. which may individually or collectively be referred to herein as “Financial Professionals”) will ensure compliance with TCA, the Code and all federal and state rules and regulations. Such State compliance will include, but not be limited to, compliance with all legal requirements regarding adequate public notice of all meetings of the Utility related to consideration and approval of debt. In the interest of transparency, all costs (including interest, issuance, continuing and one-time) shall be disclosed to its legislative body, citizens and other interested parties in a timely manner. Additionally, the Utility shall provide the Tennessee Comptroller’s office sufficient information on the debt to not only allow for transparency regarding the issuance, but also assuring that the Comptroller’s office has sufficient information to adequately report or approve any formal action related to the sale and issuance of debt. The Utility will also make this information available to its legislative body, citizens and other interested parties.

a) The Utility will file its Audited Financial Statements and any Continuing Disclosure document prepared by the Utility or it’s Dissemination Agent. To promote transparency and understanding, these documents should be furnished to members of the Legislative Body and made available by usual and customary means to its citizens, taxpayers, rate payers, businesses, investors and other interested parties.

#### **IV. CREDIT QUALITY AND CREDIT ENHANCEMENT**

The Utility's Debt management activities will be conducted in order to maintain or receive the highest possible credit ratings. The Utility, in conjunction with any financial professionals that the Utility may choose to engage, will be responsible for maintaining relationships and communicating with one or more rating agencies.

The Utility will consider the use of credit enhancements on a case-by-case basis, evaluating the economic benefit versus cost for each case. Only when clearly demonstrable savings can be shown shall an enhancement be considered. The Utility will consider each of the following enhancements as alternatives by evaluating the cost and benefit of such enhancements.

##### **1) Insurance**

The Utility may purchase bond insurance when such purchase is deemed prudent and advantageous. The predominant determination shall be based on such insurance being less costly than the present value of the difference in the interest on insured bonds versus uninsured bonds.

##### **2) Letters of Credit**

The Utility may enter into a letter-of-credit ("LOC") agreement when such an agreement is deemed prudent and advantageous. The Utility or its financial professionals, if any, may seek proposals from qualified banks or other qualified financial institutions pursuant to terms and conditions that are acceptable to the Utility's Board of Directors.

#### **V. AFFORDABILITY**

The Utility shall consider the ability to repay debt as it relates to the total budget resources, the financial performance of the applicable division of the Utility, and other revenues available to service the Debt. The Utility may consider debt ratios and other benchmarks compared to its peers when analyzing its debt including materials published by the nationally recognized credit rating agencies.

#### **VI. DEBT STRUCTURE**

The Utility shall establish all terms and conditions relating to the issuance of debt and will invest all bond proceeds pursuant to the terms of its investment policy, if any. Unless otherwise authorized by the Utility's Board of Directors, the following shall serve as the Debt Policy for determining structure.

##### **1) Term**

All capital improvements financed through the issuance of debt will be financed for a period not to exceed the useful economic life of the improvements and in consideration of the ability of the Utility to absorb such additional debt service cost. The term of debt shall be determined by, but not limited to, the economic life of the assets financed, conditions in the capital markets, the availability of

adequate revenue streams to service the debt, and the existing pattern of debt payable from the applicable division of the Utility, but in no event will the term of such debt exceed forty (40) years.

## **2) Capitalized Interest**

From time to time, certain financings may require the use of capitalized interest from the date of issuance until the Utility is able to realize beneficial use and/or occupancy of the financed project. Interest may be capitalized through a period permitted by federal law and TCA if it is determined that doing so is beneficial to the financing by the Utility's Board of Directors and is appropriately memorialized in the legislative action authorizing the sale and issuance of the debt.

## **3) Debt Service Structure**

General Obligation debt issuance shall be planned to achieve relatively net level debt service or level principal amortization considering the Utility's outstanding debt obligations, while matching debt service to the useful economic life of facilities. Absent events or circumstances determined by its Board of Directors, the Utility shall avoid the use of bullet or balloon maturities (with the exception of sinking fund requirements required by term bonds) except in those instances where such maturities serve to make existing overall debt service level or match specific income streams. Debt which is supported by project revenues and is intended to be self-supporting should be structured to achieve level proportional coverage to expected available revenues.

## **4) Call Provisions**

In general, the Utility's Debt should include a call feature no later than ten (10) years from the date of delivery of the bonds. The Utility will avoid the sale of long-term debt which carries longer redemption features unless a careful evaluation has been conducted by the Utility and/or financial professionals, if any, with respect to the value of the call option and the financial goals of the Utility.

## **5) Original Issuance Discount/Premium**

Debt with original issuance discount/premium will be permitted.

## **6) Deep Discount Bonds**

Deep discount debt may provide a lower cost of borrowing in certain capital markets. The Utility and/or financial professionals, if any, should carefully consider their value and effect on any future refinancing as a result of the lower-than-market coupon.

# **VII. DEBT TYPES**

When the Utility determines that debt is appropriate, the following criteria will be used to evaluate the type of debt to be issued.

## **I. Security Structure**

### *a) Revenue Debt*

The Utility may issue debt supported exclusively with revenues generated by one of its four divisions ("Revenue Debt"), where repayment of the debt service obligations on such Revenue Debt will be made through revenues generated from that division of the Utility.

*b) Capital Leases*

The Utility may use capital leases to finance projects assuming the Utility and/or financial professionals, if any, determine that such an instrument is economically feasible.

**II. Duration**

**a) Long-Term Debt**

The Utility may issue long-term debt when it is deemed that capital improvements should not be financed from current revenues or short-term borrowings. Long-term debt will not be used to finance current operations or normal maintenance. Long-term debt will be structured such that financial obligations do not exceed the expected useful economic life of the project(s) financed.

*i. Serial and Term Debt.* Serial and Term Debt may be issued in either fixed or variable rate modes to finance capital infrastructure projects;

*ii. Capital Outlay Notes (“CONs”).* CONs may be issued to finance capital infrastructure projects with an expected life up to twelve years; or

*iii. Capitalized Leases.* Capitalized Leases may be issued to finance infrastructure projects or equipment with an expected life not greater than its expected useful life.

**b) Short-Term Debt**

Short-term borrowing may be utilized for:

- i. Financing short economic life assets;
- ii. The construction period of long-term projects;
- iii. For interim financing; or
- iv. For the temporary funding of operational cash flow deficits or anticipated revenues subject to the following policies:
  - *Bond Anticipation Notes (“BANs”).* BANs, including commercial paper notes issued as BANs, may be issued instead of capitalizing interest to reduce the debt service during the construction period of a project or facility. The BANs shall not mature more than 2 years from the date of issuance. BANs can be rolled in accordance with federal and state law. BANs shall mature within 6 months after substantial completion of the financed facility.
  - *Revenue Anticipation Notes (“RANs”).* RANs shall be issued only to meet cash flow needs consistent with a finding by bond counsel that the sizing of the issue fully conforms to the Code and state requirements and limitations.
  - *Lines of Credit.* Lines of Credit shall be considered as an alternative to other short-term borrowing options. A line of credit shall only be structured to federal and state requirements.



- *Other Short-Term Debt.* Other Short-Term Debt including commercial paper notes, BANs, Capitalized Leases and CONs may be used when it provides an interest rate advantage or as interim financing until market conditions are more favorable to issue debt in a fixed or variable rate mode. The Utility will determine and utilize the most advantageous method for short-term borrowing. The Utility may issue short-term Debt when there is a defined repayment source or amortization of principal.

### **III. Interest Rate Modes**

#### **a) Fixed Rate Debt**

To maintain a predictable debt service schedule, the Utility may give preference to debt that carries a fixed interest rate.

#### **b) Variable Rate Debt**

The Utility recognizes the value of variable rate debt obligations in certain circumstances and that government entities have benefitted from the use of variable rate debt in the financing of infrastructure and capital improvements. The Utility also recognizes that there are inherent risks associated with the use of variable rate debt. To mitigate these risks, the Utility will:

1. Monitor historical and projected interest rates for variable rate debt
2. Reasonably limit the total outstanding variable rate debt in relation to total debt. Management will monitor interest rates and take appropriate steps to fix interest rates in the event of increasing interest costs. The analysis of variable rate debt costs will take into consideration the amount and investment strategy of the Utility's operating cash. Long term financial planning will consider the possible impact of increasing interest costs associated with variable rate debt.

### **VIII. USE OF DERIVATIVES**

As of 7/1/2011, the Utility has no outstanding derivatives with its debt portfolio. The Utility has no plans to use derivatives or other similar financial structures in the future. Prior to any reversal of this provision:

- 1) A written management report prepared by the Utility and/or financial professionals, if any, outlining the potential benefits and consequences of utilizing these structures must be submitted to the Utility's Board of Directors and the City Council; and
- 2) The Utility's Board of Directors must adopt a specific amendment to this policy concerning the use of derivatives or interest rate agreements that complies with the State Funding Board guidelines.

### **IX. REFINANCING OUTSTANDING DEBT**

Athens Utilities Board may refund debt when it is in the best financial interest of the Utility to do so. The Utility in conjunction with financial professionals, if any, shall have the responsibility to analyze outstanding debt for refunding opportunities. The decision to refinance must be explicitly

approved by the Utility's Board of Directors and the City Council, and all plans for current or advance refunding of debt must be in compliance with all state laws and regulations.

The General Manager and Superintendent of Accounting will consider the following issues when analyzing possible refunding opportunities:

**1) Onerous Restrictions**

Debt may be refinanced to eliminate onerous or restrictive covenants contained in existing debt documents.

**2) Restructuring for economic purposes**

The Utility may also refund debt when it is in its best financial interest to do so. Such a refunding will be limited to restructuring to meet unanticipated revenue expectations, achieve cost savings, mitigate irregular debt service payments, release reserve funds or remove unduly restrictive bond covenants or any other reason approved by the Utility Board of Directors in its discretion.

**3) Term of Refunding Issues**

Normally, the Utility will refund debt equal to or within its existing term. However, the Utility may consider maturity extension, when necessary to achieve desired outcomes, provided that such extension is legally permissible and it is approved by the Utility's Board of Directors and the City Council. The Utility may also consider shortening the term of the originally issued debt to realize greater savings. The remaining useful economic life of the financed facility and the concept of inter-generational equity should guide these decisions.

**4) Escrow Structuring**

The Utility shall use the least costly securities available in structuring refunding escrows. In the case of open market securities, a certificate will be provided by a third party agent, who is not a broker-dealer stating that the securities were procured through an arms-length, competitive bid process, that such securities were more cost effective than State and Local Government Obligations (SLGS), and that the price paid for the securities was reasonable within Federal guidelines. In cases where taxable debt is involved, the Utility, with the approval of bond counsel, may make a direct purchase as long as such purchase is the most efficient and least costly. Under no circumstances shall an underwriter, agent or any financial professionals sell escrow securities involving tax-exempt debt to the Utility from its own account.

**5) Arbitrage**

The Utility shall take all necessary steps to optimize escrows and to avoid negative arbitrage in its refunding. Any positive arbitrage will be rebated as necessary according to Federal guidelines.

## **X. METHODS OF ISSUANCE**

The Utility may consult with a financial professional regarding the method of selling debt. Subject to approval by the Utility's Board of Directors and the City Council, the Utility will determine the method of issuance of debt on a case-by-case basis consistent with the options provided by prevailing State law.

### **1) Competitive Sale**

In a competitive sale, the Utility's debt will be offered in a public sale to any and all eligible bidders. Unless bids are rejected, the debt shall be awarded to the bidder providing the lowest true interest cost as long as the bid adheres to the requirements set forth in the official notice of sale.

In a competitive sale, a financial advisor may bid on an issue for which they are providing advisory services only if:

- a) Authorized by the rules and regulations of the Municipal Securities Rulemaking Board (the "MSRB"), including Rule G-23, as may be amended and modified;
- b) The Legislative Body or designated official grants in writing specific authority on a transaction by transaction basis;
- c) Such sale is properly carried out through a widely and publicly advertised sale, during normal bond sale hours, and through an industry standard, electronic bidding platform; and
- d) The financial advisory fee is separately disclosed and billed from the underwriting fee.

### **2) Negotiated Sale**

The Utility recognizes that some securities are best sold through a negotiated sale with an underwriter or group of underwriters. The Utility shall assess the following circumstances in determining whether a negotiated sale is the best method of sale:

- a) State requirements on negotiated sales;
- b) Debt structure which may require a strong pre-marketing effort such as those associated with a complex transaction generally referred to as a "story" bond;
- c) Size or structure of the issue which may limit the number of potential bidders;
- d) Market conditions including volatility wherein the Utility would be better served by the flexibility afforded by careful timing and marketing such as is the case for debt issued to refinance or refund existing debt;
- e) Whether the debt is to be issued as variable rate obligations or perhaps as zero coupon debt;

- f) Whether an idea or financing structure is a proprietary product of a single firm;
- g) In a publicly offered or privately placed, negotiated sale, a financial advisor, if any, shall not be permitted to resign as the financial advisor in order to underwrite or privately place an issue for which they are or have been providing advisory services;
- h) The underwriter shall clearly identify itself in writing as an underwriter and not as a financial advisor from the earliest stages of its relationship with the Utility with respect to the negotiated issue. The underwriter must clarify its primary role as a purchaser of securities in an arm's length commercial transaction and that it has financial and other interests that differ from those of the Utility. The underwriter in a publicly offered, negotiated sale shall be required to provide pricing information both as to interest rates and to takedown per maturity to the legislative body (or its designated official) in advance of the pricing of the debt.

**3) Private Placement**

From time to time, the Utility may elect to privately place its debt. Such placement shall only be considered if this method is demonstrated to be advantageous to the Utility.

**X. PROFESSIONALS**

**1) Financial Professionals**

As needed, the Utility may select financial professionals to assist in its debt issuance and administration processes. In selecting financial professionals, consideration should be given with respect to:

- b) relevant experience with municipal government issuers and the public sector;
- c) indication that the firm has a broadly based background and is therefore capable of balancing the Utility's overall needs for continuity and innovation in capital planning and debt financing;
- d) experience and demonstrated success as indicated by its experience;
- e) the firm's professional reputation;
- f) professional qualifications and experience of principal employees; and
- g) the estimated costs, but price should not be the sole determining factor.

**2) Miscellaneous**

**b. Written Agreements**

- i. Any financial professionals engaged by the Utility shall enter into written

agreements including, but not limited to, a description of services provided and fees and expenses to be charged for the engagement.

- ii. The Utility shall enter into an engagement letter agreement with each lawyer or law firm representing the Utility in a debt transaction. No engagement letter is required for any lawyer who is an employee of the Utility or lawyer or law firm which is under a general appointment or contract to serve as counsel to the Utility. Athens Utilities Board does not need an engagement letter with counsel not representing the Utility, such as underwriters' counsel.
- iii. The Utility shall require all financial professionals engaged in the process of issuing debt to clearly disclose all compensation and consideration received related to services provided in the debt issuance process by both the Utility and the lender or conduit issuer, if any. This includes "soft" costs or compensations in lieu of direct payments.
- iv. If the Utility chooses to hire financial advisors, it will enter into a written agreement with each person or firm serving as financial advisor for debt management and transactions. Whether in a competitive sale or negotiated sale, the financial advisor will not be permitted to bid on, privately place or underwrite an issue for which they are or have been providing advisory services for the issuance.
- v. If there is an Underwriter, the Utility will require the underwriter to clearly identify itself in writing (e.g., in a response to a request for proposals or in promotional materials provided to an issuer) as an underwriter and not as a financial advisor from the earliest stages of its relationship with the Utility with respect to that issue. The underwriter must clarify its primary role as a purchaser of securities in an arm's-length commercial transaction and that it has financial and other interests that differ from those of the Utility. The underwriter in a public offered, negotiated sale will be required to provide pricing information both as to interest rates and to takedown per maturity to the Utility's Board of Directors and the City Council in advance of the pricing of the debt.

#### **b) Conflict of Interest**

- i. Financial professionals involved in a debt transaction hired or compensated by the Utility shall be required to disclose to the Utility existing client and business relationships between and among the professionals to a transaction (including but not limited to financial advisors, swap advisors, bond counsel, swap 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 allow the Utility to appreciate the significance of the relationships.

Financial 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.

## **VIII. COMPLIANCE**

### **1) Continuing Annual Disclosure**

Normally at the time debt is delivered, the Utility will execute a Continuing Disclosure Certificate in which it will covenant for the benefit of holders and beneficial owners of the publicly traded debt to provide certain financial information relating to the Utility by not later than twelve months after each of the Utility's fiscal years, (the "Annual Report) and provide notice of the occurrence of certain enumerated events. The annual report (and audited financial statements, if filed separately) will be filed with any State Information Depository (the "SID") established in the State of Tennessee. If the Utility is unable to provide the annual report to the SID by the date required, notice of each failure will be sent to the SID on or before such date. The notices of certain enumerated events will be filed by the Utility with the SID. The specific nature of the information to be contained in the annual report or the notices of significant events is provided in each Continuing Disclosure Certificate. These covenants are made in order to assist underwriters in complying with SEC Rule 15c2-12(b) (the "Rule").

### **2) Arbitrage Rebate**

The Utility will also maintain a system of record keeping and reporting which complies with the arbitrage rebate compliance requirements of the Internal Revenue Code (the "Code").

### **3) Records**

The Utility will also maintain records required by the Code including, but not limited to, all records related to the issuance of the debt including detailed receipts and expenditures for a period up to 6 years following the final maturity date of the debt or as required by the Code.

## **IX. DEBT POLICY REVIEW**

### **1) General Guidance**

The guidelines outlined herein are only intended to provide general direction regarding the future issuance of debt. The Utility maintains the right to modify this policy and may make exceptions to any of its guidelines at any time to the extent that the execution of such debt achieves the goals of the Utility as long as such exceptions or changes are consistent with TCA and any rules and regulations promulgated by

the State.

This policy should be reviewed from time to time as circumstances, rules and regulations warrant.

**b. Designated Official**

The General Manager and Superintendent of Accounting are responsible for ensuring substantial compliance with this policy.

